

Modelling Municipal Financial Conditions in KwaZulu-Natal – South Africa

Abstract

The commencement of the third millennium brought greater fiscal decentralisation in South Africa in that National Government has devolved much power and responsibilities to Municipalities. Municipalities have now many responsibilities for expenditures and revenues. Fiscal decentralisation has however created much variation in municipal financial conditions; some experience financial problems, whilst others do not. This paper presents a framework to assess the financial conditions of municipalities that adapts and reflects considerations on appropriate financial condition measures of municipalities.

In addition, municipalities need to know what factors determine the variation in their financial conditions. Therefore, the objectives of this study are, firstly, to develop two independent instruments to measure the financial condition of municipalities in the province of KwaZulu-Natal (KZN) South Africa and, secondly, to identify and examine a number of socio economic factors possible affecting the financial condition of these municipalities.

The data that was used for the study is from all 51 municipalities in KZN province from 2009 to 2015. The study used a panel data approach with two financial conditions indices as a dependent variable and a number of explanatory variables. The findings of the study suggest that in the absence of individual effects most of the selected socio-economic variables are relevant in terms of explaining some of the variation in municipal financial conditions. Cross-section fixed-effects does, however, significantly improve the overall performance of the model suggesting that it's rather the unobservable municipal unique factors affecting municipal financial conditions.

Keywords: Municipalities, Financial Conditions, Panel Data Econometrics, Fixed-Effects

JEL Classification codes: C23, G28, H72