National Budget Brief

South Africa

2020

unicef

for every child

Preface

This budget brief is one of **six** that explores the extent to which the national budget and social services sector budgets address the needs of children under 18 years in **South Africa**. The briefs analyse the impact of the coronavirus (COVID-19) pandemic on allocations for children by comparing the baseline budget introduced in February 2020 with the adjusted budget presented to Parliament in June 2020. Each brief considers the evidence and draws conclusions about how the government's emergency public finance response affects services and programmes that benefit children**.**

Key messages and recommendations

The South African economy is projected to decline by 7.2 per cent in 2020. Due to the restrictions on economic activity and a lower revenue intake, the consolidated budget is projected to have a 16 per cent of gross domestic product (GDP) deficit in FY2020, almost double what the baseline budget projected in February 2020.

The restrictions in economic activity will result in a smaller economy in 2020 and beyond. Fewer people will be employed and the impact appears to be more severe for lower household income groups. Higher income households appear to have maintained their high pre-lockdown levels of employment.

The government's response to its combined explicit and implicit contingent liabilities in the context of the pandemic was to cap its total relief contributions to 500 billion (R)(or 10 per cent of the country's GDP). While it is unclear whether additional funding will be sought to address the impact of the pandemic, given the novelty that is the coronavirus pandemic, it is appropriate that flexibility in spending and further allocations is maintained to best respond to the evolving social, health and economic situation.

The government's efficiency and equity considerations in the adjusted budget appear correct, but flaws in the implementation of measures to target poor households have reduced the overall efficiency and impact of the emergency response. The government is encouraged to:

- Expedite the processing of the special COVID-19 grant and ensure efficient payouts, including back payments to successful applicants; and
- Urgently reach out and prioritise the delivery of food parcels to households that most need food.

The above-inflationary increases through the social grants top-ups are a welcome development and should point to a future framework for adjusting social grants to make their impact sustainable and meaningful. The government is encouraged to:

- Consider extending the six-month top-up period to allow sufficient adjustment to the impact of the lockdown; and
- Consider annual adjustments that are significantly above consumer price inflation to recognise the myriad pressures on poor households' budgets.

Six out of ten children, or 62.1 per cent of children, are multidimensionally poor. This finding is consistent with an income poverty line that is based on the upper-bound poverty line which finds that 67 per cent of children are located in income-poor families.

Multidimensionally poor children are overwhelmingly located in rural areas, live in the traditionally poor provinces of Eastern Cape, KwaZulu-Natal and Limpopo, have a household head that is female and Black African, and live in households where few adults are gainfully employed.

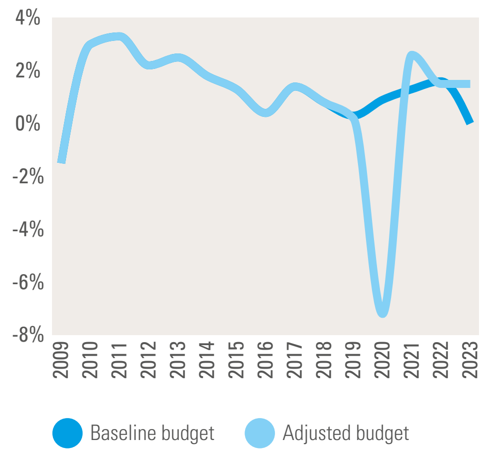
1. Macro and socioeconomic context

Macroeconomic trends

The South African economy will decline by 7.2 per cent in 2020 but is expected to make a fast recovery in 2021 and beyond (Figure 1). Noticeably, the adjusted budget's projections are more favourable than the baseline budget but given the uncertainty about the net impact of the pandemic, these projections have to treated with some level of scepticism.

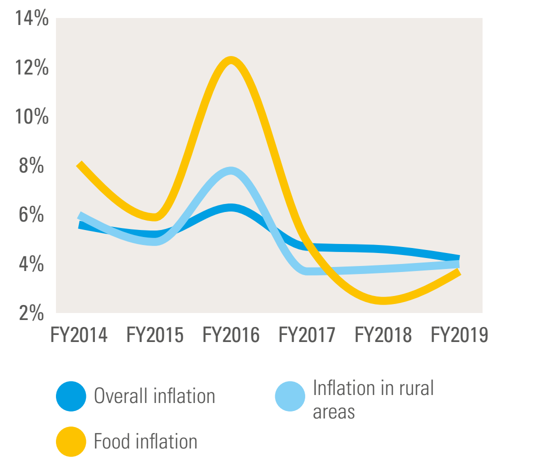
While food inflation was consistently higher than the overall inflation rate between FY2014 and FY2017, since FY2018, consumer price inflation averaged higher values (Figure 2). Lower consumer demand after the droughts in 2017 and 2018 contributed to the fall in food inflation, whereas higher energy (fuel) costs contributed to the rise in consumer price inflation.

Figure 1: Real GDP growth in baseline and adjusted budget 2020, between FY2009 and FY2023 (%)



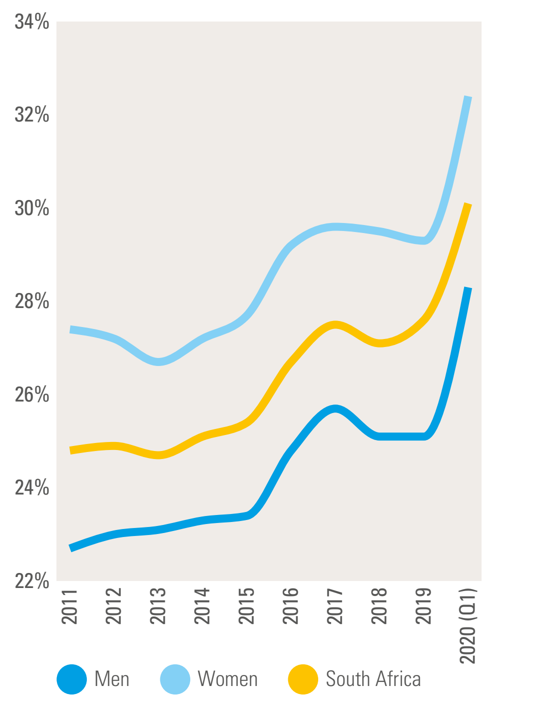
Source: South African Reserve Bank online query (for 2007–2018) for real GDP; National Treasury Budget Reviews 2019 and 2020; National Treasury Supplementary Budget Review 2020

Figure 2: Overall consumer price inflation, inflation in rural areas and food inflation for the country, between FY2014 and FY2019 (%)



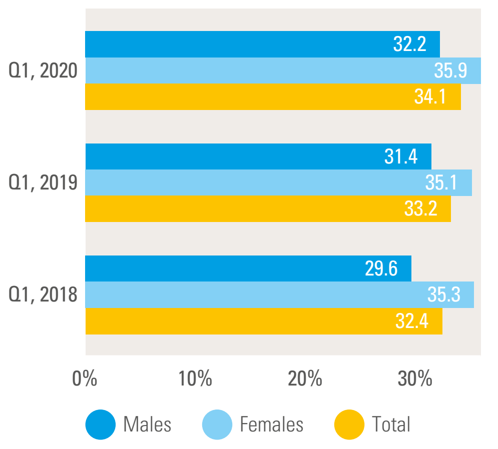
Source: Statistics South Africa online time series on consumer price inflation, <www.statssa.gov.za/?page_id=1854&PPN=P0141&SCH=7558>, own calculations | *Note:* Only food inflation values are explicitly indicated in the graph.

Figure 3: Unemployment rate by sex, between FY2011 and FY2020 (quarter 1 of 2020)



Source: Statistics South Africa Quarterly Labour Force, quarter 1, 2020 (officially released in 23 June 2020).

Figure 4: Unemployment rate for young people (15–24 years) who were not in education, employment or training in quarter 1, between FY2018 and 2020 (%)



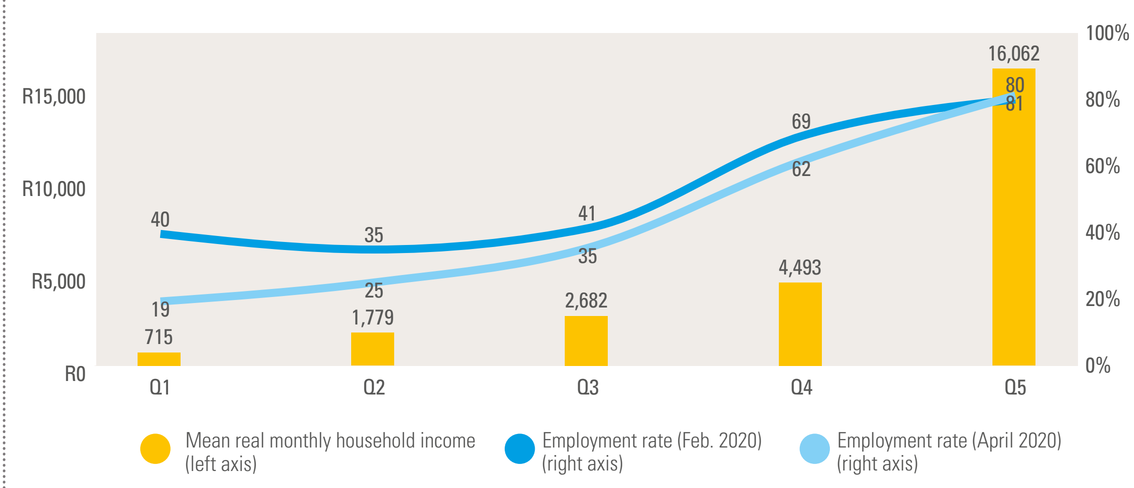
Source: Statistics South Africa Quarterly Labour Force, quarter 1, 2020 (officially released on 23 June 2020)

Annual unemployment in 2019 was 27.6 per cent and economically active women recorded an unemployment rate of 29.3 per cent against the 25.1 per cent unemployment rate of their male counterparts (Figure 3). In the first three months of 2020, the unemployment rate increased to a national average of 30.1 per cent with female unemployment at just over 32 per cent. Given the economic lockdown in progress, significantly higher numbers are expected for subsequent quarterly data.

The percentage of young people (between 15 and 24 years) who were not in employment, education or training increased from 32.4 per cent in quarter 1 in FY2018 to 34.1 per cent in the same quarter in FY2020 (Figure 4). Male unemployment is the largest contributor to the higher employment rate; it increased by approximately 3 per cent between FY2018 and FY2020, while female unemployment moved slightly from its high base of 35 per cent in FY2018.

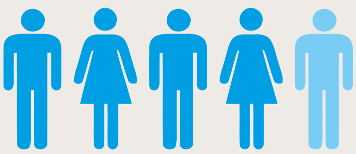
Employment was much lower in the lower household income groups prior to the

Figure 5: Real mean household monthly income (rand) by employment rate for five household income groups 2020 (February and April 2020)



Source: Kohler and Bhorat, NIDS Coronavirus Rapid Mobile Survey (CRAM), 2020, p. 17

country's lockdown and these groups share a much larger burden after the introduction of the nationwide lockdown (Figure 5). While 40 per cent of individuals in households with the lowest income had employment prior to the lockdown, that number dropped to less than 20 per cent in April 2020. Employment has remained stable for the higher household monthly income group and roughly four out of five adults remained employed between February 2020 and April 2020.



Roughly **four out of five** adults remained **employed**

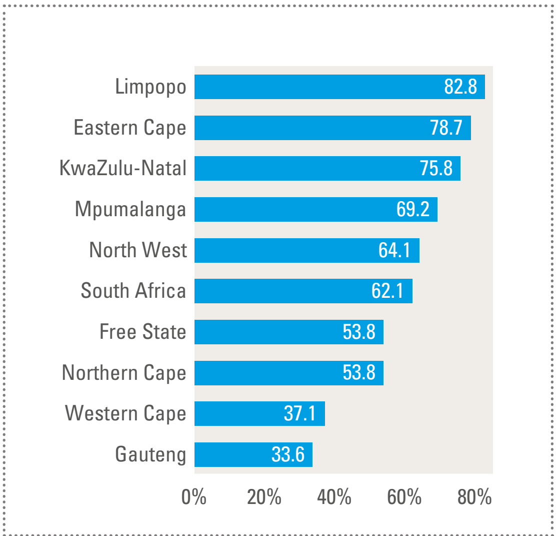
between **February 2020** and **April 2020.**

Social development trends

More than six out of ten children are multi-dimensionally poor in South Africa (Figure 6). The traditionally rural provinces share the largest burden of poor learners with Limpopo leading the country's poverty rate (82.8 per cent), while the Western Cape and Gauteng – both traditionally urban provinces – have the lowest poverty rates at 37 and 34 per cent respectively.

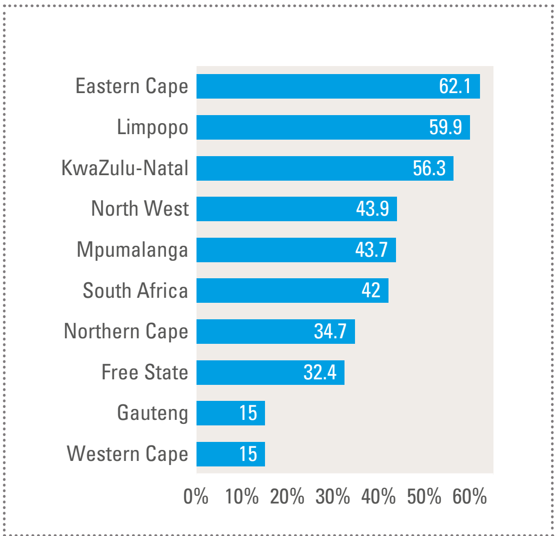
The latest child poverty study by Statistics South Africa[1] established that four out of ten children are both income-poor and multidimensionally poor (or deprived) (Figure 7). This overlap is pertinent, especially for the traditionally rural provinces of the Eastern Cape and Limpopo, whereas in the more urban provinces of Gauteng and Western Cape, only a small percentage of children are both income-poor and multidimensionally poor according to the measure used by Statistics South Africa.

Figure 6: Multidimensional poverty (deprivation) among children 0–17 years by province (%)



Source: Statistics South Africa 2020, p. 21 | *Note:* A child is considered deprived if she/he has three or more deprivations across seven dimensions (variables).

Figure 7: Overlap between money-metric poverty and multidimensional poverty for children 0–17 years by province (%)



Source: Statistics South Africa 2020, p. 21 | *Note:* Statistics South Africa uses the lower-bound poverty line (R647 per person per month) to categorise children as money-metric poor.

Takeaways

- The restrictions in economic activity will result in a smaller economy in 2020 and beyond. Fewer people will be employed and the impact appears to be more severe for lower household income groups.
- Overall unemployment climbed to 30 per cent in quarter 1 of FY2020, while the unemployment rate for women is marginally above the national rate at 32.4 per cent.
- The rate of unemployment among young females (15–24 years) is worse and stood at nearly 36 per cent in quarter 1 of FY2020.
- The country's first child multidimensional poverty study delivered sobering results with more than 62 per cent of children considered deprived; most of these children live in the traditionally poor and rural provinces of the Eastern Cape, KwaZulu-Natal and Limpopo.
- More urban provinces, such as Gauteng and Western Cape, have a much lower child poverty rate due to more developed social infrastructure in the basic education and health sectors.

2. Response to COVID-19

Budget process considerations

Annually, the government tables a budget in February and to allow for in-year changes, and an adjusted budget as well as an update of key economic assumptions is presented to Parliament in October. However, due to the impact of the pandemic and the need to provide for emergency spending, the government tabled a special adjustment budget in June 2020. The main purposes of the adjusted budget are to provide clarity on: (1) the extent and scope of the emergency response; (2) how the emergency response will be funded; and (3) the extent to which the emergency forced reprioritisation of the proposed allocations that were made in February 2020.

Legal authority for the introduction of the (special) adjusted budget is provided through the country's Public Finance Management Act (PFMA), Act No. 1 of 1999. Section 30 of the PFMA provides for the national Minister of Finance to introduce an adjustment budget to provide for emergency expenditures (section 16): (1) to account for significant and unforeseeable social and economic events; (2) to account for the shifting of funds within and between votes (spending units) in section 42; and (3) to utilise savings under a vote to defray expenditure in the same vote (but different programme) in section 43. Similar provisions are made for the provincial Minister of Finance using section 31 of the PFMA.

Given the evolving nature of the country's response to the pandemic, a second adjusted budget will be presented to Parliament in October 2020. This budget will represent a more

complete response to the crisis and will also be accompanied by a mid-year statement that updates the main macro-economic assumptions laid out in February 2020 (baseline budget) and the adjusted budget in June 2020.

Government's approach to the crisis: explicit and implicit contingent liabilities

Gamper et al. (2017)[2] **argue that expenditures made in response to disasters are government contingent liabilities.** They define contingent liabilities as "… (government) obligations that are triggered when a potential, but uncertain future event occurs." Some obligations are *explicit* and are defined in relevant policy frameworks and legislation, while others are *implicit* and depend on the perceived moral obligation and expectations that fall upon governments during disasters.

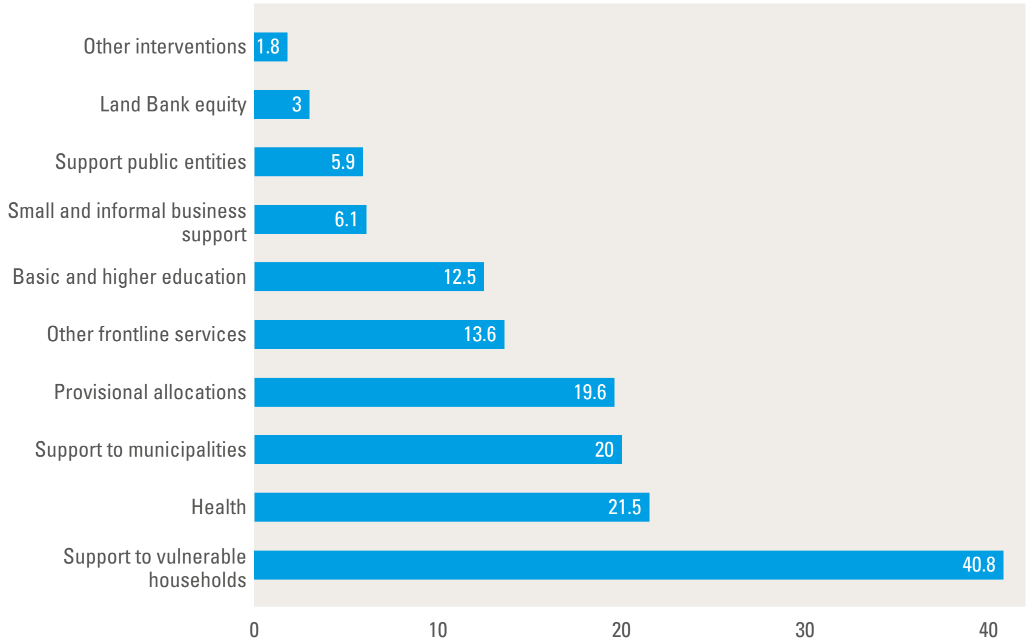
Theoretically, the government's financial obligations could range from the entire budget proposed in FY2020 (R1.9 trillion) to a more restricted amount (hundreds of billions). The financial size of the entire response will be determined by how the government **quantifies its explicit contingent liabilities *and* how it responds to implicit contingent liability claims (media coverage, moral expectations from the public, etc.)**.

The government's actual response involved a number of components that relied on both domestic and international financing. First, it mobilised the entire public sector balance sheet to finance its response (for example, loan schemes underwritten by the central bank and treasury or drawing down on social security fund surpluses to finance aid to households and businesses). Second, it took advantage of the limited social and economic movements by reprioritising baseline allocations to finance large parts of the emergency response. Third, it is using international finance institutions (BRICS Development Bank, the International Monetary Fund, African Development Bank) to support its emergency response. Finally, it announced a widely discussed R500 billion package (inclusive of fiscal and monetary interventions), suggesting that it views its expenditure responsibilities as capped to avoid being drawn into implicit liabilities that cannot be met.

Broad elements of the COVID-19 spending proposals

Overall, the largest part of the immediate emergency response is intended to cover vulnerable households through the extension and top-ups to social grants (R41 billion), support to health authorities to address the health dimensions of the pandemic (R21 billion), and support to municipalities to help address water and sanitation issues in communities and the public transport system (R20 billion). Other provisions cover issues such as the routine deep-cleansing of schools, support with education catch-up plans in basic and higher education, and relief to small and informal businesses.

Figure 8: Broad allocations in response to the COVID-19 crisis (R billion)



Source: National Treasury, Supplementary Budget Review 2020, p. 8

Takeaways

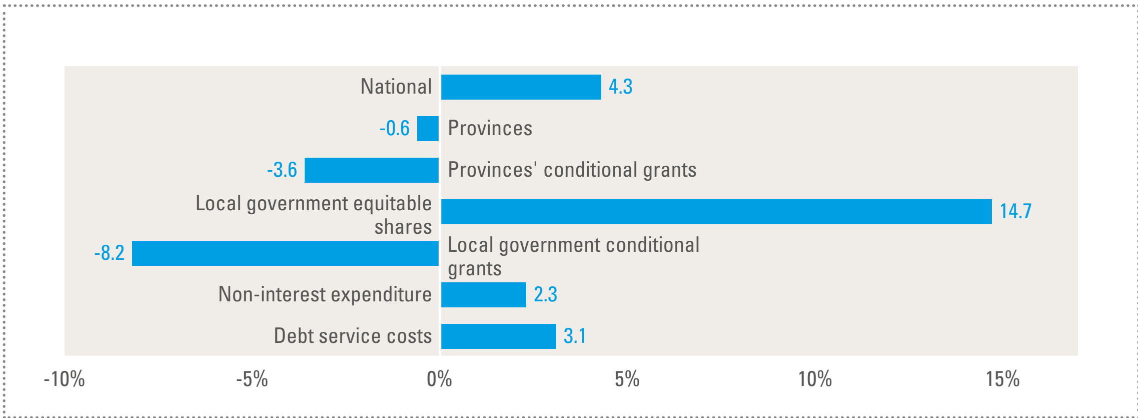
- South Africa will have two adjusted budgets in 2020. The first addresses the immediate financing needs related to the emergency (June 2020), while the second adjusted budget will take a broader view of the emergency response and the country's public finances beyond 2020.
- The country responded to the financing of the emergency response by capping the government's total contributions at R500 billion (or 10 per cent of the country's GDP). This was in direct response to its explicit and implicit contingent liabilities in the context of the social, medical and economic emergency.
- The country has relied on domestic financing, international financing and utilising the full spectrum of state assets (such as social security funds and reserves of the central bank) to finance its emergency response.
- Vulnerable households are being supported through an extensive social grants programme and various top-ups to augment the existing social grants system.

3. Assessment of reprioritisation proposals

Revised division of revenue framework 2020

Conditional grant funding at the provincial and local government level bore the brunt of government's attempt to find resources within the baseline budget to finance its emergency response (Figure 9). Local government and provincial conditional grants have been reduced by 8.2 per cent and 3.6 per cent, respectively. The provinces' equitable share remains unchanged and will be required to repurpose some of that financing to address COVID-19 issues. Local government receives additional allocations via its equitable share, which is expected to increase by almost 15 per cent. National government departments get a 4.3 per cent boost to help with the national health response and to provide critical social assistance support to vulnerable and distressed households.

Figure 9: The revised division of revenue framework (percentage change)



Source: National Treasury Supplementary Budget Review 2020, p. 9

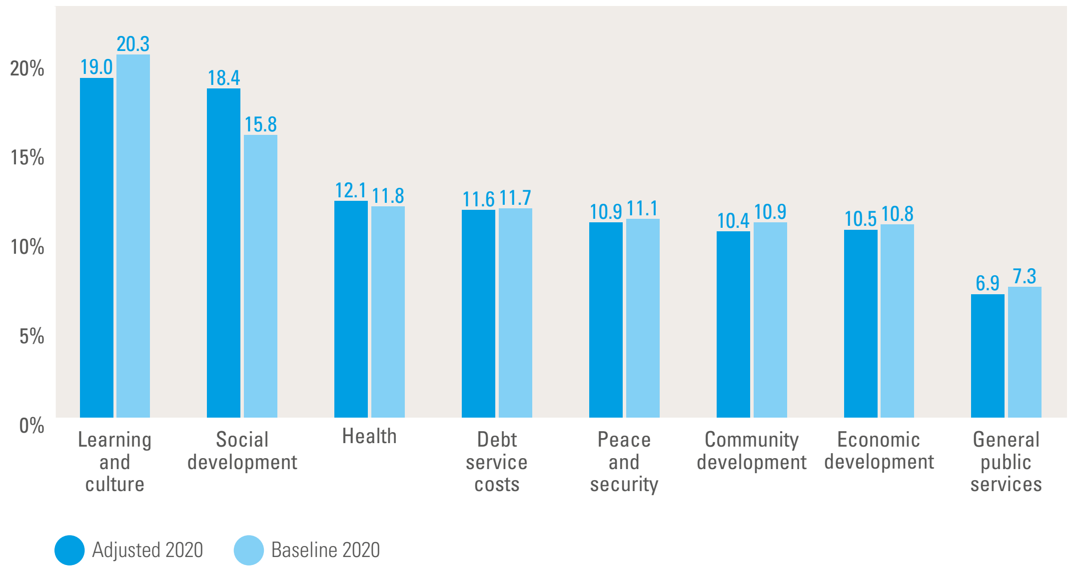
Government is adding R36 billion to the baseline budget to finance its emergency response (Table 1). Effectively, it adds R145 billion to the baseline and uses R109 billion within the baseline budgets to finance the upward adjustment in expenditure, leaving just R36 billion (or 2.3 per cent of the main budget) to support additional expenditures. National departments' baselines are cut by R54 billion, while the joint local and provincial conditional grant suspensions total more than R25 billion.

Table 1: Revisions to main budget[3] non-interest expenditure (R billion)

Main budget non-interest expenditure (baseline budget)	**1,536.7**
Proposed upward expenditure adjustments	**145.0**
Proposed downward expenditure adjustments	**-100.8**
National departments' baseline suspensions	-54.4
Repurposing of provincial equitable shares	-20.0
Provincial conditional grant suspensions	-13.8
Local government conditional grant suspensions	-12.6
Other adjustments	**-8.1**
National Revenue Fund payments	0.1
Downward revisions to skills development levy	-2.1
Lower skills development levy due to four-month holiday	-6.0
Revised non-interest expenditure	**1,572.7**
Change in non-interest expenditure from baseline budget	36.0

Source: National Treasury Supplementary Budget Review 2020, p. 9

Figure 10: Consolidated spending[4] by function as percentage of total government spending: FY2020 baseline budget and adjusted budget (%)



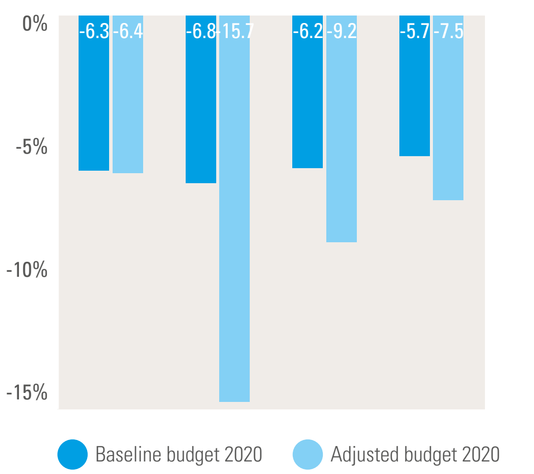
Source: National Treasury Supplementary Budget Review 2020, p. 13

Revised consolidated spending framework 2020

The largest shift in spending in the government's consolidated budget is reserved for social development (almost 3 per cent increase in shares) and a much smaller rise in health (less than 0.5 per cent). The learning and culture function suffers a small decline in shares because of the reduction in the basic education conditional grants, while debt service costs remain high at 12 per cent of available funding.

Due to the economic impact of the pandemic, the country's consolidated budget deficit is expected to increase from 6.8 per cent of the GDP in FY2020 to 15.7 per cent in the adjusted budget (Figure 11). This is a very significant shift and adds to the growing debt challenges. For the outer years, the government projects to have a smaller deficit, but the quality of the estimates is dependent on how fast the economy recovers, consensus around government's reform agenda and the extent of implementation of the reform proposals. Also, the outer year estimates are significantly higher in comparison to projections in the baseline budget.

Figure 11: Revised consolidated budget balances as a percentage of GDP, FY2020 baseline budget and adjusted budget (%)



Source: National Treasury Budget Review 2020 and National Treasury Supplementary Budget Review 2020

Takeaways

- Conditional grants for provincial and local governments were targeted for suspensions and repurposing and contribute heavily to the financing of the emergency response.
- Reduced activities, especially at public schools, appear to be the reason for such suspensions, while at the local government level, most infrastructure grants are repurposed to address immediate COVID-19 water and sanitation challenges.
- Non-interest expenditure in the main budget grew by R36 billion (or 2.3 per cent of the main budget), which is indicative of the large reprioritisations within existing baselines.
- In terms of function, social development garners the largest financing support because of the need to take care of vulnerable and distressed households during the pandemic, while the health function receives a small additional share to finance the country's national health response.
- COVID-19 has a devastating impact on the government's overall fiscal balance and has been readjusted to be almost 16 per cent of the GDP as compared to a 7 per cent deficit in the baseline budget.

4. Implications for children

Public finance considerations in the adjusted budget FY2020

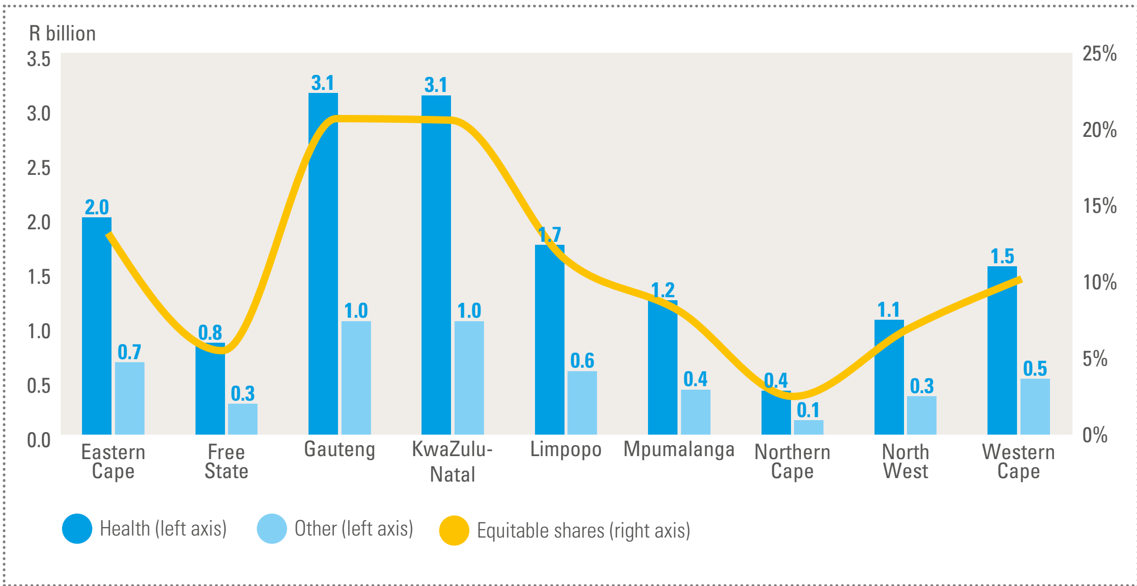
The adjusted budget is framed under very specific social, health and economic circumstances and gives different weights to the public finance goals of efficiency and equity. It takes advantage of the restricted movement of the population by suspending projects or deferring the implementation of programmes that are not deemed absolutely necessary. This allows the government to use a portion of the suspended funds to be allocated to the emergency response, thus making the most efficient use of available public resources. In principle, its equity goals appear adequate (targeting the most vulnerable households and individuals), but the relative efficiency in reaching those most affected means potentially less spending.[5] This in turn, reduces the overall efficiency and impact of the public finance response to the emergency.

While emergency public finance responses are traditionally driven by the motto of 'Go big, early and household', much of the evidence for this is based on natural disasters. Uncertainty about the shape and impact of the pandemic should produce caution and induce a flexible government response which allows government to change course when needed and draws down on the broader public sector balance sheets if and when needed. This is why the second adjusted budget planned for October 2020 will give a better sense of whether the initial emergency response was adequate and whether it has to be adjusted.

Winners and losers in the adjusted budget 2020

R20 billion of the provincial equitable share allocations was repurposed to address the health and related emergencies (Figure 12). R15 billion was 'allocated' to health-related functions and the remaining R5 billion was distributed among other essential functions in education and social welfare. The provinces' overall shares were used as guidance in terms of determining the quantum of funding to be repurposed to health and other functions. However, while it satisfies a broader equity criterion, this 'allocation' process does not necessarily direct resources to where they are needed most (as determined by infection rates). Urban provinces such as Gauteng and Western Cape have experienced the worst infection rates, and the urban parts of KwaZulu-Natal and the Eastern Cape are subjected to similar stresses, thus raising questions about the appropriateness of using the provinces' equitable shares as a guiding criterion.

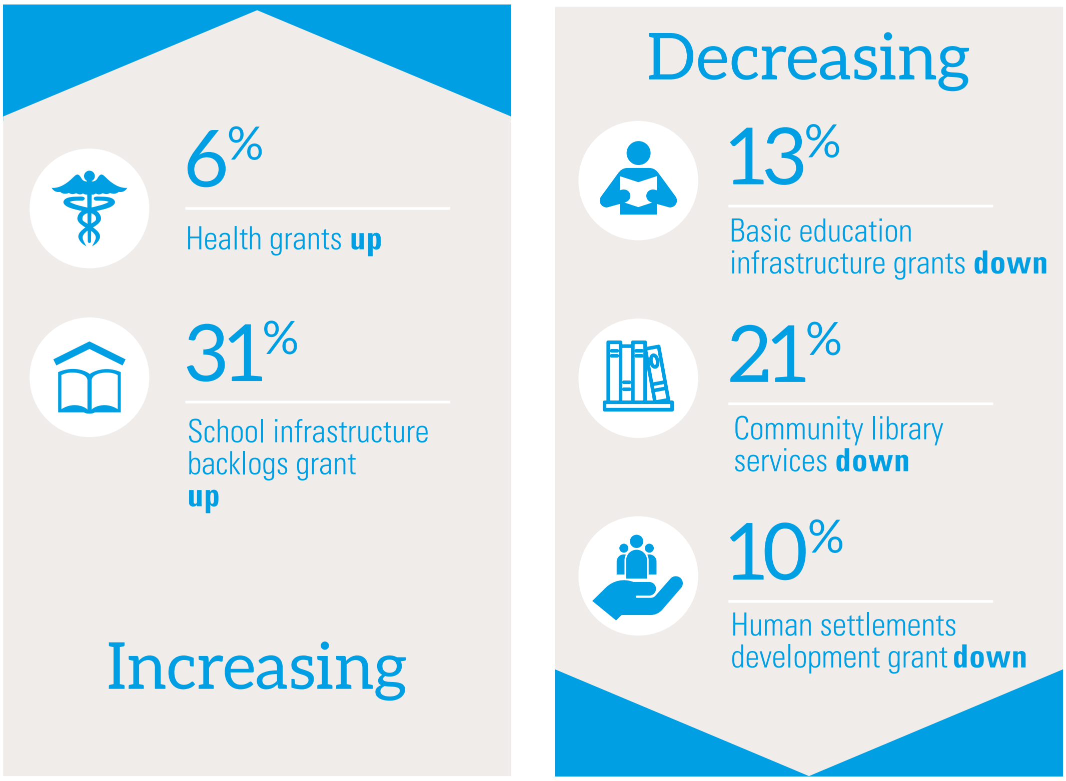
Figure 12: Repurposing of provincial equitable shares to address health and other concerns



Source: National Treasury Supplementary Budget Review 2020, p. 18 | *Note:* R15 billion (health) and the R5 billion (other) were 'allocated' using the provinces' relative share.

Infrastructure grants in basic education, arts and culture and human settlements were targeted for suspensions and repurposing (Figure 13). Basic education infrastructure grants were reduced by 13 per cent, while community libraries were reduced by 21 per cent. Health grants – given their importance in the crisis – were increased on average by 6 per cent, while the repurposed school infrastructure backlogs grant received a 31 per cent boost to provide water and other facilities in schools.

Figure 13: Changes to the provincial grant framework in adjusted budget FY2020

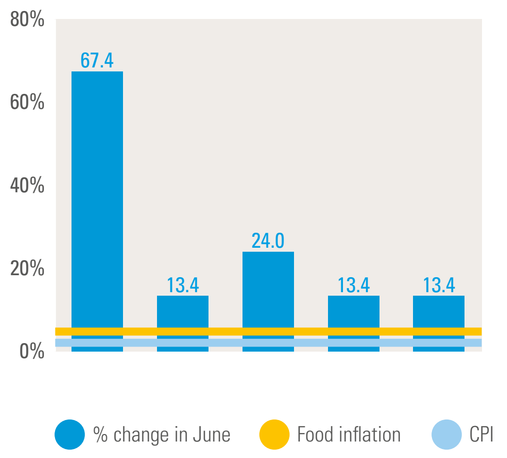


Source: National Treasury Supplementary Budget Review 2020, p. 41

Changes to local government conditional grant allocations

- For non-metropolitan municipalities, R4.4 billion of the *municipal infrastructure grant* has been repurposed to help with urgent repairs to water and sanitation infrastructure.
- For metropolitan municipalities, R2.3 billion has been reprioritised within the *urban settlements development grant* to help with the provision of water and sanitation to communities that lack access and to ensure a higher frequency and standard of service in informal settlements.
- R1.1 billion of the *public transport network grant* is reprioritised to help with the sanitisation of public transport.

Figure 14: Temporary changes in nominal value to social grants against food inflation and consumer price inflation in the adjusted budget FY2020



Source: National Treasury Supplementary Budget Review 2020, p. 15 | *Note 1:* Consumer price inflation and food inflation values are for May 2020. Grant changes were introduced in June 2020 | *Note 2:* Due to the fact that the child support grant top-up is paid out to a caregiver, the additional pay-out is regarded as a separate grant, called the caregiver grant.

The temporary changes to the nominal value of the social grants bode well for the affected individuals and households (Figure 14). These changes are way above the inflationary increases that preceded the changes in grant values in June 2020. A long-standing complaint is that annual changes to the grant system are pegged to the consumer inflation rate, whereas research[6] has shown that food inflation often outstrips consumer price inflation and that the practice of linking increases to inflation underestimated the pressure on poor households' spending power. While these changes are temporary, they provide some indication about the extent and direction of increases needed to make the social grant system sustainable and meaningful.

Takeaways

- The government's considerations of efficiency and equity in the adjusted budget appear to be correct, but flaws in the implementation of measures to target poor households have reduced the overall efficiency and impact of the emergency response.
- While the repurposing of the provincial equitable share allocations is welcomed, allocating additional health resources on the basis of the provinces' shares is likely to be less effective than using actual and projected infection rates as an allocation criterion.
- The above-inflationary increases through the top-ups to social grants are a welcome development and should point to a future framework for adjusting social grants to make their impact sustainable and meaningful.

Endnotes

1 Statistics South Africa, *Child Poverty in South Africa: A Multiple Overlapping Deprivation Analysis*, 2020, <www.statssa.gov.za/?page_id=1854&PPN=03-10-22&SCH=72653>, accessed 7 July 2020.

2 Gamper, C., L. Alton, B. Signer and M. Petrie, 'Managing disaster risk related contingent liabilities in public finance frameworks', *OECD Working Papers on Public Governance*, No. 27, OECD Publishing, Paris, 2017.

3 The main budget includes all spending financed from the country's National Revenue Fund. It will include allocations for national departments and their entities as well as equitable share transfers for provinces and local government. It also provides for the contingency reserves and debt servicing costs.

4 The consolidated budget or spending includes the main budget, provincial spending financed by own revenue (gambling tax, hospital fees, etc.) and the activities of social security funds (unemployment insurance fund, road accident fund, etc.) and public entities.

5 Concerns have been raised about the slow process of selecting and paying out the special COVID-19 grant. Companies and individuals have experienced delays in accessing funds from the government's unemployment insurance fund and there have been delays in getting food parcels to the most vulnerable individuals and households.

6 The Pietermaritzburg Economic Justice and Dignity Group has been tracking the price of a representative basket of food in KwaZulu-Natal and has consistently warned about inadequate annual adjustments to social grants.

United Nations Children's Fund
Equity House
659 Pienaar Street
Brooklyn
Pretoria
0181
www.unicef.org/southafrica

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