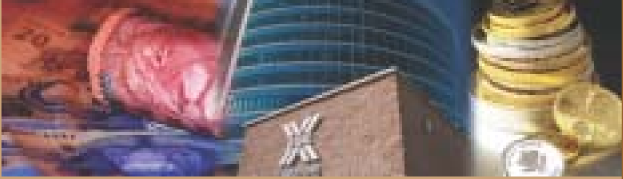


National finance

Government's macroeconomic policies aim at meeting the challenges of South Africa's social and economic development in the context of an increasingly interdependent global environment. Increasing growth to a higher and more sustainable level of at least 6% in line with government's Accelerated and Shared Growth Initiative for South Africa (AsgiSA) is a top priority.

South Africa's economy is growing at 5% a year, and contributing to job creation and rising incomes. Inflation is expected to remain at about 4,5% on average over the next three years, thus protecting the buying power of South Africans, especially the poor.

Fiscal policy framework

The Minister of Finance, Mr Trevor Manuel, presented the Budget for 2006/07 on 15 February 2006.

Tabling his 10th Budget in the National Assembly, he said main Budget revenue in 2006/07 was expected to be R446,4 billion and spending R472,7 billion – resulting in a deficit of only 1,5% of gross domestic product (GDP).

Total tax relief in 2006/07 was expected to amount to R19,1 billion, of which R13,1 billion was in personal income tax relief to individuals.

The income threshold below which no tax was payable by individuals was raised to R40 000 for the 2006/07 tax year and for taxpayers over 65, to R65 000 a year.

The maximum marginal rate of tax remained at 40%, while the threshold was raised from R300 000 to R400 000.

The South African Revenue Service (Sars) would offer a tax amnesty to small businesses with a turnover of R5 million or less, who had not been compliant with the tax system.

Taxes and penalties would be waived for the years of assessment ending on or before 31 March 2004, subject to a non-disclosure penalty of 10% on taxable income for 2005.

The annual turnover threshold to qualify as a small business corporation rose from R6 million to R14 million, and the taxable threshold for the lower 10% rate would be increased from R250 000 to R300 000.

The small business income tax exemption threshold would also be raised from R35 000 to R40 000.

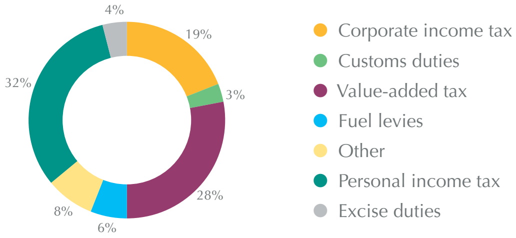
Tax on retirement funds would be halved from 18% to 9%, with effect from 1 March 2006.

The offshore foreign currency allowance for individuals was increased from R750 000 to R2 million.

On the spending side, the maximum old-age and disability grants and the Care Dependency Grant were increased 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.

Other expenditure highlights for the Medium Term Expenditure Framework included:

* significantly increased spending on education, public health, social welfare services, and housing and municipal infrastructure, local transport and water schemes.
* R3,5 billion more for national roads and rail infrastructure, and R7,1 billion for the Gautrain project
* R5,4 billion to expand and equip police and improve courts administration and justice department capacity
* R3,1 billion added to defence modernisation and infrastructure
* R900 million to foreign affairs capacity and the African Renaissance Fund
* R3,3 billion to improve the maintenance of government buildings.



Tax revenue – Source: *A People's Guide to the Budget 2006*

In June 2006, South Africa's only stock exchange, the JSE Limited, listed on its own exchange.

In a momentous occasion in the history of the exchange, guests were joined by Deputy President Phumzile Mlambo-Ngcuka, and wore a variety of hats in memory of the closing day of the old trading floor nearly 10 years ago to the day.

The JSE now joins an elite number of international exchanges – including the London and New York stock exchanges, Deutsche Borse, Nasdaq, Euronext, the Australian Stock Exchange, the Singapore Exchange and the Hong Kong Exchanges and Clearing – that have listed on their own markets.

For investors in South Africa and abroad, the move brings heightened transparency and visibility to the trading of JSE shares, which in turn has the potential to improve their liquidity and tradeability.

Debt management

Sound macroeconomic policy and fiscal management have played a central role in building South Africa's reputation as a credible and competitive borrower. The approach to debt management has assisted towards developing the financial sector as a source of capital for the public and private sectors. Improved access to capital and the development of specialised debt instruments for private borrowers have given a boost to domestic economic activity.

Government has focused on placing the management of national debt on a sound footing, and as a result, debt-service costs have been reduced considerably. The fiscus has directly benefited from declining debt service costs, which have freed additional resources for social expenditure. In 1998, for each rand of revenue collected, government spent 24 cents to service debt; by 2005, only 12 cents of every rand were spent on debt service – and this will decrease to 10 cents per rand by 2009.

Debt as a percentage of GDP has reached historic lows, increasing the financial sustainability of the economy in coming years. Net government debt as a percentage of GDP is expected to decline over the medium term to 27,7%. Foreign debt as a percentage of total gross debt remains low at 13,4%.

Financial markets

Market performance

The South African bond market is one of the most liquid emerging bond markets in the world. Turnover in listed debt declined in 2005, with volumes decreasing from R8,4 trillion nominal in 2004 to R8,1 trillion nominal, which is a drop of 4%. The decrease in nominal turnover was also reflected in the lower number of matched trades for the year, which decreased from 328 000 in 2004 to 298 000 in 2005. Turnover in the spot market increased from 34,1% of total turnover in 2004 to 37,3% in 2005.

Although turnover figures for 2005 dropped significantly, the turnover velocity of listed debt instruments remained healthy at 13 times the market capitalisation for 2005.

While 95% of market turnover in 2005 was in government and utilities stock, there was an ever-increasing amount of listings and turnover in corporate issuances and securitisations which, together in 2005, accounted for 5% of total turnover.

Secondary capital-market activity

South African bond yields declined considerably between October 2005 and February 2006. The closing yields on government bonds declined to historically low levels on 20 February 2006, with the yields on two-year R194, four-year R153, nine-year R157 and 20-year R186 government bonds declining to 6,93%, 7,05%, 7,13% and 6,81%, respectively. Factors that contributed to the decline in local yields include the firmer exchange value of the Rand, which served to lessen medium-term inflation concerns, and a lowering of the tax rate on interest income for the retirement fund industry, announced in the February 2006 Budget. After being net purchasers of South African bonds to the value of R0,4 billion in 2004, non-residents were net sellers of bonds to the value of R10,7 billion in 2005.

Managing public finances

Transforming public-sector financial management is one of National Treasury's key objectives. To this end, National Treasury has been implementing the Public Finance Management Act (PFMA), 1999 since 1 April 2000.

There have been measurable improvements in the quality of financial management in both the national and provincial spheres of government. These include among others:

- an improved linkage between planning and budgeting whereby departments are now required to compile and table strategic plans that are consistent with their budget envelope
- strategic plans and budget documentation containing improved information on measurable objectives that are expressed in terms of quantity, quality and timeliness
- departments submitting monthly expenditure reports on actual expenditure incurred as well as on projected expenditure for the remainder of the financial year
- risk-management processes now being implemented by institutions

Fact:

By May 2006, 20% of South Africa's companies fell in the 'super growth' category of firms which have grown considerably more than the average – up from 16% in 2005 and 12% in 2004 – according to consultancy Grant Thornton International.

- the establishment of internal audit functions and audit committees in all departments
- the setting of accounting standards in accordance with best accounting practices, both locally and internationally
- the finalisation and submission of financial statements to the Auditor-General (AG) within two months after close of the financial year
- the tabling of annual reports in the legislature within six months from the end of the financial year.

Taxation

Sars collected R417,4 billion in taxes during the 2005/06 financial year, exceeding its revised target of R417,05 billion by almost R337 million and its original target of R372,8 billion by R45 billion. The revenue haul will help trim South Africa's budget deficit for 2005/06 from 1,5% to 0,3% of GDP.

Personal income tax yielded R126 billion, company tax yielded R87,5 billion and value added tax yielded R114 billion. Sars also collected R8,5 billion in transfer duties, R15,7 billion in excise duties, R18 billion in customs duties; and R20,5 billion in fuel levies.

Income tax is government's main source of income and is levied in terms of the Income Tax Act, 1962.

In South Africa, income tax is levied on South African residents' worldwide income, with appropriate relief to avoid double taxation. Non-residents are taxed on their income from a South African source. Tax is levied on taxable income which, in essence, consists of gross income less allowable deductions as per the Act.

Personal income tax relief in 2006/07 amounted to 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 was R12,1 billion.

The income threshold below which no tax is payable by individuals was raised to R40 000 for the tax year beginning March 2006, and

The result placed South Africa in the top 10 on Grant Thornton's Super Growth Index, which ranks countries by proportion of super growth companies, for the third year running, reflecting the country's consistent economic growth over this period.

for taxpayers over the age of 65 to R65 000 a year. Changes to the tax brackets resulted in significant relief for all taxpayers, with an estimated 49% of the benefit going to those who earn less than R150 000 a year, and 24% of relief going to the income bracket R150 000 to R250 000. The maximum marginal rate of tax remains 40%, while the threshold was raised from R300 000 to R400 000.

Auditor-General

The Constitution guarantees the independence of the AG. The office audits national, provincial and local government. The AG has the power to audit the activities of public entities without the approval of the CEO or directors.

South African Reserve Bank

The bank, which is independent, formulates and implements monetary policy and regulates the supply of money by influencing its cost.

An important responsibility of the bank is to ensure that the banking system as a whole is sound and meets the requirements of the community.

The bank acts as a banker to other banking institutions. It is also the custodian of the statutory cash reserves and provides facilities for the clearing and settlement of inter-bank obligations.

The banking industry

At the end of December 2005, 34 banks, including 15 branches of foreign banks and two mutual banks, were registered with the Office of the Registrar of Banks. Furthermore, 47 foreign banks had authorised representative offices in South Africa. By the end of December 2005, the banking institutions collectively employed 122 135 workers.

Four major groups dominated the South African banking sector, holding 82% of its assets:

- Amalgamated Banks of South Africa Group Limited, which is internationally-owned
- Standard Bank Investment Corporation Limited
- FirstRand Holdings Limited
- Nedbank Limited.

Industry-wide net income after tax increased to 1,1% of total assets in 2005. As a percentage of equity, industry-wide net income after tax decreased from 14,7% in 2004 to 14,5% in 2005.

Insurance companies

By mid-2006, 81 long-term insurers were registered. The total net premiums received and outstanding for 2004 (unaudited figures) amounted to R153 billion, while total assets amounted to R908,1 billion.

Development Bank of Southern Africa (DBSA)

The primary purpose of the bank is to promote economic development and growth, human resource development and institutional capacity-building. The bank's mandate is focused on infrastructure.

Growth in broad money supply (M3) rose during the course of 2005 and early 2006, accelerating from 13% in the early months of 2005 to 21% in February 2006.

Banks' loans and advances to the domestic private sector remained relatively strong during 2005 and early 2006, registering average growth rates of 21% to 22%. Asset-backed credit (mortgage advances, leasing finance and instalment sale credit) constituted the bulk of the increase in banks' total loans and advances throughout 2005 and early 2006.

Growth in M3 and banks' total loans and advances was consistent with firm increases in nominal income, expenditure and wealth.

Following a reduction in the repo rate to 7% in April 2005, the Reserve Bank's Monetary Policy Committee (MPC) left the repo rate unchanged at its successive meetings until June 2006. The MPC was mindful of significant risk factors to inflation but positive that these risks were balanced enough not to require an adjustment to the policy stance.

In June 2006, the repo rate was increased by 50 basis points to 7,5%. In August 2006, it was increased to 8%.

Launched on 25 October 2004, the Mzansi bank account was conceived out of the requirements set out in the Financial Services Charter. Mzansi is supported by Absa, First National Bank, Nedbank, Standard Bank and the PostBank.

By June 2006, Mzansi had led to the creation of 3,3 million new bank account holders.