

# The Effectiveness of Governance Through Fiscal Policy Management in South Africa

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**ABSTRACT:** Fiscal Policy is an important instrument for managerial decision-making. Many countries in Africa have adopted this policy to ignite socio-economic development. In South Africa (SA), several fiscal policy strategies have been adopted and implemented since the country's transition to democracy in 1994 with the aim of stimulating economic growth. Fiscal Policy is the utmost significant tool of economic management that is used by government to achieve the growth of economic activities. It is a vital measure of economic policy that achieves the foremost objective of managing economic growth, accomplishing complete employment, preserving the stability of price, settlement of economic balance and attaining societal integrity. The objective of this paper revealed a positive relationship between fiscal policy and managerial decision making in South Africa. In addition, the findings suggests that government spending has proven unsustainable, and continued spending on some of these policies may exacerbate the country's economic situation, given the fact that its expenditure is largely dependent on income tax. Based on the findings, this paper recommends that, for the SA economy to perform better, resources should be diverted from government consumption (thereby reducing funding for some of the current fiscal policies) to investment spending (e.g., job creation, poverty alleviation and promotion of long-term economic growth through infrastructure development).

**Keywords:** South Africa, Socio economic development, Fiscal policy, Managerial decision making

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## 1. Introduction and Background

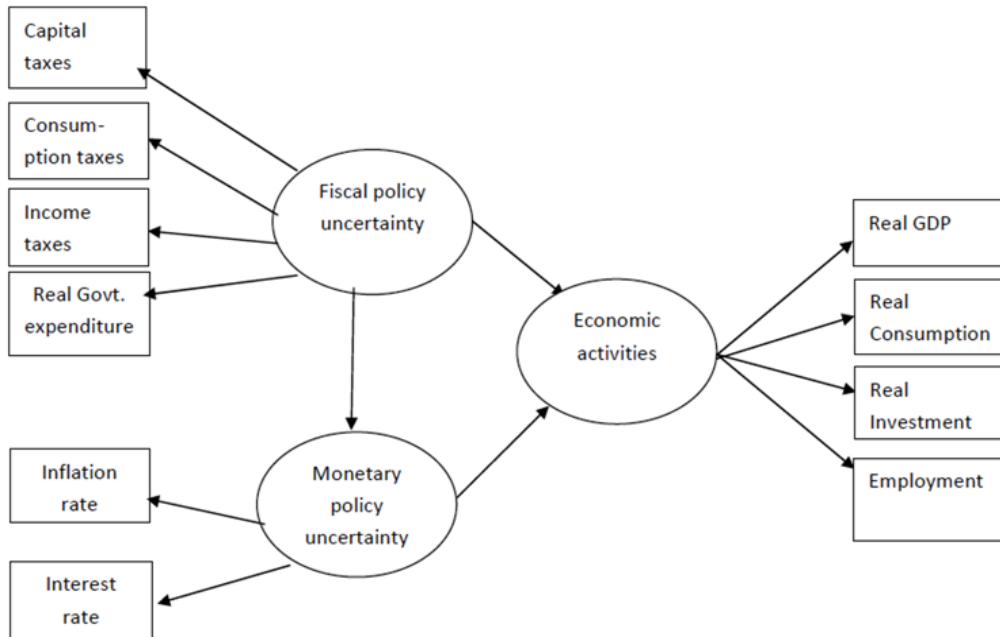
Globally, fiscal policy continues to serve as an important tool for achieving government broad economic objectives. The way a government responds to its debt positions influences economic stability, which in turn influences public debt patterns. Given most emerging economies and persistent increases in government expenditure positions, fiscal sustainability analysis is crucial to maintaining macroeconomic stability (Budina & van Wijnbergen, 2007). Kim et al. (2021) asserted that fiscal sustainability is the cornerstone of macroeconomic stability at the macroeconomic level. This is also crucial for economic growth since a country with a significant deficit is more likely to face macroeconomic instability, which may inhibit private investment.

According to Giammarioli et al. (2007), there are several methods to evaluate the fiscal sustainability of a country. The extensively applied strategy entails determining whether the government acts in accordance with the present value borrowing constraint (Schick, 2005). Thus, a government is said to be fiscally sustainable if the present value of future revenue flows is greater than the amount outstanding. SouthAfrica fiscal policy position, like that of many other developing countries, reflects how the government planned to adjust its monetary obligation. As a result, the government attempts to influence the economy trajectory through manipulating taxes and spending by adopting expansionary fiscal policy position (Abdulla, Mustafa & Dahalan, 2012).

Because of the adoption of expansionary fiscal policy as a recovery and consolidation strategy, government expenditure in South Africa is divided into two categories: government investment spending and government consumption spending (Tendengu, Kapingura & Tsegaye, 2022). Given the country persistently rising unemployment, poverty, and income distribution inequities, the role of fiscal policy in stabilising the South African economy and ensuring its sustainability is a major concern.

## 2. Review of the Related Literature

South African economy is controlled by the Monetary and Fiscal policies. We could not escape to also explain what monetary and fiscal policies are. To apprehend better we will explain the two policies. According to Omitogun and Ayinla (2007) Monetary policy is generally administered by a central bank and handles interest rates and the supply of money in circulation. Whereas Fiscal policy concerns taxation and government spending and is often determined by government legislation (See in figure 1 below). The main purpose of this assignment is to have a better understanding of Fiscal policy - a tool for managerial decision-making in South Africa. Therefore, so we are there to interrogate the relevant literature that underpins how this policy functions.



**Figure 1: Fiscal policy and Monetary policy diagram**

Ocran (2011) infers that Fiscal policy is related to the government's authority to review the government spending by reducing its size of , income as well as borrowings in order to achieve some macroeconomic goals . In addition to that, the primary goal of fiscal policy is to stabilise the government debt-to-GDP ratio by lowering the budget deficit. Furthermore, Fiscal policy tries to promote economic and social development by enacting sensible macroeconomic policies that establish a balance between government revenues, expenditure, and borrowing to achieve long-term economic growth (Ocran, 2011:604-618). To understand better Fiscal policy is generally used by policymakers in conjunction with monetary policy to ensure balanced and sustainable economic growth. This policy is the most important macroeconomic stabilisation tool at the disposal of government and policymakers to influence economic activities in the country through public revenues, according to the National Treasury (2017).

Fiscal policy and economic growth are two major issues that have been studied theoretically and empirically. Several authors sought to link these traits using theories such as the Solow growth theory, the Classical, Keynesian, and Neo-classical theories. Omitogun and Ayinla (2007) claimed, based on differences in some of these perspectives, that the Classical school argues that government debt has little effect on private sector savings in general. A government deficit funded by debt, according to this argument, discourages private-sector investment. Notable, Fiscal policy is thus viewed as a tool for overcoming economic swings. Similarly, the Neoclassical school of thought maintained that the manner in which fiscal deficits are funded had the potential to alter the amount of consumption, investment, and economic growth.

Keynes (1949) established the Keynesian theory of economic development, which called for the government to influence economic growth through changes in public spending and taxes. According to the Keynesian (1949) law, government expenditure is the fundamental engine of economic development because of its expansionary and contracting impacts on aggregate demand.

Expansionary policies are implemented when the government raises spending or lowers taxes to stimulate aggregate demand. Expansionary processes result in increased output, employment creation, and, as a result, economic growth. On the other hand, contracting measures are implemented when the government reduces spending or raises taxes in order to slow the economy (Blanchard, 2010:53-71). Wagner (1890), in contrast to Keynes (1949), believes that economic growth is a key factor that drives fiscal policy. According to Ismal (2011), improving economic activities should be at the forefront of economic development policy if growth is demonstrated to be a deterministic component of government expenditure.

Significantly, evaluating both Keynes' and Wagner's theories is essential for describing the key agents of economic development to plan proper economic policy. This assignment uses the theoretical rationale offered

by Keynesians (1949) and Wagner (1890) for the law of economic development as a tool for managerial decision-making in South Africa. However, for the purpose of this assignment these theories were deemed relevant in marking strategic decision as a managerial decision-making in South Africa by utilising fiscal policy.

### **3. Discussions**

#### **Fiscal policy to reduce poverty and inequality in South Africa**

Fiscal policy is widely seen as a vital policy instrument to ensure fair income distribution. Fiscal policy in the form of taxation and social spending influences the welfare of household members through monetary payment by way of taxes and transfers as well as through the provision of in-kind social benefits, including expenditure on free education and health care uptake (Gupta 2018).

South Africa has the world's most progressive tax systems in the world (Ehrenfreund, 2017). The income tax significantly reduces market income inequality by flattening the incomes of the wealthy and allowing the funding of social protection tools such as the welfare system and free basic services. Income tax is the government's largest tax instrument, and its share of tax revenue has increased over the past decade. Measured as a percentage of income, however, it has become less progressive over time, despite tariff increases. While income tax levels have risen, market incomes have risen more, particularly in the top decile (Goldman M & Woolard I 2022)

According to SASSA Annual Performance plan (2022- 2023) approximately 31% (more than 18 million grants) of South Africa's population depends on the social assistance programme to meet their basic needs. Furthermore, the implementation of the COVID-19 SRD special grant of R350 supports an average of 10 million citizens monthly, this, increases the number of people relying on social transfers to about 47% of the total population. This increases the number of citizens who rely on social transfers to more than 28 million which equates to about 47% of the population. This translates to R199 189 billion paid to social grants in 2021.

The Personal Income Tax (PIT) offers an opportunity to increase tax collection and reduce inequality while minimizing the increase in poverty. It therefore seems reasonable that a high inequality country such as South Africa would be relatively more dependent on an income tax than other less progressive taxes such as Value Added Tax (VAT). On the other hand, if taxing the wealthy is perceived as unfair, illegitimate, or too onerous, wealthy individuals may choose to go elsewhere with two potentially negative consequences: reduced tax revenue to fund services supplied to the rest of the population, and reduced economic growth – when these people take their companies and possibly jobs with them (Goldman M & Woolard I 2022).

National Treasury budget review (2023) states that the total consolidated government spending will amount to R7.08 trillion over the next three years, of which 51 per cent or R3.6 trillion is allocated for the social wage. Based on this information, it is clear that many people in South Africa rely on the state for income for survival. This is of particular concern as there were only 6.3 million individual taxpayers in 2022. These 6.3 million individuals (representing approximately 10% of the population) contribute 40% of South Africa's total tax revenue. Another concern is that the decline in Personal Income Tax was the result of the weak economy, which has reduced companies' ability to grow, increase salaries and hire employees. The outlook for South Africa's economy is expected to remain subdued (GDP is expected to grow between 1.4% and 1.8% through 2023) and the unemployment rate is expected to remain at unsustainable levels, making this trend likely to continue.

### **4. Findings**

#### **Findings on Fiscal Policy to reduce poverty and Inequality in South Africa**

- High income taxes will result in lower levels of consumption and savings. These in turn translate into lower economic growth.
- South Africa is using its fiscal tools to effectively reduce market income poverty and inequality through a slightly progressive tax system and very progressive social spending, yet levels of inequality and poverty remain unacceptably high.
- The government's finances are already unsustainable, and continuing spending more on social grants will only make it worse for our economy.
- The tax base is simply not strong enough to carry it anymore.
- Continuing with spending more on social grant could deepen debt and hinder economic growth.

## 5. Recommendations

### Recommendations on Fiscal policy to reduce poverty and inequality in South Africa

- In the future, tackling the twin challenges of poverty and inequality in line with fiscal sustainability requires higher and more inclusive economic growth in support of fiscal policies. This would be particularly important to meet the need for jobs and higher incomes, particularly at the bottom of the income distribution, thereby helping to narrow the income gap between rich and poor and making fiscal policies more effective.
- Innovative approaches are needed to help South Africa avoid a fiscal trap that entails a downward spiral of mutually reinforcing economic stagnation, low revenues, and spending cuts. At the same time, South Africa must make people's needs, the promotion of equality and the realization of rights central fiscal goals. This is not a choice but a constitutional obligation.

## 6. Conclusions

In conclusion, we have established that the tax burden is impacting more on individuals with low income even though they are in the lower tax brackets the effects of inflation are hitting. The government has come up with solutions such as the grant, but they have not assisted in the alleviation of poverty as the cost of living has drastically risen. It is, therefore, the reason we have mentioned in our recommendation that we have stated that the reduction of load shedding or elimination thereof will be beneficial to the South African economy as job losses will be minimised and businesses will thrive, and this will in return assist the economy by being able to collect more tax.

## Acknowledgements

The following are my MBA students who contributed in the discussions and policy debates for the paper. The proceeds is now been edited by me for submission and presentation in this conference.

Rudzani Comfort Monyayi, Lungisani Xolani Khumalo, Mashudu Ramunenyiwa, Veronica Matshediso Mahlaku and Kgomalla Joel Petje

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