



FISCAL TRANSFERS AND OWN REVENUE IN FUNDING RURAL DEVELOPMENT MANDATES

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For an Equitable Sharing of National Revenue

OUTLINE

- Role and Function of the FFC
- The significance of rural development
- The role of provinces in rural development
- Funding instruments for rural development
 - Own revenue
 - Provincial Equitable Share
 - Conditional Grants
- Challenges and opportunities for rural development
- Other fiscal policy related chapters: 4, 5, 7, 8 & 9
- Selected FFC recommendations

FFC SUBMISSION THEMATIC FOCUS

- The Thematic focus of FFC 2017/18 submission for Division of Revenue (DoR) is IGFR and Rural Development
- The Submission comprises of 11 chapters
 - Rural development & IGFR relations
 - Economic model for rural development
 - Targeted IGR transfers and rural poverty reduction
 - Land reform and rural development
 - Role of public entities in rural development
 - Fiscal transfers and own revenue in funding provincial rural development mandates
 - Fiscal instruments to fund public employment programs in rural areas
 - Financing rural local municipalities
 - Effectiveness of transfers local and district municipalities for rural development
 - Farm eviction in rural local municipalities
 - Sanitation fiscal instruments and governance to enhance rural development

DEFINITION OF RURAL

- South Africa does not have an officially accepted definition of “rural”
- FFC has adopted a broader administrative definition that combines spatial, sectoral and density factors
- Limpopo province is the most rural province according to FFC classification

	% share of B3 & B4 municipalities	% share of B4 municipalities	Composite Average	Rural Ranking
Eastern Cape	87%	38%	63%	3
Free State	75%	0%	38%	7
Gauteng	8%	0%	4%	9
KwaZulu Natal	79%	54%	66%	2
Limpopo	92%	64%	78%	1
Mpumalanga	67%	28%	47%	6
Northern Cape	92%	4%	48%	5
North West	74%	26%	50%	4
Western Cape	60%	0%	30%	8

RURAL DEVELOPMENT IS MORE THAN AGRICULTURE

- The rural economy is no longer just a farm economy
 - The role of agriculture as engine of growth within rural provinces is declining
- Rural development has evolved over time to focus on space based interventions and diversified economic activities
 - Growth in agriculture output has poverty reducing effects but non-farm sectors are more powerful tool for reducing poverty headcount
- A multi sectoral policy approach is needed to attain rural development objectives

WHY (WHAT IS) RURAL DEVELOPMENT?

- Rural spaces carry the heaviest burden of spatial inequality – poverty, unemployment etc.
- Rural economic development is about improving the general wellbeing of rural people and spaces.
- Strategies to promote rural economic development include:
 - Provision/facilitation of income earning opportunities
 - Provision of quality education and health care
 - Investment in social and economic infrastructure
 - Provision of basic services
 - Protection of the rural environment

ROLE OF PROVINCES IN RURAL ECONOMIC DEVELOPMENT

- Most functions of provinces constitute aspects of rural economic development
 - Education – increase abilities for employment and mobility
 - Health – reduce disease burden & improves productivity
 - Roads – increase mobility & access to markets
 - Housing – facilitate access to economic assets
 - Agriculture – improves food security & income earning opportunities
 - Regional planning and development
 - Environmental protection – reduce households vulnerability to environmental degradation

PROVINCIAL RURAL DISPARITIES

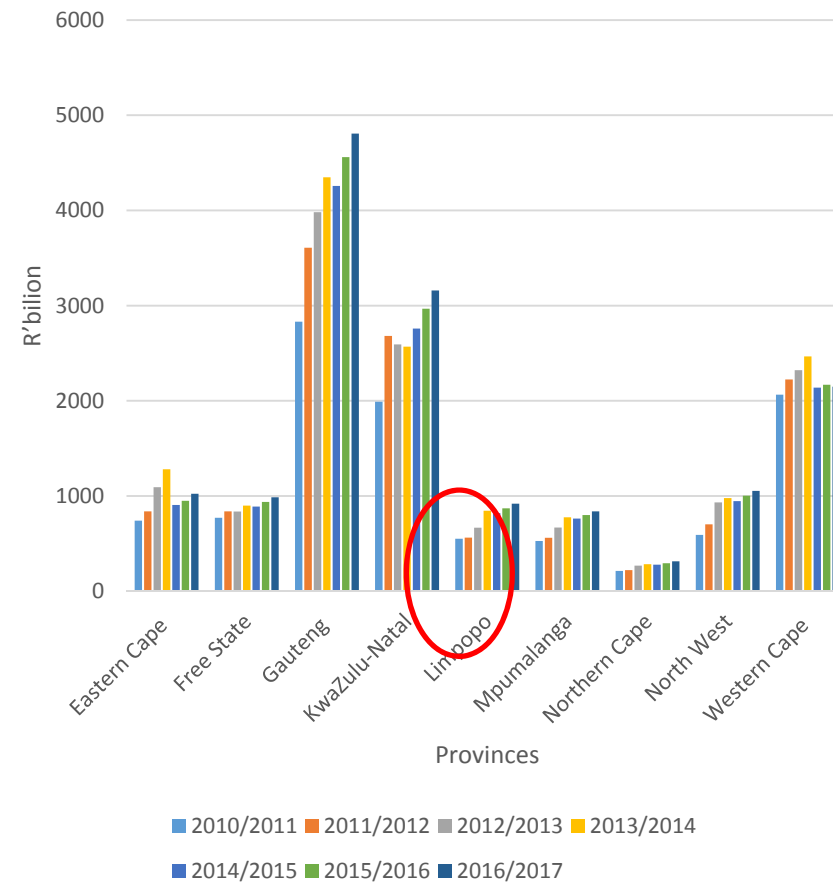
- Rurality is dynamic; there are no specific rural characteristic peculiar to rural province
 - High incidence of poverty and agriculture dominance in Gauteng
 - Per capita expenditure is higher in rural provinces
- Rural dynamism have implications for horizontal division of revenue given the need for transfers to be equitable

FUNDING INSTRUMENTS FOR RURAL DEVELOPMENT

- Provinces rely on PES, conditional grants and own revenue to fund rural development
- National transfers account for 97% of revenue
 - For Limpopo it is 98%
- Conditional grants account for 18% of total revenue
 - 13% in Limpopo
- Fiscal transfers must account for provincial disparities in the allocation and spending framework
- EFC investigated whether fiscal transfers are sensitive to the needs of rural provinces

OWN REVENUE MOBILISATION FOR RURAL DEVELOPMENT

- Rural provinces optimise revenue collection on existing sources, but further growth is constrained by weak economic base
- Notwithstanding, higher revenue optimisation rural provinces cannot implement their rural mandates without fiscal transfers



HOW DOES PES ACCOUNT FOR PROVINCIAL DISPARITIES?

- The PES is allocated through a formula that accounts for varying service needs
 - *Education share (48%)* based on size of school age population (ages 5 – 17) and the number of learners (Grade R to 12) enrolled in public ordinary schools
 - *Health share (27%)* based on risk-adjusted capitation and caseloads at hospitals
 - *Basic share (16%)* derived from each province's share of the national population
 - *Poverty component (3 %)* reinforcing the redistributive bias of the formula and based on each province's share of the poorest 40 % of the population
 - *Economic output component (1%)* based on GDP-R per region
 - *Institutional component (6%)* divided equally between the provinces
- Need indicators are not necessarily biased to rural provinces

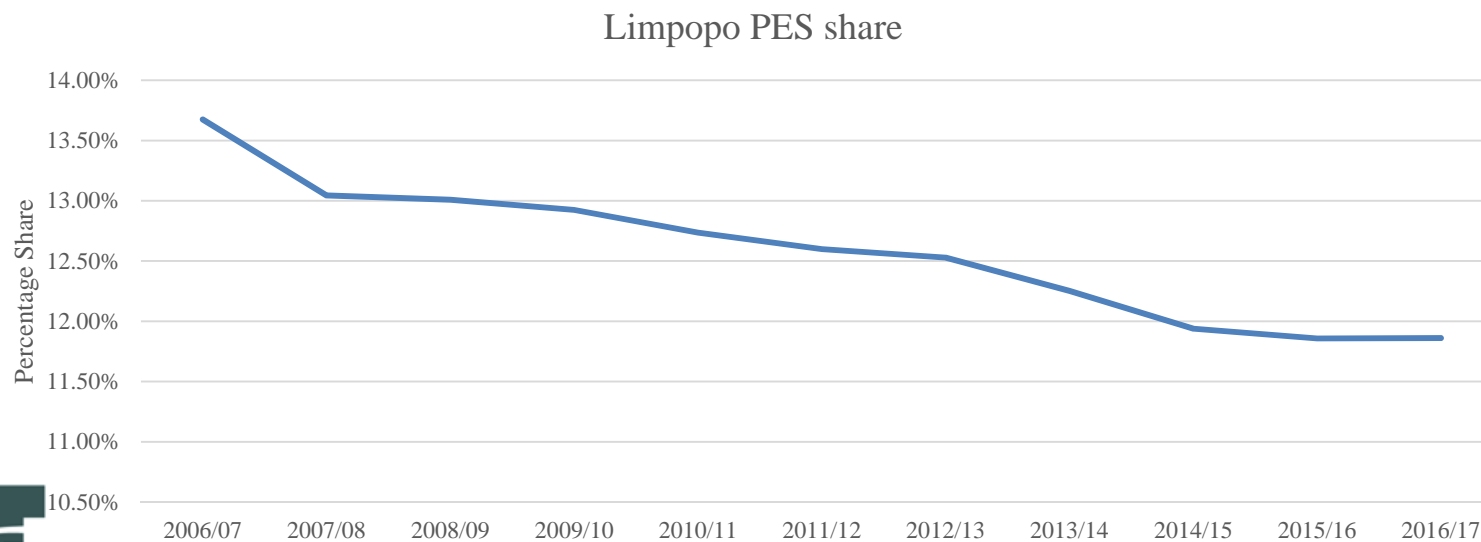
IS THERE A RURAL BIAS IN THE PES FORMULA?

- Rural provinces receive the highest per capita PES allocation
- In the long-run PES makes no discernible variation in provincial allocations to respond to the rural needs

<i>Until 2005</i>	<i>SS</i>	<i>df</i>	<i>MS</i>	<i>F</i>	<i>P-value</i>	<i>F crit</i>
Between Groups	4187334.711	8	523416.8	1.540963	0.177768	2.208518
Within Groups	12228070.8	36	339668.6			
<i>Until 2006</i>	<i>SS</i>	<i>df</i>	<i>MS</i>	<i>F</i>	<i>P-value</i>	<i>F crit</i>
Between Groups	5212226.918	8	651528.4	2.353451	0.033065	2.152133
Within Groups	12457779.15	45	276839.5			
<i>2006 onwards</i>	<i>SS</i>	<i>df</i>	<i>MS</i>	<i>F</i>	<i>P-value</i>	<i>F crit</i>
Between Groups	29238931.44	8	3654866	2.70968	0.013856	2.115223
Within Groups	72836200.03	54	1348819			
<i>From 2000 - 2013</i>	<i>SS</i>	<i>df</i>	<i>MS</i>	<i>F</i>	<i>P-value</i>	<i>F crit</i>
Between Groups	28044927.47	8	3505616	1.839764	0.077335	2.025247
Within Groups	205790803.5	108	1905470			

LIMPOPO PES SHARE TRAJECTORY

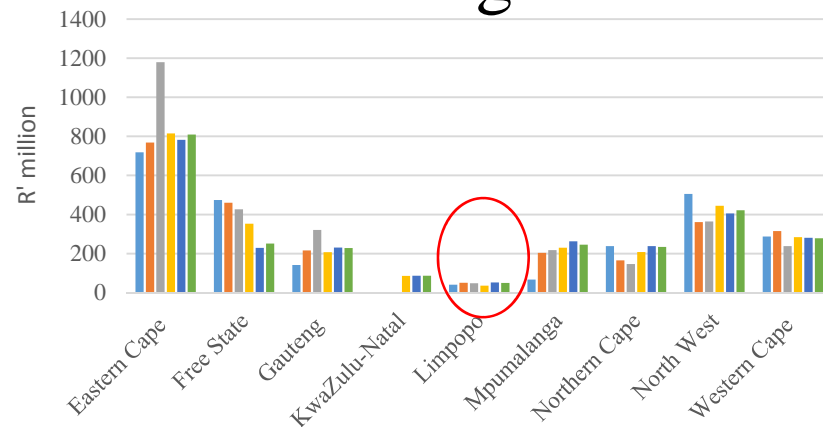
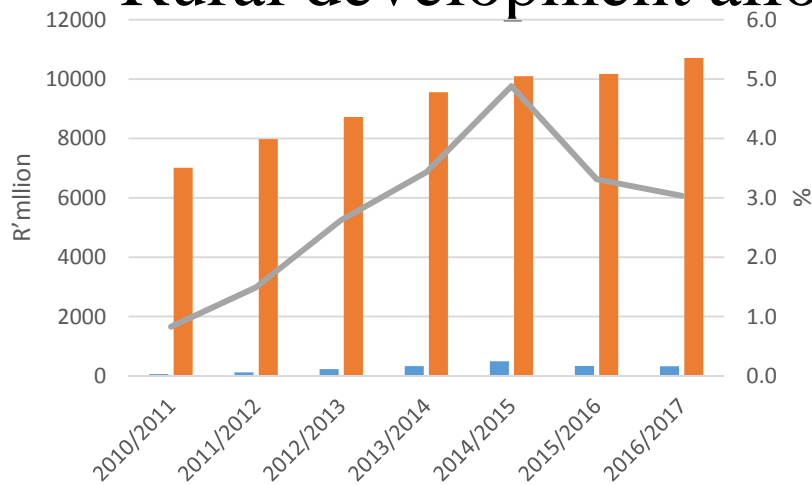
- Limpopo's share of the PES is declining gradually
 - Allocations are increasing in absolute terms
- The decline is attributed to out migration and review of components need indicators



DE-PRIORITISATION OF RURAL DEVELOPMENT IN PROVINCIAL BUDGETS

- On average rural provinces spends 4% of PES for rural development (using agriculture allocation as proxy)

- Rural development allocations are declining



RESPONSIVENESS OF CONDITIONAL GRANTS TO RURAL DEVELOPMENT

- Rural provinces are the main beneficiaries of conditional grants
 - Over 50% of key infrastructure conditional grant are allocated to the three rural provinces

Province	Provincial Infrastructure Grant (10 yrs. average)	Health facility Revitalisation (15 yrs. Average)	Education infrastructure Grant (4 yrs. Average)
Eastern Cape	17%	16%	21%
Free State	8%	5%	4%
Gauteng	14%	25%	17%
KwaZulu-Natal	20%	16%	22%
Limpopo	15%	14%	20%
Mpumalanga	7%	5%	5%
Northern Cape	5%	6%	3%
North-West	8%	6%	4%
Western Cape	6%	7%	5%

ALIGNMENT OF CONDITIONAL GRANTS TO RURAL DEVELOPMENT GOALS

- Rural development programs are agrarian in focus – but agriculture is less prominent in rural provinces.
- The allocation framework for agriculture grants are misaligned to the policy objectives
 - Northern Cape receives the largest share of agriculture grants despite contributing the least to agriculture output
- Indirect conditional grants targeted at specific rural needs are under performing
 - School Backlogs Infrastructure Grant and the Rural Household Infrastructure Grant

CHALLENGES FOR RURAL ECONOMIC DEVELOPMENT

- Absence of clear separation of responsibilities on rural development mandates across spheres creates ambiguities and duplications
- Provinces do not perceive investment in education and health as rural development activity
 - Outcomes are not physically confined to rural spaces
- Rural development is seen as the preserve of departments of agriculture and rural development
- Government service delivery and budgeting approach lack spatial focus (& rural community involvement)

OPPORTUNITIES & LESSONS FOR RURAL ECONOMIC DEVELOPMENT

- Investment in education and health improves urban-rural linkages
- Investing in rural roads foster functional and economic linkages with urban centres
- Rural development interventions must be locally driven
- Office of the Premiers can facilitate spatial targeting of rural interventions through coordinating departments responsible for rural development

LAND REFORM AND RURAL DEVELOPMENT

- Land reform policy is predominantly agrarian
 - Limited provision made for alternative land use
- Land reform program is beset by policy tensions and funding challenges
- The program have limited impact on food security and productivity
- There is need for coordination between DAFF and DRDLR and consolidation of agriculture grant to strengthen implementation



OTHER FISCAL POLICY RELATED MATTERS

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PUBLIC ENTITIES AND RURAL DEVELOPMENT

- State Owned Companies account for 20% of gross national capital formation and plays important role in regional development
- Investments By SOCs in rural areas are small and declining
- Some of the SOCs including DBSA, Land Bank and National Empowerment Fund have funding programs directed at rural areas
- SOCs could benefit from a guideline indicating what their role should be in furthering the rural development agenda

FISCAL INSTRUMENTS TO FUND PUBLIC EMPLOYMENT PROGRAMS IN RURAL AREAS

- Most of the Public Employment Programs do not have an explicit rural focus
 - EPWP are centred in metro areas while CWP have a rural focus
- Most schemes have onerous compliance requirements
- The scheme lacks multi sectoral approach; mainly focuses on infrastructure
- Labour market outcomes associated with the scheme are poor
- Need for proper targeting of schemes to address rural poverty and reduce double dipping.

FINANCING RURAL MUNICIPALITIES FOR RURAL DEVELOPMENT

- A number of rural municipalities are not self sufficient
 - 80% of municipalities are at risk dysfunctionality
- Amalgamation is seen as solution to reduce dependency on grant funding
- The Local Government Equitable share and conditional grants adequately compensate rural municipalities for lack of own revenue
- Transfers should remain the key source of funding rural municipalities

EFFECTIVENESS OF TRANSFERS TO LOCAL AND DISTRICTS MUNICIPALITIES FOR RURAL DEVELOPMENT

- Rural municipalities are less efficient than District municipalities at providing basic services
- Performance of local municipalities can increase by 60% without additional resources
- Districts are not performing their legislative functions to the full due to asymmetry in powers and functions
- Districts are more relevant and useful in rural areas than urban areas

RECOMMENDATIONS

- The provincial offices of the Premier in consultation with the provincial departments of education, health, agriculture and roads must identify the rural development needs and set annual delivery targets against which PES allocations will be assessed
- The National Treasury in collaboration with the departments of education, health and roads must ensure that the criteria for allocating infrastructure conditional grants takes into account spending efficiency, delivery targets and performance as well as the applicable national norms and standards on access to infrastructure
- The department of agriculture and national treasury must review the framework for allocating agriculture conditional grants to reduce the use of non-agriculture land size as an indicator of need and incorporate factors that are closely aligned to the objectives of the grant, in particular promotion of agriculture activity
- The department of Planning Monitoring and Evaluation must conduct a comprehensive review of expenditure outcomes associated with infrastructure conditional grants targeted at the rural provinces, to ascertain the extent to which infrastructure backlogs have been reduced and the efficacy of spend

RECOMMENDATIONS

- In order to ensure active community participation in setting rural development priorities, the provincial department health must ensure that clinics committee are functional and the provincial department of education must institutionalise community participation processes between school governing bodies and the education circuit and district offices during the planning and budgeting phase
 - Provinces must shift the role of coordinating rural development programs from provincial department of agriculture to the premiers' offices to ensure that all aspects of rural development are taken into account during planning. The office of the Premiers must ensure that rural redevelopment projects or initiatives carried by the National Department Land Reform and Rural development or any other department are subjected to the relevant community participation processes – to avoid duplications