



PARLIAMENT
OF THE REPUBLIC OF SOUTH AFRICA

PBO

**PARLIAMENTARY
BUDGET OFFICE**



PARLIAMENT
OF THE REPUBLIC OF SOUTH AFRICA

2025 Budget: Second Pre-Budget Brief on Revenue Options and Fiscal Policy

Beyond VAT, Exploring Alternative Revenue Sources and Fiscal Strategies

The Parliamentary Budget Office (PBO) has been established in terms of the Money Bills Amendment Procedure and Related Matters Act (Act 9 of 2009). The PBO provides independent, objective and professional advice and analysis to Parliament on matters related to the budget and other money Bills. The PBO supports the implementation of the Act by undertaking research and analysis for the Finance and Appropriations Committees.

Director: Prof Dumisani Jantjies

Contributors: Dumisani Jantjies, Kagiso Mamabolo, Mukundi Maphangwa, Seeraj Mohamed, Tshupo Moloi, Sithembiso Mthimkhulu, Nelia Orlandi, Lwazikazi Ntinzi, Mmapula Sekatane, and Sbusisiwe Sibeko

Enquiries: ssibeko@parliament.gov.za

Ref. no. 21/2/4 (March 2025)

To obtain additional copies of this document, please contact:

Parliamentary Budget Office

4th Floor Parliament Towers

103-107 Plein Street

Parliament of the Republic of South Africa

Tel: +27 021 403 2360

Email: pboinfo@parliament.gov.za

1. Executive Summary

The tabling of the 2025 budget has been rescheduled to take place on the 12 March 2025. This marks the first time in South Africa's democratic history that the Minister of Finance has delayed the tabling of the budget. This delay was mainly due to lack of consensus with the Cabinet about the then proposed 13.3% VAT increases leading to the new rate to be 17% from 15%. The delays have prompted debates with Parliament and broadly society as to whether government has considered other revenue sources other than VAT given its regressive nature of the consumption tax. The finance committees requested the Parliamentary Budget Office to prepare a brief in advising both Finance and Appropriations Committees regarding the implications of VAT increase and to further provide analysis of other potential revenue sources that government may consider raising revenue.

This brief provides MPs with an overview of issues to consider regarding revenue generation, particularly the proposed VAT increase in the original 2025 Budget. It examines the macroeconomic, societal, and public finance implications of increasing VAT, explores alternative revenue sources, and analyzes how the government can mitigate the impact of a VAT increase through revenue redistribution. In particular, how the additional revenue could be spent on investment and support households to ensure net positive effect.

The brief also includes an international comparison of taxation levels, exploring international experiences with consumption and income taxes. It provides options for raising additional revenue without compromising the national priorities outlined in the 2024-2029 Medium-Term Development Plan (MTDP) and emphasizes the importance of utilising additional revenue for social and economic investment and household support. In essence the brief notes that whatever or regardless on how the additional revenue is raised, the additional funds should be used for social and economic investment and support for households through various social programs.

Economic simulation included in the brief demonstrate that such spending can contribute to achieving national priorities, including boosting economic growth to 2.3%, reducing unemployment by 1% annually, lowering the debt-to-GDP ratio by 2.8% annually, reducing poverty by 1.3% annually, and improving the Gini coefficient by 0.7 percentage points by 2030.

The economic simulation further shows that the bottom two quantiles of the population contribute 30% of current VAT revenue, while the top two quantiles contribute 50%. Increasing VAT to 17% could generate R48 billion in 2025, potentially rising to R108.5 billion by 2030 if the additional revenue is reinvested in the economy.

A similar amount could be generated through a 0.5% wealth tax on the top two quantiles' net wealth. Given the regressive nature of VAT, a wealth tax may be more beneficial. The government may consider a once off non-tax revenue measures, such as utilising the Gold and Foreign Exchange Contingency Reserve Account (GFRECA) or government pension contributions holidays or any other measures, to raise additional required revenue for 2025 while preparing to implement a wealth tax on a permanent base from 2026.

Table of Contents

1. Executive Summary.....	3
2. Introduction	5
3. Background	5
4. South Africa's policy framework	6
5. The role of fiscal policy – tax in achieving development.....	6
5.2. Macroeconomic Impact Analysis of VAT Increase and Wealth Tax in South Africa	8
5.3. VAT Increase	8
5.4. Wealth Tax.....	8
5.5. Combined impact of VAT or wealth tax and social spending	9
6. Other considerations for increasing tax revenue.....	10
7. Non-tax revenue alternative measures.....	13
7.1. Rethinking fiscal consolidation for sustainable growth.....	13
7.2. Leveraging the public sector balance sheet for sustainable economic growth	13
7.3. Strengthening SARS to improve revenue collection	14
8. Global tax trends and implications for South African.....	15
8.1. High taxation in developing economies despite growth constraints	15
8.2. Divergent tax trends- developing and developed economies	15
8.3. Comparison of VAT trends in various jurisdictions.....	16
8.4. Structural issues in VAT dependence.....	16
8.5. Corporate taxation	17
9. Conclusion	17

2. Introduction

This pre-budget brief provides Members of Parliament (MPs) with important information and insights to inform their deliberations on the upcoming 2025 Budget presentation. The brief offers a comprehensive analysis of the government's proposed VAT increase, examining its potential macroeconomic, societal, and public finance implications. It delves into the complexities of South Africa's fiscal landscape, highlighting the limitations of past fiscal consolidation efforts and the urgent need for increased social and economic investment to address the nation's pressing challenges.

Beyond analysing the then proposed VAT increase proposal, the brief explores a range of alternative revenue-generating mechanisms, including a wealth tax and other innovative approaches. The brief further provides a global perspective, comparing tax structures and trends across different economies to offer insights relevant to South Africa's context. The brief emphasizes the importance of strengthening tax administration and leveraging the public sector balance sheet to mobilise resources for economic and social development.

Ultimately, this brief aims to equip MPs with the knowledge and understanding necessary to engage in robust and informed budget debates. By providing a comprehensive analysis of revenue options and their potential implications, it seeks to empower MPs to make informed decisions that priorities sustainable and inclusive growth, reduce poverty and inequality, and build a more resilient and equitable economy for all South Africans.

3. Background

The South African government's persistent pursuit of fiscal consolidation over the past 15 years has yielded unsuccessful and unsustainable results. While aiming to lower government debt, this approach has arguably constrained economic growth and proven ill-suited to address the nation's deep-rooted socio-economic challenges, notably high structural unemployment, pervasive poverty, and stark inequality.

Evidence suggests that fiscal consolidation, often presented as a temporary measure, has failed to achieve its debt reduction objectives and has instead hindered economic growth. This has resulted in inadequate support for struggling households and constrained industrial development, ultimately undermining the fight against unemployment, poverty, and inequality.

The current global landscape, marked by interconnected crises and heightened uncertainty, necessitates a reassessment of South Africa's fiscal strategy. While fiscal prudence remains important, there is a compelling case for increased government expenditure to bolster socio-economic stability, enhance household resilience, and promote industrial development. This shift in approach requires a careful examination and use of the entire government's balance sheet and a willingness to explore alternative revenue sources and strategies beyond traditional fiscal consolidation measures.

Furthermore, the pursuit of fiscal consolidation has often led to budget cuts in critical sectors like health and education, impacting the most vulnerable members of society who rely on public services. This approach has also eroded public trust in the government's ability to address pressing social and economic needs.

In contrast, many countries, even those traditionally fiscally conservative, are pursuing fiscal expansion in response to global challenges like climate change and geopolitical instability. This highlights the need for South Africa to adopt a more pragmatic and responsive fiscal policy

that prioritizes both stability and investment in its future. This is more important given that the 2025 Budget is the first budget of the 7th administration.

The prevailing focus on fiscal consolidation has neglected the critical need for social and economic investment in South Africa. The upcoming 2025 Budget presents a crucial opportunity to re-evaluate this approach and adopt a more balanced strategy that considers both fiscal responsibility and vital investments in the nation's future. This requires a thorough examination of the government's balance sheet, a willingness to explore alternative revenue sources, and a commitment to prioritizing sustainable and inclusive growth for all South Africans.

4. South Africa's policy framework

The National Development Plan (NDP) since 2013 remains the country's blueprint to address the triple challenges of unemployment, inequality and poverty in South Africa. Twelve years later, the government must admit failure thus far, and not only that it is unlikely to achieve any of these targets, but that in some areas conditions have worsened. The situation has been made more difficult by the COVID-19 crisis.

In addition to the seven priorities of the 2019-2024 Medium Term Strategic Framework (MTSF), the Presidential Employment Stimulus and the Economic Reconstruction and Recovery Plan (ERRP) are two initiatives that were aimed at providing immediate response to the severe economic impact of the coronavirus pandemic.

In the 2025 State of the Nation Address the President indicated that the 7th administration adopted the Medium-Term Development Plan (MTDP), which sets out a clear and ambitious programme for the next five years. The actions contained in the MTDP will advance three strategic priorities:

- To drive inclusive growth and job creation
- To reduce poverty and tackle the high cost of living
- To build a capable, ethical and developmental state

The most urgent task is to grow the economy so that it can create jobs, reduce poverty and improve the lives of all South Africans

5. The role of fiscal policy – tax in achieving development

It is crucial to recognise that the government's budget is more than just a financial document, it's a strategic tool for achieving societal goals and building a better future for South Africa. The South African government has prioritised addressing the interconnected challenges of unemployment, poverty, and inequality (UPI). Poverty's multidimensional nature necessitates both short-term interventions and long-term anti-poverty programs. Extreme inequality cannot be solved solely through economic growth and structural reforms, as it reflects power imbalances that require government intervention, including wealth taxation.

In an economy with high concentration, inequality, and spatial disparities, relying solely on market mechanisms will not solve economic problems or social insecurity. The government budget must address both urgent needs and long-term developmental objectives. As the country with the highest level of inequality globally, South Africa must utilize its budget and fiscal tools for redistributive purposes, particularly through progressive taxation to redistribute wealth and income.

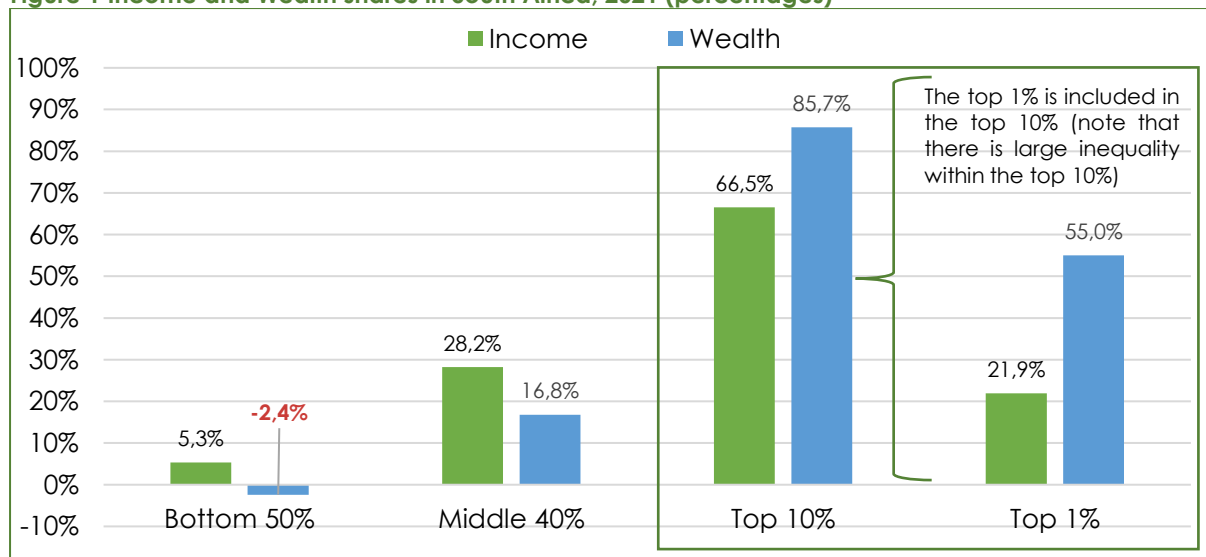
The budget can also be used to shift the economy towards a more developmental path that considers global challenges, including environmental damage and climate change. Fiscal

policy can effectively stimulate the economy in the short and long term, directing it towards a new, productive growth trajectory. Fiscal space is often greater than assumed, as expansionary programs can partially self-fund. Evidence shows that fiscal expansion does not crowd out private investment but rather tends to attract it.

Government spending on households and communities is not merely a social wage but an investment in the future productive capacity of the economy. The economy encompasses more than just GDP; it includes externalities, non-market activities, and unpaid care work, which must be considered when studying fiscal multipliers.

The influence of wealthy individuals and large corporations can distort tax policies and hinder redistribution and development. These actors often advocate for regressive taxes like VAT, which disproportionately burden the poor, instead of supporting progressive taxation. VAT, even with zero-rated items, is not a progressive tax, as its impact on well-being is greater on the poor. Raising VAT makes the tax system more regressive.

Figure 1 Income and Wealth shares in South Africa, 2021 (percentages)



Source: 2022 World Inequality Report

The Laffer curve, which posits that tax collection and economic activity decline after reaching an optimal tax level, lacks robust empirical support. It oversimplifies the relationship between tax rates and tax revenue, failing to differentiate between income groups or firm sizes and ignoring the complexities of real economic systems. Leading economists, including Nobel laureates Paul Krugman, Joseph Stiglitz, and Amartya Sen, have challenged the Laffer curve's assumptions and conclusions.

Krugman argues that the Laffer curve ignores the role of public investment in driving economic growth. Stiglitz points out the lack of empirical evidence supporting the Laffer curve and argues that tax cuts for the wealthy do not stimulate significant growth but exacerbate inequality. Sen emphasizes that tax policy should prioritize equity and social welfare over maximizing revenue.

The Laffer curve's focus on revenue collection neglects the broader impact of tax policy on equality and access to public services. It also incorrectly assumes that lower taxes will lead to higher investment, despite evidence of high levels of base erosion and profit shifting (BEPS) and low investment even when corporate profits are high.

In essence, the Laffer curve fails to provide a reliable framework for tax policy debates due to its lack of empirical support, its simplistic assumptions, and its disregard for the distributional effects of tax policies.

Redistribution and fiscal policy are vital tools for supporting development and growth. By reducing inequality, investing in human capital, and stabilizing the economy, governments can create a more inclusive and sustainable economic system.

5.2. Macroeconomic impact analysis of VAT increase and wealth tax

The Parliamentary Budget Office conducted an economic modelling exercise to assess the fiscal and macroeconomic implications of two revenue-generating policy options, VAT increase and a Wealth tax. This analysis was performed using a macroeconomic simulation model, which evaluated the potential effects of raising additional government revenue through tax reforms and reinvesting it in targeted social and economic programmes. The modelling process involved two key components: revenue assessment and spending scenarios.

The revenue assessment focused on estimating the additional revenue that could be generated through different tax policy adjustments, specifically increasing the Value-Added Tax rate from 15% to 17% and implementing a 0.5% wealth tax on the wealthy net assets. The expenditure scenarios explored how reinvesting this additional tax revenue into key social and economic programs would impact economic growth, employment, and inequality. Targeted spending areas included a;

- 6% annual increase in social grants,
- 6% expansion of public employment programs,
- 10% annual increase in social and economic investments, and
- enhanced funding for education and social services by increasing spending on salaries, goods, and services by 6% annually.

5.3. VAT Increase

Revenue generation

The modelling simulations indicate that a 2% increase in the VAT rate, from 15% to 17%, would generate an additional R48.6 billion in revenue in 2025, increasing to R108.5 billion by 2030. This substantial increase in revenue is attributed to the combined effect of the higher VAT rate and the projected rise in gross domestic expenditure due to improved GDP growth.

Distributional impact

While a VAT increase offers significant revenue potential, it's crucial to consider its distributional impact. Simulation results reveal that the bottom two quantiles of the population, representing the most vulnerable households, currently contribute about 30% of the total annual VAT revenue, while 50% of the VAT burden would fall on the top two quantiles. Therefore, a VAT increase would disproportionately impact low-income households, potentially exacerbating poverty and inequality.

5.4. Wealth Tax

Revenue generation

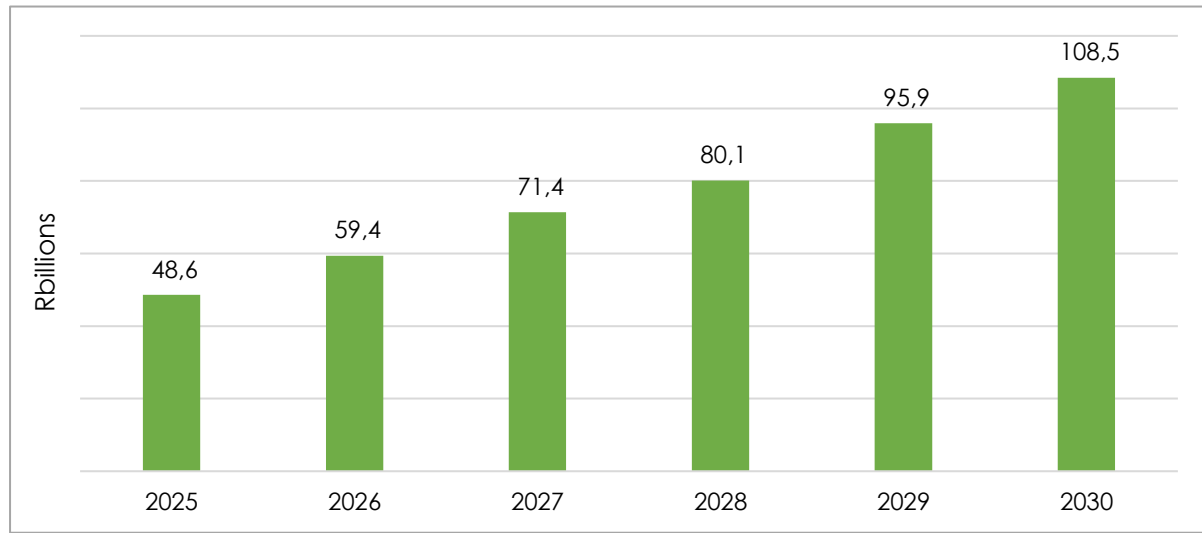
As an alternative to a VAT increase, the model also simulated the impact of a 0.5% net wealth tax. The simulations on the wealth tax make use of the net assets of the top two quantile of the population. The results demonstrate that this wealth tax would generate approximately the

same amount of revenue as a 2% VAT increase. This finding suggests that a wealth tax could be a viable option for raising substantial revenue without placing an undue burden on low-income households.

Distributional Impact

The key advantage of a wealth tax over a VAT increase lies in its distributional impact. The wealth tax would primarily generate revenue from the wealthiest segments of the population, ensuring that the burden of taxation falls on those most able to pay. This approach aligns with the principles of progressive taxation and could contribute to reducing income inequality.

Figure 2 Expected extra VAT revenue - Increase from 15% to 17% in current R billion



Given these distributional dynamics, an introduction net wealth tax would be a fairer and more equitable approach to raising additional tax revenue, as it does not place an undue burden on low-income households. While the VAT increase is a more immediate and substantial revenue source, it disproportionately affects the poor, making it a less desirable option from an equity perspective.

5.5. Combined impact of VAT or wealth tax and social spending

The simulation results show that fiscal expansion rather than consolidation will benefit the South African economy, and therefore, it is likely to increase government revenue collection as well. Raising revenue through either a VAT increase or a wealth tax — when combined with strategic social spending — can yield substantial economic and developmental benefits, refer to Table 1. Increased public investment in social grants, employment programmes, and infrastructure is expected to boost economic activity, reduce poverty, and promote more inclusive growth.

However, the PBO cautions that if this additional revenue is primarily allocated towards fiscal consolidation — debt reduction and achieving a primary surplus — rather than being reinvested into the real economy and directed toward supporting the poor, the country risks forgoing these critical macroeconomic and social benefits. Such an approach will continue to hamper economic growth, deepen inequality, and weaken long-term development by putting rigid fiscal targets ahead of inclusive and transformative policies.

Table 1 Macroeconomic and socioeconomic impacts of revenue and expenditure policy changes

Projected economic impact (2025–2030)	Social and developmental benefits
<ul style="list-style-type: none"> • GDP Growth: 1.5% → 2.3% (with revenue & spending measures) • Unemployment: Expected to decline by 1% annually • Debt-to-GDP Ratio: Projected to be 2.8% lower on average • Inflation: No significant impact 	<ul style="list-style-type: none"> • Poverty Reduction: Poverty rate decreases by 1.3 % annually • Income Inequality: Gini coefficient improves by 0.7 percentage points • Multidimensional Poverty: <ul style="list-style-type: none"> • 6.7% increase in people Not Deprived • 1.8 % annual decrease in Fully Deprived population

Ultimately, the findings of the simulation exercise suggest that progressive taxation, coupled with targeted social spending, presents a more sustainable approach to economic development. The wealth tax emerges as a good example of a preferable policy tool due to its ability to raise significant revenue without exacerbating inequality.

Numerous studies have examined the relationship between VAT and economic growth. While some studies have found a negative impact of VAT on growth, others have found no significant effect or even a positive impact. The impact of VAT on growth is likely to depend on a variety of factors, including the structure of the economy, the level of government spending, and the distributional impact of the tax (Cnossen, 2010; Keen & Lockwood, 2010).

The literature on wealth taxes is more limited, but there is growing interest in this policy option as a means of addressing rising income inequality. Some studies have found that wealth taxes can have a positive impact on growth by reducing income inequality and increasing investment (Saez & Zucman, 2019; Piketty, 2014). However, others have raised concerns about the potential for wealth taxes to discourage saving and investment (Auerbach & Hassett, 2015).

The United Nations has published a report, titled "UN Handbook on Wealth and Solidarity Taxes," in July 2024. The report provides comprehensive guidance to countries considering implementing wealth taxes. It acknowledges that taxing wealth can be complex and requires careful design and implementation to be effective. The report is meant to assist policymakers, particularly in developing countries, in navigating these complexities and making informed decisions about wealth taxation. The report is seen as a significant step towards promoting a more inclusive and equitable international tax system.

6. Other considerations for increasing tax revenue

Tax policy is a vital tool for the redistribution of income and wealth, especially in situations with extreme structural inequality like in South African context. Table 2 outline some alternative tax measures for consideration for additional revenue resources for 2025 Budget:

Table 2 Taxes, policy considerations and potential revenue impacts

Tax instrument	Tax policy considerations	Potential revenue impacts
<p>Corporate Income Tax (CIT)</p>	<ul style="list-style-type: none"> • In 2022, CIT was reduced to 27% • Government stated that the change would be fiscally neutral. Government is yet to provide analysis in this regard. • A proposal to reverse the CIT decrease if it has negative outcomes on revenue • An assessment of tax incentives to ensure they are achieving their intended economic, social, and policy goals is needed. Government should consider eliminating incentives that are not yielding intended outcomes. Redundant incentives contribute to lower effective tax rates • Greater efforts are also needed in ensuring that companies pay higher effective tax rates (closer to the statutory rate) 	<ul style="list-style-type: none"> • Increased revenue collection • Reduced foregone revenue on ineffective incentives
<p>Employment Tax Incentive (ETI)</p>	<ul style="list-style-type: none"> • ETI Act was introduced in 2014 to allow expense deductions for every young unemployed person being absorbed. • The ETI has subsequently been renewed multiple times since its introduction • Various research evidence provided to the National Economic, Development and Labour Council (Nedlac) shows that generally, the ETI has had little to no effect on creating employment for youth • Parliament could consider using this foregone revenue for other employment generation initiatives • Aggregated actual ETI credits refunds were R7.2 billion in 2020/21 and R6.6 billion in 2021/22 	<ul style="list-style-type: none"> • The cancellation of the ETI could result in R6-R7 billion a year in additional revenue • The allocation of these funds to other employment initiatives, will boost unemployment in a more tangible way
<p>Wealth tax</p>	<ul style="list-style-type: none"> • In 2021, SARS established a dedicated new unit focusing on high-wealth individuals • This process was in line with Davis Tax Commission (DTC) recommendations and may be seen as an important step in informing the debate about wealth tax given the context of South Africa where wealth inequality remains significantly high • An update on the findings of this initiative and potential areas of policy consideration should be queried 	<ul style="list-style-type: none"> • Under conservative assumptions, a wealth tax could raise between R70 and R160 billion when taxed at a level 1.5% to 3.5% of the South African according to Chatterjee, Czajka and Gethin (2021) • An analysis suggests that a 0.5%-1% net wealth tax would have raised R38.4 billion in 2023.

Tax instrument	Tax policy considerations	Potential revenue impacts
Curbing illicit financial flows	<ul style="list-style-type: none"> • According to the OECD 2022, between USD 3.5 billion and USD 5 billion (1% to 1.5% of South Africa's yearly GDP) in IFFs are estimated to be departing South Africa annually • This requires an expansion Illicit Financial Flows (IFF) framework. For example, the African Tax Administration Forum (ATAF) has argued that "a key focus of the work needs to be on developing rules that address base eroding payments such as excessive interest payments, management fees, royalties and service fees paid by African taxpayers to related entities located in no or low tax jurisdictions. Such payments are decimating the tax base of many African countries" • For IFFs to be curbed, significant efforts are required to further build SARS' capacity. 	<ul style="list-style-type: none"> • Curbing illicit flows will significantly boost tax revenue. If SARS went after 10 per cent of IFFs, government would get \$350 million (R6.5 billion rands)
Diversification of tax tools	<ul style="list-style-type: none"> • Lessons should be learnt from the Covid-19 pandemic as well as the subsequent commodity boom • Excess Profits Tax could be implemented on companies that have used the inflation upsurge to boost profit • Windfall taxes for sectors benefiting from the commodity price boom 	<ul style="list-style-type: none"> • While not a steady form of revenue, revenue generated could add additional revenue to the fiscus • In addition, excess profit taxes can also discourage supply driven
Taxing income derived from wealth	<ul style="list-style-type: none"> • Capital gains tax should be restructured and increased so that: <ul style="list-style-type: none"> • There is a longer holding periods and capital reinvestment are encouraged • A surcharge is applied to taxpayers earning high levels of capital gains • The inclusion rate is raised to 100 per cent • The inclusion of non-resident is simplified and widened • The use of share buybacks to avoid paying capital gains is prohibited • Increase Dividend Tax to 25 per cent, from 20 per cent • The securities transaction tax (STT) should be raised 	<ul style="list-style-type: none"> • The Institute for Economic Justice (IEJ) estimates that increasing the STT to 0.3 per cent can raise R1.5 billion in additional taxes • All the proposed measures would increase revenue collection as well has enhance wealth redistribution in the context of high wealth inequality
Property taxes	<ul style="list-style-type: none"> • Property taxes are the least redistributive in South Africa as they are leveraged at the municipal level • Municipalities with higher value homes/area accrue disproportionate revenues in property tax 	<ul style="list-style-type: none"> • Redistribution of revenue to municipalities that are unable to raise adequate revenue to fund basic services

Tax instrument	Tax policy considerations	Potential revenue impacts
	<ul style="list-style-type: none"> Property taxes for high value homes need to be increased Reform is required to also redistribute this revenue 	<ul style="list-style-type: none"> Increased revenue collection from leveraging taxes on higher value houses

Source: PBO

7. Non-tax revenue alternative measures

7.1. Rethinking fiscal consolidation for sustainable growth

While fiscal prudence is important, the government's unwavering focus on "maintaining primary surpluses" may hinder economic stability and the realisation of socio-economic rights. Traditional fiscal consolidation, with its emphasis on deficit reduction, often overlooks broader economic consequences, such as diminished public services, suppressed demand, and increased household financial strain.

Years of fiscal consolidations and their measures have failed to deliver the promised fiscal sustainability, instead leading to sluggish growth and recurring revenue shortfalls. The link between budget cuts and increased unemployment, poverty, and inequality is well-established, yet contractionary fiscal policy continues without thorough impact assessments in this regard. The notion that fiscal consolidation and supply-side reforms alone can drive sustainable and inclusive growth lacks strong evidence and has to be reviewed.

Successful fiscal management requires a balanced approach that combines fiscal discipline with strategic public investment. Spending on social services and social security should be viewed not merely as consumption but as investments with significant social and economic returns. Prioritising investments in social infrastructure, economic development, and essential services can stimulate demand, create jobs, and boost productivity, ultimately building a more resilient economy and improving long-term fiscal health.

Even the IMF, known for advocating fiscal discipline, now cautions against excessive austerity, recognising the need for a measured approach to fiscal consolidation to support economic recovery.¹ South Africa should shift away from austerity-driven targets and embrace a growth-oriented strategy that prioritises expanding economic capacity, supporting employment, and generating higher revenues through robust economic activity.

7.2. Leveraging the public sector balance sheet for sustainable economic growth

South Africa's fiscal policy discussions tend to focus heavily on taxation and borrowing, overlooking alternative ways to generate funds for economic development. The PBO suggests a broader approach, leveraging the entire public sector balance sheet to mobilize capital without relying on regressive tax increases.

State-controlled funds like the Unemployment Insurance Fund (UIF) and the Government Employees Pension Fund (GEPF) hold substantial assets that can be strategically invested for productive purposes. As of March 31, 2024, the GEPF had R2.3 trillion in accumulated funds and reserves, including R5.27 billion in its reserve account. Channelling some of these funds

¹Amaglobeli, David, Emine Hanedar, Gee Hee Hong, and Céline Thévenot. 2022. "Fiscal Policy for Mitigating the Social Impact of High Energy and Food Prices." IMF Note 2022/001. International Monetary Fund, Washington, DC.

towards infrastructure, industrialization, and job creation could yield significant economic returns, boosting tax revenue and lowering the debt-to-GDP ratio.

The Gold and Foreign Exchange Contingency Reserve Account (GFECRA), with approximately R300 billion, is another underutilized resource. While its traditional role is to cushion against external shocks, a portion could be strategically allocated to high-impact sectors like manufacturing, renewable energy, and digital infrastructure. Countries like China and Singapore have successfully used their central bank reserves to fund domestic investments, reducing reliance on external borrowing.

Another challenge is the significant outflow of domestic pension funds to offshore markets, limiting local capital. Policy changes that encourage pension funds to invest more domestically could unlock substantial funding for infrastructure, green energy, and state-led industrial initiatives. Redirecting even a small portion of the R2.3 trillion in pension assets towards domestic projects could stimulate economic growth, reduce reliance on foreign debt, and improve long-term employment prospects.

A strategic public investment approach is crucial for strengthening state capacity and steering South Africa towards sustainable development. High-impact public spending can drive structural transformation, enhance productivity, and promote inclusive growth. When well-executed, fiscal expansion generates long-term economic and fiscal benefits instead of unsustainable debt.

Instead of relying on conventional revenue-raising measures like VAT hikes or across-the-board spending cuts, South Africa can leverage its public sector balance sheet to explore alternative solutions. By strategically utilizing UIF and GEPF reserves, allocating a portion of SARB's contingency reserves, reforming pension fund investment regulations, and implementing a state-led industrial strategy, the government can foster economic growth, reduce inequality, and achieve macroeconomic stability without overburdening low-income taxpayers.

7.3. Strengthening SARS to improve revenue collection

The South African Revenue Service (SARS) has identified over R800 billion in uncollected tax revenue due to unpaid debts, overdue returns, and fiscal leakages. This lost revenue significantly undermines the state's ability to finance socio-economic programmes without resorting to harmful expenditure cuts and regressive tax increases. Enhancing revenue collection requires bolstering SARS's financial and institutional capacity. Key interventions include:

- **Strengthening enforcement and compliance:** Implementing stricter mechanisms to recover lost revenue from unpaid taxes, illicit financial flows, and non-compliant taxpayers.
- **Modernising tax infrastructure:** Investing in advanced digital systems to automate tax collection, enhance data analytics, and improve tax evasion detection.
- **Expanding workforce capacity:** Recruiting skilled auditors, compliance officers, and forensic investigators to improve tax enforcement and oversight.

Implementing these measures would require an estimated R20 billion over the medium term. However, given SARS's high revenue efficiency, this investment would yield a substantial return. Currently, for every R1 allocated to SARS, the agency collects approximately R141 in tax revenue, operating at a cost-to-tax-revenue ratio of just 0.71%. This means that investing in SARS is one of the most cost-effective mechanisms to enhance revenue without increasing tax

rates. A well-resourced SARS is central to improving public finances without resorting to growth-dampening tax hikes or spending cuts.

8. Global tax trends and implications for South African

Taxation structures vary significantly across different economies, influencing economic growth, investment, and income distribution. A comparative analysis of indirect and direct taxes—specifically VAT, Personal Income Tax (PIT), and Corporate Income Tax (CIT)—reveals divergent trends between developed and developing economies. While developed nations focus on consumption-based taxation with lower corporate tax rates, developing economies maintain higher direct taxation levels despite structural economic constraints.

Table 2 Comparison of South Africa's tax rates with other regions

Region /Countries	2018			2019			2020		
	PIT	CIT	VAT	PIT	CIT	VAT	PIT	CIT	VAT
ASIA- Average	27.9%	21.2%	11.7%	28.6%	21.2%	11.4%	26.7%	21.1%	11.8%
OCEANIA- Average	33.4%	28.4%	12.3%	33.4%	28.4%	12.3%	33.4%	28.4%	12.3%
LATIN AMERICA- Average	32.5%	28.0%	13.1%	32.7%	27.4%	13.5%	32.3%	27.4%	13.6%
NORTH AMERICA- Average	35.0%	26.8%	5.0%	35.0%	26.8%	5.0%	35.0%	26.8%	5.0%
AFRICA-Average	32.0%	28.3%	15.5%	32.0%	28.2%	15.6%	31.8%	28.3%	15.6%
South Africa	45.0%	28.0%	14.0%	45.0%	28.0%	15.0%	45.0%	28.0%	15.0%
EUROPE- Average	32.5%	19.5%	20.1%	31.9%	19.3%	19.9%	31.3%	19.1%	19.9%
EU-Average	38.2%	21.3%	21.5%	38.3%	21.0%	21.5%	37.4%	20.9%	21.5%
OECD- Average	42.0%	23.5%	19.2%	41.7%	23.2%	19.2%	41.2%	23.1%	19.2%

Source: KPMG online database

8.1. High taxation in developing economies despite growth constraints

South Africa, Africa, and Latin America have some of the highest PIT and CIT rates. South Africa's PIT has remained at 45% from 2018 to 2020, surpassing the OECD average of approximately 42% and Africa's average of 32%. However, SA's tax system includes significant exclusions for PIT (i.e. tax-free thresholds, deductions for medical expenses, retirement contributions, and other allowances) that effectively lower the amount of taxable income.

Similarly, CIT in South Africa is currently set at 27%, which exceeds the OECD (23.1%) and EU (21.5%) averages. However, the country's effective CIT rate is significantly lower due to various deductions, allowances, and tax incentives that reduce businesses' taxable income

VAT in South Africa stands at 15%, relatively high compared to other developing regions but still below the EU average of 21.5%. The presence of high PIT and CIT rates in economies with large informal sectors and significant unemployment places a disproportionate burden on the small formal workforce. Latin American and African tax structures rely on direct taxes like PIT and CIT, but revenue generation is hindered by corporate tax avoidance, tax incentives, deductions, exemptions, weak tax administration, and enforcement challenges.

8.2. Divergent tax trends- developing and developed economies

The rise of inequality in developed countries over the past four decades has not only widened the wealth gap but has also given the rich and large corporations greater political and economic influence, allowing them to shape tax policies in their favour. Developed economies, particularly in the OECD and EU, have exhibited a trend of declining corporate

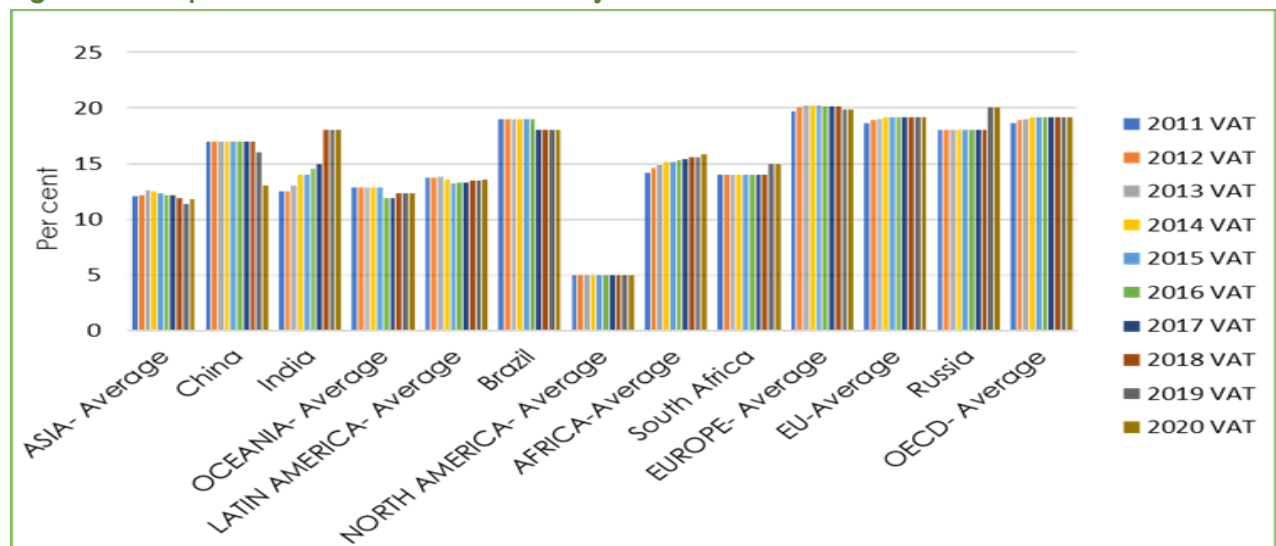
income tax (CIT) rates while maintaining stable personal income tax (PIT) levels and relying more on value-added tax (VAT). In contrast, developing economies continue to impose higher CIT and PIT but experience fluctuating VAT rates. This reflects a broader shift in OECD and EU countries towards consumption-based taxation, with an emphasis on increasing VAT while reducing CIT. Meanwhile, developing economies continue to rely on corporations and personal income taxes. A transition towards progressive wealth taxation, higher dividend taxes, resource rent levies, and financial transaction taxes could help reduce reliance on corporate and labour taxation.

Countries with lower corporate tax rates combined with state-led industrial policies, such as those in East Asia, have demonstrated higher industrial growth, emphasising the need for tax reforms aligned with industrial policy. Corporate taxation should differentiate between productive and speculative activities, ensuring that high CIT rates target rentier activities, such as financial speculation, rather than discouraging growth in productive sectors.

8.3. Comparison of VAT trends in various jurisdictions

VAT rates in developing economies remain relatively high despite lower income levels. Africa's average VAT rate was recorded at 15.6% in 2020, lower than the OECD average of 19.2% and the EU's 21.5%, yet still substantial given the region's economic structure and income disparities. Latin American countries maintain VAT rates of approximately 12%, reflecting a reliance on consumption-based taxation. South Africa increased its VAT from 14% to 15% in 2018, where it has remained stable through 2020. VAT, being a consumption tax, applies equally to all consumers but disproportionately affects lower-income groups, who spend a larger share of their income on essential goods and services. Many developing economies lack strong social safety nets or VAT exemptions for essential goods, making VAT a more regressive burden than in OECD and EU countries.

Figure 3: Comparison of VAT trends in various jurisdictions



Source: KPMG online database

8.4. Structural issues in VAT dependence

Developing economies often rely heavily on VAT due to weaker direct tax collection mechanisms, resulting in a higher tax burden on consumers rather than corporations or high-income earners. Many of these countries also lack effective tax enforcement, enabling tax avoidance by the wealthy while shifting the VAT burden onto ordinary consumers. Parliament

should note that VAT exemptions tend to be inefficient as they disproportionately benefit higher-income households, reduce government revenue, and create administrative challenges. Direct cash transfers are often more effective than VAT exemptions in mitigating the regressive impact of consumption taxes. Governments in developing economies should enhance direct tax collection, improve compliance, and close tax loopholes rather than over-relying on VAT for revenue generation. A tiered VAT system, where luxury goods are taxed at higher rates while essential goods face lower or zero VAT, could be a more equitable approach.

8.5. Corporate taxation

A trend of declining CIT rates in developed economies contrasts with persistently high CIT rates in developing regions. The OECD's average CIT declined from 23.5% in 2018 to 23.1% in 2020, while the EU maintained a stable rate of 21.5%. In contrast, South Africa, Latin America, and Africa continue to charge CIT rates of 27% or higher. Developing economies often depend on corporate taxation, particularly from large corporations, to sustain public revenues due to narrower personal tax bases and weaker enforcement mechanisms.

Empirical evidence suggests that merely reducing CIT is insufficient to attract sustained investment without complementary factors such as infrastructure, regulatory certainty, skilled labour, etc. Lowering CIT rates in developing countries, as seen in South Africa, has not consistently spurred investment due to the financialisation of non-financial corporations, which often redirect capital into tax havens or speculative financial and real estate markets. The analysis above highlights the challenges developing economies face in structuring their tax policies effectively and fairly. A balanced approach that improves direct tax collection, reduces reliance on VAT, and differentiates corporate taxation based on economic activity could foster a more equitable and growth-oriented tax system. Developing countries must ensure that tax structures support long-term economic development rather than inadvertently stifling it.

9. Conclusion

The 2025 Budget present an important opportunity for the 7th administration to demonstrate its commitment to achieving the priorities outlined in the National Development Plan and the 2024-2029 Medium-Term Development Plan. These priorities include promoting inclusive growth and job creation, reducing poverty and addressing the high cost of living, and building a capable, ethical, and developmental state.

This brief has presented a range of options for Parliament to consider in its pursuit of these goals. These options include alternative revenue sources, such as a wealth tax, and strategic spending initiatives focused on social and economic investment and household support. The economic simulations presented in this brief suggest that such measures could lead to significant progress towards achieving national priorities, including boosting economic growth, reducing unemployment, lowering the debt-to-GDP ratio, and improving income distribution.

The analysis of the VAT increase proposed in the original 2025 Budget highlights the regressive nature of this tax and its potential to exacerbate inequality. In contrast, a wealth tax or alternative non-tax measures could generate similar revenue while placing the burden on those most able to pay. The government should carefully consider these options and prioritise those that align with its developmental objectives and commitment to equity.

In addition to the recommendations outlined in this brief, the government should also consider the following:

- **Strengthening tax administration:** Enhancing the capacity of the South African Revenue Service (SARS) to improve tax compliance and enforcement is crucial for increasing revenue without resorting to tax increases or spending cuts.
- **Improving public financial management:** Ensuring efficient and effective use of public funds is essential for maximizing the impact of government spending and achieving developmental goals.
- **Promoting transparency and accountability:** Providing clear and accessible information about government revenue and expenditure is crucial for building public trust and ensuring effective oversight.

By adopting a comprehensive and strategic approach to fiscal policy, the government can effectively address the nation's challenges and build a more inclusive and prosperous future for all South Africans.