EFFICIENT GROUP Weekly Economic Newsletter

Contact Us

81 Dely Road
Hazelwood
Pretoria
0081

+27 (0)87 944 7999

info@efgroup.co.za

www.efgroup.co.za

ECONOMIC COMMENTARY

- By Francois Stofberg

The budget, another small step in the right direction

This year's government budget was not as bad as we initially thought it would be, but also not as good as we would have wanted it to be. This is a conclusion, I think, any objective viewer might reach. Overall, the budget turned out to be another small step in the right direction – despite the slanderous spend on capital expenditure, but because of the 1% VAT increase.

Government needs a new business plan. The one they've been following since 2009 (which we also like to refer to as the Z-period) has been dismal, disastrous, and disappointing. The enormous drive of government policy to redistribute wealth has done a lot for the poor over the last two decades, and especially since 2009. Splendid. Unfortunately, these same redistributive policies have in recent years done more to destroy wealth than to redistribute it. It's simple: too much of a good thing is bad for you.

First, the excessive tax burden on the wealthy (productive) side of our economy decreases their ability to be even more productive. What makes this strategy even more wealth-destructive, is the nature of what tax money is spent on. Instead of using that tax money to economically uplift South Africans, it was spent on short-term current expenditures; more civil servants, who on average earn 38% more than their private sector counterparts. Instead of using taxes to allow the private sector to produce jobs, government chose the easier way out – giving hand-outs. Now we have a dependent economy, where more people live off social grants than those who work to contribute (i.e. the productive individuals). Second, the questionable integrity of former president Zuma left the state coffers and SOEs open to raiders, fuelling the need for bail-outs which totalled too many billions of rands to count. Third, the confused ideology of the ruling party caused a severe lack of leadership, translating into a lack of clear policy, policy implementation, and long-term strategy. This is what tainted all that money we threw at education in South Africa. You would expect the best, or even some of the best results from education if you spend more on it than most of your peers. Well, we achieved the worst maths and second worst science results in the world, according to TIMS & PIRLS International Study Center.

The new business plan should therefore focus on creating wealth, rather than on redistributing (further destroying) it. For this reason, the 1% VAT hike gave me some hope. It indicates that the ruling party has finally started to understand that the productive few have been taxed too excessively and have grown tired of not seeing anything for their contribution. This point was made clear by Finance Minister Gigaba at his 2017 medium-term budget policy statement (most likely his last), when he explained that the statistics show that more individuals are avoiding their tax obligation. This is a basic economic theory illustrated by the Laffer-curve, which indicates how citizens start avoiding their tax obligations at ever-increasing speeds after a certain tax rate.

Good as it may be, a 1% VAT hike is still too little, even when considering the political pressure it might lead to. A 3% increase would have been preferred. This could have been used to alleviate pressure from the productive economy through manufacturing subsidies linked to exports, as an example. A 3% VAT hike is also not that unreasonable. India implemented a similar strategy in 2017, even though, according to GDP per capita, the average Indian is more than 3 times poorer than the average South African.

What would have made this a great budget, was if government spent less on social upliftment (e.g. grants) and more on economic upliftment (e.g. capital expenditure). This would have shown that government finally understands how to create wealth. Yet, capital expenditure will only be R151 billion next year. Our fiscal deficit (dissaving) on the other hand, will be roughly R191 billion. What this implies is that government will be destroying capital (savings) to the tune of R40 billion. This disaster is what dragged the South African economy into a new trend of low-growth, which will persist until government starts investing more. Addressing this issue would have been a quantum leap towards economic prosperity and job creation, a real radical economic transformation.