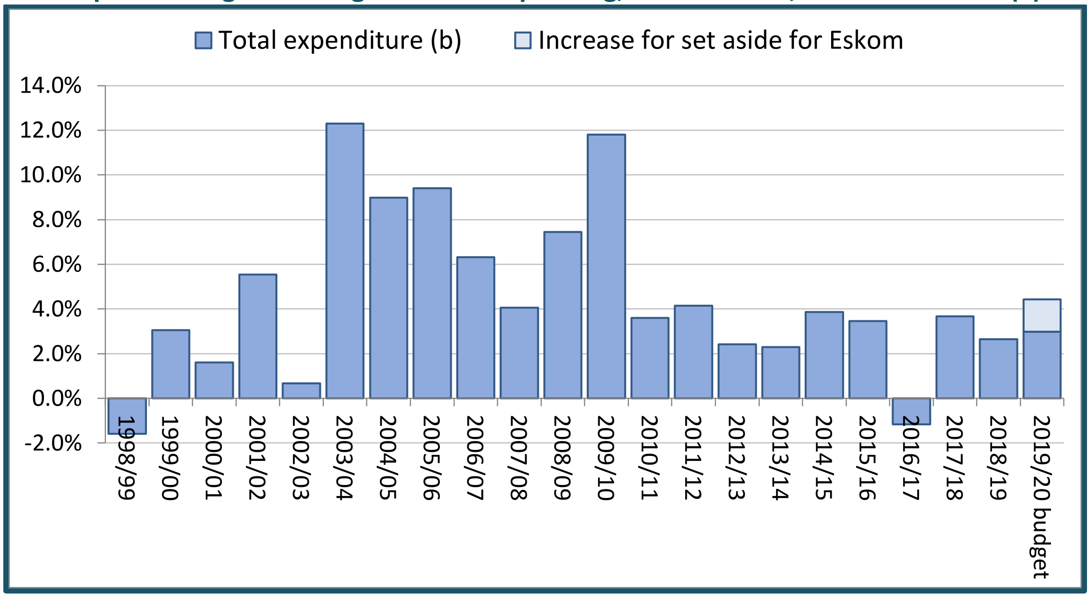
Briefing Note: The 2019 budget and industrialisation

The 2019 Budget faced tough choices. In the end, National Treasury prioritised core social services, infrastructure, and rescuing Eskom while avoiding an excessive increase in the national debt. The trade-off is a squeeze on industrial policy programmes, which will see cuts in real terms. This reality increases the importance of ensuring that other areas of state spending, especially on infrastructure, education and procurement, do more to support industrialisation and inclusive economic development.

As the following graph shows, in constant terms state spending rose an average of 7.5% a year from 2002 to 2009, financed effectively by soaring tax revenues during the commodity boom. The 2008/9 stimulus package in response to the global financial crisis raised the deficit significantly, however, and in response Treasury reined spending growth in to an average of 2.8% a year from 2010 to 2018 – still well above population growth, but far below the expansive 2000s.

The 2019 budget foresees an increase of 4.4% above inflation in total spending – the largest percentage hike since 2010. But a third of the projected growth goes into a contingency fund for restructuring Eskom, leaving an increase of 3.0% above inflation, or around R40 billion, for the rest of government spending.

Graph 1. Change in total government spending, 1997 to 2019, in constant rand (a)



Notes: (a) Deflated with March CPI and Treasury projection for 2019/20. (b) Excluding funds set aside for Eskom in 2019/20. Source: National Treasury. Budget Review 2019.

The increase in 2019/20 goes almost exclusively to the main government services – education, social grants, health and infrastructure, including Eskom. Since much of this spending goes through provinces and municipalities, their share in the total budget will rise 4.4% above inflation in 2019/20, while national departments will see an increase of only 1.2%.

In this context, the main economics departments get little in the way of additional resources, with some facing substantial cuts. The national departments responsible for overall economic governance and development – Trade and Industry and Economic Development – will jointly see a budget cut of 0.5%, mostly borne by Economic Development while Trade and Industry gets a marginal increase in constant terms.

The budget for Agriculture, Forestry and Fisheries drops almost 6% in real terms, while Mineral Resources rises 0.8% and Tourism 0.6%. An additional R1 billion will go to the Small Enterprise Finance Agency (sefa) as a transfer through the Department of Small Business Development, but the department's own spending climbs just 0.2%. As a group, excluding the transfer to sefa, the budget for these core economics departments falls by 0.1%.

Trade and Industry accounts for over half the budget of the core economics departments, with a total of R10 billion in 2019/20. Of that, the bulk goes to the Incentive Development and Administration Division (IDAD), which gets R6 billion, and the Industrial Development Division (IDD), with R2 billion.

In constant rand, IDAD's budget allocation will climb by 2.9% in 2019/20. Some R3.4 billion of its spending supports industry through the Manufacturing Incentives Programme, with almost 40% of the programme going to the clothing industry.

Trade and Industry's assistance to the auto industry involves a substantially larger cost to the fiscus, estimated at over R5 billion a year, but takes the form of tax savings and therefore does not appear in the budget. IDAD's programme to support services, mostly Business Process Services (BPS), will fall by 17% to R0.7 billion. In contrast, its financing of infrastructure will climb 18% in real terms, to R1.4 billion.

The IDD's budget is projected to fall by 1.6% in 2019/20 in real terms. Its Industrial Competitiveness programme, which centres on the Industrial Policy Action Plan, will have a R1 billion budget, a drop of 4% in real terms, while its Customised Sector Programme budget will be slightly higher, for a gain of just under 1%.

Table 1. Department of Trade and Industry budget

Programme	% change	Constant 2018 R bns. (a)	
		2018/19	2019/20
1. Administration	-8.8%	0.8	0.8
2. International Trade and Economic Development	-0.7%	0.1	0.1
3. Special Economic Zones and Economic Transformation	11.4%	0.1	0.2
4. Industrial Development	-1.6%	2.0	2.0
5. Consumer and Corporate Regulation	-5.5%	0.3	0.3
6. Incentive Development and Administration	2.9%	5.6	5.7
7. Trade and Investment South Africa	1.7%	0.4	0.4
8. Investment South Africa	-34.2%	0.1	0.1
Total	*0.3%*	*9.5*	*9.6*

Note: Deflated with Treasury projected CPI for 2019/20. Source: National treasury, Budget Review, 2019, Vote 34, Trade and Industry.

The Jobs Summit and the State of the Nation Address both point to the importance of government measures to promote industrial deepening, economic diversification and broader ownership as the basis for inclusive growth and the creation of decent work. These aims require both direct spending to incentivise innovative producers and indirect support through improved education and training as well as infrastructure, in addition to conducive macroeconomic policies. The shrinkage in fiscal space since the commodity boom ended makes alignment of all government strategies and decisions in support of industrialisation increasingly critical for achieving sustained inclusive growth.