1 Introduction

Madam Speaker, the Budget is about people, not numbers. It is an opportunity for us to reflect on the goals and aspirations of our people. To reflect on the South Africa that now exists; the South Africa from which we have come; and the South Africa which we are building for our children.

We reaffirm our unshakeable belief that we shall overcome the legacy of our past. Our struggle was never only about political democracy. It was and is about equity, about access to resources, about decent housing. It is about schools and the education of our children. It is about wiping away the hunger and the fear on children's faces. It is about lifting the despair of poverty from a parent's shoulders. It is about reaching out to the grandmother so as to ease the years of pain and humiliation etched into her face. It is about eliminating the hopelessness and despair of being jobless. It is indeed, about our families and our communities and the safety and well-being of our society.

As we stride into the new millennium we do so with the confidence that our programme for transformation is well on course. The Budget we place before Parliament today provides an expenditure framework for taking the Reconstruction and Development Programme into the 21st century.

The *Reconstruction and Development Programme* (RDP) is the policy framework within which the Government pursues its objectives. Our strategy for *Growth, Employment and Redistribution* (GEAR) is one of the principal instruments for realising these objectives.

1.1 Our legacy

The RDP and GEAR are as much about addressing the needs of our people today as they are about creating a strong country and economy - so that the legacy we leave our children and grandchildren is one we, and they, can be proud of.

- We have increased the number of children going to school by 10 per cent since 1994. Schools, colleges, universities and technikons enrol 13 million learners – one third of the population.

- We now provide a meal daily to 5 million primary schoolchildren – improving their ability to learn and giving food to children who would otherwise go hungry.

- 500 new clinics have been built, bringing health services closer to 5 million people. We provide largely free health care to 32 million people without medical aid.
- Since 1994, a million women and children in rural areas have gained access to a clean water supply.
- 1,5 million homes have been connected to an electricity supply, creating new income-earning opportunities for over 4 million people.
- 385 000 houses have been built, and 700 000 housing subsidies have been earmarked.
- 900 projects of the community-based public works programme have been implemented, creating about 40 000 job opportunities.

We have built solid foundations. We are proud of how far we have come. We have continued to transform our public services, to make them more equitable and more efficient. We have implemented new arrangements for budgeting by national, provincial and local government. And over the past year, we have consolidated our economic strength, and withstood the global economic storm.

1.2 Budget choices

We know that there are no short-cuts. Achieving sustainable growth and development requires making choices, sometimes difficult choices. It means prioritising and reprioritising. It demands a constant and honest evaluation of what we are doing and how we are doing it. It means that we have to strive to do things better.

Government's resources are finite. We can only plan to spend what we collect in taxes and what we additionally borrow at great cost from the nation's savings. Therefore we have to manage our resources prudently, focusing on the need to ensure value for money.

In addition, we have to root out corruption to ensure that every rand is spent on delivering better services to more people. Corruption eats away at the fabric of society. For that reason we have to do everything in our power to uproot it, in government and business.

Every year the Budget presents government with a unique opportunity to exercise choices to further the objectives embodied in the RDP. The Budget is the practical expression of our policies and programmes. It gives substance to what we can do today, while strengthening the possibilities for a better future for our children and their children.

Government alone cannot achieve the equity and prosperity that present and future generations demand of us. This is a collective endeavour, one that as South Africans we must all embrace. As a nation we must be unequivocal in our commitment to achieving a better life for all. The future holds opportunities we cannot afford to ignore. To ignore them means admitting failure and as South Africans this is something we cannot allow - not for ourselves, not for our children, not for our region, nor our continent.

But in truth the reconstruction and development of our country started a mere four years ago. To address this immense task successfully, we should not underestimate the enormity of the inherited problems and we must recognise that the project will not be concluded in a short period.

As elected representatives of the people we must all be restless about the pace and quality of change. We can and must do more. We must do more to create jobs and prosperity. We must go on extending the opportunity of education, health care, of decent homes and better services. Through all of this we must remain guided by the right of people to dignity and self-esteem.

2 The Medium Term Expenditure Framework

The Budget we place before this Parliament marks a radical departure from the past. Since the Budget is about the present and the future, Government has decided that the Budget should reflect both short-term and long-term decisions.

Consequently, we have developed a three-year Medium Term Expenditure Framework (MTEF) which allows us for the first time to present to this Parliament spending plans for the next three years.

The Medium Term Expenditure Framework is the operational plan by which we give substance to our reconstruction and development endeavours.

2.1 Goals of the MTEF

The first and most important goal of the MTEF is to strengthen political decision-making in the budget process. It has enabled Cabinet to make the link between the budget allocations, and the services that we intend to deliver. It has translated abstract choices about budgets into concrete choices about priorities. The medium term plans we are presenting today reflect those choices.

The second goal of the MTEF is to strengthen co-operative governance and decision making, and provide a budget framework which reflects our shared goals for the country.

The third goal of the MTEF is to make sure that every rand goes further: to deliver better services, more infrastructure, more poverty relief, and more reconstruction.

The fourth goal of the MTEF is to create an environment where public services can plan over the medium term, in the knowledge of how their budget is likely to evolve, improving over time the value for money and so delivering more and better services.

In the years ahead, the analysis underlying the MTEF will provide a tool which relates what we spend to what we buy. As this framework develops, we will focus more and more attention on reviewing the outputs of all spending programmes and activities. The point we want to get to is one where we will not ask Parliament to allocate money without a clear agreement about what that money is going to buy.

Finally, the Medium Term Expenditure Framework makes an important contribution to the transparency and openness of budget policy making.

2.2 MTEF Next Steps

The Budget Review which we publish today sets out spending plans for the national departments for the next three years, and summarises the spending projections of the provincial governments.

The role of Parliament is critical to the MTEF process. We will be voting on the 1998/99 national budget with the knowledge of the projections for the two subsequent years. Parliament therefore has a long lead time to discuss and debate the priorities and forward spending trends.

As in the past, the expenditure estimates for the year ahead, 1998/99, are set out in detail in the *Estimate of Expenditure to be defrayed from the National Revenue Fund* - the so-called "White Book" - which I table here today. The main Appropriations come before Parliament to be voted. Once these and any supplementary proposals are approved by Parliament, they will be published in the *Second and Final Print* of the *Estimate of Expenditure* - the "Blue Book". Government departments are authorised to spend only these amounts approved by Parliament.

3 1998/99 Division of Revenue

This is the first Budget to be compiled under our new Constitution, and to give effect to the new framework of relations between national, provincial and local Government. The 1998 Budget marks the introduction of an equitable share of revenue for local government.

To comply with the Constitution and the Intergovernmental Fiscal Relations Act, I am today tabling the Division of Revenue Bill, which sets out how national revenues are divided between the three spheres of government in 1998/99. It is accompanied by a memorandum that explains this division in detail. A Division of Revenue Bill will be tabled each year with the Budget.

After first setting aside enough to pay the interest costs on the nation's debt and a contingency reserve, funds are allocated to the three spheres of government.

Provinces will receive an equitable share of R79,1 billion in 1998/99, plus various conditional grants, which raises the provincial allocation to over R90 billion. While conditional grants meet specific purposes, the equitable share is designed to effect equity.

Local government's equitable share for 1998/99 will be R1,0 billion.

Each province determines its own priorities and draws up a budget in accordance with the resources it has available. With these powers come responsibility and accountability. Each province must make sure that it budgets adequately for each of the services that it provides.

The new intergovernmental fiscal system is significantly different from previous arrangements. The evolution of the new system has been accompanied by several difficulties. Strengthened cooperation between national government and provinces has contributed to resolving these problems in 1997 and lays a firm foundation for future coordination of medium term budgeting.

4 The Economy

Our policies recognise that a strong growing economy is essential to our vision of jobs, opportunity and a decent life for all. The driving force for growth is investment, investment in factories and machinery, investment in roads and houses and clinics, investment in people and their skills.

Since 1994, physical investment has increased on average by 7 per cent a year in real terms. We have similarly increased spending on education and training. The fruits of these investments are readily apparent in improved productivity, particularly in manufacturing and export-oriented business.

Sustained investment growth is the outcome of sound and credible policies. If we are to see continued growth in investment, then:

- we need to keep private and government consumption spending in check;
- we need to avoid inflation eroding the value of savings and wages; and
- we need to ensure that our capacity to export competitively keeps pace with our demand for foreign-produced goods.

4.1 Economic outlook

The economy grew by 1,7 per cent in 1997. This is below the growth expected at this time last year. We have had to take account of this in determining the resources available for government spending in the new year.

We expect investment growth to strengthen in 1998 and 1999 as export opportunities expand and domestic demand recovers. Strong productivity improvements in manufacturing have laid a firm foundation for steady growth.

We remain confident that growth of gross domestic product (GDP) of about 3 per cent will be achieved in 1998/99, rising to 4 per cent and higher as we move into the next century.

The decline in inflation has been a positive feature of the years since 1994. Persistently high inflation not only erodes incomes and distorts prices, it also entrenches a culture of dissaving because the future value of money loses meaning. We have paid a high price for inflation in both investor uncertainty and prohibitive interest rates for too long.

We project that inflation will fall to 5 per cent by 2000/01. We recognise that prices could stabilise even further, in which case our forward projections would adjust accordingly.

It is pleasing to note that improved productivity has enabled wages and salaries to increase faster than prices in several sectors. The industrial relations environment has improved considerably, in no small measure because of the efforts of the Commission for Conciliation, Mediation and Arbitration. A healthy industrial bargaining framework is one of the strengths on which we are able to build.

Creating an export-oriented economy is a key aspect of our economic strategy. The contribution of exports to GDP has increased from 27,6 per cent in 1994 to 32,8 per cent in

1997. This is a key signal of the success of our economic framework. In the three years ahead, exports are projected to grow strongly and the current account is expected to show a deficit of between 1,5 and 2 percent of GDP.

Investment must be financed by savings. Since we do not generate sufficient domestic savings to finance the levels of investment we need, we must attract foreign savings as well.

Together with the growing interest of foreign firms in direct investment, an inward flow of portfolio investment permits the economy to invest somewhat ahead of our own rate of saving. Non-residents' net purchases of bonds and equities increased from R3,4 billion in 1996 to R14,8 billion in 1997.

Gross gold and foreign exchange reserves increased By R19,8 billion in 1997 to R 36,6 billion at the end of December. This is equivalent to the value of about 10 weeks imports of goods and services.

Since government spends more than it receives in taxes and other revenues, it has to borrow. Like any household we have to borrow to finance the additional expenditure, and the more we borrow the more we have to pay in interest and the less there is available for other things.

High levels of public debt also put an enormous burden on future generations. If we borrow now, it is our children who ultimately have to pay.

Sound fiscal management is a key component of our economic policy. One important measure of this is the fiscal deficit. This government has succeeded in bringing down the deficit from 10,2 per cent of GDP in 1993/94 to a projected 4,3 per cent in 1997/98. We have done this whilst extending more and better services to more people.

The gap between revenue and expenditure in the budget tabled today is 3,5 per cent of GDP. We anticipate that the national budget deficit will be kept to 3,0 per cent in the subsequent two financial years.

4.2 Exchange Controls

In line with our policy of exchange control reform, Government will seek to ensure that the lifting of the remaining exchange controls occurs without placing undue pressure on the balance of payments.

The changes announced today have two key objectives: to strengthen South Africa's commitment to the Southern African Development Community (SADC) region through measures designed to facilitate regional capital market integration; and second, to increase the limits on the activities of individuals, corporations and financial institutions.

For new investments in SADC, South African corporations are currently allowed to transfer up to R50 million. This limit is now increased to R250 million. The limit of R30 million for offshore investment is now increased to R50 million.

In terms of existing policy private individuals are permitted to invest R200 000 per person offshore, provided they are over 18 and taxpayers in good standing. We are now increasing this limit to R400 000. However, instead of the current process which requires a declaration of good standing, a clearance certificate will have to be obtained from SARS prior to the approval of any foreign investment.

A range of other measures will also be introduced today. I have asked the South African Reserve Bank to set these out in a press statement.

5 The Spending Plans

Madam Speaker, I now turn to our spending plans for the next three years.

5.1 The Budget and the RDP

The expenditure estimates for 1998/99 are summarised in the Budget Review, together with forward estimates for the 1999/00 and 2000/01 years. The 1998 Budget and the three-year MTEF estimates give effect to our shared commitments, which are:

- Meeting the basic needs of the people;
- Accelerating infrastructure development;
- Laying the basis for sustained economic growth and job creation;
- Developing our human resources;
- Ensuring the safety and security of the citizen and the state; and
- Transforming the organs of government to reflect the developmental and people-centred nature of our democratic state.

The national Budget provides for expenditure of R201 billion for 1998/99, which is 6,4 per cent above the revised 1997/98 expenditure level. After meeting the cost of state debt, spending will be R159 billion.

Of this total, over 60 per cent will go to social services:

- welfare and social grants will take up nearly R19 billion, or 12 per cent of non-interest spending;
- health services will get R23 billion, which is 14 per cent;
- more than R45 billion will be spent on education, 28 per cent; and
- spending on housing programmes and subsidies will remain above R3,5 billion a year.

But it is not just through social services that we achieve our RDP objectives:

- capital spending on water schemes and related infrastructure will be R1,6 billion in 1998/99, increasing to R1,8 billion in 2000/01;
- spending on land redistribution and land reform will grow from R685 million to R967 million by 2000/01; and
- allocations for poverty relief projects will rise from R500 million in 1997/98 to R800 million in 2000/01.

Madam Speaker, we inherited large backlogs in our social services. Over the last two years, we have increased non-interest spending by 18 per cent, to enable us to address some of these backlogs. Growth over the next three years will be more modest, building on this substantial increase that has already occurred.

5.2 Welfare

One of the most redistributive spending programmes is social security and welfare. Social grants are paid to over 3 million beneficiaries, and are a crucial source of income to poor households, particularly in rural areas. Welfare and social security spending represents Government's primary investment in poverty alleviation.

We have substantially increased spending on welfare - from R14 billion in 1995/96 to R19 billion in 1998/99. And we have budgeted for it to increase further to over R21 billion in 2000/01.

In a drive to uproot corruption and eliminate fraud, the Department of Welfare and provincial authorities have embarked on a project to re-register about 3 million beneficiaries of social grants and pensions. This process will enable us to update and correct the data in the system, and so eliminate duplicate claims, ghost beneficiaries, syndicates and cross-provincial payments. For those who are genuinely entitled to benefits, it will mean a more efficient payment system.

5.3 Health

The main increase in health spending occurred in 1996/97 when spending increased by 24 per cent on the previous year, from R 17 billion to R 21 billion.

A new conditional grant mechanism has been put in place for support of health professional training and research and for central hospitals. Funds have been set aside for initiating a hospital rehabilitation programme. Provincial health expenditure is projected to increase by around 5 per cent a year over the next three years.

5.4 Housing

Provision of housing under the capital subsidy scheme has gained momentum, with expenditure reaching between R250 million and R300 million monthly in 1997/98. The lead time for approval of a housing project to its commencement has been reduced from eighteen to under ten months.

5.5 Land

We have initiated three major land reform programmes:

- **first,** redistribution of land - to meet the need for land, and to reverse the unequal racial geography of the country;
- **second,** restitution of land rights - to restore land which was taken from people by apartheid after 1913; and
- **third,** tenure reform ? to provide secure land tenure and to resolve overlapping and conflicting rights and claims to the same land.

5.6 Water and sanitation

The RDP water and sanitation programme will bring 25 litres of drinkable water per person per day to all communities by the year 2004. Over 1 020 water supply projects have been identified, are underway or have been completed, bringing safe water to 8,9 million people.

The working for water programme clears invading alien plants. These are labour-intensive programmes mainly located in areas of extreme poverty. This is a valuable poverty relief initiative. Employment creation is sustained through the restoration and maintenance of cleared areas. Some 7 000 hectares have been cleared and 38 000 jobs created, mainly benefiting women.

5.7 Public Works

The community based public works programme adopted in 1994 aims to contribute to infrastructural development through labour-based construction, especially targeting women. Over 900 projects have been implemented, mainly in poor rural communities, creating over 40 000 job opportunities.

5.8 Education

This Government's commitment to human resource development is evidenced by the fact that we continue to spend more on education than on any other function. Education spending accounts for more than 25 per cent of non-interest spending and approximately one-third of public sector employment.

Spending is estimated to have increased by a striking 25 per cent in 1996/97, raising significantly the base for education spending. Education spending is set to increase further, from R45 billion in 1997/98 to over R50 billion by the end of the MTEF period.

5.9 Investment in infrastructure

Capital expenditure financed by the national and provincial governments is projected to increase from R14,8 billion in 1997/98 to R16,3 billion by the end of the MTEF period. Capital spending by public corporations is also expected to grow over this period, bringing the projected contribution of the public sector to gross domestic fixed investment to about R56 billion in 2000/01, or about 7 per cent of GDP.

5.10 Capital spending

Madam Speaker, as well as social services, our RDP goals commit us to substantial investment in the nation's infrastructure. This is particularly important if we are to deliver services more equitably. From the national budget there are a number of substantial capital spending programmes. These include:

- Transfers to local government for municipal infrastructure projects, rising from R583 million in 1998/99 to R990 million in 2000/01;
- A new hospital rehabilitation programme, beginning with R100 million in 1998/99 and increasing to R500 million in 2000/01;
- Allocations for capital spending on various land and buildings projects on the Public Works vote of R1,6 billion in 1998/99 increasing to R1,7 billion in 2000/01;
- Capital spending on the Transport vote amounting to R742 million in 1998/99, rising to R 1,1 billion in 2000/01, mainly for roads projects; and
- an additional R300 million for infrastructure development, to be allocated once project proposals have been considered early in the fiscal year.

5.11 Private Public Sector Partnerships

The Government aims to extend the delivery of basic services by bringing private sector finance into infrastructure projects. Business partnerships are encouraged between municipalities and private concerns for financing, extending, operating and management of infrastructure services. A total of 18 pilot projects have been established in urban and rural areas country-wide, including water, sanitation, refuse collection and transport projects. During the 1997/98 financial year, the private sector invested R1 billion in these projects – R5 for every R1 spent by Government.

5.12 Expenditure on economic services

The Budget includes several major spending programmes in support of economic development:

- Spending on the Labour vote, which includes the phasing in of the skills development strategy, is projected to rise from R746 million in 1998/99 to R1 281 million in 2000/01;

- The Trade and Industry vote of R2 370 million in 1998/99 makes provision for increased support for small business development, industrial supply-side measures and export promotion and allocations for industrial research and technology transfers;
- Estimated expenditure of R727 million of the Department of Agriculture in 1998/99 will support agricultural research and extension services, with an increasing emphasis on the needs of emerging and small-scale farmers; and
- Tourism promotion receives R71 million of the Environmental Affairs and Tourism vote in 1998/99.

5.13 Safety and security

Government plans to increase spending on justice, police and prisons by an average of 7,8 per cent a year over the MTEF period, together with improved coordination between components of the criminal justice system and a renewed focus on integrated community policing.

Spending on safety and security is projected as follows:

- Allocations to the SA Police Service increase from R13,7 billion in 1998/99 to R15,2 billion in 2000/01;
- The Justice Department is budgeted to spend R2,2 billion in 1998/99, increasing to R2,7 billion in 2000/01;
- The Correctional Services vote increases from R4,5 billion to R5,4 billion in 2000/01; and
- The Defence vote is R10 billion in 1998/99, increasing to R11 billion in 2000/01.

5.14 Public Service Restructuring

The pace of change in the public service will be accelerated in 1998. The effectiveness of the public service is vital for the realisation of Government's vision of improved and more equitable service delivery. The right-sizing of the public service is essential for the success of the RDP. As the President said in his opening address to Parliament: "Apartheid South Africa was over-governed and over supervised. The size of the public service had nothing to do with public service. Government is not an employment agency. Put in simple terms, we need to cut spending in personnel."

Transformation requires that we have a motivated, well-trained and cost-effective public service dedicated to serving the public. The Budget sets aside several allocations to build capacity and thereby strengthen this transformation process:

- R100 million on the vote of the Department of State Expenditure for enhancing financial management in national and provincial departments.
- R200 million on the vote of Education and R100 million on the vote of Welfare to contribute to improved management and modernised information systems in the provinces.

6 Revenue proposals

Our spending commitments, unhappily, have other implications. I now turn to the revenue proposals for 1998/99.

6.1 Tax administration

Government aims to maintain and strengthen a tax system that is fair, equitable and efficient. Over the past three years we have made significant progress in removing distortions that encourage tax structuring and interfere with tax fairness. Our tax proposals this year build on this programme.

Recognising that without good administration, tax policy and tax law cannot be given practical effect, we have given priority over the past two years to building the administrative capacity of the South African Revenue Service (SARS).

The resilience of revenue collections in 1997/98, despite a slowdown in economic performance, is testimony to the success of these reforms.

6.2 1997/98 revenue outcome

The revised revenue estimate for 1997/98 is R162,6 billion, which is 0,4 per cent higher that the original budget estimate and constitutes 26,5 per cent of GDP.

This includes certain once-off repayments announced in the Adjustments Budget. Excluding these items, total receipts are expected to be within 0,1 per cent of the corresponding 1997 budget estimate. Details are set out in the Budget Review.

6.3 First print Estimate of Revenue

Before taking into account tax changes, expected revenue in 1998/99 is estimated as R174,3 billion.

Today's tax proposals bring the estimated revenue for the year to R177,6 billion, which is 26,5 per cent of GDP, unchanged on last year. The main proposals are as follows.

6.4 Tax rates for individuals

In 1997/98 we spent R2,8 billion on providing tax relief to lower income earners and restructuring personal income taxes.

We now propose to go much further. Bracket creep occurs when salaries and wages increase with inflation and tax thresholds are left unchanged, putting taxpayers in higher tax brackets and reducing after-tax income in real terms. In 1998/99 we will eliminate bracket creep and by doing so we will put R3,7 billion back in taxpayers' pockets.

This means, for example, that a person under the age of 65 and earning R25 000 per year will pay R300 less tax per year – a 12 per cent reduction in tax liability.

It is proposed that the primary rebate be increased from R3 215 to R3 515 and that the rebate in respect of individuals who are 65 years of age and older be increased from R2 500 to R2 660. The marginal rate applicable to taxpayers with taxable income in the range from R46 000 to R60 000 is reduced from 41 per cent to 39 per cent. The number of income brackets is reduced from 7 to 6. The level of income where the maximum marginal rate of 45 per cent is reached, is increased from R100 000 to R120 000.

Bracket creep affects lower and middle income taxpayers particularly severely, and so nearly half of the relief granted will go to individuals with taxable incomes of less than R60 000 per year.

Members of the House will remember that SARS was asked for the current year to collect an additional R2,5 billion. A base broadening programme is in progress, bringing more taxpayers onto the register and raising awareness of the penalties attached to non-compliance. Next year the revenue services expects to collect an additional R2 billion by way of efficiency gains and broadening the tax base. It is this effort that enables Government to make these concessions. Improved tax administration makes lower rates of tax on individuals possible.

6.5 Publication of names

On the other hand, tax evasion imposes higher tax rates on honest taxpayers.

It is only right that those who pay their due should know whose tax default they are paying for. It is accordingly proposed that the tax laws should be amended to provide for the publication of the names of persons convicted of offences in terms of these laws.

6.6 Declaration of good standing

Last year it was announced that an individual or company wanting to avail themselves of foreign currency, would be required to submit a declaration of good standing. About 4 800 investors invested approximately R610 million offshore up to 2 January 1998. Of these, it appears that 17 per cent are taxpayers who had not submitted their returns timeously, were not registered for tax purposes, or are in arrears.

These irregularities are being followed up by SARS. Changes to the procedures with regard to the declaration of good standing will be implemented. A clearance certificate will now have to be obtained from SARS prior to the approval of any foreign investment.

6.7 Tax avoidance

Aggressive structuring of salary packages erodes the tax base and puts lower paid workers who do not enjoy the same degree of tax mobility at a disadvantage. Moreover, it discriminates against smaller firms who generally do not have the capacity to manage complex remuneration packages.

Consistent with the policy stance adopted in the 1997 Budget and in line with the recommendations of the Katz Commission a number of additional measures are introduced in the 1998/99 fiscal year.

6.8 Medical Aid Schemes

We have become aware that increasingly contributions to medical fund schemes are being used to structure salary packages in a way that was never intended by the Income Tax Act. In its Sixth Report the Katz Commission considered this issue and recommended that the deductibility of the employer’s contribution be limited on a rand for rand basis.

The principle set out by the Katz Commission has been accepted by the Portfolio Committee on Finance. Having taken account of their deliberations, as from 1 April 1998, the amount by which the employer’s contribution to a medical scheme on behalf of an employee exceeds two-thirds of the total contribution, will be taxed as a fringe benefit in the hands of the employee. This proposal is expected to yield R700 million in 1998/99.

6.9 Residential accommodation

Last year certain measures were proposed to determine the taxable value of residential accommodation provided to employees by employers. To address uncertainties about the impact of the proposals, they were held over until 1998. Discussions with various interested parties have been held and agreement has been reached. Details are set out in the Budget Review.

6.10 Taxation of trusts

Madam Speaker, it is our view that trusts have become widely used for income-splitting so as to reduce the tax rate at which income is ultimately taxed. The provisions of section 25B are also used to channel losses incurred as a result of the deduction of expenditure and allowances in the trusts to their beneficiaries, who then set off these losses against their income. The use of such losses for tax purposes has become a popular way of structuring financial transactions.

In view of the widespread use of trusts as business entities and to split income, a full investigation into the taxation of trusts will be undertaken by SARS this year. Two initial steps in reforming the taxation of trusts will be implemented in this fiscal year.

First, the provisions of section 25B of the Act will be amended to provide that the losses of the trust may for tax purposes not be allowed to flow through to the beneficiaries. They can, however, be retained in the trust, where they may be carried forward to the following tax year to be set off against the income of the trust in that year. This proposal will apply in respect of all new trusts created from 11 March 1998. As far as existing trusts are concerned, it will apply from years of assessment commencing on or after 1 January 1999.

Second, it is proposed that income vesting in the trust as a taxpayer (not the income vesting in any beneficiary of the trust) be taxed at a rate of 35 per cent on taxable income not exceeding R100 000 and at a rate of 45 per cent on the amount of taxable income in excess of R 100 000.

An exception is proposed in the case of a trust created solely for the benefit of persons who suffer from a mental illness as defined in section 1 of the Mental Health Act, 1973; or a serious physical disability, where such illness or disability incapacitates the beneficiary from earning sufficient income to maintain him- or herself.

These changes will apply from years of assessment commencing on or after 1 March 1998. It is estimated that these proposals will yield an amount of R150 million during the 1998/99 financial year.

6.11 Tax on retirement funds

The tax on retirement funds was introduced following the recommendations of the Katz Commission. It was introduced at a rate of 17 per cent on certain categories of income with effect from 1 March 1996.

This tax was introduced as an interim measure and is presently being investigated in its totality to determine the most appropriate method of taxation of the flow of funds through retirement funds to the ultimate beneficiaries. No changes have been made to the rate since its introduction.

With effect from 1 March 1998, the rate will be increased from 17 to 25 per cent. It is expected that this will yield an additional R1,2 billion in 1998/99.

6.12 Fuel Levy

It is proposed to increase the fuel levy on both types of petrol as well as diesel by 10 cents per litre with effect from 1 April 1998, coinciding with the monthly fuel price adjustment, if any.

6.13 VAT

It is evident that serious VAT evasion is taking place through false declaration of exports to neighbouring countries, particularly of cigarettes and liquor. In order to curb this activity, it is proposed that liquor and tobacco products be excluded from the existing export incentive scheme. The effect thereof will be that the zero-rating in respect of such products will only apply in relation to exports where a South African vendor consigns or delivers goods to purchasers outside South Africa. The proposals will be introduced with immediate effect and a Government Gazette will be published to announce the necessary changes to the scheme.

6.14 Excise duties

Madam Speaker, let me now turn to the taxing of indulgences.

6.14.1 Tobacco

Excise duties on tobacco products are an exceptional case. The health authorities recommend duties on these products at 50 per cent of the retail price. In order to retain a tax incidence of 50 per cent including VAT it is proposed that excise duties on tobacco be increased by 29 per cent. Smoking will therefore cost an extra 46 cents for a packet of 20 cigarettes. Pipe tobacco will cost an extra R2,11 a kilogram.

6.14.2 Alcoholic beverages

This year's Budget aims to move further towards taxing alcohol products in relation to their alcohol content, while also bringing the tax incidence of beer, wine and spirits in line with broad international benchmarks. What does this mean?

It means that:

- a 340ml can of beer will cost 1,6 cents more;
- ciders will increase by 9 cents per 340ml can;
- cane spirits go up by 65,7 cents per 750ml;
- grain spirits increase by 48,2 cents per 750ml;
- unfortified wine goes up by 5,9 cents per 750ml;
- there is no change to the excise on sorghum beer.

6.15 Demutualisation charge

Madam Speaker, there is one further matter I wish to place before the House.

As is generally known by now, South Africa's two largest mutual insurers have announced their plans to demutualise. In this process the policyholders of these mutuals will become entitled to shares in proprietary life insurers. The effect is that policyholders who at present cannot access their interest in the free reserves of these mutuals, will receive shares which can be traded in the market.

The free reserves of these entities have been built up over many decades as a result of the favourable tax treatment that mutual insurers have enjoyed and are attributable to contributions made by generations of erstwhile policyholders. Today's policyholders will in effect receive a windfall gain over and above their actuarial interest in the mutual insurer.

Government has decided to impose a once-off charge on the shareholders who will receive the windfall gain.

The charge will be levied at the rate of 2,5 per cent on the free reserves of the mutual insurer as at the date of demutualisation, but will be collected by the new proprietary company on behalf of the shareholders.

Because this is a once-off charge, we will not use this revenue to finance current expenditure. Instead it will be used to capitilise a fund to be known as the Umsobomvu Fund.

6.16 Job creation

Madam Speaker, unemployment is not a mere statistic on the government's report card. Joblessness goes to the core of the well-being of our society. It destroys peoples dignity, it eats away the fabric of our communities, it means hunger and poverty, it denies people opportunities, and it robs children of their right to be children, their right to dream and to have a future.

South Africa is undergoing a demographic transition with profound consequences for social policy and economic transformation. These changes require us to focus even more acutely on job creation. The number of young people leaving secondary or tertiary education is estimated to be around 450 000 a year. This is likely to increase as the school system improves and the demographic peak reaches school leaving age. The challenge of youth unemployment is therefore one we cannot afford to ignore.

6.17 Umsobomvu Fund

Job creation is a national project that requires the talent, creativity, energy and the unwavering commitment of all our people. Unless we embrace this challenge collectively we will forever deny our country its true potential. Sustainable growth and development demands opportunities not hand-outs, it requires courage and commitment and responses which transcend narrow interests. In partnership with labour, business and organisations of civil society, the government proposes to create a new vehicle for development.

At the dawn of the 21st century, our nation must invest in its young people, arouse their skills potential, invigorate job creation and secure better lives for our children.

The Umsobomvu Fund is one instrument that government is offering at the Presidential Jobs Summit later this year. In doing so we are responding to the key objective of the Summit which is to convert the challenge of unemployment into the opportunity for job creation.

7 Conclusion

Madam Speaker, the Budget we present today is part of the first-ever Medium Term Expenditure Framework. This important change makes for greater certainty in planning and prioritising. As I have explained, the MTEF also radically alters the manner in which Parliament will participate in budget-making in future. The MTEF is the product of a high level of interaction within government, through the sectoral teams which were established, and through the more intensive Cabinet participation. The choices we have made are the result of a difficult process of prioritisation which ensures that the RDP is now fully integrated into our expenditure plans.

But this Budget also develops the choices and priorities that were reflected in the Budget last year. We are continuing to give increasing priority to social transformation.

On the revenue side are a number of significant changes – we have progressed further with the programme for equity in tax policy by eliminating the tax shelters which have been exploited by some. Moreover, we have succeeded in removing the effects of bracket creep, thereby putting an additional R3,7 billion in the pockets of working people.

We have complied with the Constitutional requirements for inter-governmental fiscal relations. The tabling of the Division of Revenue Bill, and the strengthening of the institutions like the Budget Council, place co-operative governance on a much sounder footing.

The initiative we took last year in respect of the relaxation of exchange controls has now been advanced. We are convinced that this will again have as positive an impact on capital inflows.

Finally, we have used the opportunity created by the demutualisation to create the Umsobomvu Fund. The use of the proceeds of this fund for youth employment and development will have a long-lasting benefit for all of South Africa.

This Budget was compiled by the careful weighing of competing options between different development programmes. It was shaped at a time of change in the South African economy which, in some respects, had limited the options available. This Budget places us in a position to take the RDP well into the next century. The MTEF places South Africa in the ranks of a small group of countries which have multi-year fiscal planning.

It is the product of a truly collective effort by Cabinet which I am privileged to place before this House.

It is appropriate that I conclude by expressing gratitude to those who have contributed so selflessly to these achievements:

- The President and the Deputy President of the Republic and to all my Cabinet colleagues for the understanding, engagement and support;

- Deputy Minister Gill Marcus who shared in the load and who has taken special responsibility for the building of an efficient South African Revenue Service;

- 'Team Finance', comprised of the nine MEC's for Finance who battled through this past year with us and who took responsibility for crafting MTEF's in the Provinces;

- Those support structures whose contributions have made a profound impact on that which we present today – Dr Chris Stals and his team at the SA Reserve Bank; Mr Murphy Morobe and the Financial and Fiscal Commission; Mr Jayendra Naidoo and Nedlac; and Professor Michael Katz and the Tax Commission.

- Our interactions with parliament have strengthened our performance and for managing this we must thank Mr Sipho Mpahlwa and Mr Sintle Fenyane , chairpersons of the Standing and the Select Committee on Finance, respectively.

- The leadership and staff of the three departments which are so centrally involved in budget-making:

    - Mr Trevor van Heerden, the newly appointed Commissioner for the Revenue Service and the staff of SARS for having delivered on the revenue targets and who committed themselves to further improvements in the efficiency of collections;

    - Mr Cassim Gassiep, the newly appointed Director General of State Expenditure (and his predecessor Mr Hannes Smit) and his team for the efforts at both controlling expenditure and producing the White Book;

    - Ms Maria Ramos, Director-General for Finance and to her able team in the Budget Office, an energetic team of people who have foresaken family and sleep in order to produce that which we present here today.

- My immediate family and the extended family, which is what the Ministerial staff have become;

- Finally, to each one of you, both in this Chamber and at home, for your patience in listening to us this afternoon.

It is appropriate, Madam Speaker, that I conclude with a reminder of what our President said to us from this podium a few weeks ago, "*We cannot divert from the course we have chosen. There is no other route to sustainable development.*"

8 TABLING

All that remains for me to do is to lay the following documents on the Table:

(1) Estimate of Expenditure to be defrayed from the National Revenue Fund during the financial year ending 31 March 1999 [RP2-98].

(2) Estimate of Revenue for the financial year ending 31 March 1999 [RP3-98].

(3) Taxation proposals: Income TaxTaxation proposals: Customs and Excise [Taxation proposals in respect of Customs and Excise laid upon the Table at 15:….].

(4) Division of Revenue Bill [B …-98] (in terms of section 10(1) of the Intergovernmental Fiscal Relations Act, 1997 (Act No 97 of 1997)).

(5) Budget Review, 1998 (including "Annexure E: Memorandum to Accompany the Division of Revenue Bill" tabled in terms of section 10(5) of the Intergovernmental Fiscal Relations Act, 1997 (Act No 97 of 1997)).

(6) Executive Summary of "Annexure E: Memorandum to Accompany the Division of Revenue Bill" in the Budget Review.