INSTITUTE FOR ECONOMIC JUSTICE
RESEARCH POLICY ADVOCACY

STATEMENT

Budget 3.0 must not retreat into austerity

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In the build-up to the tabling of the third edition of the 2025 National Budget next Wednesday, the division between National Treasury and the rest of our society is once again laid bare. Parliament, many political parties, labour, civil society, and the general public have all vehemently rejected National Treasury's long-standing policy of austerity. This political consensus means that the upcoming budget must cement the break from spending cuts and utilise the National Budget to achieve inclusive growth. Critical to this is the adoption of measures to raise additional revenue. These measures are required to ensure previously proposed and critically needed increases to social and economic priorities are met. Failing to do so, will have devastating consequences for those who rely most on South African public services.

Says IEJ Tax and Budget Policy Researcher Zimbali Mncube: “The growing political consensus against budget cuts, including from the main partner in the GNU, the ANC, is a vital step forward, but without progressive revenue measures to fund this shift, the opportunity to adopt a pro-poor and pro-growth budget for the first time in more than a decade will be lost.”

Below, the IEJ provides an analysis of the current political context, the impact of choices that are being made, and demonstrates how additional funds can be raised in both the short and medium term.

For media inquiries, please contact:

Dalli Weyers | dalli.weyers@iej.org.za | 082 460 2093

Briefing on issues at stake in Budget 3.0

1. National Treasury's statements in the run-up to Budget 3.0 ignore an emerging consensus on protecting the most vulnerable and raising alternative revenue measures

The protracted budget deliberations this year have meant that more stakeholders have weighed in on the National Budget than ever before. The Institute for Economic Justice (IEJ) and civil society partners have called for the need to abandon budget cuts and to "rethink the fiscal framework in line with efforts to tackle unemployment, stimulate demand, and expand supply in the economy," while putting forward credible modalities of raising additional revenue. Labour federations joined forces with social movements under the People's Budget Assembly, submitting petitions calling for an "end to the policy of budget cuts that are crippling the public sector and harming the poor and unemployed".

Major political parties have decisively broken with National Treasury's conventional wisdom. The ANC has argued that the Minister must table "a people's budget that does not retreat into austerity, nor sacrifice long-term transformation at the altar of technical compliance. Instead, it balances pro-growth policy with pro-poor spending, rooted in the developmental ethos of the Freedom Charter and the democratic values of the Constitution." Other parties within and outside of the GNU have endorsed similar sentiments, with the multi-party statement on the scrapping of the VAT hike asserting that "fiscal consolidation must not mean austerity for the vulnerable" but rather National Treasury must work with Parliament "to ensure sound, equitable and developmental financing." This marks an important break with National Treasury's ongoing desire to slash expenditure.

Despite this, parties have been less forthright in acknowledging that additional revenue must be raised elsewhere, with the notable exception of the EFF, which has proposed tackling illicit financial flows, establishing a sovereign wealth fund, implementing a wealth tax on the rich, and increasing corporate tax as alternatives to spending cuts. All parties must now rally behind practical measures to raise additional revenue, or risk the danger that their call for advancing a pro-poor and pro-growth budget will ring hollow.

Despite this emerging political consensus against cutting spending and rethinking fiscal policy, the National Treasury has refused to consider tax measures proposed by stakeholders and parties, claiming that they do not offer immediate revenue streams or would harm economic growth. This raises the risk of renewed expenditure cuts in Budget 3.0 to make up for the revenue shortfall following the VAT reversal.

2. Implications of the revenue shortfall

To preemptively justify expenditure cuts, National Treasury has deliberately exaggerated the revenue implications of removing the originally proposed VAT increase. A reversal of VAT implies a R2.7 billion gap in the current fiscal year and a R60 billion gap over the medium term, instead of the R75 billion widely quoted. National Treasury estimated that the two-phased VAT increase would have brought in R75 billion over the next three years. The VAT increase was paired with measures to relieve households, namely, additional zero-rating of goods and keeping the general fuel levy unchanged.

A reversal of the VAT and the additional zero-rating means gross tax revenue will be lower by R11.5 billion in 2025/26, R27.7 billion in 2026/27, and R29.4 billion in 2027/28, compared to Treasury's Budget 2.0. estimates. With SARS over-collecting by around R8.8 billion for 2024/25, only R2.7 billion is required to cover the gap for 2025/26. The downward adjustments in tax collection are around 1% of total government spending in the two outer fiscal years.

That there is even a "revenue shortfall" or "revenue gap" is partly a consequence of National Treasury's dogmatic adherence to arbitrary debt reduction targets. National Treasury has reiterated its commitment to these targets even within changed economic circumstances. What the National Treasury is essentially saying is that if growth and revenue are lower due to, for example, President Trump's nonsensical tariff policies, then poor South Africans should bear the brunt of this through expenditure cuts rather than allow for a simultaneous adjustment of debt targets.

If, as political parties have argued, we are not willing to let the poorest bear the brunt of adjustment through, for example, worse education, less access to medical care, and lower social grants, and National Treasury wishes to maintain debt and deficit targets, then raising additional revenue is the only logical course of action.

3. The return to austerity: A political choice that is shouldered by the most vulnerable

In light of the revenue options available to National Treasury, a return to austerity would be a political choice rather than a necessity. It is a political choice whose impact is shouldered by 12,7 million people without jobs, at least 10 million of whom are in long-term unemployment (that is, unemployed for over a year). Most of these are young people (with unemployment at 62% for 15-24 years), and Black women (with unemployment at 40%). It is a choice that will increase unpaid care work for women as public services fail, exacerbate women's unemployment through laying off teachers and healthcare workers, and make a nutritious diet out of reach for children from poor families due to the high cost of living and below-inflation increases to social grants. We have noted that SASSA, as a result of conditions imposed by National Treasury, has already begun to impose the unnecessarily stringent regulations attached to the SRD grant on other social grants to limit the number of social grant recipients - a move that will increase food insecurity.

The long-term effects of spending cuts are not just social, but also hurt growth. Since the size and growth of GDP are influenced by private and public investment, cutting government spending and increasing regressive taxes during recessionary periods often leads to lower demand and decreased revenue. This, in turn, contributes to low growth and an increased debt-to-GDP ratio. Evidence shows that the effects can last up to fifteen years, contradicting suggestions that spending cuts are a necessary short-term pain now for long-term gains.

The Finance Minister has admitted as much, saying "we [National Treasury] have been giving budget cuts for a number of years and they've not achieved the desired outcome. We've not achieved fiscal consolidation. Instead, the budget cuts have led to an increase in debt-to-GDP ratios."

While National Treasury's narrow obsession with the debt-to-GDP ratio is wrong, their concerns about the high costs of refinancing debt and undertaking new borrowing are legitimate, as real interest rates on government bonds remain high (influenced by credit rating agencies and the long-term bond market). However, as we have argued elsewhere, there are more direct ways to tackle the cost of debt that are less harmful than austerity.

Such measures could include the use of capital management techniques such as capital controls to stabilise short-term, speculative capital flows and provide room to reduce interest rates. They could also include implementing capital allocation tools such as regulated lending by banks to steer credit to productive sectors of the economy at affordable rates, including through Reserve Bank lending; central bank intervention in the primary market to purchase government bonds; and using prescribed assets to make large pools of capital available at affordable rates. These measures, however, would need coordinated macroeconomic policy intervention that breaks with the National Treasury's traditional economic thinking.

4. Alternative measures to raise revenue

Our policy proposals to raise revenue take into account that there are immediate revenue needs this year, as well as the need to think more sustainably about permanent revenue sources, and how these have to be sequenced carefully, and preceded by improved state capacity, including through improving allocations to the South African Revenue Services to administer and collect taxes.

Immediate measures to raise revenue include:

- Removing tax breaks linked to pensions or medical aid contributions for high-income earners (those earning above R1 million per year). The government spent approximately R51 billion on these in 2022/23 (equivalent to R60.4 billion in 2024/25).
- Restoring the Corporate Income Tax (CIT) to 28%. This would have raised an extra R12 billion in 2024/25.
- Drawing down from the Gold and Foreign Exchange Contingency Account (GFECRA), which still has over R300 billion. Initial withdrawals have already taken place from GFECRA, with no negative consequences, and an appropriate buffer for currency fluctuations can still be kept in place.

Medium-term measures include:

- Funding and support of measures to reduce illicit financial flows (IFFs). South Africa loses between R63.4 billion and R90.6 billion per year due to IFFs.
- Undertaking a transparent and targeted expenditure review to cut inefficient programmes.
- Implementing a net wealth tax at rates between 3% to 7% on the richest 1% could raise R70 to R160 billion.
- Implementing a financial transactions tax at 0.1% could raise R40 billion.
- Implementing a luxury VAT at 25% would generate about R9 billion annually.
- Implementing a resource rent tax to raise R38 billion.

Treasury has responded to some of these proposals. In the table below, we demonstrate some of the shortcomings of their responses and why they fail to make the case for dismissing revenue-raising alternatives.

Proposal	**Treasury's response**	**IEJ's response**
Immediate measures		
Restore CIT to 28%	It will harm growth by reducing the competitiveness of firms. A lower CIT rate encourages investment. CIT share of GDP in SA is already higher than the OECD average. CIT generates less revenue than VAT.	Treasury must show the extent to which business competitiveness would be affected by a 1p.p increase, and this must be weighed against the benefits from higher government revenue. A reduction in CIT failed to increase investment. Many other factors, including demand and the cost of inputs, affect investment. The size of the contribution of CIT: GDP reflects the size of corporate profits, not over-taxation, as the effective CIT tax rate is average. Even if revenue is smaller than a VAT increase, additional CIT revenue can be part of a package.
Remove retirement fund tax breaks on high-income individuals	The reason that there are deductions is so that when retirement funds become disposable, they are taxed. If the deductions are cancelled, the funds would not be taxed when they are withdrawn or paid out as a lump	Limiting tax breaks for retirement contributions has nothing to do with retirement contributions being a pre-tax benefit. That is, the proposal would continue to allow contributions to retirement savings to be made tax-free. It would just

	sum. Due to SA's low savings rate, one has to take into account what happens not just on the tax side but also with the savings in general. The retirement reforms have been designed to encourage savings. In this sense, rebates are important to encourage savings and thereby support investment.	reduce the tax *refund* that is provided to contributors on top of this. Levels of investment are not just determined by a limited pool of savings, but rather, it is government spending that faces a risk through the budget cuts. The highest-income earners will likely save for retirement irrespective of the incentives they get from rebates.
Further drawdown on GFECRA	Need to maintain a buffer in case of reversal of currency trends.	The GFECRA currently holds over R300 billion. A portion of this, at least R50 billion (and possibly up to R100 billion) can still be drawn upon without risking a crisis in the event of a reversal of recent currency trends as a buffer of around R200 billion will remain in place.
Medium-term measures		
Increase allocation to SARS to tackle illicit financial flows and other forms of non-compliance	Additional allocations will be made to SARS to increase tax administration capacity	Additional allocations of R3.5 billion are welcome, but total allocations are still well below what SARS asked for (+/- R17 billion), which may affect the ability to carry out objectives fully.
Taxing more wealth effectively by implementing a net wealth tax, a financial transaction tax, and a resource rent tax	South Africa already taxes wealth Imposing a wealth tax will erode the personal income tax paid by the wealthy through capital flight and generate little revenue Wealth taxes are administratively complex and costly to administer	The current resistance to taxing wealth stems from neoclassical economic theory (optimal tax theory) that assumes all taxes distort markets. The theory is based on models that ignore the real-world benefits of redistribution and the potential that this redistribution has in alleviating inequality, hunger, and supporting job creation. The degree to which capital flight happens would be influenced by many variables, such as the tax rate

		and the cost of transferring capital. It is not clear that a wealth tax applied at low rates, to a relatively small group (super-rich), would lead to such an erosion of the PIT tax base as to offset the revenues gained from taxing wealth. Furthermore, the state could consider the use of capital controls. Initial costs of setting up a system to tax net wealth are likely to be high (due to start-up costs, fixed capital, etc.). But average costs may decline once the system is established. Treasury and SARS must provide estimates for this. In other countries, administrative costs were far lower than revenue gains. The biggest concern are economic costs (e.g., non-compliance), which can also be minimised by capacitating tax authorities.

Source: National Treasury response to public hearings (2025), Rates Bill comments workshop (2025), and Budget Review (2025).

5. Looking ahead to Budget 3.0 and beyond

This year's budget has shown the need to open up the budget process to wider debate and interrogation than before. This entails meaningful consultation ahead of the tabling of the budget and adjustments. Ultimately, this will enable a shift in which the budget is not just seen as a technical exercise open to a few technocrats, but as a tool to support job creation and investment in public goods. Different stakeholders have highlighted the need for Budget 3.0 to move away from austerity and take up progressive alternative proposals to raise revenue. These can no longer be ignored if the government is to deliver on its Constitutional obligation to advance and protect socio-economic rights.

The Institute for Economic Justice (IEJ) is a progressive economic policy think tank committed to advancing economic justice, systemic change, and the equitable distribution of resources to ensure rights realisation and planetary wellbeing.

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