Hoping for a great escape

By Craig Pheiffer

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Legendary escapologist Harry Houdini began his career escaping from handcuffs but later went on to dazzle audiences with escapes from large milk cans, his specially designed Chinese water torture cell and buried caskets. The difficulty of the escapes was often ratcheted up by binding the escape vessels with chains and locks and restricting Houdini's movements with a straight jacket.


Craig Pheiffer, chief investment strategist at Absa Stockbrokers and Portfolio Management

Finance Minister Tito Mboweni faces a similar challenge when he presents the National Budget on 20 February. For Mboweni to effect a successful “escape” on Wednesday, he will need to show something of a return to the path of fiscal consolidation – budget speak for smaller budget deficits going forward – while at the same time solving for the pressing financial demands of Eskom and the other state-owned enterprises.

The taxing question

A difficult task, as the National Treasury has notched up over a decade of budget deficits, and the debt issuance to fund that overspend has grown substantially. The servicing cost of that debt is growing at the fastest pace of any item in the budget. The economy has also just recovered from a short recession and limped to a very likely sub-one percent growth rate in 2018. Tax revenues have consequently been under pressure even after a VAT rate increase last year and a personal income tax (PIT) bracket adjustment that didn’t fully account for fiscal drag. A higher tax bracket at 45% was also introduced and taxpayers are at that point where they are pondering whether working is worth the effort at all or whether working on other shores might be that much more beneficial.

South Africa’s corporate income tax (CIT) rate of 28% is among the highest globally and there is no room to increase that rate to generate higher tax revenue. The bottom line is that for the collective 80% of the country’s tax revenue that is generated by VAT, CIT and PIT, there is little room to tap the tax base that much further. It’s also questionable whether an incumbent government would hike taxes just two months ahead of a national election.

Ties that bind

Keeping expenditure within budget is a further challenge for a country that battles high unemployment and poverty levels and income inequality, and that has a high demand for basic health, education and security services. Government is currently paying out social grants to 17,5-million people and additionally has to find funding for the state-owned companies such as Eskom that will keep the lights on and give us a better chance of growing the economy and, by extension, tax revenues. These are the ties that bind.

Little room to manoeuvre

The only wiggle room for Mboweni on the revenue side is from the usual increases in sin taxes and the fuel levy. Hiking the capital gains tax inclusion rate or dividend withholding tax or holding back on increasing interest exemption thresholds is something that the minister might consider to help move an extra inch. Maintaining the expenditure ceiling and accommodating the demands of Eskom in particular remain fiercely constricting. The National Treasury has the ability to engage in more switch auctions where it swops out bonds with looming maturities for longer-dated bonds, reducing the immediate funding need (expenditure) and giving the minister more room to manoeuvre.

Facing an apparently impossible task, the success of the minister will be measured by the cheer (or not) of the currency and the markets. No visible commitment to fiscal consolidation or an accommodation of Eskom that balloons the deficit will be viewed in a poor light by the ratings agencies and the markets. The jeer from the rand, the local economy stocks and the bond market will be deafening. A smart and credible escape in front of the curtain and without smoke and mirrors would inspire rapturous applause from every quarter.

It's a very tough ask, but Houdini made a career out of escaping from tight places. Please take your seats, the show is about to begin.

ABOUT THE AUTHOR

Craig Pheiffer is the chief investment strategist at Absa Stockbrokers and Portfolio Management