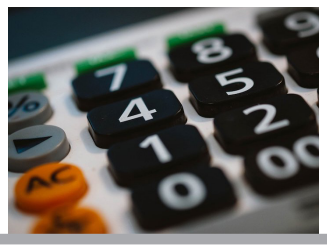
PAGE 2 >>
FINANCE//
BUDGET 2021: THE EXECUTIVE SUMMARY



PAGE 3 >>
TAX//
SUN SETS ON 12J INVESTMENT SCHEME

PAGE 5 >>
ECONOMY//
SA'S ECONOMIC RECOVERY PLAN

The2021Budget
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Cyril, Tito face Maggie Thatcher moment

When you clear away the financial debris of a horrific year, the one thing now abundantly clear is South African lawmakers need to absorb the toughest message possible for a socialist-inclined government: the economic reality that they've run out of "other people's money". With Covid-19 dealing the economy a R230bn blow (quantified today in Treasury documents), the tide has well and truly gone out. In Warren Buffett-speak, the whole world can see South Africa's ANC government has been swimming starkers for over a decade.

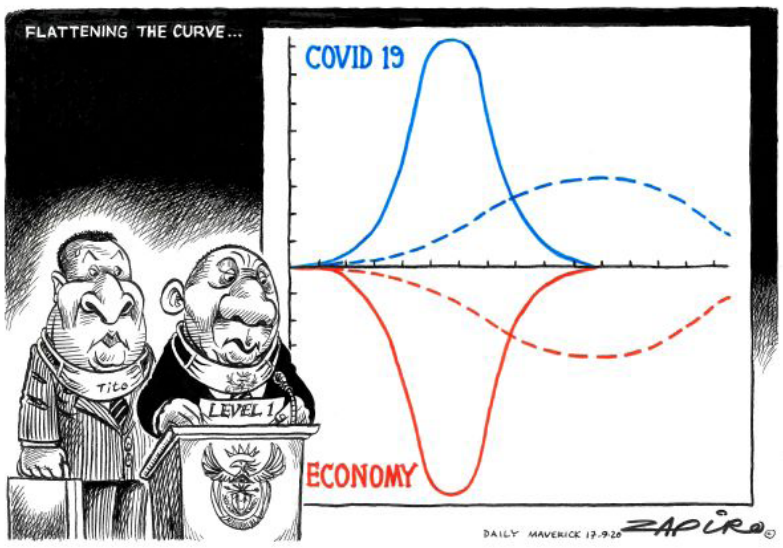
By Alec Hogg

The critical issue oft repeated in over a thousand pages of documentation provided us this morning by Treasury is clear: South Africa's public servants are busy bankrupting the nation. As a percentage of GDP, they now cost the country as much as the social democracies of Nordic nations. Fact.

Over the past decade, SA's public sector wage bill has compounded by 4% a year in real terms while the economy has grown a modest 1,5%. It's long past the point where the contracting tax base can fund this ever-growing drain on national resources. Instead, for over a decade already, the money to pay them has been borrowed - a fact reflected in the continuously escalating national debt.

The result of this: public servants now receive 47c in every rand of tax collected in South Africa. And debt-to-GDP, which was just 26% in the best year of the Trevor Manuel ministry, broke through 50% in 2017; 60% last year and is now at 80%. Even in Treasury's best case scenario (ie. public sector wages cut by R265bn in the next three years) it will reach 90%.

Even with historically low interest rates, servicing that debt takes around 20c of the taxes paid in this country. That, together with the wage bill, means there is very little left over to pay for basic necessities, let alone inject the stimulus the staggering economy desperately needs.



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And still those who lead muddy the waters. Budget commentary prattles on about the way low economic growth expands the income gap. Not a mention of addressing a 1,6% population growth rate which is a far greater issue – as the Chinese (with their One Child policy) showed the world decades back.

Then there's the hypocrisy of refusing to extend the increasingly successful 12J tax incentive scheme because it is a subsidy by society for rich South Africans.

For one thing, 12J has kept billions in SA that would otherwise have gone abroad. For another, its true cost pales into insignificance when compared with the gigantic received by global motor manufacturers through the noxious MIDP.

But it's politically unpopular to even consider that the MIDP inflates the price of SA motor vehicles by over 30% - a subsidy paid by every SA motorist. To say nothing of the impact an expensive national fleet has on forcing people to drive unroadworthy cars - with a rather obvious impact on road fatalities and costs of funding the ever-hungry Road Accident Fund (which will get another 11c a litre from us after Budget 2021).

But back to the more immediate issue of the outrageous public sector wage bill. Treasury's predictions are dire: even with a quarter trillion rand cut off the public sector wage bill in the next three years, and a mere 0.4% growth in other state spending, it will take the country until February 2026 before non-interest costs are covered by tax receipts.

So, finmin Tito Mboweni and his boss Cyril Ramaphosa are facing their Maggie Thatcher Moment, reminiscent of how the UK's Iron Lady took on the trades union in the mid 1980s.

Either these hard-boiled ANC politicians use their powers of persuasion to convince the powerful public sector trade unions of the need to sacrifice in the national interest, or they must go to proverbial war with organised labour.

In this morning's *Daily Insider* my overriding message ahead of Budget 2021 was to be sceptical. Having spent hours going through the context and details, it's impossible not to be right now. Especially on the state spending.

I remember listening to Pravin Gordhan a few years ago as he confidently told us his team would slash R25bn a year off government spending by centralizing procurement and eradicating the massive waste. Sadly, Gordhan himself was dispatched soon afterwards and his Procurement Tzar Kenneth Brown departed soon after for Standard Bank.

Then a couple years back Tito backed himself to hack the wage bill through attractive retirement packages and lowering the age when employees could participate. Those predictions turned to ashes when public servants refused to bite. Considering their conditions of service, omnipotent union reps and a long history of inflation-topping increases, why would they?

Read the article here

NUMBERS

Budget deficit reaches record high of **14%** of GDP

Tax revenue of **R99.6bn** is higher than October 2020 projection

Government spending reaches record **41.7%** of GDP

Corporate income tax rate reduced to **27%**

R10bn set aside for free Covid-19 vaccination campaign

Land Bank to receive **R7bn** over next 3 years

Click here to access the 2021 Budget coverage on BizNews.com.

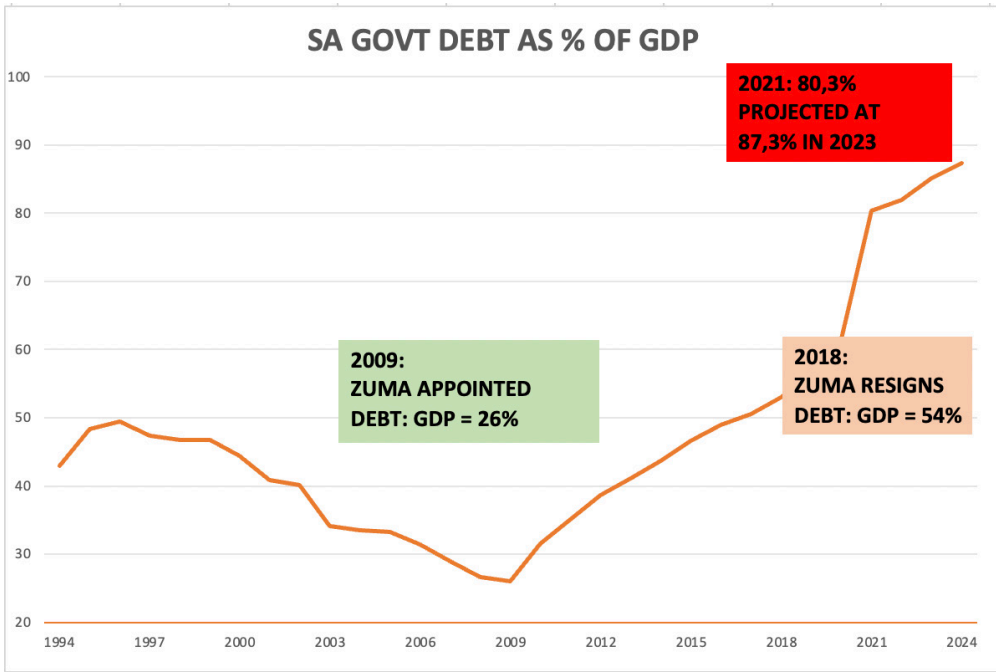
FINANCE

Budget 2021 – The Executive Summary

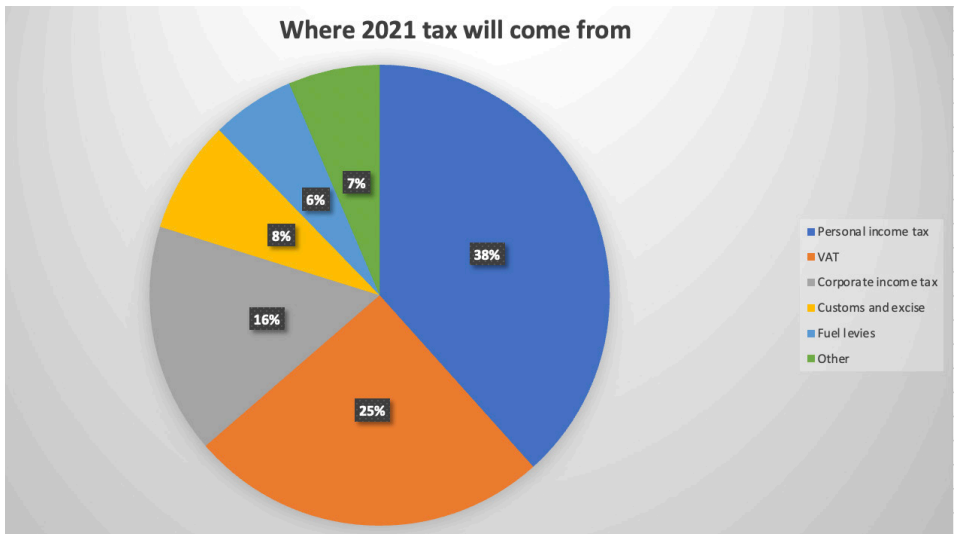
By Alec Hogg

The executive summary of the budget speech outlines Tito Mboweni's fiscal dilemma with a variety of taxes set to increase in the near future.

- The inflationary impact called fiscal drag, which costs taxpayers R11.2 a year, has been addressed through a 5% increase in tax brackets and primary rebates. The net impact is a net reduction of R2.2bn in personal income tax.
- Proposed tax increases of R40bn over the next four years, announced in the MTBPS, have been withdrawn to support an economy under severe pressure.
- Corporate income tax rate will be lowered to 27% for companies with years of assessment commencing on or after 1 April 2022. This will be done alongside a broadening of the corporate income tax base by limiting interest deductions and assessed losses.
- The Section 12J tax incentive, introduced in 2008, will not be extended beyond its sunset date at end June.
- Tax on fuel will be increased by 26c per litre – 15c for the fuel levy; 11c for the Road Accident Fund. This comes into effect on 7 April.
- Excise duties on liquor and tobacco products have been raised by 8%. As a result, alcohol is expected to contribute an extra R1.1bn and tobacco R700m in the 2021/22 fiscal year. A new export tax on scrap metal is projected to deliver R400m to Treasury.
- Government is (again) promising to address SA's rapidly rising public sector wage bill, budgeting to cut it by R265bn in the next three years. The cost of the SA public sector as a proportion of its economy is now matched only by the Nordic nations (Iceland, Denmark and, Norway); is double that of Ireland, Korea, Switzerland, and Germany; and 50% above the US, UK, and the global average.
- The State's wage bill has grown by 4% pa in real terms over the past decade compared with economic growth averaging 1,5%. Reversing this is a critical aspect of Treasury's goal to balance the nation's books – excluding interest payments – by 2025; ie bringing non-interest spending into line with total tax receipts.
- The country provided "one of the largest fiscal responses to the pandemic among developing countries" with government spending surging to a record 41.7% of GDP. This will continue in the current fiscal year with R9bn budgeted for vaccines which are expected to be rolled out in the second half of the year.
- SA's Budget Deficit has ballooned to a record 14% of GDP, virtually double the previous peak of set in 1993. A year ago Finance Minister Tito Mboweni forecast a Budget Deficit of 6.2% which would have been the second highest ever. Government spending now exceeds R2trn a year.
- Higher government spending was funded by borrowing, causing the country's debt-to-GDP ratio to jump from 65.6% to 80%. For context, this important ratio of national indebtedness only broke above 50% in 2017 and rose over 60% for the first time last year.
- Despite the sharp increase in State spending, South Africa's economy contracted by 7,2% in 2020, one of the hardest hit economies in the world. This is, however, an improvement on the minus 7,8% that had been projected four months ago. The direct cost to the economy of Covid-19 is thus quantified at R230bn.
- As a result of the economic contraction, gross tax receipts are projected to come in R213bn below what had been projected in the 2020 Budgeting process. This is, however, a R100bn improvement on the dire projections made in the MTBPS. The improvement due to easing of the lockdown in 3Q 2020, a better than expected global economic recovery (esp by China), and improved tax receipts from the mining sector.
- More than three quarters of the R213bn shortfall is due to four streams – Personal Income Tax (30%); Corporate Income Tax (19%); VAT (17%) and Excise Duty (11%).



Read the Budget Speech here



TAX

12J tax incentive is no more

By Jarryd Neves

Initially created in 2009 to drum up investment, create jobs and stimulate the economy, the 12J investment scheme is no more.

According to an assessment done by Treasury, the 12J tax incentive has not 'sufficiently achieved' its objectives, but rather provided a 'significant' deduction in tax for wealthy South African tax payers. According to Treasury, most of the investments that were supported by the tax incentive were 'low-risk or guaranteed return ventures that would have attracted funding without the incentive'.

National Treasury has gained information from 100 VCC's (Venture capital companies) and a further 360 qualifying companies in order to gauge the performance of the 12J tax incentive.

R11.5bn had been invested on which, says Treasury, a 100% tax deduction was applicable. R4.2bn was invested at a company level. For 2019/20, the tax accrued from these qualifying companies amounted to R207m, 'half of which was VAT', says National Treasury.

'Based on this information, the incentive seems to give a significant tax deduction to high net-worth taxpayers that cannot be justified given its limited economic impact'.

On the job creation front, these qualifying companies employed 8,239 people, 'of which 4,035 were in direct employment'. Of the qualifying companies to receive VCC funding, 37% added new jobs to the economy. In a recent article published on BizNews, The 12J Association of South Africa commented that up to 74% of these new jobs were 'taken up by historically disadvantaged individuals', with 25% of the investments made in rural areas.

'Over 50% of the investments appeared to be in low-risk moveable asset rental structures, low-risk income-producing investments and guaranteed-return real estates', says Treasury.

Since 2015/16, total foregone tax revenue due to the 12J incentive totals R1.8bn 'of which R1.7bn went to individuals who had a taxable income and VCC investment above R1,5 million per year'. Prior to the introduction of the R2.5m deduction cap, R745m of revenue was foregone in 2018/19, reports Treasury.

'Based on this information, the incentive seems to give a significant tax deduction to high net-worth taxpayers that cannot be justified given its limited economic impact'.

'The incentive has instead provided a generous tax deduction to wealthy tax payers', said Treasury.

The incentive, said The 12J Association of South Africa, is 'an ideal existing mechanism that should be leveraged to grow local jobs, retain local investment and develop the transformative gains that have already been made.

Consequently, the 12J tax incentive will not be extended beyond the current sunset date of 30 June 2021.

'The incentive has instead provided a generous tax deduction to wealthy tax payers', said Treasury.

Read also:

- **How to slash your tax bill, from RAs and 12J companies to tax harvesting**

PIT taxpayers who keep SA going

The latest detail from Treasury shows that a mere 113,000 people – 0.2% of the population – pay the maximum marginal tax rate of 45% which kicks in at a monthly income of R130,000. These account for 26% of all personal income tax paid in South Africa.

Another telling statistic is that only 12% of South Africans actually pay personal income tax. Two thirds of them pay less than a fifth of the total. Put differently, just over 2m taxpayers – 3,4% of the population – pay 80% of the R530bn a year that Treasury harvests from PAYE and Provisional taxpayers.

At the other end of the scale, there are now 18.2m people who receive social grants, roughly one third of all South Africans. Treasury's projects report that recipients will grow by around 300,000 people annually, reaching 19.25m by February 2024.

Table 4.5 Estimates of individuals and taxable income, 2021/22

Taxable bracket	Registered individuals		Taxable income		Income tax payable before relief		Income tax relief after proposals		Income tax payable after proposals	
R thousand	Number	%	R billion	%	R billion	%	R billion	%	R billion	%
R0 - R80[1]	7 183 913	–	256.2	–	–	–	–	–	–	–
R80 - R150	1 855 292	26.7	211.1	8.6	15.7	3.0	-1.3	9.4	14.5	2.8
R150 - R250	1 691 889	24.3	329.3	13.4	29.5	5.6	-1.8	13.4	27.7	5.4
R250 - R350	1 283 954	18.4	378.4	15.4	54.5	10.3	-2.3	16.8	52.2	10.1
R350 - R500	981 993	14.1	409.1	16.6	76.6	14.5	-2.6	19.5	74.0	14.3
R500 - R750	612 177	8.8	369.1	15.0	88.4	16.7	-2.4	18.1	86.0	16.7
R750 - R1 000	262 643	3.8	226.2	9.2	65.1	12.3	-1.3	10.0	63.8	12.4
R1 000 - R1 500	159 127	2.3	191.1	7.8	61.9	11.7	-0.8	6.1	61.0	11.8
R1 500 +	113 192	1.6	346.3	14.1	137.7	26.0	-0.9	6.6	136.8	26.5
Total	**6 960 267**	**100.0**	**2 460.7**	**100.0**	**529.4**	**100.0**	**-13.4**	**100.0**	**516.0**	**100.0**
Grand total	**14 144 180**		**2 716.8**		**529.4**		**-13.4**		**516.0**	

1. Registered individuals with taxable income below the income-tax threshold
Source: National Treasury

IN SHORT

Treasury scraps tax hikes

By Mike Cohen and Prinesha Naidoo

(Bloomberg) – South Africa signalled a shift in budgetary policy, backtracking on planned tax increases as it switched focus to reigniting the coronavirus-battered economy by bolstering consumption and investment.

Finance Minister Tito Mboweni reversed a decision to raise an extra R40bn ($2.8bn) over the next four years, allocated funds for Covid-19 vaccines and set more ambitious debt-consolidation targets, while sticking to a pledge to freeze state workers' wages. He also announced inflation-beating relief for individuals, whose taxes have been raised in five of the past six years, and a one percentage point cut in corporate tax from April 2022.

"We agree that tax increases must be kept to a minimum as we stabilise our public finances," Mboweni said in his budget speech to lawmakers in Cape Town on Wednesday. "We will not rest until we have fundamentally altered the structure of this economy."

The approach is a stark change from a decade of swelling civil service costs and bailouts to state companies that proved an increasing drain on the economy. It's the clearest sign yet that President Cyril Ramaphosa is intent on averting a debt crisis and driving through reforms needed to galvanise private investment and tackle record-high unemployment.

Political risk

The pivot toward a lesser role for the state is also politically risky and may suggest the president has stamped his authority on the deeply divided ruling African National Congress, which is preparing to contest local council elections later this year. Ramaphosa's rise to power in 2018 was backed by the party's powerful labour union allies that vociferously oppose the three-year moratorium on wage increases and favour even higher taxes for the rich.

While South Africa's finances remain precarious, the situation isn't as bleak as it was at the time of the mid-term budget in October, thanks to a commodities boom and a partial rebound in consumption and employment. The economy likely contracted 7.2% last year, the worst in almost a century, but less than the 7.8% previously forecast. It's expected to expand 3.3% this year and 2.2% in 2022.

The Treasury expects to collect R99.6bn more in the year through March than it projected four months ago, reducing the forecast for the budget deficit to 14% from 15.7%. Higher excise duties were imposed on fuel, alcohol and tobacco sales and a levy on scrap metal exports was introduced. The corporate tax rate will be reduced to 27% next year, the first reduction since 2008.

The anticipated peak for state debt was reduced to 88.9% of GDP in fiscal 2026.

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ESKOM

Eskom needs to be fixed fast

By Jackie Cameron

Covid-19 containment measures have pushed SA towards a difficult future – and the only hope of changing course is for Eskom to be fixed fast and other reforms to be implemented urgently. Also necessary will be much faster roll-out of Covid-19 vaccines in order to avoid containment measures like lockdowns and other strict rules that put a lid on business activity.

That message has been underscored in the national budget in two graphs that complement the 'hippo mouth' that Finance Minister Tito Mboweni presented in June when he explained that the country is at a cross-roads.

At the time, the upper jaw showed debt spiralling upwards, the rand weakening and capital flight; the lower jaw represented government stabilising debt, increasing revenue collection and stimulating business activity.

Adjustments to the budget tabled in February 2021 show that government officials believe the way to ensure that South Africa faces a brighter future is if there is a rapid increase in electricity supply and the faster implementation of reforms.

Also critical is to speed up vaccination roll-out to avoid waves of Covid-19 infections and lockdowns and other restrictions required to save lives.

Flashback: The 'Hippo Mouth' – SA debt outlook scenarios

SA was in trouble before the pandemic turned off global cash-flow engines, with widespread corruption at state entities, a bloated civil service and policies that tie up businesses in red-tape and favour labour dragging the economy down.

Mboweni isn't solely responsible for the plan to fix SA. Other ANC leaders need to buy in to get the country back on track.

In Parliament on Wednesday, Mboweni warned that public finances are "dangerously overstretched". SA will need to borrow well over R500bn each year and it "owe[s] a lot of people a lot of money". These include foreign investors, pension funds, local and foreign banks, unit trusts, insurance companies, the Public Investment Corporation and ordinary SA bondholders, he said.

SA expects to record its largest tax shortfall on record by the end of the tax year – and a staggering R213bn less than its 2020 Budget expectations.

Personal income tax brackets will be adjusted by 5% to provide relief to mostly lower and middle-income households and corporate income tax will be lowered. To help pay for SA's army of public servants, fuel levies and excise duties on alcohol and tobacco will increase. The government also plans to inject R13bn into improving the capability of the South African Revenue Service to improve tax compliance. Mboweni warned that some taxpayers have been identified for investigation and these individuals can expect to receive an unpleasant letter in the post in April.

Economic scenarios

The National Treasury has modelled two scenarios in addition to the baseline forecast:

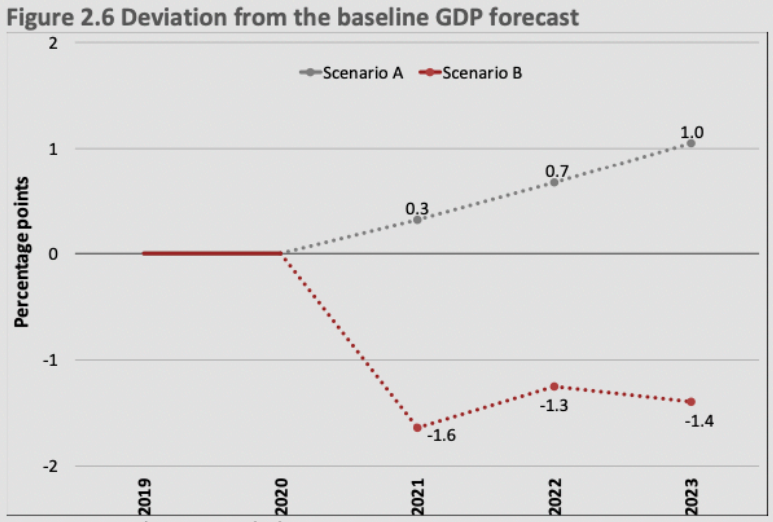
Rapid increases in electricity supply and faster reform implementation boost growth

In *Scenario A*, fiscal reforms discussed in Chapter 3 are complemented by essential economic reforms. Rapid regulatory adjustments, including raising licensing thresholds, could ease the impact of load-shedding on firms and households. Implementation of economic reforms improves confidence and the sovereign risk premium, lowering overall borrowing costs. Private-sector investment and consumption increase, reflecting more durable and sustained growth levels. Real GDP growth reaches 3.6 per cent in 2021. The long-run gains accumulate over time as the reforms are entrenched.

Additional COVID-19 waves and associated mitigation measures throttle the economy

Scenario B reflects the effects of two more waves of COVID-19 infections, assuming the vaccine rollout has a limited effect on stemming the spread of infections. This requires stricter mitigation measures that depress economic activity. In this scenario, vaccine rollout only gains traction in 2022. Economic recovery is delayed and the momentum from late 2020 is reversed, leading to long-lasting effects and further reducing growth potential. The hospitality and tourism, entertainment, trade, services and transport sectors are particularly negatively affected. The economy grows by only 1.6 per cent in 2021, with a base effect into 2022. Production levels remain lower than currently forecast over the long run.

Figure 2.6 Deviation from the baseline GDP forecast



Source: National Treasury calculations

Read full Budget Speech

Eskom can't play the blame game anymore

By Melani Nathan

Since I can remember, Eskom has leaned heavily on South Africans, regularly asking users to reduce their demand. Timers on geysers, low energy usage appliances, and boiling just what you need in the kettle have become very South African habits. Consumers were led to believe that paying ever-increasing tariffs (to cover the costs of plant maintenance) and reducing electricity usage would make a difference.

As Eskom gets the go-ahead to increase tariffs and change its fee structure, it should be noted that this time, the consumer isn't at fault and Eskom can't play the blame game any longer.

In March 2020, South Africa's industry and economy came to a near standstill when the country went into lockdown to prevent the spread of Covid-19. Businesses that ordinarily consumed large amounts of energy ceased their operations. In the 14th week of 2020, Eskom's "Electricity Sent Out" (ESO), which reflects demand, fell to about 32% lower than the same week in 2019. The ESO stayed below the weekly levels recorded in the prior year, except for the week of traditional festive holidays in December.

Despite a large reduction in demand, Eskom has been unable to provide an adequate, stable supply of electricity. Eskom says it is implementing a maintenance programme to improve generation and plant performance but warns that significant improvements can only be expected in September 2021.

Loadshedding has been at the worst level since 2015 (103 days of loadshedding) with 52 days of scheduled rotational power cuts in 2020.

The 'Electricity Availability Factor' measures the operationality of Eskom power plants. This counter was lower than in 2019, showing a deterioration in plant performance and maintenance. As economic activity resumes in the country, the unreliable electricity supply is constraining recovery. By the government's own admission, reform is urgently needed. Eskom's operation Vulindlela aims to:

- Reduce the administrative burden of generation projects smaller than 50 megawatts while ensuring that they meet the necessary environmental approvals and do not risk the stability of the grid.
- Fast track the procurement of additional electricity in line with the Integrated Resource Plan 2019

Read the article here

SA ECONOMY

Treasury's progress on the economic recovery plan

By Justin Rowe-Roberts

Treasury has outlined its progress on the economic recovery plan, which focuses on electricity generation, creating employment, supporting industrial growth, the infrastructure rollout and creating an enabling business environment. South Africa's economy has been ravaged over the last few years, with many of the issues starting within government, creating a domino effect on the rest of the economy.

Finance Minister Tito Mboweni delivers the 2021 Budget Speech in Parliament. [Photo: GCIS]

Electricity generation

The government will ease electricity embedded generation for firms and municipalities, which will be complete within three months. This is positive news for the country's corporate activity, especially sectors heavily dependent on electricity generation. Eskom's inability to produce consistent electricity generation has been one of the many factors behind the depleted South African economy. Many of the large multinational companies in South Africa will be able to generate their own independent electricity supply, which should have a positive knock-on effect to the rest of the economy.

The Independent Power Producer Office will announce successful bids received for emergency power to compensate for Eskom's electricity shortfall. These projects are expected to generate power from July 2022. This is a cause for concern given the immediate need to reboot the South African economy. Firms simply cannot afford to lose any more business hours, especially given the already tough macro-economic environment businesses find themselves competing in.

Creating employment

By the end of January 2021, over 430,000 jobs of varying duration had been supported through the public employment initiative and an additional 180,000 jobs are in the recruitment process. Although this seems promising on face value, it is a far-cry to the number of jobs that have been lost due to Covid-19 and the ensuing lockdowns. The country's unemployment figures were released yesterday, with the unemployment rate ballooning to 32.5%. However, the expanded definition, which includes discouraged workers is around 42.6%, which accounts for 11.1 million people.

South Africa is desperate for structural reforms to be implemented by government to allow the private sector to blossom.

Supporting industrial growth

There have been investments made to support production in various sectors of the economy, however, the quantum of support is minuscule to what is needed in order to drive growth in these industries. The government has lost billions in tax revenue through empty-headed prohibitions on the alcohol and cigarette industries. Yet, in their progress on the economic recovery plan, the Treasury mentions investments into the agriculture and textile industries which collectively total R1.3bn. Although this number might seem large, it will not even touch sides in rebuilding these industries and promoting growth.

Infrastructure rollout

The long-awaited infrastructure spend drive has been estimated at R340bn. This government spend should be a much-needed tailwind for the construction industry, which is one of the largest employers of workers in South Africa. This is arguably one of the more positive pieces of news to emerge from Treasury's economy recovery plan. The R340bn project should grow jobs and drive growth, although no timeline has been communicated, which is a considerable concern given the urgent need for the infrastructure drive to be rolled-out.

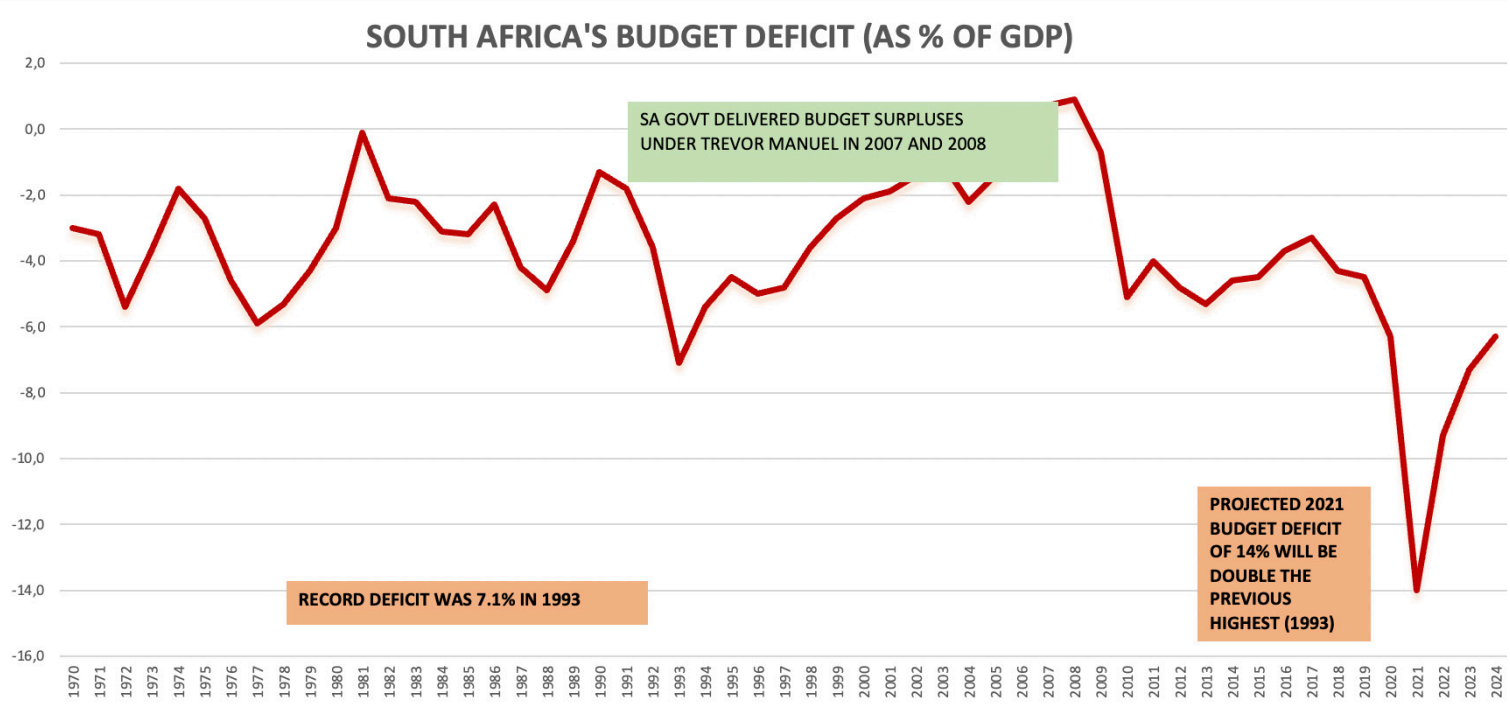
Creating an enabling business environment

The government has defined its plans to grow and promote a beneficial business environment for all companies. This begins with small-to medium-sized firms, many of which have already been consumed as a result of the pandemic. The importance of small-to-medium businesses in the economy cannot be understated, as they are a crucial source of jobs in a country with dire unemployment.

Read also:

- **Expropriation threat is enough to stall economic recovery – Anthea Jeffery**

Graph: South Africa's budget deficit



The 2021 Budget graphs paint an uphill battle for Finance Minister Tito Mboweni and South Africa's taxpaying citizens.