

**SUBMISSION MADE TO THE
PARLIAMENTARY JOINT BUDGET COMMITTEE (JBC) ON THE RECENT
MEDIUM TERM BUDGET POLICY STATEMENT
by
RAYMOND PARSONS
ECONOMIC CONSULTANT TO
BUSINESS UNITY SOUTH AFRICA (BUSA) AND
OVERALL BUSINESS CONVENOR AT THE NATIONAL
ECONOMIC DEVELOPMENT LABOUR COUNCIL (NEDLAC)
IN CAPE TOWN ON TUESDAY 1 NOVEMBER 2005**

EMBARGO : TUESDAY 1 NOVEMBER 2005 AT NOON

Chairperson – members of the Parliamentary JBC – may I express my appreciation for the opportunity of appearing before this Committee on behalf of Busa (Business Unity SA) to offer some *selective* comments on last week's Medium Term Budget Policy Statement (MTBPS) tabled in Parliament by the Minister of Finance.

Let me say at the outset that Busa has welcomed the overall thrust of the latest 'mini-Budget', which again reinforces predictability and certainty in fiscal policy, as well as underpinning SA's current economic performance. Busa also believes that the expected growth rate in 2005 will be about 4.5% and expects that – once the full year survey data has been incorporated into the national accounts – growth estimates may well be revised upwards.

SA is still building on the policy foundations that have been underway over the past decade and the latest 'mini-Budget' is another step in the 'work-in-progress' upon which the country has been engaged. While the focus is on economic growth, there are important implications for equity and empowerment, as well as being the dynamic that underlies job creation. Unfortunately, despite the better growth platform, the level of output growth has been unable to act as a generator of sufficient new employment.

Basically this has occurred because the pressure of new work-seekers into the labour market has outweighed the rate at which new jobs have been created. In reality the sheer speed of divergence between the growth of the labour force and the growth of formal sector employment (significant by world standards) has kept unemployment at unacceptably high levels. The informal sector in SA continues to be small by peer country standards. Growth has not been 'jobless' but insufficient to create enough jobs to absorb the expansion in the labour force.

In Busa's view the mooted 6% growth rate, which would double the size of the SA economy every twelve years, is a growth rate that can help to meaningfully address these challenges and is rightly a growth rate to be aspired to by SA. At current growth rates of about 4% per annum, it would probably take about twenty years to double the size of the economy. Clearly there would be considerable advantages and social benefits if the 'resource envelope' of the SA economy could be enlarged by adding 50% to the economic growth rate over the next few years. The fiscal gains from recent growth and tax revenues now need to be reinvested in future growth and development in a balanced way.

The 'mini-Budget' is a curtain raiser for the main Budget in February 2006 and outlines the financial and economic architecture that will shape the contours of the Budget next year. Given the aspect of the MTBPS allocated to me today – 'Employment and Economic Growth' – I will limit Busa's remarks in the time available to those aspects of employment and economic development which the 2006 Budget should further embody or encourage directly or indirectly, given the challenges of unemployment and poverty in SA.

In view of the fact that I am today speaking on behalf of a business organisation – and given the time constraints – I would like to single out one aspect of our growth and development strategy which Busa sees as crucial to employment and economic development. Central to the micro-reform and the 6% economic growth framework is the theme of encouraging *enterprise development*, especially at the small and medium levels. It is not that this does not form part of the official economic strategy, but that certain aspects require greater emphasis and implementation in the period ahead – some of which may lie outside the mandate of the Ministry of Finance alone.

Why are SMEs important? International experience in both developed and developing economies have demonstrated the extent to which growth in small and medium businesses has unlocked the majority of employment created in those countries. If we can replicate an appropriate enterprise strategy for SA it will help to unleash new opportunities for millions of people in the country. It will also help to empower a substantial proportion of the population. Over time, the small and medium businesses that succeed today become the large businesses of tomorrow.

Building on the partnership and work done in the 2003 Presidential Growth and Development Summit (GDS), Busa suggests that the progress made so far could be widened and deepened as follows:-

1. Firstly, to dedicate a large part of the 'message' of the 2006 Budget to additional ways in which enterprise, especially small enterprise, can be further encouraged. Research the recent Small Business Project (SBP) estimated the scale and regressive distribution of regulatory compliance costs to be about R79 billion or about 6.5% of GDP, of which SMEs incur the largest costs of compliance. Analysis of the regulatory complexity in the SBP report reveals that the five most time-consuming and troublesome regulations cited by respondents were – in ascending order – RSC levies and SETAs training levies, PAYE and UIF, SARS tax administration, labour laws, CCMA/bargaining councils and VAT. Busa recognises that the government has taken steps to address some of these most troublesome regulations – such as eliminating RSC levies and better VAT arrangements. If some of the resources currently spend on compliance costs were reduced, business could use the freed-up capital in more productive ways. Perhaps it might be helpful in the next Budget Speech to set a target for reducing the cost of regulatory compliance from the current estimated 6.5% of GDP to a figure more in line with SA's major competitor nations, say, over a period of five years.

2. Secondly, on the assumption that 'prevention is better than cure' Busa believes that SA should adopt a Regulatory Impact Assessment Strategy (RIAS) which tests the impact of new legislation on investment, growth, jobs and empowerment. Busa acknowledges that much work has already been done by government on this proposal but wishes to emphasise its likely benefits. The overriding goal of RIAS is to ensure that regulation achieves its goals in the most efficient way, and in a way that facilitates investment, growth, employment and development. RIAS should not be seen as a static post-event damage control, but as a dynamic learning and facilitation process, which will ensure continual best practice in policy development and be of immense value to parliament itself. RIAS has been adopted by a number of developed and developing countries in recent years. Once again, the National Treasury, which ultimately has to

fund legislative and regulatory expansion, would have an interest in seeing such a mechanism developed to help encourage fiscal discipline.

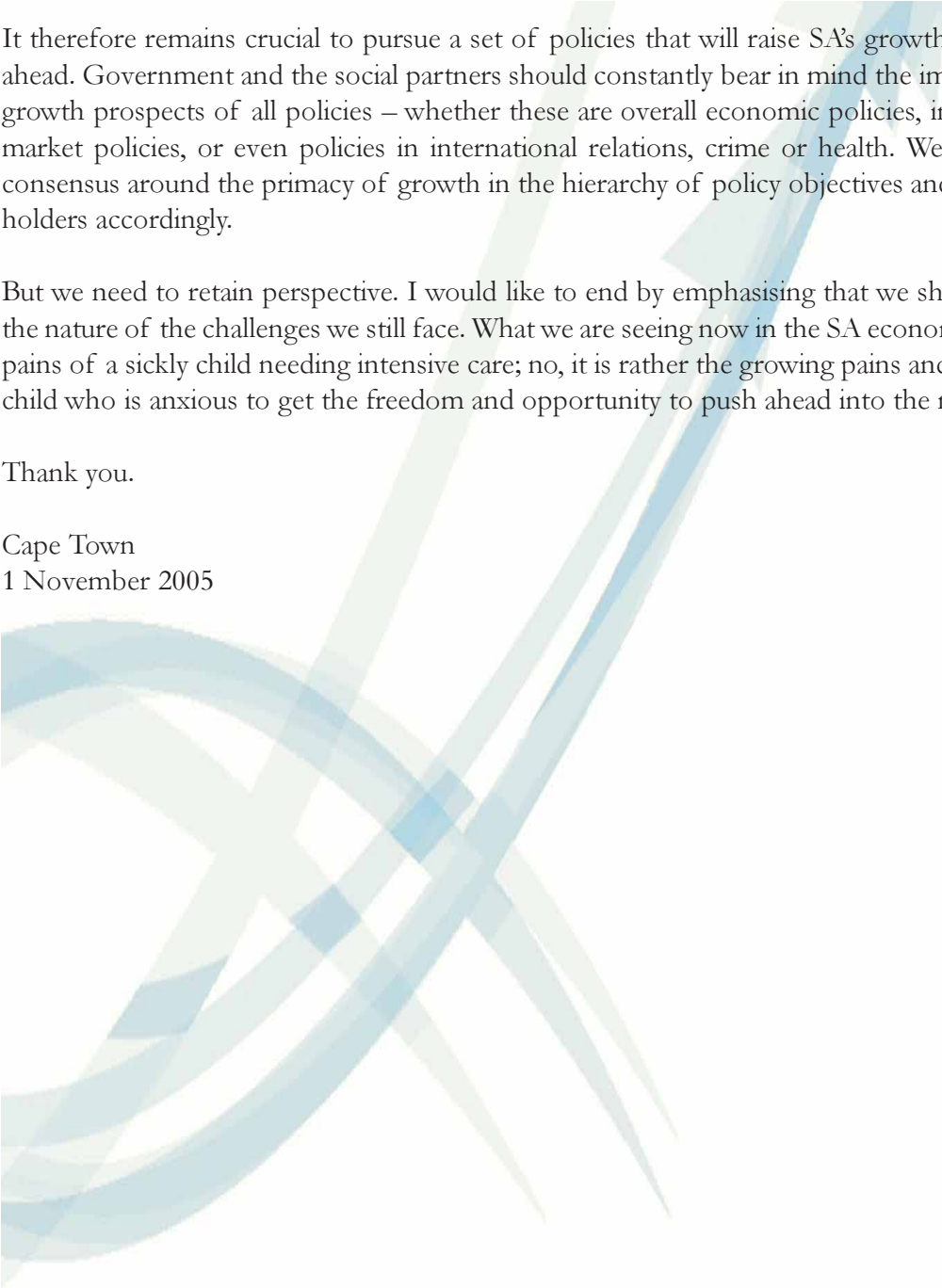
3. Thirdly, Busa welcomes the steps taken by government to boost infrastructural spending and investment. What remains important now is to ensure that a number of key areas such as rail and ports have sufficient skills and capacity to develop the necessary efficient and cost-effective infrastructure and services required. Busa reiterates the need to greater cooperation between the private and public sectors and that the challenges of capacity-building are shared wherever possible. Progress cannot only be measured by the amount of funds allocated, but by tangible evidence of productive investment to support growth and job creation.

4. Fourthly, partnerships at the local level should be encouraged to facilitate real delivery of services. Current estimates suggest that 60% of government's programmes are delivered at local government level, although it is at this level where large capacity constraints exist. The Growth and Development Summit (GDS) recognised the importance of active participation of business in the development of Integrated Development Plans at that level. Efforts by organised business at local level to work with local authorities, particularly in the promotion of SMEs remains a challenge largely as a result of a lack of enthusiasm on the part of the authorities. Mechanisms to promote partnerships at this level need to be explored and possibly the Ministry of Finance could assist in this respect.

5. Finally, to reach a 6% growth rate will require that SA's levels of savings and fixed investment (presently at about 15% and 17% of GDP respectively) and the country's relatively low level of foreign direct investment (FDI) should be at much higher levels. Indeed, total fixed investment probably needs to be in the region of 23-25% of GDP to support a 6% growth rate. However, at the macro-level the reform agenda is unfinished. At the fiscal level the positive signal sent to investors that - through cutting direct taxes - SA is keen to attract investment, must be built on. The revised growth outlook, robust tax revenues and a declining burden of debt service costs clearly allow a range of acceptable policy options in the February 2006 Budget. If we also take into account that nearly two-thirds of the revenue overruns come from corporate taxes, emphasis in the main Budget should also fall on a further reduction in company tax to help reduce the costs of doing business in SA and to encourage investment to the levels we want to see it.

I emphasised at the outset that inevitably my comments on a broad subject like 'Employment and Economic Growth' in the context of the mini-Budget would certainly be selective in relation to what is a broad canvass. There are no 'silver bullets' that will simply quantum leap SA's investment, growth and employment performance in the immediate future. Rather, a continued combination of suitable policies - at both the macro and micro levels - that foster competitiveness, build long-term confidence and which make SA an attractive place to do business over the long haul are necessary.

We have already made substantial progress in generating a clear and credible macroeconomic framework over the course of the past decade - as the MTBPS again shows - and in reforming certain parts of the microeconomy and in developing black economic empowerment and transformation policy for the country. Reducing unemployment will continue to require a holistic approach, going beyond fiscal policy. Growth is a *necessary* condition, but not a *sufficient* one, if we want to maximise the number of jobs created at any given growth rate. For the moment the issue of the skills deficit is now more important to SA than the fiscal deficit in helping to boost future growth and employment.



It therefore remains crucial to pursue a set of policies that will raise SA's growth rate to 6% in the years ahead. Government and the social partners should constantly bear in mind the implications for economic growth prospects of all policies – whether these are overall economic policies, industrial policies, labour market policies, or even policies in international relations, crime or health. We need to build a strong consensus around the primacy of growth in the hierarchy of policy objectives and mobilise the key stakeholders accordingly.

But we need to retain perspective. I would like to end by emphasising that we should not misunderstand the nature of the challenges we still face. What we are seeing now in the SA economy are not the aches and pains of a sickly child needing intensive care; no, it is rather the growing pains and impatience of a robust child who is anxious to get the freedom and opportunity to push ahead into the next growth phase!

Thank you.

Cape Town
1 November 2005