

MEMORANDUM : 2020 REVISED FISCAL FRAMEWORK : Public Sector Remuneration

1. *Background*

This is a response to the call for public submissions and comments on the 2020 Revised Fiscal Framework. It deals briefly with just one aspect, namely the current negotiations regarding public sector remuneration.

2. *Rationale*

The rationale behind this submission is that monetary and fiscal policy are the main levers open to the State and the Reserve Bank in dealing with the Covid-19 pandemic; both have an impact on household finances. It is therefore logical to consider the effects of both when considering the overall welfare of households, and specifically when addressing the merits of salary increases in the public sector.

3. *Basic principle*

The fundamental point made here is that the action of the Reserve Bank in reducing interest rates by 275 basis points significantly reduces the cost of household borrowings, and this benefit should be taken into account in determining what is a fair level of salary increase, if any, at this time.

4. *Illustration*

Consider the position of a public servant with taxable income of R584 201 (a convenient figure as it reflects one of the tax thresholds for the tax year 2021, from which a marginal rate of 39% applies)¹ and a bond of R1m, bearing interest at 10% p.a. prior to the onset of the pandemic.

Tax payable amounts to R155 505, less the primary rebate of R14 958, ie R140 547, and income after tax will therefore be R443 654 (R584 201 – R140 547) assuming no other income or deductions. Interest at 10% on R1m would amount to R100 000, thus leaving R343 654 as income after tax and interest payments².

Following the reduction in interest rates of 275 basis points, the interest burden will fall by R27 500, and income after tax and interest payments will increase from R343 654 to R371 154, ie by 8.0%.

In short, this demonstrates, on the assumptions made, which it is submitted are reasonable, that without any salary increase, a public servant will effectively be 8% better off, courtesy of the Reserve Bank (it can be demonstrated, similarly, that even if remuneration were to be **cut** by 5%, the public servant would still be 2.6% better off after tax and interest).

¹ This figure will be close to the median income of public servants at levels 09-12 – see “2017 Medium term policy statement”, Annexure B, Table B.5 which gives the figure as R576 294; increases since then will have taken the figure above the amount of R584 201.

² Actual cash paid will exceed this as an amount of capital redemption will be required; this will depend on the terms of the loan, but does not affect the principle illustrated here.

5. *Additional considerations*

A single example, set at what is believed to be a reasonable level, has been used to illustrate the basic point. It would be wise to consider a variety of scenarios, using information to which it is presumed that Treasury will have access, in order to establish a clear pattern on which discussions and negotiations could be based.

In particular, not all public servants will have bonds, and the level will of course vary; however it is likely that there will be some form of borrowings, for example vehicle finance and credit card funding.

Clearly the benefit of the 275 basis points cut in interest rates will be felt most by those who have borrowed most. It may therefore be argued that to take savings in interest costs into account in wage negotiations works unfairly against those who have been prudent and not taken on credit; and also does not allow for those who have chosen to rent rather than buy.

Realistically, however, persons who have not borrowed, or have modest amounts of debt are already better placed to weather the crisis. In relation to those who are not home owners but are renting, there should be an indirect benefit insofar as it may be possible to negotiate a lower rental (as is already widespread in commerce), particularly if the landlord has borrowed to fund the property and is now benefitting from lower interest rates.

However I am now entering the realm of debate as to what is fair and how individual choices and preferences affect outcomes. That is not the purpose of this submission, which is simply to draw attention to what the writer believes to be an important factor in addressing the level of remuneration in the public sector in the current changed circumstances.

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30.6.2020