Budget Speech

2006

Minister of Finance

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There are no joys without mountains having been climbed. There are no joys without the nightmares that precede them and spring them into light…

The joys that spring from the challenges are profound. And the challenges will always be there. As long as there are human beings there will be challenges. Let no one speak (to me) of frontiers exhausted, all challenges met, all problems solved. There is always the joy of discovering, uncovering, and forging new forms, new ways,…

Ben Okri, A Way of Being Free, 1997

Madam Speaker

In tabling the 2006 budget proposals for the further consideration of this House, we also place before the nation an account of the mountains we have climbed and the frontiers before us. Our budget proposals are closely bound up with this journey, with our conception of democracy, with the progressive realization of social and economic freedoms to which we aspire, with our understanding of the service delivery obligations of government alongside the development impetus of active citizenship, our faith in these joys and these challenges.

We are able to report that the economy expanded by about 5 per cent last year, and we anticipate continued growth of about 5 per cent a year over the period ahead. Business confidence is strong, investment and employment creation have gained momentum, inflation and interest rates remain moderate. The revenue outcome for 2005/06 will be about R41 billion more than we expected this time last year, creating room for both expenditure growth and tax relief in this year's budget.

"Umnotho ukhulile, asivuneni, inala ifikile!" Nhlanhlayenkosi Mhlungu writes: "This is the year of plenty, when all South Africans will reap the fruits of economic growth!" ***TLALA O KOTSING!***

We have, as always, received a great deal of advice on what might be done in these happy circumstances. Government departments have tabled a thousand new service delivery proposals and expanded spending plans. Taxpayers have promised to invest more and work harder if more money is left in their hands. Citizens and civil society organisations have again been generous in providing tips for Trevor, highlighting frankly and precisely what the frontiers and challenges are that have yet to be addressed, that all possible joys may be uncovered. Sipho Makola proposes, for example, a tax deduction on dating expenditure: "It's really difficult lately to find a woman without first dating her and such expenditure is sometimes beyond our budgets. We either date or forever remain bachelors…"

Madam Speaker, to budget is to choose. Democracy and freedom have laid on this House the solemn duty of safeguarding the transparency and integrity of these choices.

The budgetary choices we make give life and meaning to the Age of Hope of which President Mbeki so rightly spoke in the State of the Nation Address. The budget tabled here today gives practical effect, Mr President, to our programme of social cohesion, and in particular to prioritising the needs of the poor, for that is what it means for rich and poor to share the privilege of a common nationhood.

There is no simple index of fiscal solidarity that measures progress along this redistributive trajectory. The "social wage" comprises many overlapping areas of public investment and service delivery.

This is a mountain to be climbed in stages, joys to be reached step by step.

I refer, for example, to the growth in income support to vulnerable households through social security and social assistance grants. This has been the fastest growing category of government expenditure since 2001, and now amounts to R70 billion a year, 3,4 per cent of GDP, and reaches more than 10 million beneficiaries. Social grants contribute more than half of the income of the poorest 20 per cent of households, and have doubled in real terms over the past five years. Recent survey data has provided clear empirical evidence of significant improvements in child nutrition associated with the child support grant, which in turn positively affect cognitive ability and school outcomes. ***TLALA O KOTSING!!***

I refer also to the expansion of primary health care since 1994. More than 1300 clinics have been built or upgraded, 2300 have seen new equipment installed, childhood immunization programmes have been extended, and our health services receive 101 million patient visits a year – about 8 or 9 visits per family. HIV treatment programmes are in place at 192 health facilities. Over the MTEF period ahead, 46 hospitals will undergo physical rehabilitation and administrative overhaul as part of the nationally coordinated Hospital Revitalisation Programme.

I refer to steady progress in school enrolment, to the fact that 64 467 classrooms have been built in the last 10 years, that 114 000 study awards were made by the National Student Financial Aid Scheme in 2005, that 207 497 young people have registered for learnerships since the introduction of the skills development programme, funded in part through tax subsidies. School fees will be phased out in low-income communities this year, and Minister Pandor confirms that in three weeks time the last remaining seventeen trees will no longer substitute for classrooms.

I refer to the fact that 3½ million homes have been connected to the electricity grid since 1994, water supply infrastructure now reaches some 90 per cent of the population and the sanitation backlog is steadily declining. R23 billion will be spent on government subsidies for 500 000 housing units over the next three years, complemented by rising expenditure on community sports facilities, police stations, transport infrastructure and administrative services.

I refer to our commitment to ensure that no household is denied the simple dignity associated with basic water, sanitation and energy supplies. Data supplied by the Department of Provincial and Local Government indicate that 165 water service authorities currently provide 3,9 million poor households with free basic water, and free basic electricity reaches 2,9 million households.

In 2005 the government spent R4800 a year, per person, on community and household services and income transfers, compared with R2000 a decade ago – an increase of nearly 50 per cent in real terms.

What has made this possible? There are no joys without mountains having been climbed…

Part of the answer lies in financial policy and debt management: in 1998, for every rand of revenue collected, 24 cents was spent on servicing state debt; in 2005 the debt cost 14 cents, and by 2009 it will be 10 cents.

Part of the answer is in the substantially improved growth of the economy on the strength of sound macroeconomic, fiscal and monetary policies. Part of it is in the considered reprioritisation and forward-looking policy reforms that underlie our budget choices.

But the greater part is in the quality and energy of people working together, citizens and civil servants, community activists and businesspeople, workers and managers. It is not the rand cost of public services that counts in the daily experience of women and children, workseekers, victims of crime, the elderly or those with disabilities. It is the quality of care in the paediatric ward, the time it takes to process a business application, the effectiveness of court processes, the attention to special learning needs in the classroom, that make a difference to people's lives and well-being. As we celebrate the progress made in meeting household and community needs, we are also conscious of the work that lies ahead. Quality of care and efficient public services still require greater effort from all of us: improved public administration, and also the kind of citizen activism that contributes constructively to community development. As we give consideration to another expansionary budget framework for the period ahead, we need to pay tribute to the special character of selflessness that lies behind social progress and development – people working together, because that is what is needed to get things done.

I have in mind people like the 22-member team known as the Madida Hotshots, led by Christopher Kasayi from Jansenville in the Eastern Cape, formerly unemployed and now skilled and dedicated firefighters in our Working on Fire programme, who joined their counterparts from the Western Cape in bringing under control 17 forest fires in the Boland and Table Mountain areas during the past month, under difficult and hazardous conditions.

I have in mind 63-year old court maintenance officer Hester Kok, and her network of community workers in Kalahari communities such as Askam, Rietfontein, Philandersbron and Loubos. Through the efforts of local volunteers like Gwendolene Gooi of Rietfontein, also known as "Blommetjie", people in these very remote settlements are assisted to receive maintenance payments on predetermined dates and without the exorbitant expense and huge inconvenience of a monthly taxi trip to Upington.

I have in mind people like Jabulisile Gumede, one of the founders of the Inanda Greening Project, which has established mini-nurseries at 30 schools in the areas of Inanda, Kwa-Mashu and Ntuzuma, contributing to local vegetable gardens for school feeding and income generation.

I have in mind Galeshewe community member Peter Nkota, who assists the police in visiting schools in the area twice a week to alert children to the risks of alcohol and sexual abuse, and has worked with youth leaders and justice officials to create a new mobile court to deal more promptly with local crime.

As we reflect on our macroeconomic performance, tax proposals and aggregate spending plans for the MTEF period ahead, Madam Speaker, I know that Members of the House, and others listening at home or in places of work, will join me in remembering the special efforts of ordinary citizens, and the dedicated work of our teachers, doctors and nurses in weekend casualty wards, police men and women fighting crime, administrators creating order out of chaos: those who every day live the nightmares that precede our joys, and turn them into light.

KUMPONDO ZANKOMO!!
MAHUBE A NAKA TJA KGOMO!!

Economic outlook

Growth and international developments

Madam Speaker, the South African economy has grown more strongly over the past year than we anticipated. Our expectation in February last year was that gross domestic product would increase by 4,3 per cent in 2005; the revised estimate is 5 per cent. This follows a significant upward adjustment in growth for the previous year published by Statistics South Africa last November, and is further evidence that both economists and statisticians, as a personality-type, are prone to pathological caution.

Indeed, when the full accounting is done towards the end of this year, we may find that our economy grew by 5½ or 6 per cent last year. The extraordinary pace of vehicle sales, rising house prices, traffic congestion and VAT receipts all point towards this conclusion. Rising employee tax registrations and the records and financial performance of the Unemployment Insurance Fund confirm that employment is rising strongly. Labour force and household survey data indicate that job creation is now proceeding at about 350 000 new opportunities a year, or about 1 500 new jobs every working day.

This is in part the outcome of economic restructuring and policy reforms over the past decade. Stronger economic growth now rests on a stable macroeconomic foundation and healthy investment trends.

Incomes and opportunity are still profoundly unequal in our economy, however. Growth brings with it broadening participation in the world of work and improved opportunities for those who rely on marginal and vulnerable second economy activities. To overcome poverty and inequality, the pace of this restructuring needs to accelerate.

EKUNYAMEZELENI KUKHO UMVUZO!!

We have indeed already achieved a considerable acceleration in sustainable growth, but we are mindful that the present buoyancy of business and consumer confidence is, in part, a cyclical trend. Commodity prices are at record levels, supported by strong growth internationally, global productivity growth is robust, while inflation and interest rates have remained at moderate levels. Preliminary indications are that South African exports grew by over 12 per cent in real terms last year, which is a remarkable turnaround after several years of disappointing trade performance.

However, our appetite for imported goods and services has also grown strongly, and so the deficit on the current account of the balance of payments has deteriorated from less than 1 per cent of GDP in 2002 to over 4 per cent last year. We rely increasingly on capital inflows from abroad to finance the excess of expenditure over the value of domestic production.

There is no shortage of liquidity internationally, and so inflows on the financial account comfortably exceeded our requirements in 2005. The Reserve Bank's gross foreign exchange position improved from US$14,9 billion at the end of December 2004 to US$22,2 billion in January 2006. This is a healthy financial development, but we cannot assume that global circumstances will always work in our favour. As has happened several times in the past decade, financial flows could swing away from emerging markets, and these enormous shifts in global money cannot be predicted. Commodity prices may stay high for another year, perhaps several years, but one day they will retreat. We are conscious of the disquiet of many manufacturers about the current strength of the rand, but on the other hand, we know from past experience that a rapid exchange rate depreciation would have disruptive effects on prices and balance-sheets. Our task, as government, as households, as the business sector, is to turn the opportunities before us into lasting progress, to translate the resource gains of an economic upswing into real investment in productive capacity, to moderate our consumption tendency, to broaden and diversify economic activity. Two particular frontiers loom large in the period ahead: the challenge of investment, and the challenge of skills.

So let us remember: ***ISISU SIBEKELWA NGAPHANDLE***

Investment and skills development

There are encouraging signs that the investment trend is upwards. Gross fixed capital formation has increased by at least 8 per cent annually since 2003, and we anticipate investment growth of between 9 and 10 per cent a year over the next three years. The construction sector reports strong growth in building contracts awarded and increased employment. Cement sales rose from 7,9 million tons in 2000 to 10,7 million tons in 2004, and by a further 11½ per cent in the first three quarters of last year. Some R4,4 billion is currently being invested in expanded capacity by our cement producers. Public sector infrastructure spending increased particularly sharply last year, as investment in electricity generation capacity, ports infrastructure, water schemes, roads and telecommunications projects all gained momentum.

Investment in organisational and human capacity is no less important than physical infrastructure – in the long run it is the firmest foundation of growth and development, and for the medium term there are several pressing skills constraints to address. Opening the doors of learning is about building and equipping classrooms, it is about how we train our teachers, it is about the learning materials in our schools, it is about how we pay our educators and how we promote better school management, it is about building a culture of enthusiasm and enterprise in our school communities. Recapitalisation of our further education and training colleges will get under way this year, and the revised skills development strategy for the 2005-2010 period was launched in March last year. Training related to employment programmes in housing, roads, water services and agriculture was prioritised in 2005, and has already benefited 80 000 learners. Building sound institutional capacity in municipalities and addressing associated skills constraints are clearly key challenges for public service delivery, and are the focus of several interventions for the period ahead.

There are no joys without mountains to be climbed…

Infrastructure investment, and skills development, are the main frontiers ahead, these are journeys that have just begun, and they promise unbounded opportunities for discovery, unprecedented opportunities for initiative and partnership.

Accelerated and shared growth

But economic growth, and broad-based development, also depend on other institutional dynamics, or may be held back by particular barriers or constraints. The Accelerated and Shared Growth Initiative is designed to ensure that we understand these dynamics fully, and to prepare appropriate policy interventions. It recognises that the challenges in specific sectors – our chemicals industry, clothing and textiles, business services, tourism and hospitality, agriculture and food processing – require focused analysis and specific solutions. It also recognises that work needs to be done on several broad aspects of our economic prospects and policy framework:

- The level and stability of the exchange rate, and its impact on exports as part of a growth strategy
- The role of public infrastructure in lowering the costs of economic activity
- Appropriate, efficiently administered labour market institutions, empowerment policies and skills development
- The role of industrial policy, competition and trade policies
- The need to increase innovation and investment in new technology capable of competing internationally
- The role of financial markets in supporting investment activity.

For the three-year planning period of the 2006 Budget, export growth is expected to benefit from continued commodity demand globally, favourable tourism trends and several industrial expansion and diversification projects. Strong investment growth by the public and private sectors and moderate growth in household consumption are anticipated, contributing to an overall economic expansion of about 5 per cent a year, with a deficit on the current account of the balance of payments averaging 4,3 per cent of GDP.

Our export performance will, as always, depend greatly on the economic fortunes of other regions of the world economy. Growth in the world economy is expected to remain reasonably strong, averaging about 4,3 per cent over the next three years. In the developing and emerging economies of the world, economic growth is particularly brisk. Africa's economies are expected to grow by nearly 6 per cent in 2006. The commodity price cycle and sustained economic reform in many countries have underpinned the stronger growth rates of recent years.

Consumer price inflation has remained within the target range of 3 to 6 per cent since September 2003, reaching a low point of 3,1 per cent in February last year. Excluding transport costs, which have increased in response to higher oil prices globally, CPIX inflation for the year to December was just 2,8 per cent. Consumer price inflation is expected to average about 4½ per cent a year over the next three years.

In sum, Madam Speaker, the economic outlook is exceedingly favourable – more promising than has been seen in forty years, but we recognise the need for both restraint and redoubled efforts, so that we take full advantage of the opportunities before us. And our policy stance, unlike that of forty years ago, emphasises development opportunities for all South Africans, built on a foundation of social solidarity and a shared economic destiny, a partnership in which citizens and the state face shared challenges, to meet shared joys.

INJOBO ENHLE ITHUNGELWA EBANDLA

Exchange controls, amnesty and international financial cooperation

Completion of exchange control and tax amnesty

Madam Speaker, I am pleased to be able to announce the completion of the adjudication of applications received in respect of the exchange control and tax amnesty announced in February 2003.

A total of 42 672 applications have been dealt with, and a total of R68,6 billion in foreign assets have been disclosed. The regularisation of the foreign asset holdings and tax obligations of the vast majority of applicants means that they can now manage their financial affairs without fear of criminal or civil prosecution. It also raises the declared income tax base by some R1,4 billion, and contributes to the statistical records of the Revenue Service and the Reserve Bank.

The R2,9 billion in revenue raised through amnesty levies will be assigned to joint public-private partnership investments in community infrastructure and business development in low-income neighbourhoods. R2,5 billion of this is set aside for spending within the MTEF period ahead.

Further steps in exchange control reform

The completion of this amnesty process, Madam Speaker, lays a foundation for a more orderly process of portfolio diversification by South Africans. The offshore individual allowance will accordingly be increased from its present limit of R750 000 to R2 million per person. To encourage participation in projects supportive of the NEPAD development goals, the present foreign direct investment threshold of 50 per cent will be lowered to 25 per cent for investments in Africa by South African corporates and mandated parastatals. Further details will be provided by the Reserve Bank.

International financial cooperation

South Africa’s international engagement is organised around four themes: consolidation of the development agenda for Africa, cooperation between developing nations, improved global governance and strengthening bilateral relations.

Regional integration remains a key policy initiative. It is given practical effect in the revised Southern African Customs Union Agreement, which establishes joint institutions and a development-oriented distribution of customs and excise revenue between its members.

Our international financial engagement also includes participation in the Financial Action Task Force, the standards-setting body for combating money-laundering and terrorism financing, which is currently meeting in Cape Town under the chair of Professor Kader Asmal. It involves 45 governments of the major economies of the world, and in assuming the presidency for this year, the Government has signalled South Africa’s continued commitment to combating financial abuse, both domestically and as part of this international effort.

Fiscal policy and the budget framework

Madam Speaker, South Africa’s economic outlook both supports a more expansive fiscal stance, and is itself a consequence of steady improvement in fiscal trends. Members of the House who have been with us since 1994 know that as we enter a new phase of policy development, under the accelerated and shared growth initiative, we do so on the strength of continuing implementation of our reconstruction and development programme, which itself was supported by the macroeconomic consolidation initiated in 1996 as the growth, employment and redistribution strategy. In the noise and haste of economic policy debate, we forget too easily that there are long lead times in the practical implementation of policy. Our present economic performance reflects the choices we made a decade ago, and the economic reforms now in progress will yield their returns five and ten years from now.

There are no joys without the nightmares that precede them and spring them into light…

Fiscal policy and budget trends

Between 2000 and 2004, general government capital formation increased by 4,8 per cent a year and investment by public corporations by an average

7,4 per cent a year, in real terms. Higher growth in investment of 10 per cent and 15 per cent a year is projected for the period 2004 to 2008. Real wage and non-wage consumption expenditure are expected to increase by 3 per cent and 8,4 per cent a year, respectively. Interest on public debt will continue to decline as a percentage of GDP, and general government tax revenue will stabilise at about 26½ per cent of GDP.

These are the statistical indicators of steady improvements in the quality of the public finances – robust revenue performance, declining debt costs, rising investment and a more healthy balance between personnel expenditure and the maintenance of facilities, acquisition of equipment and support services that allow public servants to work efficiently and effectively.

Main budget revenue in 2005/06 is expected to amount to R411,1 billion, or R41,2 billion more than the original estimate and 18,2 per cent more than 2004/05 revenue. As noted already, we under-estimated the impetus of the economic recovery last year, buoyant trade and rising commodity prices have favourably impacted on corporate profits, and there has been a strong demand boost to both VAT receipts and import taxes. But the revenue performance is also testimony to the success of the sweeping tax reform agenda of the past decade, and the growing competence and effectiveness of the South African Revenue Service.

The anticipated expenditure outcome for 2005/06 of R419 billion takes into account two additional allocations, placed before the House today as a further adjustments appropriation bill for unforeseeable and unavoidable expenditure. The first is an amount of R2,7 billion to relieve the cash flow crisis of the Road Accident Fund and contribute to addressing its backlog in claims settlements. The second is a R2 billion capital investment in Denel Corporation, to enable it to proceed with the restructuring necessary to achieve solvency and profitability.

The difference between revenue and expenditure is a budget deficit of R7,9 billion in 2005/06, or 0,5 per cent of GDP. At this time last year, we anticipated a deficit of R48 billion, 3,1 per cent of GDP. Members of the House are entitled to ask: What will be done with the extra R40 billion we planned to raise? The answer has three parts.

- The first is that we will begin the new year with a net debt position equivalent to 30,8 per cent of GDP, down from 33,2 per cent at the end of 2004/05. Lower debt means lower debt service costs in years to come, and lower interest rates across the entire economy.
- The second is that we are able to table an MTEF that provides for greater expenditure growth over the period ahead than we otherwise could have.
- The third is that we again have room for moderate tax relief, while taking into account that the revenue outcome this year is in part cyclical and temporary.

For the MTEF period ahead, budget plans are set out in considerable detail in the *Budget Review*, and I propose to highlight just a few key features. In recognition of the social and development challenges ahead, we propose to raise about 26 per cent of GDP in revenue, after providing for payments to our Southern African Customs Union partners which will amount to R19,7 billion next year – a considerable contribution to promoting development and trade with our neighbouring economies.

State debt cost will decline from 3,3 per cent of GDP in 2005/06 to 2,7 per cent in 2008/09. The budget framework again contains an unallocated contingency reserve, rising to R8 billion in the outer year. After taking into account these amounts, R418,2 billion is allocated for national, provincial and local government expenditure in 2006/07, rising to R507,6 billion in 2008/09.

The national budget deficit is expected to be 1,5 per cent of GDP next year, falling to 1,2 per cent in 2008/09. Taking into account social security funds, provinces, public entities, local government and public enterprises, the public sector borrowing requirement is expected to average 2,4 per cent of GDP over the period ahead.

Infrastructure spending

These projections allow for a marked increase in infrastructure and capital spending by the public sector over the next three years. Infrastructure spending has lagged somewhat behind budget allocations in recent years, and so concerted efforts are now in progress to strengthen capacity to plan, implement and monitor these programmes more effectively. Within the Treasury, efforts are concentrated on support for provincial and municipal planning and construction contract management. The Development Bank of Southern Africa is currently assembling a task force of engineers and project managers, to be named *Siyenza Manje*, to contribute to operational and strategic capacity in distressed municipalities, and to accelerate the roll out of basic services. Under the Department of Public Works and the Construction Industry Development Board, an assessment of the state of public infrastructure maintenance is under way and improved maintenance standards and management systems will be implemented. Under the umbrella of Project Consolidate, we will give focused attention to municipal financial management and procurement administration.

Alongside enhanced planning and project management capacity, Madam Speaker, we are also reinforcing our tools and procedures for fighting corruption and waste. Supply chain management reforms include rules to prohibit illegitimate business activity of public employees and elected office-bearers, and improved guidelines for tender practice, transparency, prompt payment and performance management. Where necessary, investigative powers and early intervention capacity over all three spheres of government will be developed, to complement the resources of the prosecuting authorities.

The scale of this programme, stepping up public sector project management capacity, is considerable. The Treasury infrastructure database currently has some 15 000 entries, and our provincial files a further 10 000 projects. Many of these are comparatively small public works projects that require straightforward tendering and contract management procedures. This provides growing opportunities for small business development and empowerment. There are also several major projects, which in turn generate more complex business development programmes, often associated with deliberate skills development and mentorship. I am pleased to note that joint initiatives, involving public and private sector stakeholders, are in progress to contribute to the institutional capacity needed for success in this broad-based development and empowerment journey.

The investment programme is now well under way, and we will continue to see steady growth in infrastructure spending in the government accounts, in company reports and project announcements, and in the dust and noise of increasingly busy construction sites.

Madam Speaker, the 2006 Budget includes a contribution to our investment commitments for the 2010 Soccer World Cup. Details of project allocations have not yet been finalised, but we will spend up to R5 billion in dedicated infrastructure for the World Cup, of which R3 billion is set aside over the next three fiscal years. I understand that both the national football side and the cricket team have volunteered to do unpaid clearing of building rubble.

There are no joys without the nightmares that precede them…

EKUNYAMEZELENI KUKHO UMVUZO!!

Tax proposals

Let me turn, Madam Speaker, to the tax proposals for the 2006/07 year.

Government's approach to meeting the state's revenue requirements has several components: broadening the tax base, improving tax administration and building a culture of tax compliance, and lowering the tax burden associated with unduly high rates of tax. These are general goals of sound tax design, and contribute to economic growth and tax fairness, and in addition we seek to contribute to government's economic and social objectives where this can efficiently be done through the tax structure.

A measure of the success of this approach is that revenue collections have remained robust, relative to national income and output, while at the same time rates of income tax on businesses and individuals and on international trade have been lowered in line with international trends.

Several specific concerns are addressed in this year's tax proposals:

- long-term retirement savings
- small business development
- investment in research and technology
- skills development, and
- home ownership.

The South African Revenue Service is also implementing several reforms aimed at reducing compliance costs, enhancing service to taxpayers and improving tax and customs administration over the period ahead.

As announced last year, the regional service and joint service council levies will fall away in July this year. This amounts to effective tax relief on the business sector and other employers of about R7 billion a year, and lowers the costs of job creation. It also reduces the monthly administrative burden on companies. Municipalities will receive compensating income through an increase in their equitable share grants from nationally collected revenue.

It has also been agreed that municipal property rates revenue will be zero-rated for VAT purposes with effect from July 2006. This will result in a benefit of about R1 billion for municipalities, and will also contribute to simplifying their accounting and tax records.

Personal income tax

Personal income tax relief this year will amount to a total of R13,5 billion, partially offset by an increase in the withholding rate on motor allowances and amended treatment of company car benefits. The net benefit in personal income returned to taxpayers is R12,1 billion.

The income threshold below which no tax is payable by individuals is raised from R35 000 to R40 000 for the tax year beginning next month, and for taxpayers over the age of 65 to R65 000 a year. Changes to the tax brackets result in significant relief for all taxpayers, with an estimated 49 per cent of the benefit going to those who earn less than R150 000 a year, and 24 per cent of relief going to the income bracket R150 000 to R250 000. The maximum marginal rate of tax remains 40 per cent, while the threshold is raised from R300 000 to R400 000.

The domestic interest and dividend exemption for taxpayers under the age of 65 is raised from R15 000 to R16 500, and for senior citizens the threshold increases from R22 000 to R24 500. The proportion of the exemption applicable to foreign interest income and dividends is raised from R2 000 to R2 500.

As announced last year, the deemed private usage applied in calculating tax on motor vehicle travel allowances increases to 18 000 km per year. The monthly taxable benefit of a company car increases to 2,5 per cent of its value with effect from next month. In keeping with these changes, the proportion of a motor vehicle allowance subject to PAYE tax will be increased from 50 per cent to 60 per cent, and a new cost table will be published. The anticipated gain to the fiscus is R1,4 billion in 2006/07.

Members of the House will recall that a revised tax regime for medical scheme contributions and medical expenses was announced in the 2005 Budget. It has the effect of raising the tax benefit for middle and lower-income earners, while restricting the tax allowance in respect of more expensive medical schemes. Monthly monetary caps for medical scheme contributions have been introduced and the threshold for individual tax-deductible medical expenses is raised from 5 to 7,5 per cent of income. Taxpayers 65 years and older will continue to enjoy a full deduction of all medical expenses. These changes take effect on 1 March 2006.

Transfer duty

Tips for Trevor this year included an interesting perspective from Norman Greenfield, who suggests that “The high costs of transfer are deterring retirees from downsizing, depriving younger people of the housing stock. Could transfer duty be waived after age 60 or 65? There is only a limited time left to amortise it…” There are ages to take into account on both sides of a property transaction so this is probably not the right way to proceed. But I agree that a decrease in transfer duties will encourage the secondary housing market and contribute to promoting home ownership. With effect from 1 March 2006, houses costing less than R500 000 will attract no duty. The 5 per cent rate will apply between R500 000 and R1 million, and 8 per cent thereafter. The flat 10 per cent rate for companies and trusts is reduced to 8 per cent. Taking into account the substantial increase in property prices in recent years, I know that this will be welcome relief to all home buyers, and especially first-time entrants to the property market. The cost to the fiscus is R4,5 billion.

The threshold exemption for stamp duties on leases is raised from R200 to R500 per agreement, reducing the compliance burden for taxpayers and the administrative load on the Revenue Service.

Monetary thresholds for donations tax, estate duty and capital gains tax

The tax system contains various monetary thresholds relating to individuals that have not been adjusted for inflation for several years. Changes proposed with effect from 1 March 2006 include the following:

- The annual donations tax exemption is increased from R30 000 to R50 000
- Exemption from estate duty is raised from R1,5 million to R2,5 million
- The annual capital gain exclusion will increase from R10 000 to R12 500
- The primary residence exclusion from capital gains tax will increase from R1 million to R1,5 million
- The capital gain exclusion on death will increase from R50 000 to R60 000.

Tax on retirement funds

As part of a broader review of public policy relating to social security and retirement saving, the tax treatment of retirement funds and aspects of industry practice have come under scrutiny over the past year. The tax regime aims to encourage South Africans to make provision for their retirement, and options for achieving this more effectively have been intensively assessed. In order to contribute to the build up of retirement savings and taking into account that interest rates have stabilised at lower levels, the present tax on retirement funds will be reduced from 18 per cent to 9 per cent with effect from 1 March 2006, at a cost of R2,4 billion.

Regulatory reforms relating to cost disclosure, the structure of commissions and governance of funds will be proposed in a policy paper to be released shortly. Our pension reform aims to ensure that the benefits of the favourable tax regime are passed on to retirement fund members in the form of improved returns, that retirement savings are not depleted by excessive charges and penalties.

Although not a question of tax policy, I have been reminded by many retired correspondents this year that civil pensions, and many private pension arrangements, have in the past not adequately kept pace with inflation. Mr Rademeyer reminds me that I too will grow old. I have taken note, and would welcome appropriate remedies. I do agree that preservation of the real value of pensions should be a central principle of our retirement industry reform programme.

Small business development

Following various stimulus measures aimed at small business development in the 2005 Budget, a number of monetary thresholds adjustments will take effect in the year ahead.

- With effect from tax years that start on 1 April 2006 or after, the annual turnover threshold to qualify as a small business corporation will be raised from R6 million to R14 million, the taxable income threshold for the lower 10 per cent rate will be increased from R250 000 to R300 000 and the small business income tax exemption threshold will be increased from R35 000 to R40 000
- One-time capital gains tax relief will increase from R500 000 to R750 000 after 1 March 2006, and
- The asset value threshold for immediate depreciation will increase from R2000 to R5000.

These measures will cost an estimated R400 million.

The South African Revenue Service will also offer a tax amnesty to small businesses with a turnover not exceeding R5 million, who have not been compliant with the tax system. One of the aims of the amnesty is to afford those who have been historically marginalized an opportunity to regularise their tax status. Taxes and penalties will be waived for years of assessment ending on or before 31 March 2004, subject to a non-disclosure penalty of 10 per cent based on taxable income for 2005. The first phase of the amnesty will take effect between August 2006 and May 2007, and will focus on the taxi industry. A second phase will extend the amnesty to other small businesses later in the year.

Allowances for learnerships, scholarships and research and development

Madam Speaker, I am pleased to be able to confirm that the learnership allowance introduced in 2002 will be extended for a further five years in view of its contribution to encouraging on-the-job training and skills development. The allowances will also be increased in value, at an estimated cost of R80 million. A more favourable allowance will be introduced with effect from July 2006 for the additional expenses associated with employing disabled persons as learners. An enhanced learnership allowance for the business process outsourcing sector is under consideration.

With effect from 1 March 2007, a simplified set of rules for the tax treatment of bursaries and scholarships provided by employers will be introduced.

To encourage businesses to increase investment in technology and innovation, the deduction for current research and development expenditure will be increased from 100 per cent to 150 per cent, and a more favourable regime for depreciation of R&D capital expenditure is proposed.

Excise duties on alcohol and tobacco products

Members of the House will be aware that the Minister of Health has not relaxed her vigilance regarding tobacco products and alcoholic beverages. To the extent that this commitment contributes to reduced consumption, the fiscus is disadvantaged. Happily we can more than compensate through raising rates of duty, and I trust that the House will welcome the following measures as enthusiastically as in the past.

Excise duties on sparkling wines rise by 20 per cent, unfortified wine by 12½ per cent and other alcohol products by between 9 and 10 per cent this year. Tax on cigarettes, cigarette tobacco, pipe tobacco and cigars will increase by 10 per cent, 5 per cent, 8 per cent and 5 per cent, respectively. These changes take immediate effect, and will raise R1,4 billion in revenue.

My officials have again neglected to recommend changes to the tax on traditional beer and beer powder.

Fuel tax

No increase in the general fuel levy is proposed this year.

However, an additional 5 cents a litre on petrol and diesel will go to the Road Accident Fund, with effect from 5 April 2006.

This will bring the tax share of the pump price of petrol to between 28 and 29 per cent – down from about 36 per cent a year ago.

Following a review of international practice, it is proposed that the fuel levy rebate to encourage a domestic biodiesel industry should be raised from 30 per cent to 40 per cent.

It has been agreed that the new diesel-powered electricity generation plants planned for the national electricity network should be fully exempt from fuel levies.

Overview of tax relief and tax administration reform

Madam Speaker, these and other tax measures, together with an ongoing programme of improvements in tax administration, are discussed in more detail in the *Budget Review* and will be elaborated in further communication from the South African Revenue Service. The list of tax-exempt public benefit activities has again been refined, and deductible donation status will be extended this year to organisations undertaking conservation, environmental and animal welfare activities. Work is still in progress on some reforms, such as the proposed diamond export levy, tax treatment of the synthetic fuels industry, mining royalties and tax incentives for environmental rehabilitation funds.

Corporate taxpayers will welcome moves towards a self-assessment system, and the introduction this year of an advance tax ruling procedure. The record 3,7 million individual income tax returns filed in 2005 is evidence of a growing culture of tax compliance, and plans for the phasing in of electronic filing by individuals are now in place.

On the subject of tax compliance, there was this tip in my mail, from a taxpayer whose name I had best withhold: *Eienaars wie strandhuise besit en oral in Suid-Afrika woon verhuur hul tweede huise aan vakansiegangers. Ontduiking van betaling kan plaasvind … ek stel voor dat huisverhuringsfirmas by u geregistreer word en verplig word om 'n sekere bedrag terug te hou om oorbetaal te word as belasting…*(Owners of beach houses who live elsewhere in South Africa rent their second houses to holidaymakers. Evasion of tax takes place… I propose that home rental agencies should be registered and required to withhold a certain amount to be paid over as tax…) It's just a tip; I'll pass it on to the Commissioner…

The overall impact of the tax proposals is to reduce the tax burden by R19,1 billion, bringing total main budget revenue to an estimated R446,4 billion for the 2006/07 year.

Hard work by dedicated officials of the Revenue Service, and the honesty and good judgement of those who pay their taxes on time, are features of the mountain to be climbed, towards our season of joy.

Division of revenue

Madam Speaker, the Constitution requires that nationally raised revenue should be equitably shared between national, provincial and local government, in line with their respective functions and fiscal capacity.

The Division of Revenue Bill sets out these allocations and details of the various conditional grants to provinces and municipalities, which include funding flows for several key development programmes.

Two significant changes in the division of revenue take effect this year. The national Department of Social Development takes full responsibility in April 2006 for social assistance grant programmes, administered through the newly established South African Social Security Agency. This means that R61 billion shifts from the provincial share to the national share. The second change is that R7 billion is added to the local government equitable share in 2006/07, and R24 billion over the MTEF period, to compensate for the removal of RSC levies as a municipal revenue source.

Allocations for national department functions amount to R215,0 billion next year, provinces receive R176,7 billion and R26,5 billion goes to local government. All three shares grow strongly over the MTEF period, providing for balanced and progressive support for the objectives of economic growth, broad-based empowerment and social development.

In 2006/07, R150,8 billion will be distributed between provinces in terms of the equitable share formula, which takes into account population size, education and health needs, amongst other factors. R18,1 billion will be distributed through the municipal equitable share formula. The Financial and Fiscal Commission has again provided valued advice on the structure of the distribution formula, the design of several conditional grant programmes and the design of the local government equitable share formula.

After the transfer of responsibility for social assistance grants to national government and several other adjustments, conditional grants to provinces are budgeted to grow from R19,2 billion in 2005/06 to R30,4 billion in 2008/09. Growth is mainly due to increased allocations for the housing and human settlement grant, the hospital revitalisation programme, forensic pathology services and a new grant for recapitalisation of further education and training colleges.

Social and community development

The success of these programmes, as in so many areas of social development, relies on both competent planning and administration and the dedication and commitment of community partners. Four recently upgraded hospitals in Piet Retief, Colesberg, Calvinia and Swartruggens, bring to these communities the benefits of new buildings, fully equipped wards and newly trained management teams and clinical personnel. In the coming year new or upgraded hospitals will be completed in another four communities in the Western Cape, Limpopo and Eastern Cape. Madam Speaker, our revitalised hospitals are truly a new joy sprung from past nightmares: safe, clean, modern and properly administered.

Effective housing and community development initiatives, similarly, rest on dynamic local joint initiatives, state and citizen in partnership. In Newtown, at the heart of Johannesburg's regeneration zone, in view of the Nelson Mandela Bridge, for example, the Brickfields and Legae housing projects, undertaken in partnership with the Johannesburg Housing Company, has seen 537 families recently moved into new affordable apartments designed around safe play areas and community facilities.

And the revitalisation of education institutions brings light and joy equally profound. In 1994, the Tsolo Special School in the Mhlontlo Municipality north of Mthatha, housed 72 mentally disabled learners in two dilapidated pre-fabricated classrooms which also served as hostels. Today there are 240 learners, in three new hostels, with a fourth under construction, 10 new classrooms and facilities for practical and occupational learning in leatherwork, hairdressing and switchboard operation.

Shared and accelerated growth, Madam Speaker, is partly about how we mobilise joint resources and initiative of the public and private sectors in pursuit of the development goals for which our main provincial and local government grants have been established. We have a new funding programme for our further education colleges – their contribution to meeting the skills needs of the economy depend on stronger linkages with employers and enterprises. We will introduce this year a new grant programme for local development projects – this will specifically target public-private partnerships to invest in infrastructure and community services in low-income residential neighbourhoods.

Medium term expenditure estimates

Let me turn to the main expenditure proposals for the MTEF period ahead. Details are set out in the *Budget Review* and the *Estimates of National Expenditure.* Members of the House will find a wealth of information on the links between spending plans and the service delivery objectives and targets set out for each vote and departmental programme – information intended to support the work of Parliamentary committees, the media, civic organisations and indeed anyone with an interest in public affairs.

2006 Budget priorities

A core priority is to strengthen education, public health services and social welfare services. These are largely provincial responsibilities, and so the largest adjustment in the 2006 Budget is to the provincial equitable share, which receives an additional R30,9 billion over the next three years. Increased resources for schools, an expansion of pre-school learning opportunities, implementation of the new curriculum for grades 10-12 and stepped up school building and equipment programmes will be prioritised. Approximately R4 billion will be spent over the MTEF period on social sector employment programmes: home-based community care and early childhood development, community health workers and social development partnerships with non-governmental organisations. Care of child-headed households, strengthening of HIV and Aids programmes and appropriate management of children in conflict with the law are among the social service priorities.

Education, health and welfare services also feature strongly in adjustments on the national budget. Higher education and recapitalisation of further education institutions receives R2,4 billion more, revitalisation of hospitals and forensic pathology services a further R1,6 billion, and social assistance grant programmes an additional R2,7 billion.

Income transfers to households, mainly through our social assistance grant programmes, have increased from R42,9 billion in 2002/03 to R74,2 billion last year – an increase of 20 per cent a year. The 2006 Budget provides for continuing growth in eligible beneficiary numbers, and social grants will increase in real terms on 1 April. The maximum old age and disability grant and the care dependency grant will increase by R40 to R820 a month, the foster care grant by R30 to R590 and the child support grant by R10 to R190 a month. We are mindful that these amounts are modest in relation to household needs, although alongside education this is the largest programme of expenditure on the budget. The challenge remains, to balance these income support commitments with continued strengthening of expenditure on infrastructure and service delivery.

Housing and municipal infrastructure, local transport and water schemes are allocated an additional R9,3 billion in this budget. A new subsidy programme for community libraries will be introduced, and cultural institutions and sports promotion receive supplementary funding.

R3,5 billion is added to our national roads and rail infrastructure spending plans, and R7,1 billion is set aside as a national contribution to the Gautrain rapid rail project. Industrial development zones, the pebble bed modular reactor project, various research and technology initiatives, tourism promotion and support for the business process outsourcing industry receive additional funding allocations.

R5,4 billion will go to expanding and equipping the police service and improvements in courts administration and capacity of the Justice Department. R3,1 billion is added to defence modernisation and infrastructure, and R900 million to foreign affairs capacity and the African Renaissance Fund.

R3,3 billion is proposed for improved maintenance of government buildings and R2 billion will supplement the capacity of the Revenue Service and investment in government financial management systems.

Consolidated expenditure growth

The 2006 Budget Review provides a new and more complete classification of government expenditure, Madam Speaker, extending our data to include a further 66 public entities and government business enterprises, many of which have substantial economic infrastructure and development responsibilities. The main research organisations are now included, 22 sector education and training authorities, 15 water boards, the Marine Living Resources Fund, the National Roads Agency, the Post Office and the South African Bureau of Standards. The resulting consolidated statistics provide a compelling picture of government at work, of decisive reprioritisation in favour of social and household services, and of robust growth in spending on economic infrastructure.

Spending on community development will increase by 29 per cent a year over the next three years. Support for housing, agriculture and land affairs increases by nearly 16 per cent a year, and investment in transport and communication by 18 per cent.

Non-interest government expenditure will grow by an average of 11,6 per cent a year over the MTEF period ahead, or 6,7 per cent in real terms.

2006 Appropriation Bill

Madam Speaker, the 2006 Appropriation Bill provides for expenditure of R260,0 billion in the financial year ending 31 March 2007. Direct charges against the National Revenue Fund will amount to R52 billion in state debt cost, R150,8 billion in provincial equitable share allocations, R5,5 billion in skills development funds and R1,3 billion in other statutory amounts and standing appropriations. I need to advise that an amount of R600 million remains unallocated at this stage, to provide for possible cost implications for national departments of the new Government Employees' Medical Scheme, and to contribute to the planned new and refurbished stadiums for the 2010 World Cup. A contingency reserve of R2,5 billion is set aside. Subject to finalisation of business plans, allocations may be made from these funds in the Adjustments Budget for the capital requirements of state-owned enterprises, and we anticipate that the recent flooding in some parts of the country and fire in others may require emergency relief allocations.

ISISU SIBEKELWA NGAPHANDLE

Having reached this place, on our mountain journey, Madam Speaker, let no one speak of frontiers exhausted…We have ahead of us the joy of discovering, uncovering, and forging new forms, new ways…within an expenditure framework designed to accelerate growth, broaden reconstruction and development, and reinforce the partnerships between state and citizen on which our progressive democracy rests.

INJOBO ENHLE ITHUNGELWA EBANDLA

Madam Speaker, the preparation of a Budget relies on the hard work of many people, both in the Treasury and in other national and provincial departments. It also depends on understanding and good will of Cabinet colleagues, and most especially on President Mbeki's wise leadership. Our task has been aided this year by the energetic guidance given by Deputy President Mlambo-Ngcuka to our growth initiative. Members of the Ministers' Committee on the Budget, and especially Deputy Minister Jabu Moleketi, have shared in the difficult task of assessing spending proposals and reviewing policy options.

We have had another fruitful year of engagement with the Provincial Executive Council Members responsible for finance. They have brought both energy and good judgement to the enormously important challenge of deepening the quality of provincial budgeting and service delivery.

Governor Tito Mboweni and the staff of the Reserve Bank have steered an excellent course at the helm of our monetary ship.

The Financial and Fiscal Commission was ably led by Renosi Mokate until her move to the Reserve Bank, and we welcome Bethuel Setai as the new chair of this important advisory team.

We have also benefited from the advice of the business, labour and community representatives in the Public Finance chamber of Nedlac, and the support of its head, Herbert Mkhize.

Pali Lehohla continues to drive ongoing improvements in the extent and quality of government statistics, supported by a new Statistics Council chaired by Howard Gabriels.

I would like to express special appreciation to Nhlanhla Nene, chair of the Portfolio Committee on Finance, Tutu Ralane who chairs the Select Committee on Finance, and the joint chairs of the Budget Committee, Buti Mkhalipi and Louisa Mabe, who now take on responsibility for the next phase in the 2006 Budget process.

Thanks, finally, to Pravin Gordhan and the staff of the Revenue Service, who have surpassed all expectations, and Lesetja Kganyago, who leads the National Treasury with inimitable flair and conviction.

Having reached this place, let no one speak of frontiers exhausted…We have ahead of us the joy of discovering, new forms, new ways to accelerate growth, broaden reconstruction and development, and give light to the shared nationhood on which our progressive democracy rests.