Country Case Study 5:

Operationalising the MTEF as a tool for Poverty Reduction: South Africa

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Abbreviations & Acronyms

ANC	African National Congress
DoR	Division of Revenue
FFC	Fiscal and Financial Committee
GEAR	Growth, Employment and Redistribution
MEC	Member of Executive Council
MinComBud	Ministers' Committee on the Budget
MTBPS	Medium Term Budget Policy Statement
MTEC	Medium Term Expenditure Committee
MTEF	Medium Term Expenditure Framework
NCOP	National Council of Provinces
RDP	Reconstruction and Development Programme
SALGA	South Africa Local Government Association

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1. Background[1]

The Medium Term Expenditure Framework (MTEF) was introduced in the 1998/9 financial year as part of a wide package of budget reforms in provincial and national government. Apartheid left South Africa with a high degree of inequality in wealth, income and in access to public services. Although the previous dispensation developed a pool of expertise and structures for financial planning and management, these were concentrated in the Pretoria bureaucracy, leaving corrupt and bloated bureaucracies within local authorities and apartheid's system of 'independent homelands', many of which failed to maintain any systems of accounts at all.

Exacerbating these challenges was the quasi-federalist negotiated political settlement of 1994. The creation of nine autonomous provinces with very different economic and demographic profiles, infrastructure, public sector capacity and development imperatives made the process of socio-economic redress and budget reform even more complex.

Against this background, the National Treasury[2] embarked on an ambitious programme of budget reform. It sought to meet the imperatives of the Reconstruction and Development Programme within the constraints of a large inherited debt, inflated expectations of the disenfranchised majority, vast social needs and the need to re-integrate into the global economy. But the most compelling reasons for the programme of budget reform were problems inherent in the budget: a rising deficit, poor delivery of services and a lack of transparency and accountability.

The historical budget system in South Africa, which evolved from the Westminster tradition, contains several weaknesses. First, within the previous budget process there was no link between planning and budgeting with directorates for each of these functions usually kept separate within the same departments. Planning was seen as a political process and budgeting as a technical exercise. Policies were not required to be costed and in most cases the data and methodology for doing so accurately did not exist.

Second, budgeting was incremental with small adjustments being made to allocations with little thought given to the activities being funded or to the long term goals of the relevant department. Activities were seldom reviewed to ensure that they were still necessary or that money was being spent effectively. Thus once an activity was in the budget, it was virtually impossible to remove it. As a result there was unsatisfactory evaluation of policies and programmes within departments from both a cash management and planning point of view. The focus of attention was on securing more money, not on delivery. It was therefore seldom necessary to restructure or evaluate the budget, since new programmes could be added to justify larger budgets.

Third, prior to the elections in 1994, Parliament had an even smaller role in the budget than it does now. Apart from the obvious racial bias of Parliament, Committees also tended to be part-time, and met only to approve the actions of the executive. This was particularly true of the budget. The ability and opportunity for the public or organised civil society to interact with the process was also even more limited than it is now.

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[1] This section is largely based on Walker and Mengistu 1999.

[2] The national Department of Finance was renamed as the National Treasury in 2000.

Fourth, the budget reporting format of the previous system only reported inputs to departments, but did not describe what that money would purchase (outputs) or how such expenditures would contribute to departmental aims (outcomes). Types of expenditure were listed without providing information on the purpose of that expenditure. The result was that the budget on its own did not provide much insight into government's policies nor its use of scarce resources. Although the budgeted amounts were voted on, virtually no departments supplied regular updates on actual expenditures to Parliament. The lack of spending trend information also made it difficult for Parliament to assess if budgets submitted were realistic. In fact the lack of standardisation in vote and programme structure made it almost impossible to compare expenditures across provinces for certain key expenditures, or to build an accurate composite picture of government spending.

These issues were not of pressing concern in the 1960's and 70's. The booming economy produced large revenues and there was a lack of pressure to reform and redistribute as most resistance movements had been squashed or driven underground by the political repression following the Defiance Campaign of the late 1950s. This changed when the economy slowed down in the 70s and political resistance resurfaced around the 1976 Soweto uprisings.

During the 1980's the first attempt at multi-year budget planning was made. The Manual on the Financial and Planning System of the State replaced the Budgeting by Objectives Manual in 1985 (this suggests some form of program budgeting – can anything be said about lessons from this experience to inform the current attention being given to performance indicators?), I don't have more than is given in points one, two and four above in an attempt to introduce multi-year budget planning. Spending agencies were requested to compile realistic budgets on the basis of policy priorities. For the first time departments were also asked to submit estimates for longer than the standard 12 months. In the absence of supporting initiatives and a clear link between budgets and planning, however, the initiative failed. Departments were obsessed with the annual cycle and the approach was abandoned.

The National Treasury first started to work on a Medium Term Expenditure Framework in 1994. It was a very closed, internal process restricted to senior government officials. Once the model was completed, and preliminary results available, these results were presented to Cabinet. Although Cabinet accepted the need to reform the budget system and effect transformation within a sustainable fiscal framework they rejected the 'second' MTEF as presented. The problem was less with the methodology itself than with the exclusive nature of and the lack of consultation in the process followed.

The present MTEF was introduced in 1997. The 1998/9 budget was the first prepared under the 1996 Constitution and the first year of implementation of the MTEF. The first Medium Term Budget Policy Statement (MTBPS) was published at the end of 1997 for the 1998/99 fiscal year. This pre-budget report presented government's overall fiscal policy objectives (balance between expenditure, revenue and the deficit) and its budget policy objectives (the relationship between spending decisions and policy priorities) for the forthcoming budget and the following two fiscal years.

The National Treasury admits that the first set of expenditure estimates were less than perfect, but in order to initiate the process it was more important for departments to produce the estimates than to predict expenditure accurately. A change in mindset was a fundamental part of the new process, and it was important to get departments and provinces to begin thinking in a new way, even if their first attempts were technically inaccurate. Similarly, it was important for all departments to produce these estimates, so that the process was inclusive. It would force all departments, irrespective of capacity, to begin to re-evaluate their activities and to undertake some kind of forward planning.

The introduction of the MTEF reflected many lessons learnt in the first two efforts at introducing it. Most importantly South Africa's commitment to cooperative governance has addressed the conflictual nature of the budget process without removing the imperative of fiscal discipline. The Budget Council[3] was a key innovation, as were the sectoral teams in encouraging a more collegial or cooperative approach to resolving budget conflicts. The idea of the Budget Council or 'Team Finance' is to reach consensus among provincial finance ministers on the distribution of revenue. It is not clear, however, that the Budget Council would have been as successful had there been more provinces controlled by opposition political parties.

Other measures to secure political commitment to the MTEF and reprioritisation include the formation of the Ministers' Committee on the Budget (MinComBud) and is supported by a number of discussion forums which includes the sectoral teams, a provincial Premier's forum and national and provincial Medium-Term Expenditure Committees. The South African approach has placed greater emphasis on political involvement throughout the process than is the case in many other countries. The MTEF has endeavoured to involve politicians in overseeing and managing the entire process, for the first time creating a link between policy planning and budget drafting. This required overcoming a certain resistance on the part of politicians, partly by keeping the process simple and accessible, and making explicit the political accountability involved.

As was the case in the first two efforts at implementing an MTEF, the Treasury took the lead in introducing and coordinating the MTEF process. Even though it had opted for a cooperative process that is mediated by various intergovernmental and inter- sectoral fora, it remains the driving force in the creation and coordination of these fora.

The MTEF was implemented across all departments as opposed to a focus on getting it right in some sectors. The Treasury was of the opinion that there were more benefits to getting estimates from all spending agencies than accurate analysis within a restricted number of sectors. There seems to be rationality in this – sectors differ so that lessons learned in some areas may not be easily transferred to analysis of other sectors. Demand creates its own capacity so that spending agencies will not begin to conduct analysis or collect data until they are forced to do so.

Given the transitional state of local government at the time, the MTEF process was not introduced in this third sphere of government. More recent efforts at introducing it at this level are described below.

2. The MTEF Process and the Organisational Framework

The South African MTEF process is a combination of a 'top-down' and 'bottom-up' process. Indicative aggregate envelopes, both government- wide and sectoral, are established before any individual spending bids are considered. A single ceiling is set for recurrent and capital expenditure and departments are expected to accommodate the uneven nature of capital expenditure in their three-year planning and projections. Once the bottom-up planning process has been completed, national cabinet and provincial executive councils do however consider and revise these envelopes. Subsequently spending agencies go through another round of planning based on their finalized allocations.

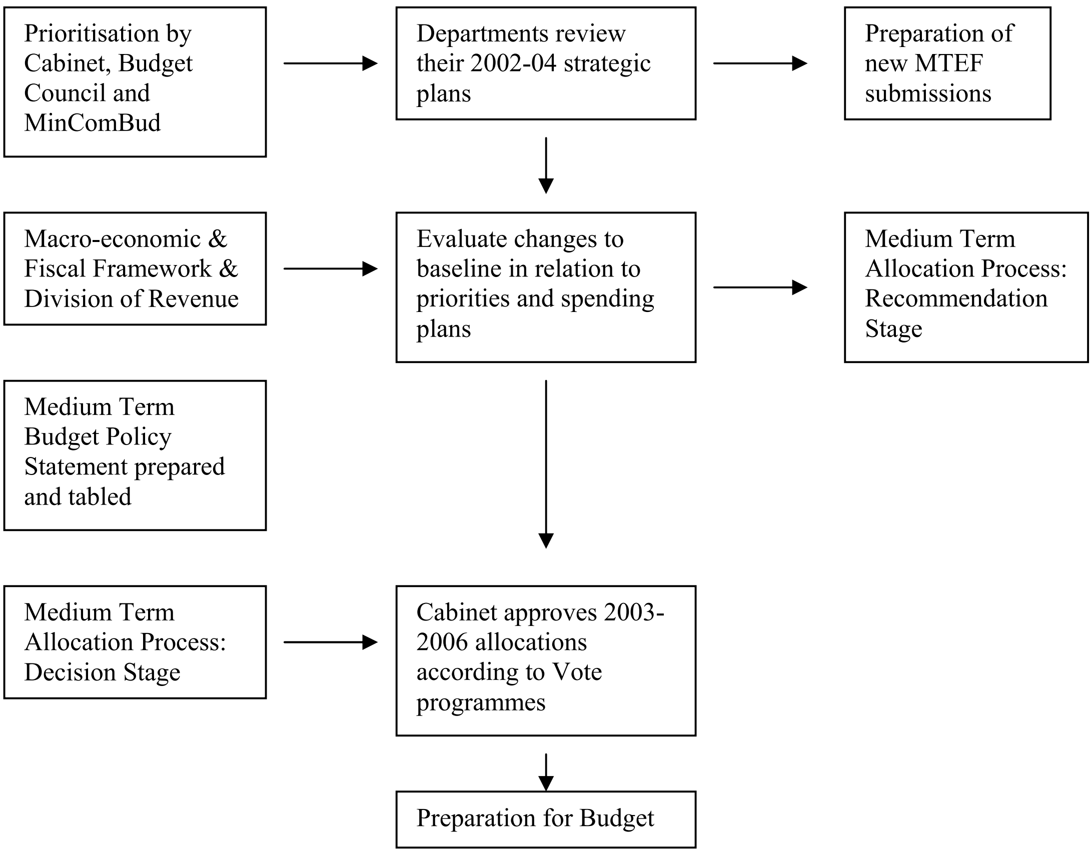
[3] The Budget Council is a consultative body, consisting of the Minister of Finance, the nine provincial MECs for Finance, the Heads of Treasury, Treasury advisors and the Director General of Finance. The Council makes recommendations to the Cabinet on fiscal and financial matters affecting provincial government.

The MTEF process and budget process are integrally related in South Africa. All draft budgets and bids for additional funding are required to include a consideration and projection of their medium-term impact. The rolling process restarts shortly after budgets have been tabled in parliament. The 2003//2004 budget process, for example, was initiated in April 2002, stretching through the year and past the start of the fiscal year on 1 April 2003.

Political consultation in the budget process takes place through the Executive (in the formulation of the budget) and the legislature (in the legislation of the budget). After the budget is tabled in *Parliament*, parliamentary debate on the budget takes place. The budget is first sent to the National Assembly Finance Committee, who has seven days to hold public hearings on the budget and compile a report for Parliament. Portfolio Committees also hold hearings on individual votes. The Finance Committee presents its report to the whole National Assembly, and the budget is debated for about a week. Once the National Assembly has voted its approval, the budget passes on to the National Council of Provinces (NCOP). If it gets a positive vote from the NCOP, it is passed on to the President for signing.

MinComBud (the Ministers' Committee on the Budget) is the most important vehicle through which political involvement in the MTEF process is achieved. MinComBud is formal subcommittee of the Cabinet that considers policy changes with budgetary implications before making collective recommendations to Cabinet. National Cabinet makes all the final decisions on Government's medium-term policy and spending priorities. This includes the macro and fiscal framework, the Division of Revenue, the MTBPS and changes to the medium-term allocations to national votes and provincial govenrments. Discussions on the provincial policy priorities and the finalization of provincial department allocations take place in Provincial Executive Councils. A detailed description of the MTEF process follows below.

Figure 1: Detailed Description of the MTEF Process



2.1 Prioritisation

From April to September, in the prioritisation stage of the process, the Ministers' Committee on the Budget (MinComBud),[4] the Budget Council and the Cabinet deliberate the policy priorities for the new medium-term expenditure period.[5] This takes place at meetings of the provincial Budget Lekgotlas[6] (May), MinComBud (May and June), a national Cabinet meeting (June), the extended Cabinet Lekgotla (July) and the Budget Council Lekgotla (August).

It is also during this period that the respective Ministerial letters from every department, outlining key policy changes and priorities, is submitted to the Minister of Finance. This is a departure from previous years, when the Ministerial letter was included in the MTEF budget submission. It is expected that the early submission of the Ministerial letter will facilitate improved evaluation of budget submissions and assist in defining national, provincial and local spending pressures.[7]

2.2 Review of strategic plans and preparation of new MTEF submissions

Immediately after the previous budget has been tabled, provincial and national departments revise their strategic plans for the next three-year period. These strategic plans are an innovation of the previous year's budget cycle and are intended to form the policy framework within which budgets and new bids are prepared. Strategic plans also contain performance indicators that are suppose to reflect the policy goals contained in the strategic plans. In mid-April, the National Treasury sends out guidelines to all national departments and provincial treasuries for the preparation of the budget submissions. At this stage provinces and national departments also receive their indicative allocation on the basis of which they start their first round of planning. Are there clear links between indicative ceilings as they role over, eventually into budget allocations? To what extent are indicative allocations for the out-years an indicative budget? See the section on the 'Basis and Process of Setting Resource Projections' below

From April to August national and provincial departments prepare their MTEF budget submissions. National departments have to follow specific guidelines and formats in preparing their MTEF submissions, while provincial treasuries circulate their own guidelines for provincial departments' MTEF submissions. The national Treasury Regulations determine that budget circulars issued by provincial treasuries must be consistent with any budget circular issued by the National Treasury to provincial Treasuries.

Joint sectoral technical committees (the 4x4s)[8] meet in June and July to discuss and formulate recommendations regarding key provincial spending pressures and the implementation and

[4] The Ministers' Committee on the Budget (MinComBud) plays a key role in generating political support for the budgeting process. Some of the policy and budgetary issues they consider include the government's medium-term policy and budgetary priorities, the macroeconomic and fiscal framework and the Division of Revenue between the spheres of government, the Medium Terms Budget Policy Statement and recommended changes to the MTEF allocations to national votes.

[5] National Treasury, Republic of South Africa (2002) Medium Term Expenditure Framework Treasury Guidelines: Preparing Budget Submissions, p. 5.

[6] 'Lekgotla' is a local name for a policy planning event.

[7] Ibid., p. 6.

[8] 4x4s are joint technical committees which examine spending trends in a sector and model the anticipated budgetary effects of new policies. Sectoral and treasury officials from provincial and national governments are represented.

administration of conditional grants.[9] Committees exist for the Health, Education and Social Development sector. Efforts have also been made to establish Housing, Infrastructure and Transport committees. The findings of these committees guide and support provincial and national departments in the preparation of their budget submissions.

2.3 The review of the budget framework and the division of revenue

Between June and September, discussions take place between the three spheres of government on two key issues:

- the overall budget framework, including fiscal policy, growth in overall spending, inflation projections and debt servicing costs;
- the division of revenue between national, provincial and local government, i.e. the vertical division of revenue

A Division of Revenue (DoR) workshop takes place in early August. The DoR workshop reviews the macroeconomic and fiscal framework, main conditional grants to provinces and primary spending pressures on each sphere of government. The workshop is chaired by the National Treasury's Director General and attended by national departments, provincial treasuries and local government representatives.[10]

Also in September, the Budget Council and Budget Forum[11] meet to discuss the fiscal and macro framework and the respective provincial and local government allocations. MinComBud presents its recommendations to the extended Cabinet at the end of September. Cabinet's comments on the fiscal and macro framework and the DoR are taken into account when the MinComBud prepares the revised memorandum on the DoR, which is then decided on by Cabinet in mid-October in preparation for the presentation of the MTBPS.[12]

2.4 The medium-term allocation process: recommendation process

Provincial and national Medium Term Expenditure Committee (MTEC)[13] hearings take place in August and September and are responsible for evaluating the MTEF budget submissions of departments. They look at how departments are proposing to reprioritise within the baseline allocations. Departments are also permitted to present 'options' in their submissions for increases or decreases to MTEF allocations. The MTEC hearings' outcome is recommendations to the Minister of Finance on changes to the MTEF allocations to national departments based on the macro and fiscal framework and the DoR.[14] Provincial MTEC hearings also take place in September and follow the same procedure, with provincial executive councils making final decisions about departmental allocations.

[9] The Technical Committee on Finance and the Joint Sectoral Technical Committees (referred to as the '4x4s') support the Budget Council. The purpose of these teams is to improve intergovernmental relations and the exchange of information, with a long-term perspective on spending and policy. They are advisory bodies and do not have decision-making powers.

[10] Hickey, A & van Zyl, A. (2002) *2002 South African Budget Guide and Dictionary*, Cape Town: IDASA, p. 57.

[11] The Budget Forum is the local government counterpart of the Budget Council.

[12] National Treasury, Republic of South Africa (2002) *Medium Term Expenditure Framework Treasury Guidelines: Preparing Budget Submissions*, p. 8.

[13] The MTEC is a technical committee, comprising senior officials of the National Treasury, as well as representatives from other departments, including the Presidency. The MTEC evaluates if departments' MTEF budget submissions are consistent with government's policy objectives and if it is affordable given the available resources.

[14] Hickey, A & van Zyl, A. (2002) *2002 South African Budget Guide and Dictionary*, Cape Town: IDASA, p. 58.

At the end of October, the Minister of Finance reviews the MTEC's recommendations on changes to the MTEF allocations to national votes and tables these before MinComBud. The Finance Minster also reviews the final allocations to provincial and local government, and tables these before the Budget Council and Budget Forum respectively. Cabinet meets in early November to discuss the recommendations of MinComBud, the Budget Council and the Budget Forum. Cabinet makes the final decision on the changes to the MTEF allocations of national votes, as well as the final allocations to provincial and local government. In mid-November these allocations are set out in Treasury letters to national departments and provincial treasuries.[15] Departments and provinces subsequently adjust their budgets as a result of the above process.

2.6 Medium-term budget policy statement

The Minister of Finance tables the MTBPS before Parliament at the end of October, together with the Adjustments Estimate. MinComBud first meets to discuss the outline and key themes of the MTBPS in early October. The Minster of Finance drafts the MTBPS and, together with the Adjustments Estimate, it is considered and approved by Cabinet before being tabled before Parliament.

Is it merely a statement of fiscal policy or does it also include something on sector priorities (and provincial/centre splits)? See paragraphs on page 5 above. Can you comment on the usefulness of this step? The MTBPS is the end result of the first, and relatively closed, round of budget planning. While its contents cannot be directly influenced by parliament and civil society, it does serve the purpose of publicizing government thinking before the tabling of the budget in February.

2.7 The medium-term allocation process: final stage

The final stage of the budget process involves the preparation of the budget documentation that is tabled before Parliament on Budget Day, and the budget documentation that is tabled before provincial legislatures. In December national departments are required to submit the first draft of their chapters of the Estimates of National Expenditure and Provinces to submit the printer's proof of their budgets.[16]

At the beginning of January the following year, the draft DoR Bill is submitted to the Financial and Fiscal Commission (FFC), provincial finance ministers and local government representatives, before it is approved by Cabinet. In February the National Budget, together with the DoR Bill and the Estimates of National Expenditure is tabled before parliament. Provincial budgets are tabled before the provincial legislatures in February and March.

There are a lot of linked processes here which seem to work pretty well (true?) but is there a concern that the process is just too lengthy (does it distract management from the implementation phase)? Not as far as I know. Some provinces do however still lack the capacity to participate fully in all these structures & processes.

[15] Ibid. , p. 9.
[16] Ibid., p. 9.

3. MTEF Structure and Coverage

The introduction of medium term expenditure planning in the 1998 budget year extended the annual agency and programme forecasts to cover a three-year period. The MTEF covers a three-year period that starts with the year for which the current budget is being prepared and includes the two subsequent financial years. Every year the first year of the MTEF is voted into law as the budget. The next year, 'year two' becomes the baseline for the new budget cycle and a new outer year is added to make the new 3 year MTEF.

The out-year estimates of the South African MTEF are indicative allocations of funds to the sector/agency/programme for those years. In the first few years of the MTEF these numbers were too unreliable to really be used as indicative allocations, but the idea was that they would ultimately be used in this manner.

As a result of the close integration of the budget process and the MTEF planning cycle, the structure of expenditure and financing categories are identical in the budget and the MTEF. The pre-budget statement (MTBPS) presents of the data in a more aggregated form than it appears in the provincial and national budgets themselves, but the disaggregated data are presented in the budget documentation that is presented when the budget is tabled.

Currently the documentation that is submitted annually to Parliament on Budget Day includes a Division of Revenue Bill, an Appropriation Bill and a Tax Amendment Bill, backed by the Estimates of National Expenditure, the Budget Review (an analysis of budget policy), and the Budget Speech. Consolidated national data is published in the Budget Review, while the Estimates of National Expenditure provide data and contextual information, including performance information, for each national vote/department.

Provinces prepare their own budgets, which they submit to their provincial legislatures. As from 2002 the provinces are required to publish Budget Statements One (equivalent of the national Budget Review) and Two (equivalent of the Estimates of National Expenditure), which provide an overview of the provincial socio-economic context, consolidated budget information, revenue and expenditure information, as well as performance information, for each department. These documents are supported by a Budget Speech. Another document, the Intergovernmental Fiscal Review, is published by the National Treasury later in the year and adds sectoral contextual information for provincial expenditures. It also consolidates all provincial budget and expenditure information, focussing on the main functions, thus providing the information needed to make inter-provincial comparisons.

The budget deficit is presented in the budget itself and taken up by the press and analysts as the litmus test of the government's financial position. The 1999 MTBPS expanded the analysis of the fiscal framework to the wider general government and public sector accounts, including specific reference to the public sector borrowing requirement in relation to the deficit. There are some concerns that the schedule of contingent liabilities is defined too narrowly. The national budget excludes contingent liabilities such as university debt, non-departmental organisations, research councils, government agencies and social security and other funds. The Budget Review contains information on financial guarantees furnished by national government, but does not cover all potential shortfalls that may have to be covered by the budget, such as those incurred by public entities or public enterprises. The debt table excludes extra-budgetary institutions (EBIs) and social security funds, making it difficult to assess the full fiscal liabilities of the consolidated government. The budget documentation contains no information on quasi-fiscalities[17] and only limited information on tax expenditures.[18] It also does not include a statement of financial assets and liabilities or one of net worth.[19]

The provisions of the Public Finance Management Amendment Act extend to provincial and national public entities. However, whereas the new legislation establishes a central list of EBIs, it does not require consolidated reporting by government on its extra-budgetary activities and, secondly, the lists still excludes certain institutions,[20] such as those of higher education. The 1998 Budget Review included a table that gives the consolidated revenue, expenditure and deficit/surplus for EBIs. This table was omitted in the 1999 Budget Review and subsequent documents. This is an instance of information that is volunteered – i.e. not required by law or regulation – one year and then not published subsequently. However, officials from the National Treasury indicated that the reason for withdrawing this table is because it was based on projections and was not comprehensive. They are currently putting in place systems to gather actual data from all public entities - of which there are far more than was originally thought (Barberton 2002: 233).

Efforts to improve reporting on extra-budgetary activities are ongoing. In the 2002 Budget Review information was published on a range of national funds and accounts, including skills development funding, international development co-operation and consolidated information on social security funds. Progress is also being made with reporting on other public entities, such as the Road Accident Fund, and government enterprises in the Estimates of National Expenditure.

The National Treasury has also made an explicit effort to include information on the fiscal activities of the wider public sector. This includes information on the wider public sector borrowing requirement over the medium term and the setting of fiscal policy aims (on general government expenditure, capital formation, saving, interest on debt and tax revenue) for the wider public sector. Information on the public sector borrowing requirement now includes various funds and trading accounts, the social security funds, provinces, EBI's and local authorities and local government enterprises, as well as public corporations and central government enterprises. Provincial business enterprises still appear to excluded (Barberton 2002: 233).

4. Basis and Process of Setting Resource Projections

For the period 1996-1999 the interaction between the fiscal framework and the macro-forecasts was based on a set of policy guidelines in the medium term macro-economic strategy document, known as GEAR. GEAR was drafted by a panel of economists in a closed process and was based on SARB, the Council for Scientific and Industrial Research (CSIR), and University of Stellenbosch models. Although these models and forecasts were not open to independent assessment, they were generally seen as credible. As from the 2000 fiscal year the National Treasury has used its own in-house CGE

[17] Quasi-fiscalities would result from government activities or regulations that have indirect fiscal implications, either on the tax or revenue side. Examples would be subsidised lending to preferential sectors of the economy, multiple exchange rates or charging less than commercial prices for goods delivered through the public sector. In 2001 government brought the financing of the Electrification Fund on budget. Previously it had been financed by Eskom, the state owned electricity utility.

[18] Tax expenditures would be the cost of tax concessions, for example the cost of excluding certain categories of mining companies from a general company tax. In the 2002 Budget Review information is given on the cost of the wage incentive and the strategic investment programme.

[19] A strong argument can be made that focus on the deficit as an indicator of fiscal position can be misleading, especially in cases where governments sell off assets in order to reduce the deficit. Changes in net worth, which includes assets and liabilities as variables, provide a longer term focus to assessments of fiscal position.

[20] In fact it is only now emerging how many public entities there are. The lists that were published with the PFMA were by no means complete, and there is a process to rectify this.

model to make macro-economic forecasts. This model is supported by data from the SARB and analytical work done at the University of Stellenbosch.

Medium-term spending plans of national and provincial departments are prepared within the context of the Government's macroeconomic and fiscal framework set out in the previous budget. The framework set out in the previous budget outlines the 'resource envelope' within which budget submissions are prepared.

The macroeconomic projections and fiscal framework are revised during the year, as updated economic data become available. Macroeconomic projections are drawn from the National Treasury macroeconomic model. One of the most striking features of the South African budget is the significant revenue over runs over the last few years. This is the result of bringing more people into the tax net rather than an increase in the tax rates or the introduction of new taxes. The South African Revenue Service has therefore found it difficult to accurately project revenue collection.

Table 1: Revised Estimates of Main Budget Revenue and Expenditure 2000/01 – 2001/02

	2000/01			**2001/02**		
ZARMillion	**Budget Estimate**	**Outcome**	**Deviation**	**Budget Estimate**	**Outcome**	**Deviation**
Revenue	210400	215592	5192	233438	248438	15000
Expenditure	233452	233942	490	258318	262590	4272
Deficit	**-23052**	**-18350**	**4702**	**-24880**	**-14152**	**10728**

Source: Budget Review 2002:54

Table 2: Macro-economic projections 2000/01 – 2002/03

	2000/01		**2001/02**		**2002/03**	
	2000 Budget Estimate	**Outcome**	**2001 Budget Estimate**	**Revised**	**2001 Budget Estimate**	**Revised**
Gross Domestic Product (ZAR bill)	885.2	910.5	987.2	990	1069.3	1082.8
Real GDP Growth	3.6	3.4	3.7	1.9	3.5	2.7
GDP Deflator	5.5	7.2	6.0	6.6	4.7	6.5
CPIX	6.6	7.8	6.2	6.5	5.2	6.7

Source: Budget Review 2002:44 and Budget Review 2001:38

Table 3: Financing of net borrowing requirement 2000/01 – 2001/02

	2000/01			2001/02		
ZARMillion	**2000 Budget Estimate**	**Outcome**	**Deviation**	**Budget**	**Revised**	**Deviation**
Domestic short-term loans (net)	3500	4979	1479	3500	-7590	-11090
Domestic long-term loans (net)	10140	6406	-3734	-7354	-11061	-3707
Foreign loans (net)	4612	1902	-2710	11304.0	33117	21813
Change in cash and other balances	2000	4377	2377	0	-2971	-2971
Total financing (net)	**20252**	**17664**	**-2588**	**7450**	**11495**	**4045**

Source: Budget Review 2002:108 and Budget Review 2001:100

Is there a deliberate policy of being conservative with revenue forecasts? See above

5. Basis and Process of Setting Aggregate Limits and Broad Allocations

The two out-years are generally rolled over directly as baseline for the budget planning of all provincial and national departments. The allocations for the new year 3 are calculated by adding a standard adjustment for growth and inflation determined by the Treasury's CGE model (6% in 2002/3) to year 2. Baselines could also be adjusted in the Adjustments Estimates as a result of unavoidable and unforeseen expenditure such as floods or epidemics.

The general approach of the Treasury has been to emphasize stability, smooth growth and minimal changes to the baseline. There has therefore been very little cutting of forward projections. If the provincial or national treasury has perceived excess resources in any one department the approach has rather been to avoid additional allocations to that budget, rather than cutting the baseline. This approach has been made possible by the large revenue over-runs and the resulting solid growth in expenditure over the last 5 years.

The national treasury sets overall limits for each of the national departments as well as each of the provinces. The provincial treasuries in turn set limits for each of their provincial budgets. South Africa does not have separate development and recurrent budgets, so separate limits are not set for these. Limits are also not set for capital and current expenditure. However some provinces have been known to ring-fence capital expenditure or earmark specific revenues for capital expenditure – thus effectively setting limits on recurrent expenditure within the total envelope for the relevant department.

The aggregate limit and broad allocations in the budget is in principle the same as the expenditure figure from the MTEF macro projections. In South Africa this limit is provisionally arrived at and revised as firmer data become available throughout the budget process. Cabinet and the MinComBud is involved in the discussion and ratification of each of these revisions, the most important the before the publication of the MTBPS and the finalization of the budget in January.

The setting of 'measurable objectives' as part of the budget process was only introduced 2 years ago and is still in the process of refinement. Currently the emphasis is still on making sure that inputs reflect policy. The phasing in of performance indicators has been done by specifying a minimum standard for each budget cycle. In 2001, for example the Treasury requested that each Department specify and quantify indicators, while in 2002 it added the requirement of timelines and costs in reaching the targets. See conclusionPerformance targets are self-set by the department or agency concerned, but these are discussed and refined in discussions with treasury and intergovernmental fora. These discussions generally focus on the link between the performance targets and policy as it is outlined in the departmental strategic plans. Currently no link exists between this process and the setting of expenditure allocations.

Another important feature of the South African system is that there is no intention of setting up a system of outcomes based budgeting. While departments are asked to draw direct causal links between inputs and outputs, they are only expected to explain how and to which desired outcomes their outputs would contribute. The Treasury in particular places emphasis on the complexity of the linkage between outputs and outcomes and does not intend holding service delivery departments responsible for specific outcome targets. So the key question that is asked is which mix of outputs would best contribute to reaching a specific outcome, but this question is only answered indicatively. There is no direct mapping of outputs to outcomes.

The one indirect link between outputs and inputs exists in efforts by the treasury to ensure that the budgets of provincial social service departments reflect their main cost drivers. In the case of Health and Education 'baseline' budgets are generated by a personnel expenditure model (other cost drivers are not currently considered) and in the case of Social Development the modeling of provincial commitments for the payment of social security grants generates the baseline. The levels of grant and salary expenditures are the result of central government decisions and are therefore beyond provincial discretion, thus effectively forcing the generation of certain minimum outputs; i.e. the number of grantees, the level of grants and the salary levels of teachers) in these sectors.

As we will indicate below, there is no cross sectoral programme of poverty reduction. As a result there is also no systematic monitoring of performance targets towards the realization of such a programme.

6. Policy, Planning, the MTEF and Budgeting

One of the main reforms in the 2002 budget process was the integration of strategic plans into the budget process. The integration of strategic planning, budgeting and the monitoring of service delivery, is intended to strengthen the link between service delivery and the benefits and costs of those services. Integrating strategic planning should ultimately result in better budgeting over the medium term.

Strategic planning and prioritisation is the starting point for preparation of the departmental budget submission as it is intended to guide departmental reprioritisation within the medium-term baseline allocations and provides the rationale for policy options regarding changes to baseline allocations over the next 3-year period. Amongst others the strategic plan is required to include the mission and strategic measurable objectives and outcomes for the departments programmes.

The MTEF provides a solid framework for the integration of strategic planning and budgeting. The agreed three-year expenditure envelope and policy priorities create an environment of certainty in which departments and prepare strategic plans and budgets.

National and provincial departments are required to prepare strategic plans in terms of the *Treasury Regulations, 2001 and the Public Service Regulations, 2001***.**[21] Departments are not required to prepare separate draft strategic plans, but are expected to integrate their strategic planning procedures and results into the budget submission. After they have received their final allocations, more detailed strategic plans have to be tabled before Parliament or the relevant provincial legislature within 15 working days of the tabling of the annual national or provincial budget.

A department's strategic plan should identify the key areas where the department will focus in its pursuit of government's policy priorities, as well as the strategies to achieve them. The strategic plan has to include the following: a department's aims based on its mission statement; key objectives in line with government's policy priorities; the core and support activities required to achieve the key objectives; service delivery indicators to measure the success of the department in achieving its objectives; as well as the resources needed to sustain its activities.

Published strategic plans also increase the transparency and accountability of government departments to Parliament. It enables Parliament to better assess proposed programmes

The 2002 budget submission guidelines attempt to strengthen the link between Government's priorities and spending plans even further by requesting a ministerial covering letter that identifies the key departmental policy shifts and priorities, reports on the processes followed to reprioritise within baseline and add spending plans for the third year of the new medium-term period. The letter is also required to detail how the proposed policy options for changes to baseline allocations are in line with the department's medium-term policy priorities. [22]

As was indicated above, the emphasis in the departmental allocation process is currently on stability and slow and steady growth. Apart from the adjustments to the baselines, departments can bid against additional funds that become available over and above the aggregate baseline. Departments are thus not asked to evaluate their entire budget from scratch through a zero-based budgeting excercize, but rather just to motivate for any additional allocations that they require. Some departments use zero-based budgeting excercizes to identify areas that would qualify for additional allocations.

The requirement not to motivate for the whole budget but only for additional allocations could have meant that the budget continuously expands, that efficiency gains become moot. However, this year (ie for 2002/3) treasury is requiring in addition that departments must demonstrate how they have freed up some resources of their own to pay for their new policies, or requested additional expenditures (or at least those that are not driven by increases in the cost drivers, such as higher enrolment, or increased HIV Aids expenditures etc) . Only then will Treasury consider providing additional funds. (presumably this is backed by a Cabinet requirement that off-setting savings be identified).Not sure that I understand this comment.

These 'options' are presented to provincial and national MTECs that evaluate them on the basis of available resources and their linkages to strategic plans. When motivating for additional allocations, departments are asked to prepare 'options' that show:[23]

- the possible change to a department's medium-term baseline allocation

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[21] National Treasury, Republic of South Africa (2001) Medium Term Expenditure Framework Treasury Guidelines: Preparing Budget Submissions, April.

[22] National Treasury, Republic of South Africa (2002) Medium Term Expenditure Framework Treasury Guidelines: Preparing Budget Submissions, p. 7.

[23] Ibid p.35

- how the option for changing the medium-term baseline allocation of the department contributes to the strategic priorities, objectives and policy developments of the department outlined at the start of the budget submission.
- the capacity and ability of the department to plan, budget for, implement and monitor the option.
- how the option was costed. Emphasis is placed on identifying all direct and indirect costs and any new capital or non-recurrent costs and operating costs required to provide the output specified be detailed.

7. The MTEF, Budget Execution and Quality Information

The tables presented below and in section 4 demonstrate the remarkable improvement in the information provided by the treasury. The documentation presented on budget day and during the year now includes regular actual expenditure reports, strategic plans for each department and output indicators.

The weakest area is still the production of and reporting on performance indicators. Most departments still produce too many to report on. These indicators are often also a random mix of input, output and outcome indicators. The national Treasury has emphasised the production of output indicators in order to make sure that departmental outputs reflect sectoral policies. The Presidency has put greater emphasis on the monitoring and evaluation of outcome indicators while it is not clear how this debate is developing, the Treasury is using its influence to promote its position in provinces and national departments.

There has been a particular improvement in the quality of budget estimates, and in the spending of departments. It would appear that the massive national under-spending and provincial overspending of 1997 is a thing of the past. The absolute deviation as a percentage of total national budget expenditure was less than 5 percent for both 1999 and 2000, down from 13.68 percent in 1997 (Barberton 2002: 236). The following table presents total under-expenditure, and total over expenditure of the national departments for the years 1997 to 2000.

Table 4: Total under-expenditure, and total over expenditure of the national departments for the years 1997 to 2000.

(in R million)	1997	1998	1999	2000
Amount overspent	6487	4746	3028	1593
Amount underspent	2004	225	455	2785
Total absolute deviation	8491	4971	3483	4378.5
National votes & statutory amounts	62082	78333	82967	90473
Average absolute % change from planned expenditure on votes	13.68	6.35	4.20	4.84

Source: Budget Review 1999, 2000, 2001 and 2002

The measures that have been put in place to ensure the execution of budgets include the establishment of internal audit committees and the issuing of monthly actual expenditure reports. We discuss two of the measures below.

7.1 Overspending and liability

In terms of the Public Finance Management Act (PFMA), overspending can only be authorised by the relevant provincial or national legislature. When it is not authorised, it becomes a charge against future allocations of the province or department. In terms of the PFMA any accounting officer guilty of financial misconduct in terms of the Act, may be liable to disciplinary as well as criminal proceeding. The maximum punishment for the latter is up to 5 years imprisonment.

7.2 Underspending and roll-overs

One of the firmest measures discouraging underspending is the set of Treasury regulations governing rollovers. Even if granted, rollovers are governed by a whole series of limitations controlling the kind, size and purpose of rollovers allowed. Funds for specific purposes may also not be rolled over for more than one financial year, unless approved in advance by the relevant treasury. Requests for rollovers must include

- the purpose for which the funds were appropriated;
- the reasons why the funds were not spent;
- proposed changes to the use of the funds, if any; and;
- a disbursement schedule indicating the month(s) in which the expenditure is expected to be incurred.

Roll-overs are however not automatic, even when applications meet all these requirements. Decisions to roll over are based on the priorities and pressures identified in the new budget cycle.

8. The MTEF and Local Government

In South Africa's system of cooperative governance there is no formal or practical division between the budget and MTEF processes of provincial and national government. These two processes are intricately woven together into one integrated process. We describe it as such in this paper.

The third sphere of government, while formally part of the system of cooperative government, largely operates a separate budget process. For various reasons this sphere was left out of the budget reforms of the late 1990s and the Public Finance Management Act of 1998 that consolidated many of these reforms. The recently tabled Municipal Finance Management Bill will attempt to introduce many of these reforms at local government level, one of which is MTEF budgeting.

In preparation for the introduction of these reforms, the national Treasury has encouraged medium term budget planning in 30 of the 282 local authorities. These were identified as 'budget reform pilot sites'. Anecdotal evidence suggests variable success in this endeavour.

For the 15% or so of local government revenue that comes from transfers from national government in the form of block and conditional grants, medium term projections have been part of the reform process since the inception of the MTEF process.

Is the cooperative governance approach seen as roughly getting the balance right between the different levels of government (many supporters of decentralization have seen MTEFs as centralizing)? This debate is politically loaded in SA, I would therefore prefer not to deal with it here, especially given the 'technical' nature of this paper. Are you happy with this judgement. I did recently do a paper on this exact topic, so I could add quite easily if you would prefer.

9. Conclusions

South Africa's macro-economic policies are key in its drive to eradicate poverty . The Growth, Employment and Redistribution strategy was a macro development strategy that relied largely on private sector investment to stimulate growth and create employment. GEAR ran from 1996-2000 and its performance and key assumptions are currently being revised.

South Africa does not however has a consolidated formal poverty reduction strategy. The closest that it got to formulating such a strategy was the Reconstruction and Development Plan (RDP) that was very broad and contained few specific implementation strategies and outcome targets. The general approach has been to reprioritise within sectors, but not to try to coordinate poverty reduction efforts between them.

The most important effect of the RDP was to encourage sectoral reprioritisation of expenditure. Between especially 1994 and 1998 social service departments shifted substantial resources to services used by the poor and marginalized. Efforts to coordinate these sectoral initiatives have however come to naught. In 1994 an RDP office was opened to serve this purpose. When this office was closed down in 1996 it was replace by a Policy Coordinating Unit in the office of the President. These coordination efforts failed because of their lack of integration into the budget process. The most recent efforts at thinking through the poverty linkages and trade-offs between services have come from the Treasury. This is an encouraging development given the treasury's centrality in the budget process. It controls the incentives that could enforce the compliance of departments with efforts at interdepartmental coordination.

The main advantage of the absence of a explicit poverty reduction strategy is to have focussed attention on re-prioritisation within departments. Great strides have been made at targeting especially social service sectors at the poor. The obvious price that has been paid is a lack of consideration of interdepartmental reprioritisation. Current shares of the total budget are thus more the result of historical patterns than explicit policy decisions.

The MTEF process in South Africa is also still challenged by questions of sequencing. The main fault-line here runs between the political process of policy planning and the budget process itself. The most important innovation here has been the formulation of strategic plans in each department. These plans are intended to inform the allocation process continuously and force departments to think through the medium term implications of policy changes for the budget. In many cases however, the formulation of strategic plans is still an exercise in compliance and is not being used as a management tool. As a result many of them are vague and not designed to inform the budget process.

Performance indicators fall into the same category, with many departments not making good progress in formulating useful indicators. It may however be too early to assess the results of these reforms, since they were only introduced in the 2001 budget cycle. What is encouraging is that Treasuries are using these strategic plans and performance information in consideration of departmental bids for funding over and above their baseline. The incentives are thus being set up for departments to use these tools in the formulation of their budgets.

What is of particular concern in the development and enforcement of these reforms is the lack of effective oversight by provincial and national legislatures. The job of lead agencies in the process such as the Treasuries could be supported a lot more by legislatures that engage with the non-financial information prepared by departments. Neither national nor provincial legislatures seem to have found a way to deal with the mass of new information coming their way in a systematic manner.

Probably the biggest success story of the budget reform process, along with the intrasectoral reprioritisation mentioned below, has been the reeling in of under and over-expenditure. The fact that medium term projections are reliable has assured the integrity of the whole system. It is therefore now possible to build on the financial information in the consideration of non-financial information such as strategic plans and performance information. It is hard to see how this would have been possible if there had still been large variations between printed and actual expenditure data.

While there have therefore been key gains in operational efficiency, the debate around allocative efficiency is not nearly as well developed. This evidenced in the absence on an overarching poverty reduction strategy.

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