2022 Budget predictions

Reform to grow

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Economic and fiscal policy

Economic growth

PwC wish

In PwC's recently released 25th Global CEO Survey, 70% of South African CEOs polled expect local economic growth to improve slightly (27%), moderately (40%) or significantly (3%) this year. (This is close to the global total of 75%.) Our wish is for Budget 2022 to be encouraging to the business community and to lift business sentiment by providing an update on progress made in structural reforms.

Our real GDP growth forecasts

- *2021: 4.2%*
- *2022: 2.3%*
- *2023: 1.8%*
- *2024: 1.8%*

Our nominal GDP growth forecasts

- *2021: 8.8%*
- *2022: 7.2%*
- *2023: 6.4%*
- *2024: 6.3%*

PwC prediction

The MTBPS was quite conservative in its GDP growth forecasts for 2022-2024 in order to bring more realism into the outlook for fiscal revenues. We expect this conservative stance to be replicated in Budget 2022, although a slight upward revision could be expected for the current calendar year.

The Finance Minister is likely to give an update on progress under Operation Vulindlela. It is expected that many of the key necessary structural reforms would have seen little to no progress in fixing, so the Finance Minister might need to be creative in how he communicates this.

Fiscal balance

PwC wish

South Africa's fiscal balance is now on a narrowing trend. Our wish is for the Finance Minister to stick to the hard line he set in October 2021 to substantially narrow the fiscal deficit over the medium term. As such, he will need to show financial prudence when talking about the idea of a basic income grant. There have been enough comments from government officials about the prospect of such a grant and we would like to see a more robust comment from the Finance Minister about the financial viability of such a scheme.

PwC prediction

The fiscal balance will benefit from stronger-than-expected revenues. However, there will also be pressure on the expenditure side to accommodate a change in social grant payments. Any budgeting for a basic income grant could significantly increase overall spending.

Our budget balance predictions are:

- 2021/22: -7.0%
- 2022/23: -4.9%
- 2023/24: -4.8%
- 2024/25: -4.6%

Expenditure

PwC wish

MTBPS 2021 reported that consolidated government spending will be cut by 2.5% in 2022/2023 to R2.075tn. While the spending cut is coming off a high base in 2021/2022, it is nonetheless unprecedented. There has never been a decline in nominal fiscal spending (from one year to the next) under the leadership of an ANC government. We hope that the planned cut in spending will remain in the revised fiscal framework, as it is an important component in reducing the fiscal deficit over the medium term.

Debt

PwC wish

MTBPS 2021 reported noticeably better debt-to-GDP ratios due to the rebasing of national accounts earlier in the year. Our wish is for the improved historical readings and recent projections to remain conservative. These debt metrics need to remain on a better footing in order to improve the sovereign credit rating.

We'd also like to see an update on the Eskom debt situation, which is one of the biggest obstacles for the power utility to improve its financial position and take on available external financing towards greening the power system.

We hope that the Finance Minister holds firm on a previous pledge to no longer provide bailouts to SOEs.

PwC prediction

Debt projections will be revised based on changes in the fiscal deficit. With the deficit expected to be even smaller than envisaged in October, the outlook for debt-to-GDP is again looking better compared to the previous budget address.

SOEs

PwC wish

A comprehensive cost-benefit analysis of the contribution of SOEs to South Africa's society and economy is urgently required. With a view to improving this contribution, Budget 2022 should announce that appropriate assessments will be conducted in this regard. This will enable a determination of which long-term plans and funding mechanisms benefit South Africans the most. (We made this point ahead of Budget 2021 as well.)

We would like to see a comprehensive update on the restructuring of Eskom. While there has been some progress in restructuring the utility, the process is behind schedule and weighing on the South African economy every day that it is delayed.

Credit ratings

PwC wish

It is possible that South Africa's credit ratings have bottomed out, with Fitch Ratings revising the outlook on its "BB"- rating from 'negative' to 'stable' in December 2021. We hope that the improvement in fiscal and debt metrics following the GDP rebasing will put an end to the decline in ratings.

PwC prediction

The budget speech usually makes limited reference to credit ratings. However, this would be an opportune time for the finance minister to highlight any progress made in the key areas observed by ratings agencies as they assess sovereign ratings. It is an opportunity to reflect on some good news around public sector finances.

Taxes

2021/22 tax revenues

PwC prediction

The 2021/22 fiscal year has seen a remarkable recovery in tax revenues after falling R175 billion short of the original budget estimate in the 2020/21 fiscal year as a result of the COVID-19 pandemic. National Treasury understandably took a conservative view on its revenue estimates for 2021/22 in Budget 2021.

After forecasting total tax revenues of R1.365 trillion in Budget 2021, National Treasury made a significant upward revision to this figure in MTBPS 2021 by R120 billion, to R1.485 trillion. This revised estimate is still conservative in our view and we expect that actual tax revenues could come in up to R200 billion higher than the original Budget 2021 estimate, assuming the strong performance in CIT collections continues through March.

By far the biggest contributor to the surplus is corporate income tax (CIT), which could exceed the original budget estimate by about R120 billion, primarily driven by the resources sector due to high commodity prices.

Personal income tax (PIT) collections are also performing relatively strongly and could exceed the original budget estimate by about R40 billion. VAT also continues to perform better than anticipated and could exceed the original budget estimate by about R10 billion.

2022/23 tax revenues

PwC wish

It is hoped that National Treasury will not increase taxes. Given the significant improvement in revenue collections for 2021/22, as well as the outlook for 2022/23, National Treasury is in a position to adopt tax policies that are supportive of economic growth.

PwC prediction

In MTBPS 2021, National Treasury estimated tax revenues for 2022/23 at R1.527 trillion, only 2.8% higher than the estimate for 2021/22 and slightly lower than the estimated nominal GDP growth for the year of 2.9%. A cautious approach was adopted in this regard, with National Treasury stating that the windfall commodity revenues are unlikely to provide significant additional revenues beyond 2021/22, and slow employment growth constraining PIT projections. While the above concerns (and other risks to GDP growth) are real, they are perhaps too conservative.

At a more realistic, but still conservative, nominal GDP growth rate of 5% (which is below the general market consensus forecast, including our own), a 2021/22 tax revenue baseline that is R50 billion higher than that in MTBPS 2021 and a tax buoyancy ratio of 1 would suggest 2022/23 tax revenues of R1.612 trillion, an increase of R85 billion over the MTBPS 2021 estimate. We expect that National Treasury will increase its tax revenue forecast to be close to this number.

Given the better-than-expected performance in revenues, we do not expect to see significant changes in taxes, similar to the position adopted in Budget 2021 where there were no changes to taxes on a net basis, with relatively small real increases in indirect taxes offset by real decreases in PIT.

Governance of South African Revenue Service (SARS)

PwC wish

It is hoped that changes to the governance of SARS will be made during 2022.

PwC prediction

While SARS has implemented a number of the recommendations of the Nugent Commission, certain of the recommendations relate to the governance of SARS and require changes to the South African Revenue Service Act. Budget 2021 indicated that a discussion document proposing legislative amendments to SARS governance would soon be published. Unfortunately, the discussion document has yet to be published. With the Zondo Commission having also made a recommendation with respect to the appointment of the Commissioner of SARS, it is expected that Budget 2022 will give renewed urgency to these reforms.

Dividends tax

PwC prediction

We do not anticipate any change to the dividends tax rate for 2022/23.

Corporate income tax

PwC wish

Ideally, the budget would map out a path for the reduction in the CIT rate from 28% to 25% over the medium term in a tax neutral manner, as the tax base is broadened.

PwC prediction

No changes are expected to the general corporate income tax rate of 28% in 2022/23, nor to the inclusion rate for capital gains tax.

Broadening of the tax base and reduced CIT rate

In Budget 2020, it was announced that Government would, over the medium term, restructure the corporate income tax base by broadening the base and reducing the CIT rate. The purpose of doing so is to promote economic growth.

In Budget 2021, it was announced that the measures for the broadening of the tax base through limiting assessed losses and interest expense deductions and the consequential reduction in the CIT rate to 27%, would be postponed to 2022 due to the pandemic.

The legislative amendments to broaden the tax base were included in the 2021 tax amendments. However, Government has (in order to create space for economic recovery) postponed the introduction of the measures until a date to be announced in the annual budget.

Following these developments, the reduction of the CIT rate to 27% is, at the earliest, expected to be announced in Budget 2023 and implemented in 2023/2024.

OECD BEPS project

South Africa is a member of the Steering Group of the Inclusive Framework (“IF”), which is tasked with examining income tax challenges associated with the digitalisation of the economy.

In Budget 2021, Government indicated that if a consensus-based solution could not be delivered by the IF, it will consider the appropriateness of a unilateral approach to these issues.

In October 2021, South Africa committed to the new international tax framework developed by the IF (i.e. a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy).

Following these developments, a unilateral approach is not likely and it is expected that Government will pledge, in Budget 2022, its continued support to the implementation of the new framework. This should entail the drafting and implementation of domestic legislation to give effect to the proposed Pillar II minimum tax measures (noting that the IF aim is for this legislation to be brought into law in 2022, to be effective in 2023) and entering into a multilateral instrument to give effect to other elements.

Incentives

In Budget 2021, it was announced that the tax incentive regime will be reviewed with a view to reduce incentives to create an environment that is conducive to broad-based economic growth and that avoids complicated incentives for specific sectors or groups of taxpayers.

The review commenced in 2021 and will likely continue in 2022/23.

However, the Research and Development incentive (with a 1 October 2022 sunset date) is expected to be extended, with some refinements to the current provisions to improve its effectiveness.

A redesigned energy efficiency incentive may also be introduced.

Advance pricing agreements

Budget 2022 will likely introduce an Advance Pricing Agreement Programme whereby taxpayers can agree with SARS on transfer pricing for cross-border transactions between connected parties.

Oil and Gas (“O&G”) regime

Budget 2021 announced a move towards a fairer and more certain fiscal and regulatory regime for upstream O&G and that a discussion paper would be issued on the potential tax reforms.

The discussion paper was published for public comment in December 2021, essentially proposing state participation in net revenue/production (in the form of a 20% carried interest) combined with a flat-rate royalty of 5% on gross sales.

It is unlikely that Budget 2022 will make any definitive announcement in this regard, as the consultation process will still need to be concluded. However, the required legislative changes may follow the completion of the consultation process during the course of the year.

Personal income tax

PwC wish

Tax rates

In an ideal world, we would like to see real PIT relief. Realistically, this is not likely until such time as the fiscal deficit is brought under control and the tax base is increased.

Remote working

As many salaried employees are currently incurring (and will continue to incur in the year ahead), non-deductible expenditure due to remote working arrangements. It is hoped that National Treasury's review will be expedited and that Budget 2022 will at least introduce some tax relief for expenses that result from this new way of working.

PwC prediction

Tax rates

In recent years, the PIT tax burden has increased significantly, growing from 6.6% of GDP in 2006/7 to a record high of 9.3% of GDP in 2019/20 and an expected 9% of GDP in 2021/22. At the same time, the taxpayer base on which PIT is collected has narrowed, resulting in this increased tax burden being borne by a small proportion of the PIT taxpayer base.

In Budget 2021, National Treasury noted that South Africa has the highest PIT burden among upper middle-income countries, alongside one of the highest top personal income tax rates. It also noted that further increases in PIT would put additional pressure on households that have been negatively affected by the pandemic and undermine the chance of a stronger economic recovery. Finally, National Treasury indicated that, rather than increasing rates, it aims to reduce the rate over time by increasing the tax base through greater economic growth, employment and enforcement.

We expect that National Treasury will continue with this supportive approach. Although no significant reductions in PIT rates are expected in Budget 2022, it is likely that, similar to last year, full fiscal drag relief adjustments to the PIT brackets will be given in order to support the economic recovery. If real tax relief should be granted, it is unlikely to be significant.

Medical tax credit

Similar to Budget 2021, an inflationary adjustment to the medical tax credit is expected.

Retirement reform

A paper titled 'Encouraging South African households to save more for retirement' was released for public comment in December 2021. The paper proposes the introduction of a two-pot system for retirement contributions, i.e. a retirement pot (two-thirds) that will not be accessible prior to retirement, while the other (savings pot) would allow pre-retirement access (one-third). It is further envisaged that vested rights on accumulated retirement savings prior to the new two-pot structure taking effect will be protected. Amongst others, the paper explores options for the tax treatment of the savings pot and whether changes to the tax treatment of retirement savings should be made in this regard.

In many respects, the most attractive option (of the alternatives proposed in the document) is to keep the current tax design for the retirement system. By retaining the current design, the significant complexity that will come with the introduction of a new tax system for the tax treatment of the savings pot will be avoided and taxpayers will not be disincentivized to save for retirement. Although there are concerns with respect to potential tax arbitrage opportunities, it is expected that the current tax design will be retained for the new retirement system for now. An announcement on the introduction of the two-pot retirement system can be expected in Budget 2022.

"Exit tax" – retirement funds

In Budget 2021, a proposal was made to introduce an exit tax on retirement savings when an individual ceases to be a South African tax resident. This proposal was met with severe criticism on a number of fronts, including the practical feasibility thereof and whether it would be enforceable under certain double tax treaties, which grant sole taxing rights on pensions to the country of residence of the individual. National Treasury has indicated to Parliament that it proposes starting the process of entering into the renegotiation of the affected tax treaties. We expect to see a formal announcement to this effect in Budget 2022.

Remote working

It was announced in Budget 2021, that National Treasury would commence with a review of the tax provisions for travel and working from home as part of a multi-year project.

National Treasury has informally asked for public comments on the topic. It is expected that the review will continue this year and that no policy changes are likely in Budget 2022.

Estate duty and donations tax

PwC prediction

The tax rates for estate duty and donations tax were recently increased. They also only raise around R3 billion in revenue between them. Despite calls from some quarters for the introduction of wealth taxes (of which estate duty and donations tax are a form), it is unlikely that any changes will be made in this regard in Budget 2022. Nor is it likely that the introduction of any new wealth taxes will be considered at this time.

VAT

PwC prediction

VAT rate

As the social relief of distress grant has been extended for another year, we expect that this will be funded out of the additional tax revenues expected over and above what was estimated in MTBPS 2021.

Although there have been calls for the introduction of a permanent basic income grant, which would likely necessitate substantial tax increases to fund it, we don't expect that there will be any change in the VAT rate at this stage.

Ad valorem duties

PwC prediction

We do not anticipate any significant changes to the rates of *ad valorem* excise duties.

Fuel levies

PwC wish

Rising fuel prices over the last year have hit South Africans hard and the warnings sounded by economists that the prices are expected to continue to rise during 2022 do not bode well for individuals and businesses.

As higher fuel prices will place upward pressure on consumer inflation, the hope is that the general fuel levy will not be increased in 2022.

PwC prediction

General fuel levy

In Budget 2021, the general fuel levy was increased by 15c/litre, in line with inflation. At that stage the pump price of 93 octane petrol in Gauteng was R15.50. The current price is R19.89. Although we would love to see the general fuel levy not being increased to help mitigate the impact of high fuel prices, we don't think it is likely that Government will do so.

The most likely scenario is an inflationary increase of around 20c/litre.

Road Accident Fund levy

In Budget 2021 the RAF levy was increased by 11c/litre, slightly higher than inflation. The ability of Government to pay down claims will necessitate above-inflation increases over an extended period of time. Accordingly, it is expected that an above-inflation increase in the RAF levy of 13 to 15c/litre can once again be expected in Budget 2022.

Transfer duties

PwC prediction

Given the state of the economy and the residential property market (in which property prices are under pressure), no increases in transfer duties are anticipated. However, despite price pressures, the number of transfers appears to be better than expected and transfer duty collections are running well ahead of budget forecasts for 2021/22. It is possible that some relief in the tax brackets could be introduced in Budget 2022.

Excise duties

PwC wish

Illicit trade, particularly in cigarettes, is a growing concern. We would like to see the budget propose concrete measures to address illicit trade.

PwC prediction

Budget 2021 introduced a higher-than-inflation increase (of 8%) in excise duties on tobacco and alcohol products and announced a review of the policy framework for both alcohol and tobacco during 2021/22. This review has commenced and it is expected that it will continue during 2022/23.

For tobacco products, South Africa's targeted incidence is set at 40% of the retail selling price of the most popular brand in each category.

The targeted excise incidence for spirits is 36%, for beer it is 23% and for wine it is 11%.

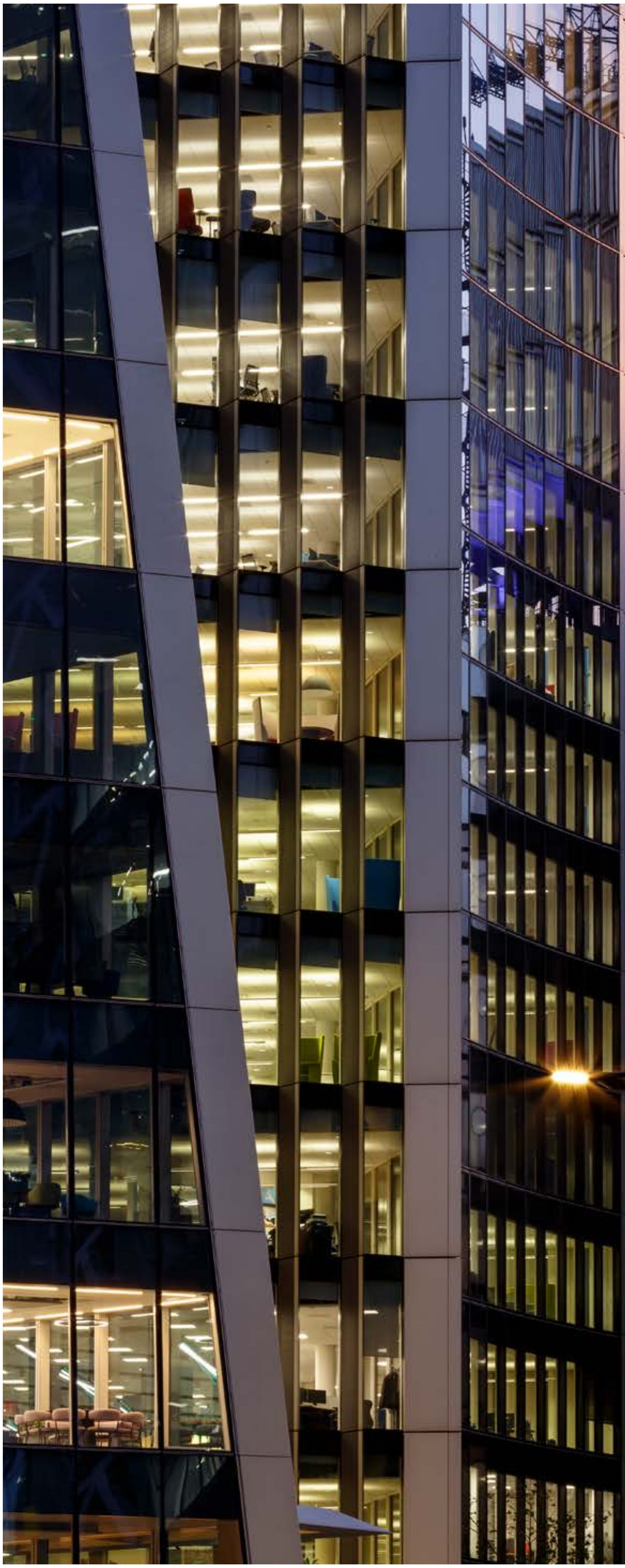
For Budget 2022, it is expected that the excise incidence will move further above the targeted incidence for each category and that above-inflation increases will likely be announced while the review of the excise duties on these products continues in 2022/23.

Vaping products

Budget 2020 announced a proposal to implement an excise duty for heated tobacco products.

In December 2021, a discussion paper on the "Taxation of electronic nicotine and non-nicotine delivery systems" was published for public comment which, in summary, recommends that South Africa implement a specific excise tax on both the non-nicotine and nicotine solution. It is proposed that a 40% incidence guideline be used.

It is expected that Budget 2022 will introduce a specific excise duty for vaping products.



Environmental taxes

PwC prediction

In Budget 2020, Government announced that an environmental fiscal reform review paper would be published. It was stated that this paper would explore the potential for new environmental taxes and reforms to existing instruments, such as, for example:

- restructuring the general fuel levy to include a local air pollution emissions component;
- alleviating traffic congestion through road pricing charges and design options for an annual carbon dioxide tax on vehicles, in collaboration with the Department of Transport and provincial governments;
- reviewing inefficient fossil fuel subsidies, including the VAT zero-rating of transport fuels;
- considering product taxes on electrical and electronic waste; and
- reviewing the tax treatment of company cars to incentivise the use of more fuel-efficient vehicles.

This paper has yet to be published by National Treasury. It is anticipated that Government will continue to review environmental taxes and increasing developments in this area are likely.

Carbon tax

National Treasury is keeping its cards close to its chest on how it envisions the rollout of Phase 2 of the carbon tax, commencing on 1 January 2023. However, announcements in this regard can be expected in Budget 2022.

Reasonable predictions that could be made are:

- The carbon tax rate will increase from R134 per t/CO2e to R144 or R145 per t/CO2e for 2022 (CPI + 2%).
- The carbon tax allowances, as they currently stand, are likely to be amended during the course of 2022 – specifically the basic tax-free allowance, currently set at 60%, may be reduced and phased out over time.
- The carbon budget allowance, aligned to the voluntary carbon budget programme, will be phased out at the end of 2022. The Climate Change Bill will mandate participation in carbon budgets and it is expected that taxpayers that exceed their carbon budget will be subjected to a penal carbon tax rate of around R600 per t/CO2e for every ton of emissions above their assigned budget.
- We also anticipate that the application of the carbon tax may be expanded in Phase 2 to also cover the Agriculture, Forestry and Other Land Use and Waste sectors, which are currently excluded from the scope of the tax.

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