THE INDEPENDENT INSTITUTE OF EDUCATION

Varsity College

CORPRO SA
CORPORATE PROJECT CONSULTANTS SOUTH AFRICA

ECONOMICS
(the best subject)

PRESENTED BY

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The Public sector.
Chapter 16

Learning Unit 3

Learning Outcomes.

List the components of Government sector in SA,
Discuss four reasons for government involvement in the economy,
List the three broad functions of government,
Explain how the government intervenes in the economy,
Discuss government failure,
Discuss nationalisation and privatisation,
Define and explain the term “fiscal policy”,
Explain the reasons for the increase in government spending in SA,
Explain how government spending is financed,

Learning Outcomes.

Explain the criteria for a good tax,
Explain the different types of tax,
Demonstrate, through calculations, the difference between the marginal tax rate and the average tax rate with regard to personal income,
Distinguish between progressive, proportional and regressive taxes in SA,
Explain the incidence of tax,
Explain, with the aid of a diagram, the impact of a specific excise tax.

The Public Sector.

1. Central government.
2. Regional (or Provincial) government.
3. Local government.
4. Public corporations.

Role of Government in the Economy.

Mixed economies:

- government and
- private sector and
- market forces.

1. Market forces and private initiative more efficient in economic problem,
2. Government enforcement of rule under which makes agreements,
3. Government correct market failures,
4. Markets efficient but not always equitable.

Market failure.

Market system unable to achieve an efficient allocation of resources.

Not: nothing good happened,

But best available outcome has not been achieved.

Does government intervention improve or worsen the problem?

Market failure.

1. Monopoly

- Do nothing – profits will attract new entrants,
- Impose price control,
- Tax full excess profits,
- Regulate through competition policy.

Natural monopoly – capital expenditure and scale of production supply whole market eg power station.

Market failure.

2. Public goods

- Failure to provide sufficient quantities of certain goods and services.

- Rivalrous in consumption vs non-rivalrous in consumption and
- Excludable vs non-excludable.

- Not all goods provided by public sector are public goods.
- Characteristics of goods and service not **provider** determine public vs private goods.

Market failure.

3. Externalities

- Negative externalities – external costs and
- Positive externalities – external benefits.

Restrict discussion to externalities in production only.

- External cost of production eg pollution.
  - Tax or requirement to correct.
- External benefits of production eg some forms of medical care – polio.
  - Subsidies or compensation.
- Coase theorem – negotiate cost for other parties.

Market failure.

4. Asymmetric information

- Perfect competition requires perfect information.
- Ignorance and uncertainty brings asymmetric information – hazardous effect of smoking.

5. Common property resources

- Belongs to no-one and available free of charge to anyone but rivalrous in consumption eg Fish resources.

Further reasons for government intervention.

1. Income distribution.
2. Macroeconomic growth.
3. Merit goods.

How does government intervene.

1. Public provision,
2. Market participation,
3. Government spending and transfer payments,
4. Taxation,
5. Regulations.

Government failure.

1. Government officials – human beings with their own motives, ambitions, objectives and faults.
2. Two types of officials:
   - Elected (politicians) – vote maximising.
   - Appointed (bureaucrats) – maximise budget and staff component, no market test.
3. Rent seeking – payment above what market would pay eg farming subsidies.

Nationalisation and Privatisation.

Nationalisation: the transfer of ownership from private enterprise to government.

Privatisation: the transfer of ownership of assets from the public sector to the private sector.

Commercialisation or **corporatisation** is the transformation of state owned enterprises into commercial entities, subject to commercial legal requirements and governance structures, while retaining state ownership.

Fiscal policy and budget.

Fiscal policy: a policy in respect of the level and composition of

- Government spending,
- Taxation, and
- Borrowing.
- **Budget**: main tool in fiscal policy.
- Instrument of demand management – influence demand in economy.
- Expansionary fiscal and monetary policy.
- Restrictive or contractionary fiscal and monetary policy.
- Delays or lags.

Government spending.

Government spending as portion of total spending in the economy.

SA:

- Changing consumer preferences – more spent on services,
- Political and other shocks eg war,
- Redistribution of income – low income determine votes,
- Misconceptions and entitlements – “free services” or government’s capacity is unlimited,
- Population growth and urbanisation.

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Government spending.

Refer treasury report

Taxation.

Good tax

Adam Smith:

1. Equitable
2. Economical
3. Convenient
4. Certain

Modern version:

1. Neutrality
2. Equity
3. Administrative simplicity

Different types of Taxation.

Direct tax
Indirect tax

General tax
Selective tax

Progressive tax
Proportional tax
Regressive tax

Personal income tax.

Taxable income
Marginal tax rate – additional rand taxed
Average tax rate (effective) – ratio tax to income
Progressive tax
Capital gains tax (CGT)
Tax calculations

Companies tax.

Proportional tax.

Refer rates

Value added tax.

30 September 1991

Regressive tax.

Refer rates

Excise tax.

Ad valorem excise tax

- Percentage on the value of the product.

Specific excise tax (only investigate)

- Specific fixed amount on each unit.

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- Refer figure 16-3