CHAPTER 8

The Role of PES and Conditional Grants in Funding Provincial Rural Development Mandates

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8.1 Introduction

Throughout developing nations, intergovernmental fiscal transfers are the focus of much attention because of growing concerns over deeply entrenched regional development inequities. Historical and market-led patterns of development, resulting in the skewed distribution of economic activity, cause regional disparities that often require equalisation through fiscal transfers to offset the developmental gap. Regional disparities manifest in a number of ways and have a number of policy implications (Blochliger and Charbit, 2008). This chapter examines rural under-development, which is one of the key manifestation of disparities in South Africa.

South Africa is characterised by disparities across provincial jurisdictions. About a fifth of South Africans live in rural areas where population sizes and income levels are low and the unemployment rate is high (NPC, 2011). Rural populations are spatially dispersed, which increases the cost and difficulty of providing rural services effectively, resulting in extensive service backlogs. Similarly, rural areas have limited economic activities and a narrow tax base, which prevents them from mobilising sufficient resources to finance their own development programmes. This leaves them dependent on national government for both fiscal transfers and interventions. A number of policy documents have identified rural development as a crucial remedy for regional disparities, ranging from the spatial approach of investing in rural nodes contained in the Integrated Sustainable Rural Development Strategy (ISRDS) of 2000 to a service-delivery oriented Comprehensive Rural Development Programme (CRDP[39]) of 2009 (Mabugu, 2015).

The intergovernmental fiscal relations (IGFR) system is also designed to address regional disparities and in particular rural development. The Constitution assigns the multi-faceted rural development function across the three spheres of government. The responsibility for rural development permeates through the different spheres and sectors of government. Traditionally, provincial rural development responsibilities included regional planning, schooling and health facilities, housing, roads and agriculture. However, the Constitution makes no spatial distinction when assigning or classifying functions. It requires (in Section 214(2)) for economic disparities between and within provinces to be taken into account when determining their respective equitable share entitlements. Accordingly, the provincial equitable share (PES) and various conditional transfers allow for different aspects of rural development in both their allocation formulae and spending activities. For instance, the poverty component of the PES is intended to provide a rural bias in the allocation framework in the same way as grants do, e.g. the Rural Household Infrastructure Grant (RHIG) prioritises the provision of sanitation within rural communities.

The renewed emphasis on rural development, within the context of regional disparities, raises questions about the sources, composition and effectiveness of funding for rural development. Without a clear framework of provincial rural development functions and coordinated spending, the transformation of the rural landscape will remain an elusive ideal. Against this background, this chapter looks at how responsive the PES and conditional grants are to the needs of rural provinces, by assessing the extent to which the fiscal transfers respond to rural challenges. It examines the sensitivity of these transfers to the needs of the rural provinces, the effectiveness of the backlogs component of the infrastructure conditional grants in channelling resources towards rural provinces, and the rural development programmes funded through the PES and conditional grants.

The research objectives are:

- To assess the responsiveness of the provincial horizontal transfers (equitable share formula and selected provincial conditional grants) to the needs of rural provinces.
- To examine whether rural provinces experience peculiar developmental needs or challenges associated with their rural conditions.
- To assess the extent to which rural provinces prioritise rural development through discretionary and conditional allocations and identify constraints hampering the prioritisation of rural development.
- To make recommendations for the Commission's 2016/17 Annual Submission to the Division of Revenue

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[39] The CRDP is the Department of Rural Development and Land Reform's flagship policy that has two focus areas: (i) an integrated programme of land reform and agrarian change, and (ii) a rural development strategy, and is targeted at 27 districts. (See Chapter 3 for more details.)

8.1.1 Problem statement

In South Africa, rural provinces carry the highest poverty burden because of historical social engineering policies, weak regional economies, and the inability of provinces to effect change through development interventions and allocated resources. The higher poverty burden imposes additional demands for services and funding on the rural provinces. However, the funding framework for provinces is not sensitive enough to the different developmental needs and the inherent cost disabilities of rural provinces.

Maladministration practices and fiscal management failures provide evidence of the inability of the rural provinces to intervene in their spaces through the powers and functions assigned to them by the Constitution. Whereas such failures reflect poor fiscal choices, the lack of appropriate skills in the rural areas may exacerbate management inadequacies and thus reinforce rural under-development.

As provinces rely almost entirely on national transfers for revenue, their spending discretion (i.e. their ability to direct resources towards province-specific needs) is limited. The PES, which accounted for 78% of total provincial revenue in 2013/14, is normally tied to national priorities and statutory responsibilities. Similarly, conditional grants can only be spent on specific sector and expenditure activities. Of course, assuming national priorities match local preferences, provinces can invest within their space where the needs are greatest.

8.1.2 Methodology

The study employs a multi-pronged methodological approach. Firstly, a qualitative comparative analysis of the fiscal transfers is carried out, focused on the design and mechanism for addressing spatial disabilities. Secondly, a quantitative analysis of the PES formula and allocation is undertaken that looks specifically at the composition of components and need indicators, and per capita allocation per province. A panel data analysis is used to assess the degree of variance in per capita allocation per province. The results are corroborated by an in-depth budget review of the two biggest provincial conditional grants and selected conditional grants with a rural focus, to help establish the extent of rural development prioritisation within the different provinces.

8.1.3 Linkages to the Division of Revenue theme

The Division of Revenue is underpinned by the principles of equitable distribution of resources to minimise the fiscal gap across jurisdictions. The allocation criteria for both the PES and conditional grants include the principles of equitable distribution of resources. However, the extent of the equity is a subject of ongoing debates, as the IGFR system evolves and the different interests advocate for a fair share. South Africa has a unique duo spatial characteristic, where under-developed rural regions coexist alongside affluent urban centres, and so the varying needs of these two spaces have to be reflected in the allocation framework. The consensus among policy-makers is that rural spaces have structural inabilities that require a separate funding instrument or approach. This study seeks to provide answers to the ongoing impasse regarding the effectiveness of fiscal transfers in addressing rural development.

8.2 Addressing Regional Disparities through Fiscal Transfers

Development disparities between and within regions are a global phenomenon, found mostly in low-to-middle income countries, and emanate from skewed factor endowment and economic activity distribution, and deliberate government policies to promote one region ahead of the others. To reduce regional economic and social disparities, countries have adopted regional policies to develop activities in the rural sector. They include policies that emphasise economic growth as a remedy to reducing inequities, direct national government interventions through social services and infrastructure, and the decentralisation of expenditure responsibilities to subnational governments (Kirori, 2015 and Fan et al., 2009).

Many countries have embraced fiscal decentralisation as a fundamental policy for rural development, despite concerns of adverse redistributive effects. For instance, Kenya has created a number of decentralised structures (local authorities and regional development authorities) and institutional interventions for developing rural areas, such as the Special Rural Development Programme and the District Focus Strategy for Rural Development. Districts or regional development authorities are responsible for planning, financing and implementing rural development initiatives. These development programmes cover rural access roads, basic education, water, agriculture support, employment and development finance. However, the regional development authorities lack independent budgets to drive development and the powers to coordinate plans and budgets of national ministries on a district-by-district basis, and rely on budgetary allocations and appropriated aid for revenue (Kirori, 2015).

Kenya's approach to rural development resembles that of India where District Rural Development Agencies (DRDAs) are responsible for coordinating, supporting and facilitating rural development programmes designed by the Ministry of Rural Development. Like Kenya, India's programmes are multi-dimensional, entailing poverty reduction, rural employment, housing, roads and improving agricultural productivity, etc. The DRDAs implement central and state government schemes because they lack the legal status of a government tier. Similarly, municipalities are not autonomous institutions of local self-government but are mostly assigned the responsibility to implement national or state (provincial) projects.

Between the early 1990s and the mid-2000s, Brazil's rural development model evolved immensely, from an agrarian focus to a welfare orientation, to the current integrated approach aimed at ending poverty and inequality through intergovernmental interventions. Much of Brazil's success in addressing rural under-development is attributable to the two national welfare-type programmes that have since been decentralised to local municipalities: the Bolsa Familia – a conditional cash transfer scheme – and the School Meals Programme (Schneider et al., 2010). In Brazil, municipalities are also responsible for health and education, which constitute an important part of development. Each municipality receives the Municipal Participation Fund (MPF) whose allocation criteria take into account population size and production capacity. This means that, generally, municipalities with smaller populations receive higher per capita allocations. The transfer allocation framework does not distinguish between rural and non-rural municipalities. A recent study showed that socio-demographic characteristics, such as the human development index and Gini coefficient, "do not help to understand most of the fiscal inequality found across municipalities". Therefore, they are unlikely to bring about fiscal equalisation when incorporated into the transfer system (Politi and Mattos, 2013: 15).

8.3 Rurality and Provinces

Efforts to classify territories according to their degree of rurality – for policy purposes – have not been entirely successful. The anomalies that characterise rural spaces are acknowledged, but the factors that cause such anomalies cannot conclusively determine whether or not a space is rural. Some factors may be inherent to rural space, while others are only associated with the space. In the absence of a universal definition of rurality, policy-makers need to adopt a working definition of rurality suited to the policy goals being pursued (Du Plessis et al., 2002). This is because different definitions generate different outcomes (see Table 49).

Rurality's distinctive characteristics include a small population size, sparse settlements (low densities), distance from large population concentration areas and reliance on agriculture for economic activity (Monk, 2007). Other attributes, which are not limited to but are generally closely associated with rural spaces, include higher levels of poverty and aging and unemployed people, low transportation connectivity and lack of access to basic amenities (i.e. education and health facilities, water, electricity and sanitation). Chapter 11 provides a detailed discussion on rural sanitation.

This study explores three methods of categorising provinces as rural:

- Provinces that include former Bantustans – territories set aside for black people under apartheid in South Africa – and characterised by sparse settlements, extensive land under traditional leadership and high levels of under-development (Khunou, 2009). Bantustans were mainly concentrated in KwaZulu-Natal, the Eastern Cape, Limpopo, North West and parts of the Free State. To this day, provinces into which Bantustans were assimilated continue to be associated with poor socio-economic conditions and high levels of rurality (UNDP, 2014).
- Provinces that have the most B3 and B4 municipalities based on a composite index (see Chapter 1 for a description of this method). According to this index the three most rural provinces are Limpopo, KwaZulu-Natal, and the Eastern Cape.
- Provinces that have certain rural attributes. This chapter categorises provinces using a combination of factors that are inherently and indirectly associated with rural spaces. They include sparsity, demographics, socio-economic attributes, access to services and connectivity using proxy variables. Provinces are assigned a score of one to nine for each variable, where one represents a low and nine a high degree of rurality.

Table 49 show the results of this third classification. Gauteng and North West have the lowest, and the Northern Cape and Western Cape the highest rurality score. However, these results are inconsistent with the other two methods of classifying provinces by rurality. What Table 49 shows is that rurality is dynamic. No specific rural characteristics are peculiar to a provincial territory. For instance, of all nine provinces, Gauteng has the highest degree of rurality for aging and reliance on agriculture, whereas provinces traditionally regarded as rural (former Bantustans) fare relatively better in terms of access to amenities and connectivity. These results may have implications for the design and division of the fiscal transfer system across provinces and the prioritisation of funding to address different rural development needs.

Table 49. Classification of provinces by rural attributes

	Density	Rank score	Population >60yrs	Rank score	Poverty headcount	Rank score	Number of clinics/ 1600 m²	Rank score	Number of schools/ 1600 m²	Rank score	Agriculture output/ 5000 m²	Rank score	Road KM/200 m²	Rank score	Total rank score
Eastern Cape	40	6	772 787	7	2051837	7	7	3	53	3	138 584	2	38,11361337	5	33
Free State	22	8	279 496	2	665691	2	3	7	16	8	318 542	5	42,51765281	3	35
Gauteng	720	1	1 116 021	9	2238403	8	28	1	181	1	1 465 196	9	58,6847966	1	30
KwaZulu-Natal	113	2	933 083	8	3179382	9	10	2	102	2	1 185 957	8	45,37697953	2	33
Limpopo	44	5	516 596	5	1676781	6	6	4	50	4	256 345	3	34,96444051	7	34
Mpumalanga	56	3	344 977	3	1088648	5	5	5	37	5	522 449	6	36,11345905	6	33
North West	35	7	119 501	1	222647	1	1	9	2	9	72 690	1	39,04205353	4	32
Nothern Cape	3	9	349 547	4	881407	4	4	6	24	6	261 835	4	13,79078074	9	42
Western Cape	47	4	590 971	6	861974	3	3	8	18	7	726 314	7	25,17869079	8	43
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Sources: Regional Explorer, Department of Education 2013; HST, 2013

8.3.1 Provincial disparities in South Africa

The disparities across the nine provinces of South Africa are examined through the per capita gross regional product (GRP), the percentage of population living below the poverty line and the per capita expenditure. Table 50 shows significant variations in the per capita GRP and poverty. For instance, Gauteng's per capita GRP is almost twice that of rural provinces. Similarly, compared to other provinces, poverty levels are higher in the three most rural provinces (the Eastern Cape, KwaZulu-Natal and Limpopo). However, when observed over a long period, these disparities across provinces dissipate, implying some level of convergence in their development trajectory. This convergence is also evident through provincial per capita expenditure. Overall, these results suggest that there is little evidence to corroborate the existence of disparities between provinces in South Africa, which makes the targeting of resources to selected provinces for rural development unjustifiable.

Table 50. Provincial development disparities

Province	GRP per capita Rands	% population below food poverty line	Population aged 15+, completed grade 7	Expenditure per capita Rands
Eastern Cape	34 140	29.1%	76.9%	9 157
Free State	56 869	22.3%	82.1%	10 279
Gauteng	80 534	16.2%	91.1%	6 539
KwaZulu-Natal	45 513	28.9%	80.4%	9 267
Limpopo	39 274	29.1%	77.8%	9 251
Mpumalanga	51 395	24.4%	80.3%	8 542
Northern Cape	56 213	18.4%	76.7%	11 509
North West	46 362	22.7%	76.9%	8 673
Western Cape	68 727	13.7%	89.5%	7 996

8.4 Design of the IGFR System and Implications for Rural Development

Decentralisation is a fundamental principle of South Africa's IGFR system, calling for community-centred responsibilities to be devolved to the lower levels of government, and participatory governance at institutional and community levels to facilitate development. In the Constitution, Section 40 establishes three distinctive, interrelated and inter-dependent spheres of government, while Section 152 requires government to involve the community in the processes of local decision-making. In the context of rural development, decentralisation enables people, especially the poor and marginalised, to determine their own development trajectory, to control the fiscal resources for implementing local rural development programmes and to hold authorities accountable (UNDP, 2004).

The link between rural development and decentralisation is clear, but rural development – conceptually and practically – is inherently fluid. This often means that in the process of participation and negotiation (between and within government and the community) consensus cannot be reached on what rural development should entail. As the previous chapters have indicated, rural development is not only vague but also multi-dimensional. It includes wide-ranging imperatives, such as improving the quality of life of the rural poor, reducing poverty and sharing growth, ensuring food security and managing natural resources sustainably (Phuhlisani, 2009). In recent years, rural policy has taken a more integrated paradigm, promoting joint action among rural agents and coordination of different government levels and sectors in addressing rural development challenges, including (but not limited to) agriculture, education, health, infrastructure and employment (Albala and Bastiaensen, 2010).

In a decentralisation process, local communities should ideally engage and agree on rural development priorities and use available resources to address their specific regional inequalities. However, decentralisation does not always leads to local governance that in turn leads to local development and to poverty reduction. The relationship between decentralisation and rural development is not linear and is affected by the contestations inherent within the design and functioning of the IGFR system (UNDP, 2004). The IGFR system often lacks mechanisms that allow local demands to be integrated within a framework of national goals and strategies, while subnational governments do not always have the necessary resources to address local specific rural development needs, including delegated responsibilities (Wong and Guggenheim n.d.). Overlapping responsibilities between subnational and national government also creates intergovernmental and fiscal tensions, which undermine or duplicate rural development efforts. These tensions manifest in national government dominating the rural development agenda, which contributes to the disconnection with locally driven rural development. Most national rural development policies are region- and sector-neutral and fail to take into account the heterogeneity of rural spaces (Schejtman and Berdegue, 2008).

Decentralised rural development requires a number of fundamentals to be in place (World Bank, 1998). National government must provide institutional capacity to enable rural development programmes to be implemented, help subnational governments to identify local needs and encourage resources to be used where the needs are greatest. To minimise costs, the community should as far as possible be directly involved in implementing rural development projects. This requires strong political commitment to transferring appropriate powers and responsibilities to the subnational governments, sufficient funding to enable the subnational governments to carry out the prescribed mandates, and capacitated community institutions able to implement the relevant elements of rural development.

Decentralisation is a necessary condition for rural development, which should be carried out by the level of government closest to the community. The key question is whether the functions allocated to provinces constitute rural development and whether the responsibilities are amenable to participatory governance.

8.5 Provincial Rural Development Mandates

According to Schedule 4(A) of the Constitution, urban and rural development is a concurrent responsibility of national and provincial governments. The Constitution does not explicitly indicate how the various activities should be shared between the two spheres. This lack of specificity lies at the centre of uncertainties over how different spheres perceive their respective roles in (and contributions to) rural development. Complexities ingrained in the definition of rural development further reinforce these uncertainties.

Before outlining the specific provincial rural development mandates, the concept of rural development needs to be unpacked. Rural development is widely accepted as being concerned with poverty reduction and improvements in general standards of living (World Bank, 1998). The provincial functions of education, health, welfare services, housing, public transport, roads and agriculture potentially constitute rural development, as they reduce poverty and improve living standards. Agricultural growth has been a major driver of poverty reduction in developing economies: a 1% increase in agricultural productivity is associated with a 0.6–1.2% reduction in the number of people living on less than a dollar a day (Thirtle et al., 2001). Access to assets such as land, housing and livestock is also a crucial strategy for addressing rural poverty (IFAD, 2011). The impact of roads on rural poverty is mixed: investment in roads is found to be poverty neutral because rural populations travel infrequently, and yet roads provide increased mobility and accessibility to services, so long as motorised transport is available (Bryceson and Bradbury, 2006). Education and health expenditure has a significantly positive impact on poverty (Gounder, 2012). Yet provinces do not always perceive their education and health spending as rural development, partly because sector policies are mostly driven from the centre, and partly because sectoral allocations and investments are not space-based, and the outcomes are not physically confined to a rural space (as in the case of investments in roads and agriculture).

8.5.1 Community participation and provincial rural development

As previously indicated, in a decentralised government system, rural development needs to embrace community participation, as communities are better able to identify specific rural development needs. However, the way in which the delivery of provincial functions is structured does not provide sufficient room for optimum community participation. For instance, in the case of education, the law makes no provision for a local council or committee to oversee the education needs of the entire community, but instead relies on school governing bodies, which typically focus on individual schools. District and circuit offices are the provincial structures that are closest to the community. However, they are located far away from rural villages and have no decision-making powers. Similarly, the disconnect between schools and communities means that schools rarely draw on the various sources of expertise (such as unemployed graduates and retired professionals) and support structures available in their surrounding communities. The Department of Education (DOE, 2005) recommends that community structures be involved in school decision-making processes at district, local and national government level. These recommendations were implemented in an experimental study, which found that schools in communities where Community Education Forums were established had better attendance by parents at school meetings, more information-sharing about children between parents and teachers, and greater use of community expertise and skills. Bringing schools and communities together is difficult and challenging, but necessary in order to stimulate functional linkages between education and development (Gardiner, 2008).

The importance of community participation in primary health care and rural health services development is uncontested (Preston et al., 2010). Provinces have district health authorities (which coincide with municipal boundaries) to facilitate interaction between health-care providers and the community in order to improve community health. Section 42 of the National Health Act (No. 61 of 2003, amended 2013) provides for clinic and community health centre committees, which must include local councillors, community members and the head of the health centre. These structures are meant to enable local communities to identify their own health-care needs and to have a say in how the budget is allocated and how health services are planned and delivered. As is the case in education, community participation within health-care services is absent or ineffective (HST, 2008). Resources, especially budgets and staff, are still managed centrally, limiting the ability of districts and communities to channel resources towards local priorities. Community involvement is carried out only for the purpose of legitimising programmes, while clinic committees are not fully functional[40] and their role is limited to conflict resolution, health education and facilitating voluntary services (ibid).

Other provincial rural development mandates make no provision for regular interface other than through ward committees, whose role is limited to local government issues and beleaguered by structural limits to power and party political tensions (Smith, 2008). For instance, development planning of housing and roads in South Africa is top-down (Xala, 2005). The only community participation for built environment functions occurs through the local

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[40] Local councillors' representation is very small, and they are not allocated resources to carry out their duties.

government integrated development plan (IDP) processes, which lack provincial participation. Similarly, community participation in agriculture is scant. Community participation during land reform tends to decline after land transfer (Jacobs and Price, 2003), and the failure of community agriculture projects funded by provinces may be because of the lack of community participation (Mwale et al., 2012).

Legislation provides for sufficient decentralised structures for provinces to fulfill their rural development community participatory requirements. However, provinces do not appear to regard community participation as a critical component of their rural development mandates.

8.6 Provincial Rural Development Programmes

Provinces and national government have similar rural development approaches and sub-programmes. The provincial departments of agriculture and rural development carry out many of the programmes, which are overwhelmingly dominated by agrarian activities, project-oriented and supply-driven, unsystematic and spread thinly across rural villages. These departments are involved in delivering agriculture-related programmes, such as the revitalisation of irrigation schemes, livestock improvement, milling plants and silos in CRDP sites, food nutrition and provision of boreholes and agriculture inputs to communities. Unlike their national counterparts, some provincial agriculture and rural development departments include the services delivered by other departments within the rural space. For instance, the Mpumalanga annual report for 2014 shows the contribution made by the departments of social development, education and economic development in providing youth centres, training ECD professionals and establishing a bakery, among other things.

Overall, rural areas are receiving considerable attention from provincial governments, especially agriculture, but it is unclear whether the programmes are delivering the full complement of services required for rural development. Although the CRDP provides government with an opportunity to coordinate interventions towards areas with the greatest needs, the programme is likely to be undermined by isolated departmental planning processes – sector departments plan separately from municipalities (the custodians of rural spaces) which leads to duplication (PSC, 2009).

When the CRDP was introduced in 2009, most provincial departments of agriculture were already implementing aspects of the programme but had to establish a new "rural development" sub-programme in order to conform to national government requirements. These sub-programmes are meant to coordinate rural development programmes, but placing the coordination role within the provincial department of agriculture constitutes unnecessary duplication, as the Offices of Premiers are mandated to play a coordination role. The Offices of the Premier are also best placed to provide central and strategic coordination from a multi-sectoral rather than an agricultural perspective (The Presidency, 2008).

8.7 Funding Instruments for Rural Development

Provinces rely for their funding mostly on transfers (up to 97%) from national government. comprising the PES[41] and a number of conditional grants. The PES, which represents 81% of national transfers to provinces, is a general purpose grant that provinces can spend at their discretion. Conditional grants, which make up 19% of transfers to provinces, are intended to fund national priorities across a range of mandates. These intergovernmental transfers must be equitable, and their allocation and spending must take into account the interjurisdictional fiscal and development disparities. Therefore, the PES allocation framework and selected provincial conditional grants include variables that directly and indirectly compensate for "ruralness".

In existence for over 18 years, the PES formula has undergone several reforms, including the introduction of components aimed at explicitly addressing rurality. The most notable are the backlogs component (introduced in 2000) and the poverty component[42] (introduced in 2005), which replaced the social welfare component in the PES formula. The aim of the backlogs component was to fund the capital needs of historically neglected provinces or former Bantustans, which included the Eastern Cape, KwaZulu-Natal and Limpopo. The three provinces accounted for 65% of the education backlog factor and 70% of the rural factor within the backlogs component. Similarly, the poverty component was intended to reward provinces with the highest incidence of poor people – generally presumed to be concentrated in the rural areas. The backlogs and poverty components both have a weighting of 3% in the overall PES formula (National Treasury, 2000; 2005).

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[41] The provincial equitable share is distributed across the nine provinces through a deterministic model or formula made up of components and variables which proxies provincial expenditure mandates and needs.

[42] The poverty component was a compromise following the removal of the social welfare component and the shifting of a social security function from provinces to national government. The 2005 reforms revealed distortions between the weights assigned to components in the formula and expenditure levels, which resulted in some provinces (mostly rural) being short-changed by the shifting of social security funds. The poverty component was introduced to compensate provinces that were spending far beyond the social welfare weighting.

The backlogs component has since been removed from the PES and replaced by a myriad of infrastructure conditional grants, which are considered more suited to addressing specific regional development disparities, such as rural under-development. Notwithstanding these grants, the PES formula continues to be criticised for perpetuating regional imbalances. Its poverty component, which is largely regarded as being pro-rural, is small and uses a variable that is not necessarily peculiar to rural areas as a measure of need. As discussed earlier, poverty is increasingly becoming urban. Other important (and larger) PES components, such as education and health, are seen as insensitive to rurality because their underlying indicators of need do not specifically distinguish between rural and other developed areas.

Overall the PES formula is perceived as unresponsive to rural development, which is confirmed by a simple ANOVA[43] test. Table 51 compares the variation in provincial PES per capita allocations between 2000 and 2013. When the backlogs component was active (between 2000 and 2005), no discernible variation is found in the per capita PES allocations to rural and non-rural provinces. Only from 2006, following the wholesale PES reforms, do the allocations show statistically significant variations across provinces. However, the variations only appear when Gauteng is included in the analysis, suggesting that the PES is not responsive to rurality. Even when the ANOVA test is applied over a long period, from 2000 to 2013, the results show no material difference in the allocations for all provinces. Overall the results overwhelmingly suggest that the PES formula is not sensitive to rurality and imply a need to redesign the PES formula.

Table 51. Variation in per capita provincial allocations

Until 2005	*SS*	*df*	*MS*	*F*	*P-value*	*F crit*
Between groups	4187334,711	8	523416,8389	1,540963125	0,177767769	2,208518074
Within groups	12228070,8	36	339668,6335			
Until 2006	*SS*	*df*	*MS*	*F*	*P-value*	*F crit*
Between groups	5212226,918	8	651528,3647	2,35345129	0,033064753	2,152132879
Within groups	12457779,15	45	276839,5367			
2006 onwards	*SS*	*df*	*MS*	*F*	*P-value*	*F crit*
Between groups	29238931,44	8	3654866,43	2,7096799	0,013855733	2,115223279
Within groups	72836200,03	54	1348818,519			
From 2000 - 2013	*SS*	*df*	*MS*	*F*	*P-value*	*F crit*
Between groups	28044927,47	8	3505615,933	1,839764043	0,077334919	2,025247482
Within groups	205790803,5	108	1905470,403			

Source: Author's estimates

8.7.1 Rural responsiveness of the backlogs component replacement grants

After the backlogs component was removed from the PES in 2005, conditional grants were introduced within the broader provincial fiscal framework to address (among other things) historical infrastructure backlogs in the rural provinces (National Treasury, 2005). Conditional grants are appropriate instruments for funding specific regional expenditures needs that cannot be accommodated by general transfers. Grants include the Health Facility Revitalisation Grant and the Provincial Infrastructure Grant, which were discontinued in 2011 and disaggregated into the Education Infrastructure Grant and the Provincial Roads Maintenance Grant.

Unlike the PES, infrastructural conditional grants are not formula-driven and do not derive each province's share from expenditure indicators, despite being introduced to remedy historical infrastructure backlogs largely in the rural hinterlands. The allocations for infrastructure grants to provinces are based on the number of projects approved and were recently linked to a two-year planning and approval process to minimise under-spending. In this allocation model, the responsibility for addressing rural development challenges falls on provinces rather than the grant design.

As Table 52 shows, South Africa's three most rural provinces (the Eastern Cape, KwaZulu-Natal and Limpopo) combined were allowed over half (52%) of the Provincial Infrastruc-

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[43] ANOVA is a statistical tool used to evaluate whether there is any significant difference in the means of three or more independent data groups.

ture Grant and just under half (46%) of the Health Facility Revitalisation Grant (although over 15 years, Gauteng received the largest share, i.e. 25%). These three provinces also accounted for nearly two-thirds (63%) of the relatively newer Education Infrastructure Grant. Between 2000 and 2015, most of the allocations went to the rural provinces, which indicates that infrastructure conditional grants are responsive to rural needs. However, whether such infrastructure allocations are of value to rural provinces is a matter that requires further research. For instance, research needs to establish the specific types of infrastructure needed in each region and whether a province should invest in deep remote areas (where the marginal returns to infrastructure decrease rapidly due to high costs and low usage levels) – or whether a more feasible rural development remedy for these remote areas would be to move people out of the fragile lands into areas with more jobs (Fan and Zhang, 2004).

Table 52. Average provincial share of the infrastructure allocations (2000–2015)

Province	Provincial Infrastructure Grant (10-year average)	Health Facility Revitalisation Grant (15-year average)	Education Infrastructure Grant (4-year 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%

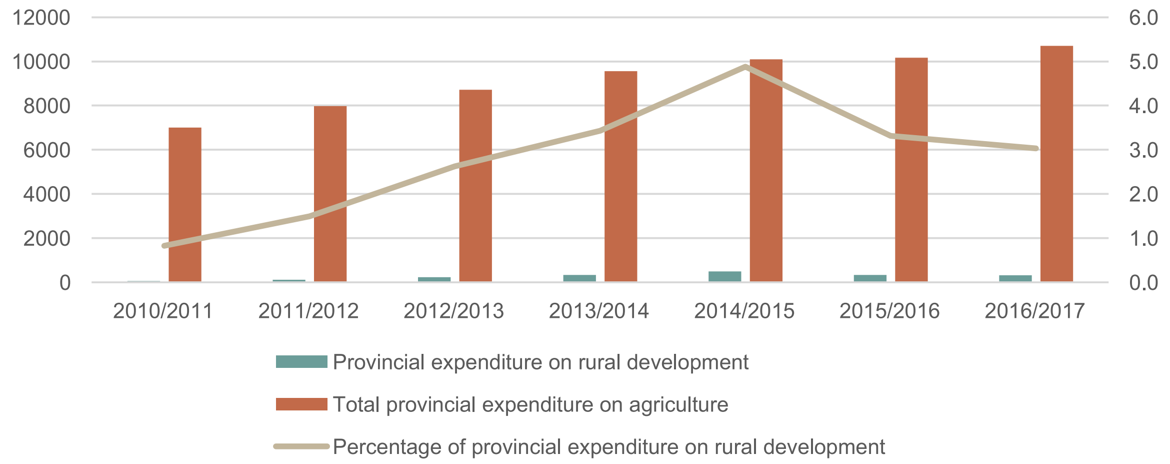
Source: Author's compilation

8.7.2 PES expenditure on rural development

The task of channelling PES towards priority areas rests entirely with the provincial legislatures and executives, albeit within the bounds of national policies and national norms and standards. Funding allocated to rural development depends on the importance attached to it by the respective provinces. As most provincial rural development activities are focused on agriculture, the allocations to the sector provide an indication as to what extent agriculture is prioritised.

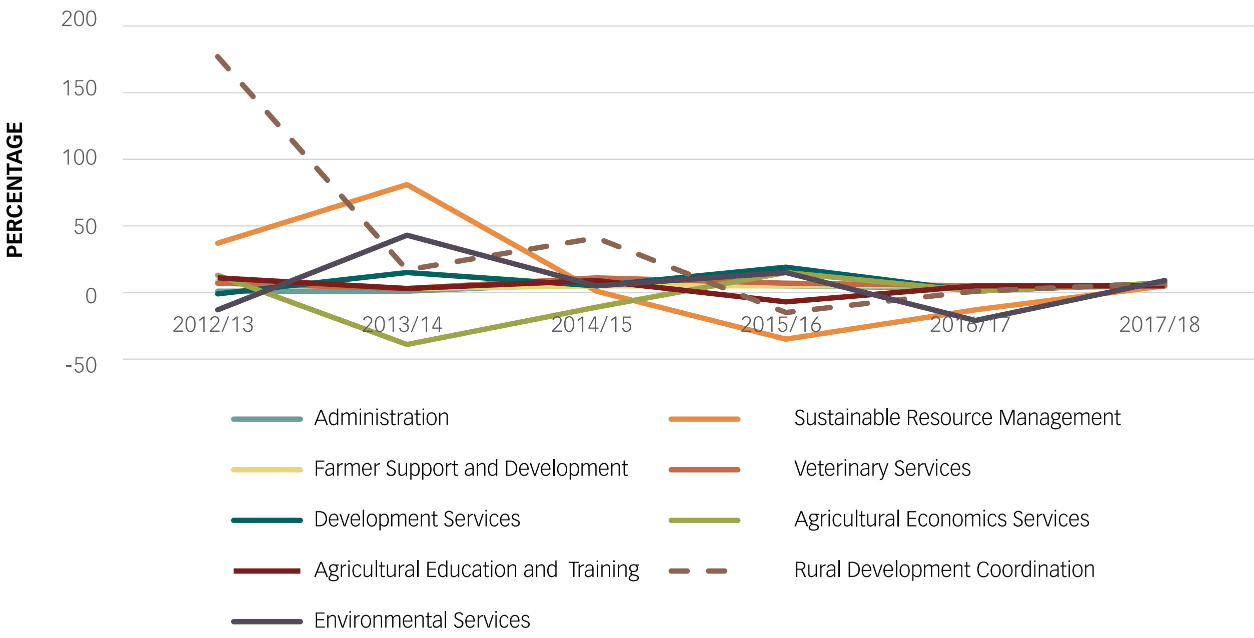
Provinces spend on average approximately 3% (or R10-billion) of their PES allocation on agriculture (Figure 73). Unsurprisingly, the three rural provinces (the Eastern Cape, KwaZulu-Natal and Limpopo) allocate the most (4%), while Gauteng allocates the least (1%). In 2016/17, rural development programmes received just under 3% of the total agriculture budget, compared to 0.08% in 2010/11 and 5% in 2014/15. The growth, albeit from a low base, of the provincial rural development budget coincided with the reintroduction and re-emphasis on rural development through the CRDP in 2009. Allocations to the CRDP are notably small because it is new and because provinces locate many activities that are associated with it under different programmes. For instance, food security initiatives, which generally sit under rural development, are part of the provincial farmer support and development programme. The rural development programme within the provincial department of agriculture is largely limited to consultation with the community (National Treasury, 2015).

Figure 73. Provincial agriculture and rural development expenditure (2010–2017)



Source: National Treasury (2015)

Figure 74. Agriculture expenditure growth rates by programme (2012/13–2017/18)

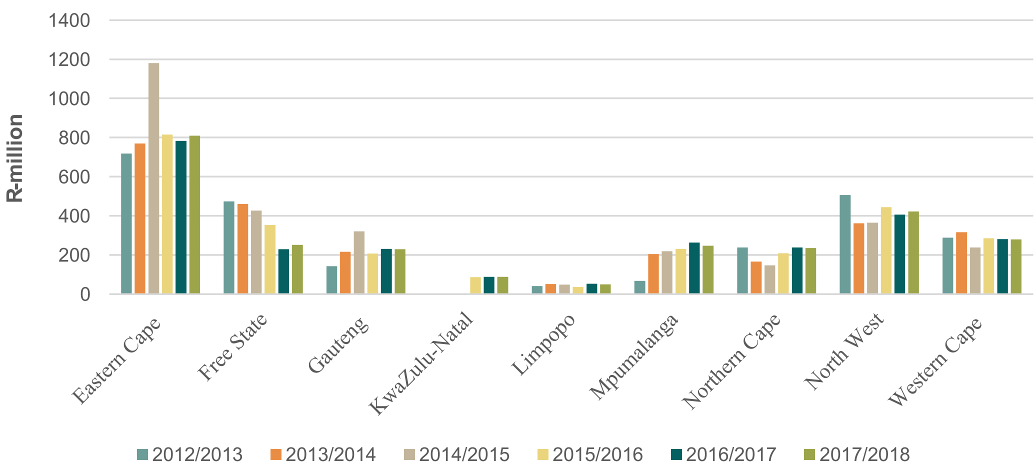


Source: National Treasury (2015)

As seen in Figures 73 and 74, rural development expenditure grew fast at the beginning of the period, presumably driven by the attention from the Presidency, but then tapered off. The decline in rural development programme allocations from 2014/15 coincided with the overall national expenditure slowdown but also reflects some de-prioritisation of rural development. National priority programmes are usually allocated bigger allocations at inception in response to policy "hype". However, as implementation challenges become apparent, allocation declines, resulting in devastating consequences for delivery goals. The RHIG, which is discussed later, is a typical example

A comparison of rural development expenditure (Figure 75) found that the Eastern Cape allocates the highest budget for rural development, while Limpopo spends the least, despite being a rural province. However, the data provides no conclusive indication of whether or not provinces are prioritising rural development. This is because (a) the extent of rural development needs in each province is unknown; (b) provincial expenditure reports do not give any spatial indication of where funds are spent – expenditure on other functions, such as education, are standardised across beneficiaries irrespective of space, while access to health-care facilities or spending per patient is not determined by a person's place of origin (HST, 2015).

Figure 75. Rural development expenditure trend by province (2012/13–2017/18)



Source: National Treasury (2015)

This expenditure review shows that provinces perceived generally as rural (with the exception of the Eastern Cape) allocate very little of their own discretionary funding to rural development, which is defined in the narrow sense as part of the agriculture department's sub-programmes. Admittedly the size of the provincial agriculture and rural development budgets are an insufficient measure to determine provincial prioritisation of rural areas.

8.7.3 Conditional grant expenditure on rural development

Conditional grants are another important source of finance for rural development, albeit driven from the centre. The current provincial fiscal framework consists of many conditional grants specifically targeted at various aspects of rural needs. The main ones are three agricultural grants: the Land Care grant, the Comprehensive Agricultural Support Programme (CASP, including Fetsa Tlala) grant, which have been in existence since 2000 and 2005 respectively, and the Ilima/Letsema project, which commenced in 2008. The 2014/15 budget allocated a total of R2.4-billion to the three grants: 78% to CASP, 19% to Ilima 19% and 3% to Land Care. These grants have overlapping objectives, which include increasing agricultural productivity, poverty relief and sustainable resource management. Their allocation framework is neither rural nor agriculture biased, whereas these grants are focused on agriculture, which has been shown not to be a dominant economic activity in rural provinces. For instance, the Northern Cape receives the largest share of CASP (34%) and Ilima (19%) grants despite contributing the least to total national agricultural output (Table 53). Conversely, the Western Cape, which is commonly regarded as an urban province, has the second highest agricultural output after KwaZulu-Natal, ahead of provinces perceived as rural. These findings dispel the view that rural areas have a strong agricultural base, and hence rural development strategies should be agrarian in focus.

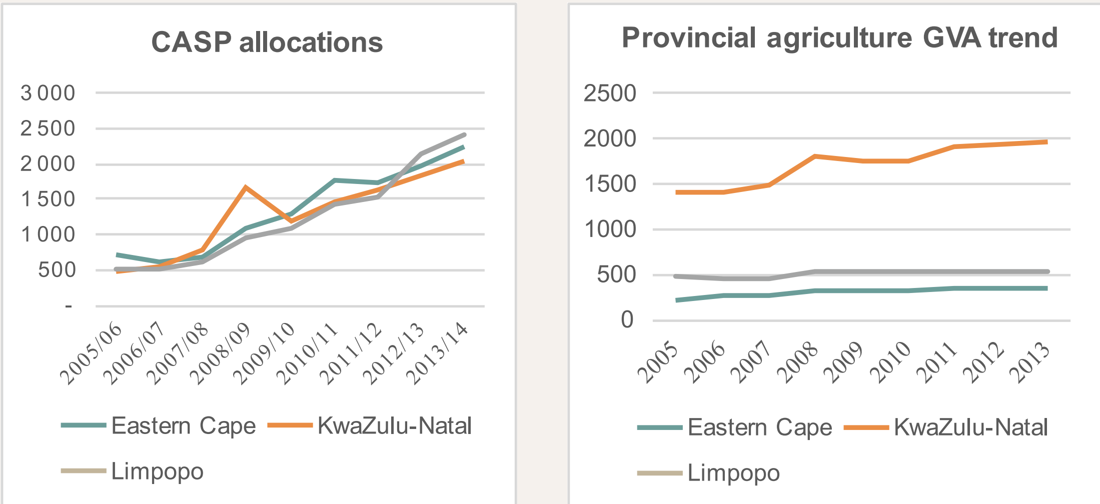
Table 53. Comparison of provincial agriculture conditional grant allocation and agriculture output

Province (R'000)	2013/14 CASP allocation	% share of CASP allocations	2013/14 Illema allocations	% share of Illema allocations	% Share of agriculture output
Eastern Cape	223 626	12%	45 567	10%	6%
Free State	140 274	7%	57 999	13%	10%
Gauteng	55 880	3%	17 538	4%	6%
KwaZulu-Natal	202 522	11%	65 768	14%	26%
Limpopo	239 978	13%	43 845	10%	8%
Mpumalanga	130 986	7%	43 845	10%	9%
Northern Cape	641 306	34%	84 393	19%	6%
North-West	170 714	9%	43 845	10%	6%
Western Cape	106 376	6%	51 737	11%	22%

Source: National Treasury database.

The skewed distribution of the allocations stems from the land area/mass being considered as a more important variable that the other factors that account for rurality, such as households involved in agriculture, restituted land, food insecurity, deprived areas and land degradation (National Treasury, 2015). The CASP allocation criteria appear to be entirely driven by land size, as the allocations reflect the province's respective land area. This is totally inconsistent with the grant objectives, especially that of increasing productivity. A simple comparison of provincial CASP allocations and agriculture GVA for the three rural provinces shows an unrelated growth pattern, with GVA growing at a flat rate and CASP at a steeper rate. Agriculture transfers do not appear to have any effect on provincial GVA (Figure 76).

Figure 76. CASP allocations and agriculture GVA in rural provinces (2005/6–2013/14)



In addition to the traditional agriculture-focused conditional grants, the current provincial fiscal framework provides for sectoral grants to finance specific rural infrastructure challenges. In 2009, the government adopted the Medium Term Strategic Framework (MTSF) in response to which (in particular Outcome 7), several departments introduced new conditional grants to fund priority rural infrastructure needs, including sanitation and school infrastructure. The Department of Water and Sanitation has taken over from the Department of Human Settlements the oversight of the indirect conditional RHIG that funds sanitation infrastructure, while the Department of Education established the Accelerated School Infrastructure Delivery Initiative (ASIDI) to address school infrastructure in the rural areas. The ASIDI is also funded through an indirect conditional grant called the School Infrastructure Backlogs Grant (SIBG).

The RHIG was introduced 2009/10, with an MTEF allocation of R1.2-billion, while the SIBG was introduced in 2011/12 with an initial MTEF allocation of R8-billion. The SIBG delivery targets are to replace 496 mud schools and provide water to 1307 schools, sanitation to 536 schools and electricity to 1434 schools within a three-year period. The Eastern Cape receives the largest share (more than 90%) of the SIBG and the second largest share (29%) of the RHIG (KwaZulu-Natal receives 34% of the RHIG). Both grants are allocated on the basis of backlogs, but the RHIG is restricted to the 27 CRDP districts. Since inception, the two grants have been characterised by significant under-spending (Table 54) and implementation challenges, and have failed to meet the government target of eradicating rural infrastructure backlogs by 2014 (FFC, 2015; AGSA, 2015).

Many of the conditional grants aimed at addressing rural development challenges are profoundly controlled by national government, either through stringent, nationally determined conditions or outright central management of the grants. For instance, in 2013, part of the CASP allocation was diverted into the national Fetsa Tlala (End Hunger) Food Production Initiative, with national government directing provinces to allocate 70% of the CASP to Fetsa Tlala. In the case of the SIBG, the allocation criteria are subjective, as the grant is mainly allocated to the Eastern Cape, over and above the School Infrastructure Grant allocated to all provinces. Lastly, control of the RHIG has been at the centre of controversy and contestation between national departments and across spheres, presumably because national government wants to control and direct where resources are allocated.

Table 54. Special rural development conditional grants (R-million)

Year	SBIG		RHIG	
	Aggregate allocation (R-millions)	% spent	Aggregate allocation (R-millions)	% spent
2010/11			R100	62%
2011/12	R700	10.9	R258	31
2012/13	R2 065	42%	R340	60%
2013/14	R1 960	70%	R106 (direct) R100 (indirect)	100% 75%

Source: National Treasury– (2010; 2011; 2012; 2013; 2014)

8.8 Main Findings and Conclusion

Internationally, no blueprint exists for designing institutional and funding arrangements for rural development. Each country organises its fiscal arrangements in accordance with the ideological orientation of its IGFR. There are visible attempts to devolve rural development responsibilities to subnational structures, in particular the districts, but in most cases rural development projects are strongly influenced and controlled by central government.

Provincial developmental trajectories are clearly converging, which counters the need for a special funding dispensation to address rural development or prioritise rural development.

Citizen participation is an important aspect of rural development because it enables the active involvement of the community in identifying their developmental needs and channelling resources towards immediate needs. However, structures created to facilitate interface between provinces and communities are ineffective and dysfunctional.

Provincial rural development mandates straddle many concurrent functions, creating fiscal tensions and duplications but also causing misperceptions of whether the responsibilities undertaken by provinces in education and health constitute rural development or not.

The PES is a key funding instrument for provinces but appears less responsive to rural challenges, as the per capita PES allocations do not differ across provinces (with the exception of Gauteng). PES allocations are primarily driven by population distribution rather than rural need indicators. Incorporating the rural indicators of needs (and the ability to collect own revenue) in the fiscal transfer frameworks may disadvantage the rural provinces because characteristics such as poverty are peculiar to both rural and urban provinces.

Notwithstanding the unresponsiveness of the PES, rural provinces allocate a small portion of this discretionary funding instrument to agriculture. The education and health budgetary allocations from the PES are found to be rural-neutral, partly because expenditure levels at schools and health-care centres are standardised across beneficiaries and not dependent on a person's place of origin. The rural provinces account for a larger share of the infrastructure conditional grants allocations, but questions remain regarding the extent to which these funds have been used to address rural infrastructure backlogs, and how infrastructure investments contribute to better expenditure outcomes.

Misalignment is evident between the allocation formulae of agriculture grants and the policy objectives for promoting agriculture output and food security. The other non-infrastructure conditional grants for promoting rural development are generally managed and implemented centrally and dominated by national policy imperatives. However, centrally controlled grants are associated with poor spending performance and insufficient reporting on expenditure outcomes.

8.9 Recommendations

Related to the Division of Revenue

1. The Provincial Offices of the Premier, in consultation with the provincial departments of basic education, health, agriculture and rural development and roads, should identify the rural development needs in the province and set annual delivery targets against which PES allocations will be assessed by oversight bodies. Departmental budgets and expenditure reports should be disaggregated in accordance with municipal boundaries to help ascertain the extent to which PES allocations are targeted to rural areas' needs.

2. The National Treasury, in collaboration with the departments of basic education, health and those responsible for provincial roads, should ensure that the criteria for allocating infrastructure conditional grants take into account spending efficiency, delivery targets and performance, as well as the applicable national norms and standards. This should assist with the monitoring of provinces in meeting their developmental goals and facilitate targeted intervention where a province consistently fails to meet delivery targets.

3. The Department of Agriculture, Fisheries and Forestry and National Treasury should review the framework for allocating agricultural conditional grants, to reduce the weighting of agricultural land size and poverty relief, and to incorporate factors that are closely aligned to the objectives of the grant, in particular the promotion of emerging farmers or agriculture production in the rural areas, as stipulated in the Agriculture Policy Action Plan.

4. The Department of Planning, Monitoring and Evaluation should 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 the spend. The outcome of the review should be used to form the basis of any adjustments to infrastructure grants earmarked for rural development.

Related to coordination, community participation and prioritisation

1. In order to ensure active community participation in setting rural development priorities, the provincial Department of Health must ensure that clinic committees are functional, while 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 programmes from the provincial Department of Agriculture to the Office of the Premier to ensure that all aspects of rural development are taken into account during planning. The Office of the Premier must ensure that rural redevelopment projects or initiatives carried by the national Department of Rural Development and Land Reform or any other department are subjected to the relevant community participation processes – to avoid duplications.

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