

# Budget 2024: Mixed expectations in an election year

By [George Herman](#)

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With the budget speech being delivered in an election year Citadel's chief investment officer, George Herman expects to hear populist promises and over-optimism which is geared more to voters than the financial markets.



Source: [Fxabay](#)

“We will need to scrutinise the numbers coming out of the budget very carefully to see if Finance Minister Enoch Godongwana’s budget proposals are viable and achievable given the country’s high debt burden and strained tax base,” says Herman.

“The biggest issue to contend with on the income side of the budget is the declining economic growth profile globally and specifically in South Africa. The benefits we had seen from higher commodity prices have now subsided and corporate tax is truly under pressure which means that the revenue will be lower.”

**Tax and VAT expectations remain positive:** Corporate income tax was recently reduced, and analysts do not expect the decision to be reversed, says Herman.

“Personal income tax has been resilient and when you take into account that it is an election year, we do not expect any major changes or surprises for our taxpayers. With the number of taxpayers in the highest bracket having grown we could see an increase of tax in this bracket.

"There is however a possibility that this is due to pure bracket creep (a situation where inflation pushes wages and salaries into higher tax brackets, without real earnings increases). It is estimated that bracket creep could increase tax take by between R15bn to R20bn, which will cover a few holes." In terms of VAT, Citadel's analysts do not expect a VAT increase – again because it is an election year – which will "leave the income side of the budget quite static".

**Government expenditure and the continuing wage bill dilemma:** The expenditure side of the budget is a "tougher story" as there are many aspects of it that need to be watched, says Herman.

"The first issue is that over the last two years, there has been under-budgeting in terms of the government wage bill. The employee wages that were agreed on during negotiations did not filter through to the budget and in fact, last year's medium-term budget and the budget as it stands today still shows over-optimistic numbers.



### What economists will be listening for in the budget speech

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"This is an enormous swing factor as the overall increases promised to government employees – which according to the agreement equated to around R45bn – has unsurprisingly led to substantial under-budgeting by Treasury.

"National Treasury earlier indicated that it would make up the shortfall through the reduction of the state's workforce and natural attrition.

"Unfortunately, this has not taken place, which means the government's wage bill remains a problematic item on the expenditure side."

Herman points out that the increase in social grants is another point to be watched as it is a big-ticket item on the expenditure side of the budget. "Temporary measures like the Social Relief of Distress Grant has been extended twice now and looks to be made permanent."

**Debt servicing and State-owned Enterprise (SOE) bailout woes:** "A big issue in a world with rising interest rates is the rising debt-servicing cost, and in this year's budget we will find that South Africa's debt-servicing cost has become the single largest component on the expenditure budget.

"We are paying more for debt servicing now than any other subcategory in the budget – more than education, healthcare and policing – which should be a wakeup call to the government in terms of the fiscal restructuring that needs to take place."

Herman says the financial markets are eagerly awaiting comments on any structural reforms that would come into play in the coming year.

"An important one to watch out for would be SOE bailouts. For instance, the Eskom numbers have been in the budget for quite some time and a good future trajectory of those numbers has been pencilled in, but more recently Transnet also asked for bailouts, and we know the Post Office is going to need some budget as well. Suddenly the risk becomes enormous.



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"Foreign investors are factoring in several risks that face the country and have now become quite aggressive sellers of South African bonds.

"All of which adds to higher risk premiums (around the value of the rand and bond yields) and more expensive servicing of government debt."

#### **Key numbers the market will be watching:**

- **The main budget deficit:** For the next financial year the budget deficit is expected to peak in the region of 4.5% of gross domestic product (GDP).
- **Gross debt-to-GDP:** We are now approaching 80% gross debt-to-GDP, a monumental increase over the last two decades and a problematic number for an emerging market that requires economic growth and job creation to survive.
- **The Gold and Foreign Exchange Contingency Reserve Account:** There could be a monetisation of some of its unrealised profits.  
"The state's contingency fund is a complex tool to rebalance the South African Reserve Bank's balance sheet.

If some of our reserves are reduced, sold and monetised, the short-term effect is that it will have a positive impact on the rand as some flows might come into the country; but the negative effect would be that our level of currency reserves will reduce, increasing the fragility of the rand in the medium term. The markets will be looking for an announcement on this issue."

Herman expects the markets to applaud the use of currency surpluses to reduce long-term government debts, but if these capital gains are used to cover short-term expenditures and cashflows this will be deemed "very bad, and the market would be negative around such an outcome if that had to happen".

The currency markets and the debt markets are sensitive to the budget, specifically because of the big issues hanging over our country.

#### **ABOUT THE AUTHOR**

George Herman is Citadel's chief investment officer.

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