Fiscal Brief – August 2022

2021/22 Financial Year Analysis

PARLIAMENT
OF THE REPUBLIC OF SOUTH AFRICA

Parliamentary Budget Office

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1. PURPOSE

The Fiscal Brief aims to provide Members of Parliament (MPs) with an update on the outcomes of the implementation of the 2021 national, provincial and municipal budgets. This brief is based on the Public Finance Management Act (PFMA) section 32 reports for national and provincial departments released on 29 April 2022 as well as the Municipal Finance Management Act (MFMA) Section 71 quarter three reports released on 5 May 2022. The section 32 reports provide a full 2021/22 financial year data while the section 71 reports provide data for the first three quarters. The results from the section 32 and 71 report are preliminary.

2. CONSOLIDATED NATIONAL AND PROVINCIAL FINANCIAL HEALTH STATUS

This section of the brief highlight some of the findings of the Auditor General South Africa (AGSA) audit outcomes of the 2020/21 financial year. This analysis provides background to the current assessment of the financial state of departments.

Financial and performance audits are critical important for oversight and for tracking service delivery. The 2020/21 AGSA report acknowledges that there have been improvements to financial and performance outcomes in the third year of the current administration. Between 2019/20 and 2020/21 financial years, out of the 376 auditees that underwent assessment, the overall outcomes of 50 audits improved, 297 audits remained unchanged and 29 audits regressed. Notably, the audit outcomes for the key service delivery departments within the health, education, human settlements and public works sectors were worse than those of other departments. When taking into account the financial health of auditees – this includes indicators such as deficit, and inability to pay creditors and/or paying, an inability to recover debt, or dipping into the next year's budget to cover the current year's expenses - the AGSA concluded that only 30 per cent of the budget was managed by auditees in good financial health. Between 2018/19 and 2020/21 financial years, of the 157 departments considered, the financial health status of 21 of the departments has improved, 118 departments remain unchanged and 13 departments had regressed.

Table 1 shows that expenditure by departments exceeded their revenue by R41.74 billion. This is worrying, and ongoing concern. Over 60 per cent of departments had insufficient funds to settle all liabilities that existed at the end of the 2021 financial year. This shortfall means that these departments started the 2021/22 financial year with part of their budget effectively pre-spent. Departments had already spent more than 10 per cent (R31.08 billion) of their 2021/22 operating budgets excluding employee costs and transfers. These preliminary charges against the 2021/22 budgets have adverse implication for the amounts available for service delivery in 2021/22.

Table 1: Financial health indicators for national and provincial departments

Indicator	2020/21
Deficit (expenditure exceeded revenue)	R41.74 billion
Number of departments with deficit	32% (50)
Cash shortfall (bank overdraft less prepaid expenses/advances plus money to be surrendered to treasury)	R33.29 billion
Number of departments with cash shortfall	61% (89)
>10% of following year's budget (excluding employee cost and transfers) will fund the current year's shortfall	18% (27)
Bank in overdraft	19% (30)
Estimated settlement value of claims against the state at year-end	R166.07 billion
Number of departments with unsettled claims	94% (138)
Claims settlement value >10% of following year's budget (excluding employee cost and transfers)	37% (55)

Source: AGSA

The legal claims settlements against the state remain substantive high. Departments paid out R166.07 billion in claims in 2020/21, yet 94 per cent of departments remained with unsettled claims. The vast majority of claims against the state involved the departments of health, police and home affairs. Amendments have been proposed to the State Liability Bill, but these mainly focus on medico-legal claims. The amendments proposed are intended to help government realise the MTSF target to reduce the contingent liability of medico-legal cases by 80 per cent (< R18 billion) in 2024. However, continued efforts are required to remedy the root causes of litigations against the state in the other sectors (for example police and home affairs). Claims against the state negatively impact funding available for departments to cover their operational costs.

Unauthorised expenditure doubled to R3.21 billion, compared to 2018/19. The AGSA attributed the significant increase in unauthorised expenditure to departments overspending their budgets. Budget cuts and reprioritisation, along with emergency spending, in response to the covid-19 pandemic, resulted in reduced budgets for operational expenditure for a number of departments. This raises the question of whether the pandemic response was adequately implemented. Only 44 per cent (R218.5 billion) of the R500 billion emergency rescue package was used. The total budget allocation, for the COVID-19 rescue, to the national, provincial, and local governments was R190 billion, of which, R45 billion was not appropriated. The provincial health and education departments alone incurred R2.83 billion in unauthorised expenditure. Departments from the Eastern Cape, the Free State and the Northern Cape were responsible for 87 per cent of this unauthorised expenditure.

Compliance to laws and regulations also remains a significant concern for oversight. Irregular expenditure by provincial and national departments in the 2020/21 financial year amounted to R166 billion. Non-compliance was responsible for R103.6 billion of irregular expenditure. The majority of irregular expenditures due to non-compliance, R77.5 billion, were caused by increased NSFSAS non-compliance with bursary regulations. The 2020/21 audit by the AGSA shows that departments were unable to operate within their budgets, which resulted in deficits, cash shortfalls and bank overdrafts. This context is crucial for our understanding of the preliminary outcomes of expenditure and revenue in the 2021/22 financial year analysis.

3. NATIONAL GOVERNMENT

National government is responsible for providing services in terms of:

- Central Government Administration;
- Justice & Protection Services;
- Financial & Administration Services;
- Economic Services & Infrastructure Development; and
- Social Services.

This section provides an analysis of the preliminary expenditure and revenue outcomes against the budget at the national level for 2021/22. This analysis is based on expenditure by national vote portion of the consolidated budget.

3.1. Revenue Overview

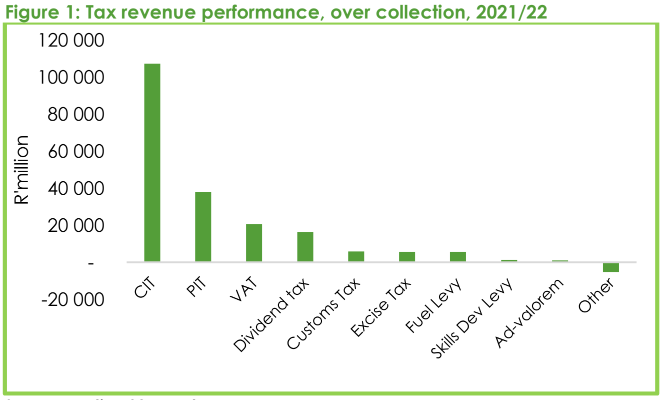
Table 2: Tax revenue, collection against budget, April 2021– March 2022

	2021 BR Estimates		2021 Revised estimates		Actual collection as a % of targeted: Apr-Mar 22		Actual collection as a % of targeted: Apr-Mar 21	
R million	R billion	Y-on-Y % change	R billion	Y-on-Y % change	R billion	Y-on-Y % change	R billion	Y-on-Y % change
Personal Income Tax	515 957	13.3	542 000	19.3	553 951	13.7	487 011	-7.7
Value Added Tax	370 177	22.9	373 637	29.9	390 847	18.0	331 197	-4.5
Corporate Income Tax	213 133	24.1	288 730	80.9	320 447	58.5	202 123	-4.4
Fuel Levy	83 148	31.6	89 647	31.1	88 884	17.7	75 503	-5.8
Dividend tax	16 837	18.6	29 853	44.8	33 308	34.1	24 845	-11.0
Custom Duties	53 967	15.0	55 740	36.8	59 913	26.7	47 290	-14.7
Specific Excise Duties	43 734	20.5	42 295	25.2	49 567	53.6	32 273	-31.1
Skills Dev Levy	17 813	57.8	18 933	86.1	19 336	57.8	12 250	-33.7
Ad-valorem	3 537	8.8	4 415	37.9	4 725	39.5	3 386	-17.9
Other	47 811	171.2	40 166	17.3	42 779	26.4	33 833	-8.3
Gross Tax Revenue	1 365 124	21.7	1 485 416	33.5	1 563 757	25.1	1 249 711	-7.8

Source: section 32 reports

In the 2021 adjustments budget (Nov 2021), gross tax revenue collection for 2021/22 was revised to R1 485.4 billion or R120.3 billion more than the 2021 budget estimates of R1 365.1 billion. By the end of March 2022, R1 563.8 billion had been collected representing 25.1 per cent (R314.1 billion) increase compared to the same period in 2021. This collection rate was 5 per cent (R78.3 billion) higher than the revised estimate announced in the 2021 adjustments budget. Year-on-year, corporate income tax (58.5% or R320.5 billion) was the tax instrument with the highest collection rate and was the main driver of the actual collection in gross tax revenue that was higher than the estimated collection. The tax instrument with the second and third largest actual collection rate were skills development levy (57.8% or R19.3 billion) and specific excise duties (53.6% or R49.7 billion), respectively, on year-on-year. The South African Revenue Service (SARS) collected higher than expected taxes from all tax instruments compared to a year ago where all tax instruments regressed when the country was still in strict lockdown as a result of Covid-19 Pandemic.

Figure 1: Tax revenue performance, over collection, 2021/22

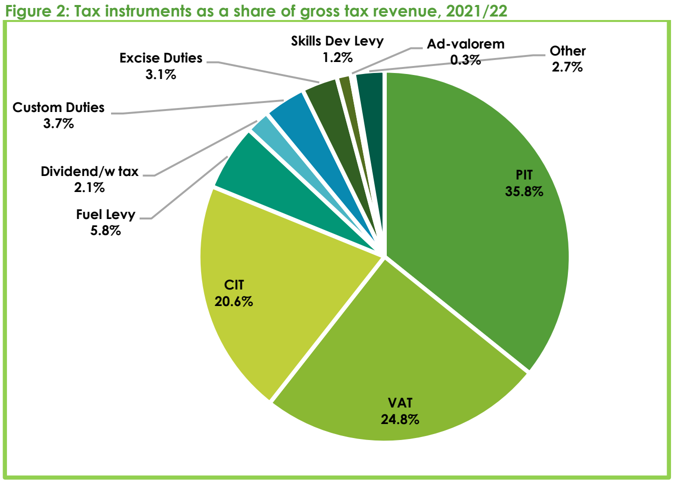


Source: section 32 reports

Figure 2 shows that the largest contributions to total tax revenue collection in 2021/22 from PIT (35.4%), VAT (25%) and CIT (20.5%). These three instruments combined contribute more than 80 per cent of total tax revenue. There has been much improvement in the collection of CIT, which breached 20 per cent as a share of total tax revenue in 2021/22 compared to 16.4 per cent in 2020/21. Tax revenue as a share of the Gross Domestic Product (GDP) increased from 22.5 per cent in 2020/21 to 25 per cent in 2021/22. PIT, VAT and CIT combined was 20.2 per cent of GDP. The estimation of tax revenue as a share of GDP is dependent on two factors, i) the level of growth in gross tax collection at particular level of the GDP and ii) the level of growth in GDP, given the gross tax revenue collection.

The collection on tax revenue was boosted by the commodities boom and corporate earnings more broadly. These developments resulted to buoyant tax revenue collections (the percentage change in revenue associated to a one percent change in GDP) because of the GDP improvement for much of the reporting period. The PBO's Quarterly Economic Briefs (QEB) analysis shows how GDP has performed in 2021 and in the first quarter of 2022.

Figure 2: Tax instruments as a share of gross tax revenue, 2021/22



Source: section 32 reports

3.2. Expenditure Overview

In the 2021 adjustments budget, the consolidated budget expenditure for 2021/22 was revised upwards from R1 832.4 trillion to R1 895.9 billion (30.3% as a share of GDP) compared to R1 804.2 billion (32.4% as a share of GDP) in the previous year.

Table 3: Consolidated government expenditure, 2021/22

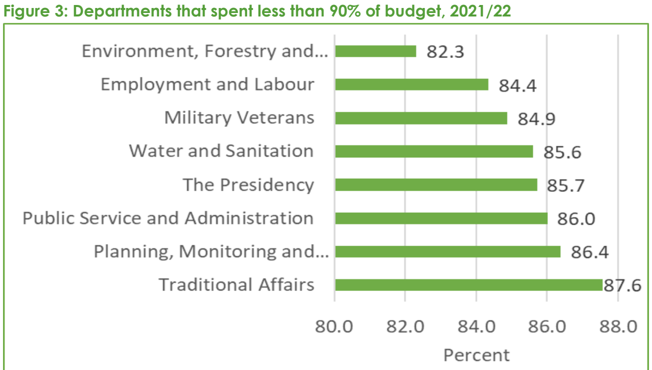
		Budget expenditure	Actual Expenditure	% YTD
2021/22	Appropriation by vote	1 028 457 408	1 013 244 492	98.5
	Direct charges against NRF	875 671 823	873 698 419	99.8
	Provisin not allocate to vote	-8 174 793	-	-
	Consolidated Expenditure	**1 895 954 438**	**1 886 942 911**	**99.5**
2020/21	Appropriation by vote	1 025 349 737	1 003 374 091	97.9
	Direct charges against NRF	782 517 261	784 618 698	100.3
	Provisin not allocate to vote	-3 692 917	-	-
	Consolidated Expenditure	**1 804 174 081**	**1 787 992 789**	**99.1**

Source: section 32 reports

As shown in table 3, the aggregate actual expenditure was R1 013.2 billion (98.5% of the budget) end of March 2022. This amounted to more than R15 billion in underspend compared to R21.9 billion a year ago. The total underspend for the departments of environment, forestry and fisheries, water and sanitation, and employment and labour, amongst others, was R4.8 billion. It remains concerning that some departments are struggle to spend their budgets given the societal needs for service delivery (see Figure 3). Conversely, the departments of social development and health spent R967.4 million (or 4%) and R265.7 million (or 0.4%) spent more than their budget allocation respectively by end of March 2022. The Direct charges against the National Revenue Fund (NRF) were R873.7 billion (99.8% of the budget) by end of March 2022 compared to R784.6 billion (100.3% of the budget) in the previous year.

Figure 3 illustrates the eight departments that had spent less than 90 per cent of their budget by end of March 2022. These departments contributed R2.5 billion to overall underspending by votes. Five out of the eight departments were allocated budgets of less than R1 billion.

Figure 3: Departments that spent less than 90% of budget, 2021/22



Source: section 32 reports

Expenditure by economic classification at a national sphere shows that more than two-thirds (67.6% or R695.2 billion) of the expenditure budget is allocated for transfers and subsidies. Followed by current payments (25.9% or R266.8 billion). Payment for financial assets was relatively higher than usual due to appropriation to to the Department of Public Enterprise to settle government guaranteed debt for Eskom and South African Airways (SAA) and National Treasury for an equity injection into South African Special Risk Insurance Association (SASRIA). Departments were unable to spend all their capital expenditure budgets (83.6%) by end of March 2022.

Table 4: Departments' expenditure by economic classification, 2021/22

Expenditure by economic classification (April - March 2022)			
Economic class	**Adjusted Budget**	**Expenditure**	**% spent**
Current payments	266 764 509	255 965 951	96.0
Transfers and subsic	695 224 520	693 576 443	99.8
Capital assets	15 784 108	13 202 739	83.6
Financial assets	50 684 271	50 499 359	99.6
TOTAL	1 028 457 408	1 013 244 492	98.5

Source: section 32 reports

Table 5 shows top five departments in terms of largest budget allocation. More than one-fifth (22.6% or R232.2 billion) of the total expenditure budget by vote was allocated to Social development, of which 100 per cent was spent by the end of March 2022. The Cooperative governance department (9.9% or R101.3 billion) received the second largest annual budget and spent 97.2 per cent of this budget by the end of March 2022.

Table 5: Departments with a relatively small budget, 2021/22

Vote R'000	Revised Budget	Actual Expenditure	YTD %
Social Development	232 146 315	233 113 723	100.4
Cooperative Governance	101 259 931	98 460 169	97.2
Police	100 473 833	99 595 392	99.1
Higher Education and Training	97 889 005	97 415 014	99.5
Transport	65 425 538	64 902 196	99.2

Source: section 32 reports

Table 6 shows bottom five departments in terms of the least budget allocation. The civilian secretariat for the Police Services received (0.01% or R151 million) the smallest annual budget allocation of all department. It spent 91.6 per cent by the end of March. Traditional affairs (0.02% or R172.7 million) is amongst the departments with a relatively small annual budget.

Table 6: Departments with a relatively large budget, 2021/22

Vote R'000	Revised Budget	Actual Expenditure	YTD %
Civilian secretariat for the Police Services	151 043	138 407	91.6
Traditional Affairs	172 690	151 236	87.6
National School of Government	214 297	210 624	98.3
Public Service Commission	286 271	265 721	92.8
Independent Police Investigative Directorate	353 778	347 906	98.3

Source: section 32 reports

3.3. Budget and revenue development

The SARS collected more than R1.5 trillion in tax revenue in 2021/22, a 25.1 per cent increase compared to the previous year where gross tax revenue collection regressed. The commodities boom and corporate earnings more broadly, were behind much of the increase. This increase would slightly reduce the actual budget deficit.

3.4. National Government Analysis Summary

The 2021/22 financial year has seen a relatively large improvement in annual real GDP, which increased by 4.9 per cent in 2021 after a decrease of 6.4 per cent in 2020[1]. The improvement in GDP was assisted by elevated commodity prices for much of the reporting period. Notable improvements were reported especially in the mining and quarrying, finance and manufacturing sectors. As a result, government's tax revenue collections have also increased. However, expenditure by some national votes have exceeded prior year spending patterns. Numerous departments (34 departments) struggled to spend all of their allocated budgets by the end of March 2022 despite the importance of services they are mandated to provide to citizens. For instance, The Department of Water and Sanitation spent 15 per cent (R2.6 billion) less than their annual budget when water supply and access remains a problem in some parts of the country.

4. PROVINCIAL GOVERNMENT

Provincial governments play an important role in the provisioning of basic education, health services, roads, housing and social development. Provincial treasuries play an important role in implementing public financial management in a decentralised fiscal context as delegated by the Public Finance Management Act, 1 of 1999. Similar to the section on the national government, this section provides analysis of expenditure outcomes against the budget at provincial levels for 2021/22 financial year. Unlike municipalities, provincial governments have very limited revenue raising capabilities.

4.1. Provincial receipts

Over 97 per cent of the receipts of provincial governments are allocated from the NRF. The provinces had collected 100 per cent of the budgeted receipts by end of March 2022. In terms of own receipts, the provinces had on aggregate collected over 99.7 per cent of the 2021/22 (R20.7 billion) estimated budget.

Table 7: Provincial receipts, 2021/22

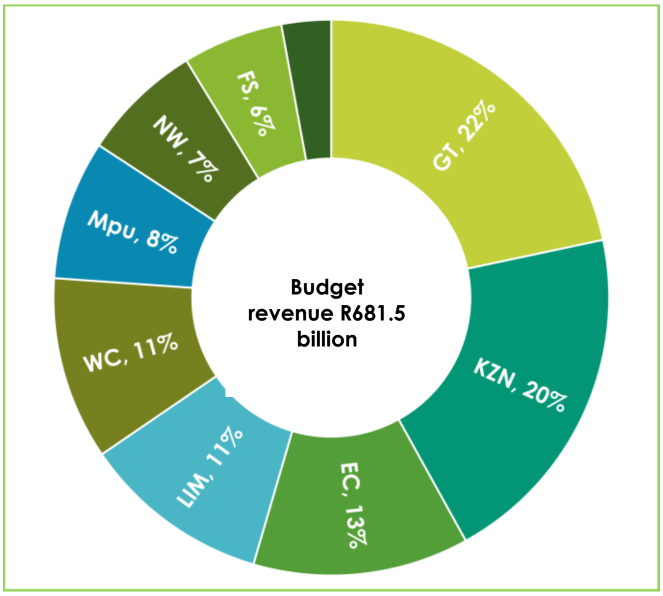
Actual against budget receipts R'000 - March 2022			
Receipts	Adjusted Appropriaiton	Actual collection	%
Equitable Share	544 834 911	544 834 911	100.0
Conditional Grants	115 923 955	115 915 602	100.0
Transfers from NRF	**660 758 866**	**660 750 513**	**100.0**
Tax Receipts	14 906 504	14 923 284	100.1
Sales of Goods and Services other than Capital Assets	3 357 117	2 738 349	81.6
Transfers Received	32 888	33 237	101.1
Fines, Penalties and Forfeits	266 653	316 175	118.6
Interest, Dividends and Rent on land	1 742 142	1 976 123	113.4
Sale of Capital Assets	67 553	123 293	182.5
Financial Transactions in Assets and Liabilities	384 964	586 227	152.3
Provincial Own Receipts	**20 757 821**	**20 696 688**	**99.7**
TOTAL: RECEIPTS	**681 516 687**	**681 447 200**	**100.0**

Source: section 32 reports

Provincial government funding consists mainly of a provincial equitable share and conditional grants. The equitable share is determined by an equitable share formula which is updated every year with the relevant provincial socio-economic and demographic data. The formula has six components with education and health being the largest based on the demand and the need for education and health services. The remaining four components enable provinces to perform their other functions, taking into consideration the population size of each province, the proportion of poor residents in each province, the level of economic activity and the costs associated with running a provincial administration.

Gauteng received the largest share (22%) followed by KwaZulu Natal (20%) and Eastern Cape (13%). Northern Cape (3%) and Free State (6%) gets the lowest allocations as determined by the equitable share formula structure.

Figure 4: Provincial budget share by province, 2021/22

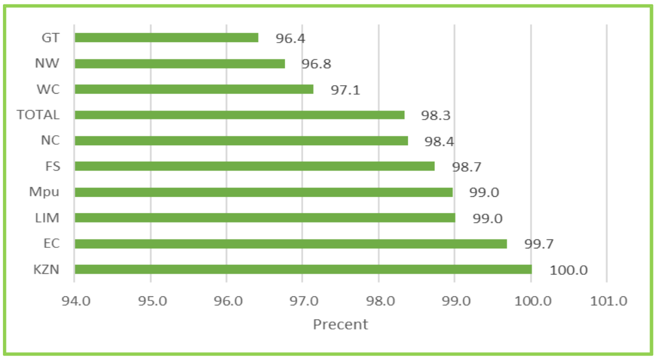


Source: section 32 reports

4.2. Provincial Expenditure

Figure 5 shows expenditure by province. Gauteng, which received the largest budget allocation, had spent 96.4 per cent of their budget by end of March 2022. Other provinces that had spent less than 98 per cent of their budgets were North West (96.8%) and Western Cape (97.1%) around the same period. Only Kwa-Zulu Natal spent 100 per cent of their budget.

Figure 5: Expenditure by province (%), 2021/22



Source: section 32 reports

[1]StatsSA: Gross Domestic Product (GDP), 4th Quarter 2021

Table 8 shows total provincial expenditure by economic classification. On aggregate, provincial expenditure allocation for the previous year, 2021/22, was R690.3 billion. Of the total budget, current payments consist of more than 80 per cent (R582.7 billion) of the budget followed by transfers and subsidies at 13.1 per cent (R90.7 billion). It is also worth noting that Compensation of Employees (COE) accounts for about 75 per cent (R417.2 billion) of current payments or more than 60 per cent of the total provincial expenditure budget. This reflects the personnel heavy services provided by provincial departments (i.e. health and education).

Goods and services accounted for about 26 per cent (R145.5 billion) of the current payments budget and more than 20 per cent of the total provincial expenditure budget. Provinces have on aggregate spent just about 99 per cent of their current expenditure budgets by end of March 2022. There was overspending on interest & rent on land as well as financial assets and liabilities. Interest & rent on land was driven by GP (RR65 million), NC (R12.8 million) and FS (R11.8 million). It is a concern that GP budgeted R111 thousand for interest & rent on land whereas they spent significantly more. Similarly, with KZN and FS, R273 thousands and R6 million was budgeted respectively.

Table 8: Provincial expenditure by economic classification, 2021/22

Expenditure by economic classification R'000 (April - March 2022)			
Economic class	**Adjusted Budget**	**Expenditure**	**% spent**
Current payments	562 727 233	556 869 283	99.0
COE	*417 176 460*	*416 527 973*	*99.8*
Goods and	*145 536 612*	*140 238 294*	*96.4*
Interest & rent on	*14 161*	*103 017*	*727.5*
Transfers and subsidies	90 701 576	88 472 902	97.5
Capital assets	36 851 906	33 716 201	91.5
Financial assets	20 000	150 211	751.1
TOTAL	**690 300 715**	**679 208 597**	**98.4**

Source: section 32 reports

Provincial payments for capital assets allocation was R36.9 billion for 2021/22. The provinces spent 91 per cent (R33.7 billion) of their budgets by the end of March 2022. More than 70 per cent (R27.1 billion) of the capital assets budget was allocated for building and other fixed structures. About a quarter (24.5% or R9 billion) is allocated for machinery and equipment.

Table 9: Overall provincial payment for capital assets, 2021/22

	Adjusted Appropriation	Actual payments	% Spent
Buildings and other fixed structures	27 058 537.40	24 743 579.70	91.4
Machinery and equipment	9 019 787.50	7 181 650.12	79.6
Land and sub-soil assets	527 550.00	1 452 803.00	275.4
Software and other intangible assets	224 517.40	317 845.70	141.6
Biological assets	15 417.00	18 027.00	116.9
Heritage assets	6 097.00	2 295.00	37.6
Payments for capital assets	**36 851 906.30**	**33 716 200.52**	**91.5**

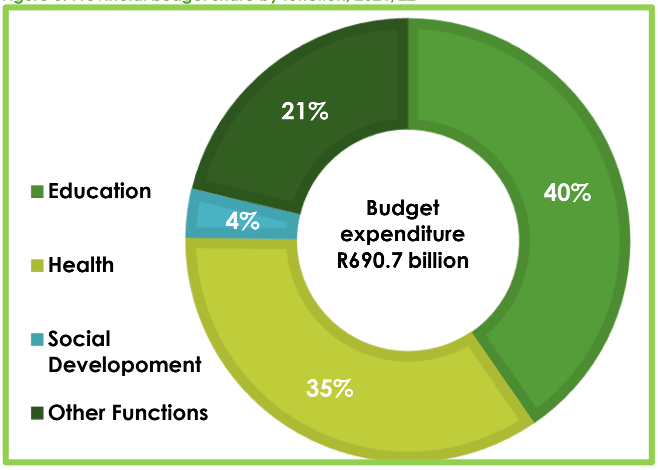
Source: section 32 reports

Overall payments for capital assets by function show that for provincial education spending was above 90 per cent except for Western Cape (76.8%) and Limpopo (86.1%) that spent below 90 per cent of their capital budgets. Health experienced difficulties in to spend their capital budget. By social development function, North West (48.5%) and Limpopo (64.5%) struggled to spend their budgets while Mpumalanga (116.7%), Free State (113.1%) and Gauteng (103.8%) over spent on their budgets.

4.3. Provincial budget analysis by function

Figure 6 shows that Education (40% or R279.1 billion) and Health (35% or R240.2 billion) were the largest expenditure functions of the provincial sphere of government.

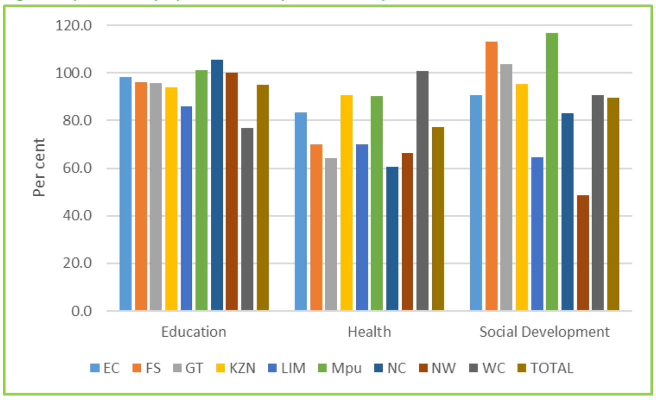
Figure 6: Provincial budget share by function, 2021/22



Source: section 32 reports

Overall payment for capital assets by function shows that for education, provinces were spending almost all of their targeted budgets, except for Western Cape (76.8%) and Limpopo (86.1%) that spent below 90 per cent of the budget. They were notable more struggles by health function to spend their capital budget. By social development function, North West (48.5%) and Limpopo (64.5%) struggled spending their budget while Mpumalanga (116.7%), Free State (113.1%) and Gauteng (103.8%) over spent their budget.

Figure 7: provincial payments for capital assets by function, 2021/22



Source: section 32 reports

While spending targets in the health, education and social development sectors are generally being met, there are concerning trends in terms of performance for these sectors. The 2020 Trends in International Mathematics and Science Study (TIMSS) results show that grade 5 scores achieved are 374 and 324 for mathematics and science respectively. Math results show a slight drop from 376 in 2015. Both results were below the 2023 target of 426, which indicates that the MTSF Grade 5 TIMSS mathematics score target of 426 in 2023 may not be attainable. The proxy for quality education is tracked through the number of learners achieving 60 per cent and above in Mathematics and Science in grade 12. The 2020 results reflected rates of 13.2 per cent and 15.3 per cent respectively in the two subjects.

In December 2020, StatsSA reported that the proportion of children (up to four years old) attending an early childhood development (ECD) programme declined between 2018 and 2019 — from 43.9% to 40.7%. In an ECD report commissioned by DBE, it was reported that According to data collected starting in August 2021, 42 420 early learning programmes (ELPs) were counted that collectively had 1 660 316 children enrolled. There were 6.2 ECD programmes per 1000 children between 0-5 years nationwide. It is important to note that there are also a significant number of children in unregistered ECD centers. Some emerging data on ECD shows that COVID-19 has adversely impacted this sector. According to statistics SA the percentage of children aged 0–4 years that remained at home in 2020 with a parent, guardian, other adults or children was 67.1% in 2020. The number of children remaining at home has increased from 59.3% in 2019. The significant increase is largely due to increases in unemployment, income losses, and crèche closures during the pandemic.

In Health, the numbers are also concerning. According to StatsSA data, South Africa's average Life Expectancy (LE) at birth was 65.5 years, in 2020, against the MTSF target of at least 70 years by 2030. According to StatsSA, South Africa's Infant Mortality Rate (IMR) was 23.6 deaths per 1 000 live births in 2020 compared to 22.1 per 1 000 in 2019. The under-5 mortality rate (U5MR) was estimated at 34.1 deaths per 1 000 live births in 2020, while the country's U5MR was 28.5 per 1 000 in 2019. The MTSF target is to decrease the IMR to less than 20 deaths per 1 000 live births by 2024 and the under-5 mortality rate to less than 25 deaths per 1 000 live births by 2024. If the decline continues, the target will not be met.

4.4. Provincial Government Analysis Summary

Provinces generally spent close to 100 per cent of their budgets by end of March 2022. However, Gauteng (96.4%) could not spend all their budget. Claims, for example, are unbudgeted expenditure which may negatively impacts the funding available to provide services. Despite spending being on track with budget, there are serious concerns around outcomes. The health and education indicators are particularly concerning. The PBO is currently undertaking a research analysis on policy outcomes. These reports will be available later in the year.

5. LOCAL GOVERNMENT

The core services that local governments provide - clean drinking water, sanitation, electricity, shelter, waste removal and roads - are basic human rights, essential components of the right to dignity enshrined in our Constitution and Bill of Rights. Local governments (municipalities) have been primary spheres of government for the delivery of services in South Africa. As per the 1998 Local Government White Paper, municipalities render services at a charge to citizens to generate revenue. Unlike the national and provincial government sections above, this section on local government provides an update for the nine months of the 2021/22 financial year until end March 2022 for expenditure outcomes against the budget at local government levels. The municipal budget cycle timeline runs different from national and provincial spheres, starting from 1 July to 30 June of the following year. This section begins by outlining the financial health status of municipalities to contextualise our revenue and expenditure analysis.

5.1. Financial health status of municipalities as of April 2022

AGSA audits have continuously alerted government that local government finances continue to be under severe pressure, which has negative implications for service delivery. The number of municipalities in financial distress has risen from 86 in 2013/14 to 175 in 2019/20, and 123 municipalities passed unfunded budgets in 2019/2020. As of April 2021, the total deficit in local government was R6.63 billion (lower than R7.4 billion in the previous year), and expenditure exceeded revenue at year-end at 55 municipalities. The PBO is concerned about the dipping into future budgets to address current and emerging needs.

Ineffective financial management remains a worrying concern. Only 25 per cent of municipalities submitted credible financial statements for audit in the 2020/21 financial year. Which means, 75 per cent of municipalities were not able to submit quality financial statements for auditing. AGSA attributes the ineffective financial management to non-payment by municipal debtors, poor budgeting practices, and ineffective financial management.

Table 10: An overview of the financial health of municipalities in 2010/21

Creditors greater than available cash	
Creditors > available cash at year-end	47% of municipalities
Expenditure of exceeded their revenue at year-end	26% of municipalities
Current liabilities greater than 50%	
Current liabilities > 50% of next year's budget at year-end	52 (29%)
Unauthorised expenditure	
Unauthorised expenditure	R20.45 billion
Unauthorised expenditure incurred by 104 municipalities relating to non-cash items#	R13.25 billion

Source: AGSA

#Excludes 57 outstanding audits
*Excludes 18 municipalities where the financial statements were not reliable enough for financial analysis (i.e. those with adverse or disclaimed audit opinions)

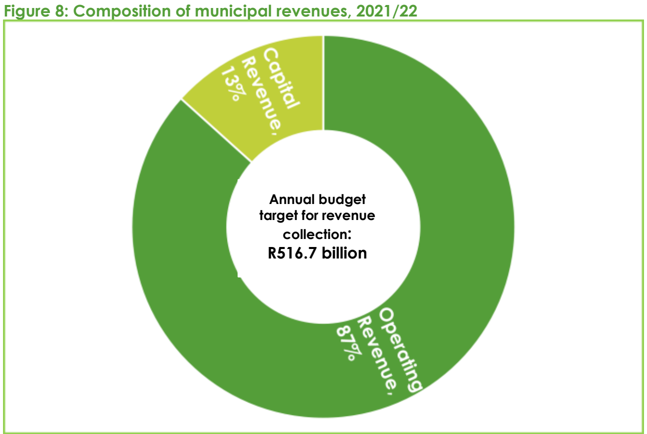
In the 2020/21 assessment, the AGSA reported that financial health of over a quarter of municipalities is so dire that there is significant doubt that they will be able to continue operating as going concerns in the near future. This problem should be of great concern to the government and assertive action should be taken to mitigate the political, social and economic risks that would be associated with this level of failure.

For a number of years, the AGSA has also pointed to the material irregularities that undermine service delivery at the municipal level, namely procurement and payments, interest and penalties, revenue management, and investments and assets. The total financial loss of these material irregularities was estimated to be R3.9 billion, R1.6 billion of which was money lost by municipalities that had invested in the VBS Mutual Bank. This is an increase from the previous year, where material irregularities amounted to R2.04 billion, with a total of 75 of the material irregularities identified.

5.2. Municipal revenues in 2021/22

Despite the financial distress experienced by municipalities due to the pandemic shocks, Figure 8 shows that the municipalities aggregate annual targeted revenue for 2021/22 was R516.7 billion. This was R33.1 billion more than in the same period in 2020, which suggests an improvement from the previous year. Of the annual estimated revenue, more than 85 per cent (R447.9 billion) is for operating revenue whilst the balance (15%) is capital revenue.

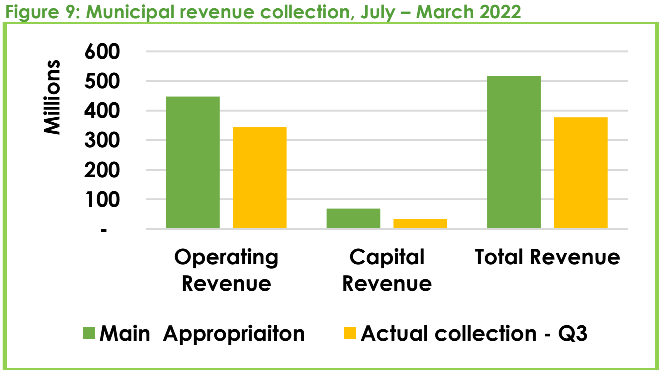
Figure 8: Composition of municipal revenues, 2021/22



Source: Section 71 reports

By the end of March 2022, municipalities had on aggregate collected more than 73 per cent (R377.4 billion) of the 2021/22 estimated revenue of which 76.6 per cent (R 343.2 billion) was on operating revenue by end of March 2022. This means that municipalities were on track to achieve their operating revenue targets by the end of the year. Municipalities had only collected 49.8 per cent (R34.3 billion) of capital revenue by the end of March 2022. This slower than expected collection rate might result in an under collection on capital revenue by the end of the financial year.

Figure 9: Municipal revenue collection, July – March 2022

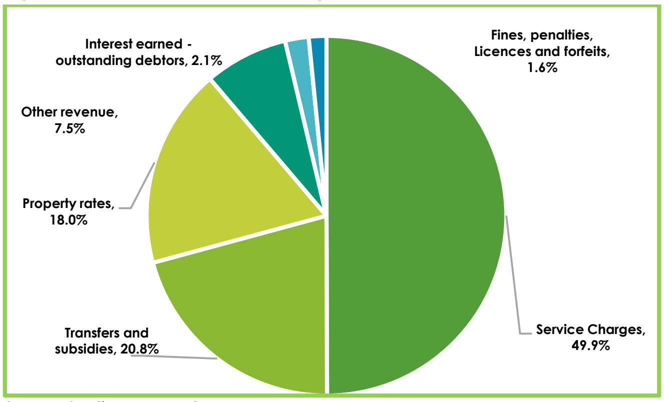


Source: section 32 reports

5.3. Operating revenue

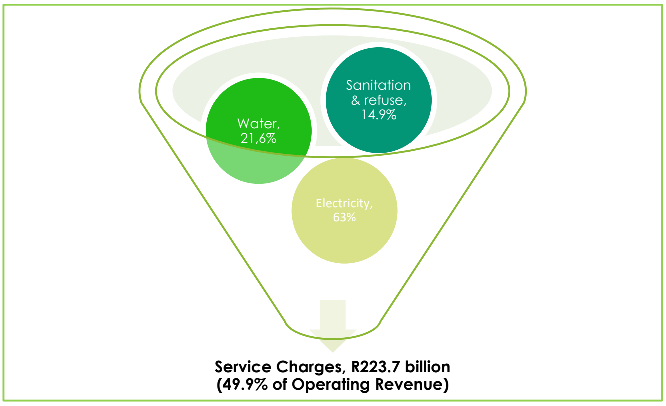
As shown in Figure 10, half of the aggregated operating revenues are generated from municipal service charges (49.9% or 223.7 billion), followed by transfers and subsidies (20.8% or R93.3 billion, and property rates (18% or R80.6 billion). These are the three main sources of municipal operating revenue constituting 88.8 per cent of total operating revenue.

Figure 10: Composition of operating revenues, 2021/22



Source: Section 71 reports

Figure 11: Composition of Service Charges, 2021/22



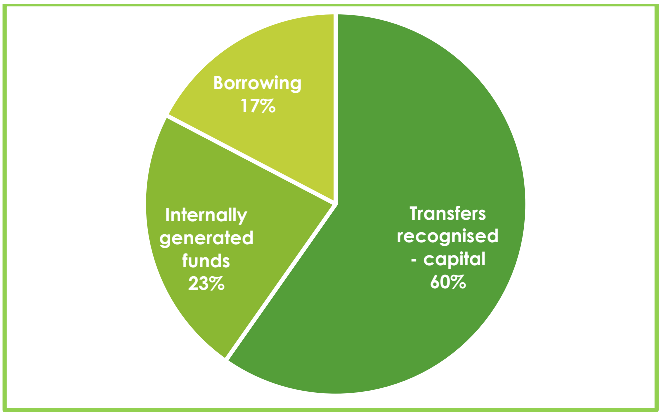
Source: section 71 reports

Of the R233.7 billion aggregated service charges, electricity (63%) contributed the largest share, followed by water provision (21.6%), and sanitation and refuse (14.9%). Despite electricity being the largest share of revenue, municipalities across the country owed Eskom R35.3 billion as of March 2022.

5.4. Capital revenue

Of the capital revenue, 59.8 per cent was from government transfers, 22.9 per cent was from internally generated funds and 17 per cent was from borrowing.

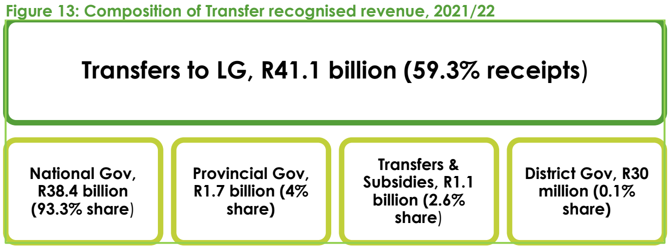
Figure 12: Composition of capital revenue, 2021/22



Source: section 71 reports

On aggregate, municipalities' estimated transfers recognised(capital) were R41.1 billion for the 2021/22 financial year. By end of March 2022, 59.3 per cent (R24.6 billion) was received. In terms of proportional share, the largest budgeted transfer recognised capital receipt is from National government receipts (93.3% or R38.4 billion) and the lowest was from District municipal transfers (0.1% or R30 million).

Figure 13: Composition of Transfer recognised revenue, 2021/22

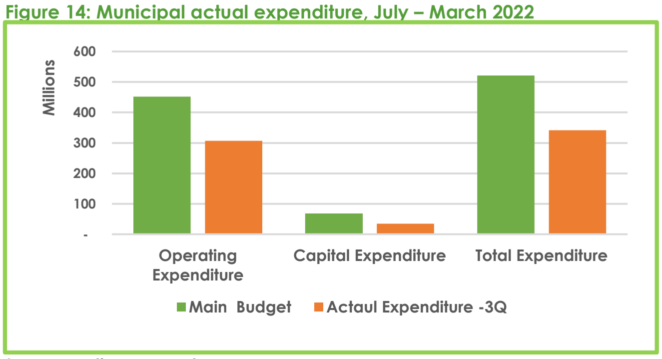


Source: section 71 reports

5.5. Municipal expenditure

By the end of March 2022, municipalities had on aggregate spent 65 per cent (R342 billion) of total budgeted expenditure. In the same period, municipalities had spent 67.8 per cent (R306.7 billion) on operating expenditure. Only 51.3 per cent (R35.4 billion) of the capital budget had been spent by the end of March 2022. This slower than expected spending in nine months might result in delayed service delivery to people.

Figure 14: Municipal actual expenditure, July – March 2022

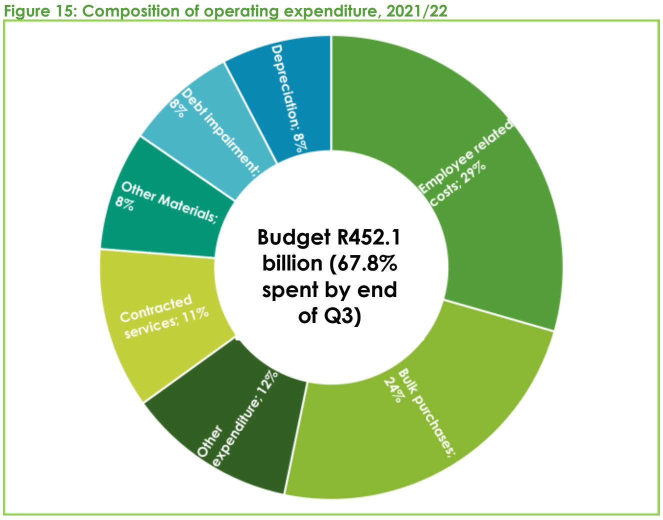


Source: section 71 reports

5.6. Operating expenditure

The drivers of operating expenditure at a municipal level are compensation of employees (29.4% or R133.1 billion) with the largest budget, followed by Bulk purchases (23.8% or R107.7 billion). Contracted services (11.2% or R50.7 billion) is the third highest expenditure item.

Figure 15: Composition of operating expenditure, 2021/22

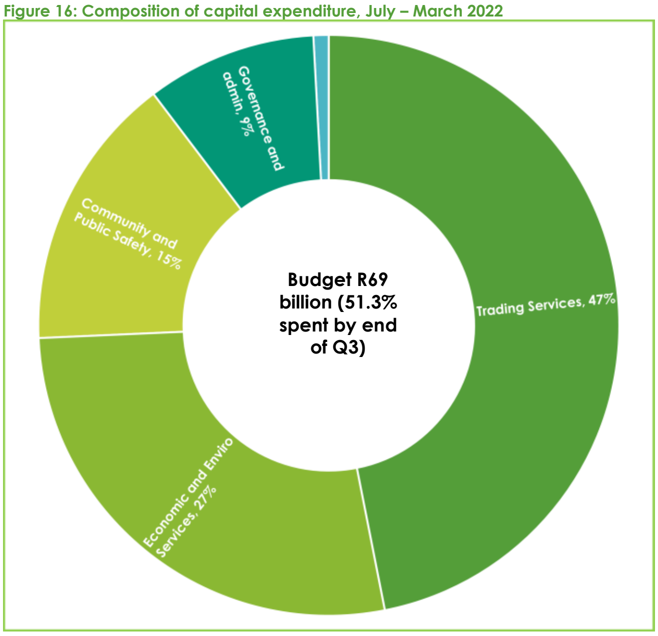


Source: section 71 reports

5.7. Capital expenditure

The capital expenditure budget for 2021/22 was R69 billion. The largest share of the capital expenditure budget was allocated to Trading services (46.9% or R32.4 billion) and 54.5 per cent had been spent by end of March 2022. This follows economic and environmental services (27.4% or R18.9 billion) and 62.8 per cent had also been spent by end of March 2022.

Figure 16: Composition of capital expenditure, July – March 2022

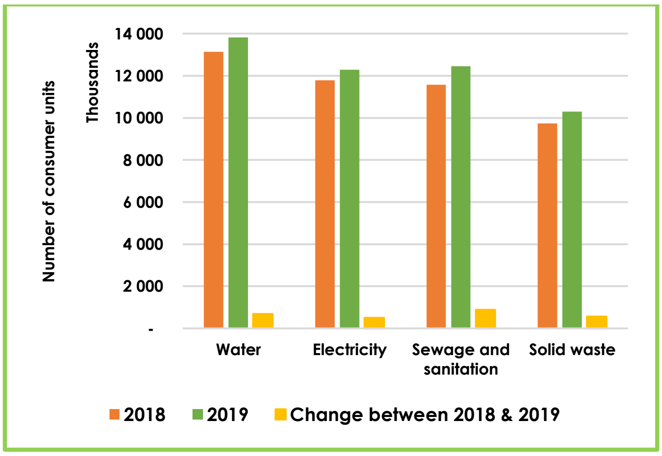


Source: section 71 reports

5.8. Municipal service delivery status

In 2021, Statistics South Africa (StatsSA) released the 2019 Non-Financial Census of Municipalities Survey (NFCS) findings to provide information that can serve as a framework for policymakers and other stakeholders for planning and monitoring. The census enables users to analyse the services provided by municipalities in terms of water, electricity, solid waste management, sewerage and sanitation.

Figure 17: Number of consumer units receiving basic services from municipalities, 2018 and 2019



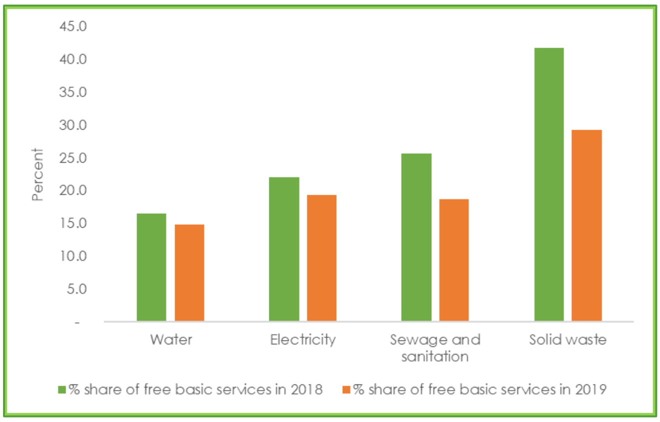
Source: NFCS 2018 and 2019

The number of consumer units receiving basic water services from municipalities increased by 5.2 per cent (681 194) from 13.1 million in 2018 to 13.8 million in 2019. Those receiving electricity services increased by 4.2 per cent (498 389) to 12.3 million in 2019. In terms of sewage and sanitation, the number of consumer units receiving municipal services increased by 7.6 per cent (878 308) to 12.5 million in 2019. The survey also showed that 10.3 million consumer units received solid waste management services from municipalities in South Africa. The number of households funded for free basic services in the national budget increased from 8.7 million in the 2014/15 financial year, to 10.36 million in 2020/21. However, the number of actual beneficiaries was lower than the funded number of households. The NFCS) report for 2019 shows that:

- 3 million consumers benefited from free basic water services,
- 2.1 million consumers benefited from free basic electricity
- 2.3 million received free sewerage and;
- 2.4 million benefited from free solid waste management.

In 2019, there were 132 303 fewer consumer units receiving free basic electricity services than in 2019. Consumer units receiving free basic sewerage and sanitation in 2019 decreased by 645 866 compared to 2018. Compared to 2018, there were 315 714 fewer consumer units that received free basic solid waste management services in 2019. Access to basic services has increased, yet, the provisioning of free basic services has declined. The current provisioning of free basic services is not adequate and infringes on governments' constitutional obligations to indigent households.

Figure 18: Consumers receiving free basic services as a share of total consumers in 2018 and 2019



Source: NFCS 2018 and 2019

Poor service delivery has disproportional impacts on different households (along racial, gendered and geographic lines), because it is predicated upon a set of distributive relations across different social groups. COVID-19 has brought to the fore, the centrality of (social) reproduction – household duties such as cooking, cleaning, water and fuel collection, child care, or elder care. These activities, which are disproportionately undertaken by women and girls, are exacerbated by the lack of access to basic services. According to the South African Police Service's (SAPS) Incident Registration Information System (IRIS)[2], a total of 909 protest actions took place from 1 August 2020 to 31 January 2021. Dissatisfaction with service delivery has often been cited as the most important reason for the increase in service delivery protests within South Africa.

5.9. Local Government Analysis Summary

Municipal services are intended to be a tool to address poverty and inequality issues, raise living standards and facilitate economic opportunities[3]. Our findings demonstrate that more needs to be done at the local government level to realise these objectives. The current revenue estimate for municipalities is R516.9 billion, whereas the planned expenditure is R521.1 billion for the 2021/22 financial year. This means municipalities will have a deficit in their budget balance of R4.4 billion.

Financial mismanagement in municipalities continue to affects financial and operational challenges that hinder local government from delivering basic services which are usually closely related to one another. As the AGSA notes, basic discipline and processes should be in place at municipalities, such as procuring at the best price, paying only for what was received, making payments on time, recovering the revenue owed to the state, and safeguarding assets.

At the same time, the distress being exhibited by local governments could be indicative of a broader issue of insufficient funding. Not all local governments are able to generate revenues needed to provide basic services for all in an equitable manner. It should be asked what options municipalities really have? If they increase prices of basic services to increase their revenues, they would decrease affordability of these services and further exacerbate the inequalities that exist. Thus a greater call needs to be made for the review of the local government revenue model as well as the assumptions of revenue generation. The 2020/21 audit shows that the arrears (including interest) payable to Eskom and the water boards by municipalities amounted to R25.37 billion and R13.29 billion, respectively An alternative model should prioritise affordability of basic services and the provisioning of free basic services to all indigent households.

[2] South African Police Service (SAPS) Incident Registration Information System (IRIS)

[3] Public Affairs Research Institute (PARI), Access to basic services report