# Economic Landscape of South Africa

## INTRODUCTION

One of the leading economies in Africa, with a well-developed infrastructure and established trade links with the rest of the continent, South Africa is a suitable base for generating investment and trade with the rest of Africa, particularly in the sub-Saharan region.

The country accounts for approximately 40% of all industrial output, 25% of gross domestic product (GDP), over half of generated electricity and 45% of mineral production in Africa, whilst only representing 3% of the continents surface area. The South African economy is predominantly based on free market principles, with some areas of state control.

## POSITIONING AND ALLIANCES

South Africa, due to its geographical location on the southern tip of Africa, is well positioned to provide easy access to the rest of Africa via neighboring countries, such as Namibia, Botswana, Zimbabwe, Mozambique, Lesotho and Swaziland.

South Africa was admitted to the BRIC group of countries of Brazil, Russia, India and China (now called BRICS) in 2011.

South Africa forms part of the The Southern African Development Community (SADC). The SADC was established as a development coordinating conference (SADCC) in 1980 and transformed into a development community in 1992.

The SADC is an inter-governmental organisation whose goal is to promote sustainable and equitable economic growth and socio-economic development through efficient productive systems, deeper co-operation and integration, good governance and durable peace and security among fifteen Southern African Member States.

## SOUTH AFRICAN GOVERNMENT NATIONAL DEVELOPMENT PLAN 2030 (NDP)

The NDP defines a desired destination and identifies the role that different sectors of society need to play in reaching that goal. The NDP aims to eliminate poverty and reduce inequality by 2030.

## PROGRESS SINCE 1994

A detailed economic report on South Africa titled, “Two Decades of Freedom” which was released by Goldman Sachs, benchmarked economic progress of South Africa since the change in government in 1994.

According to their report, there have been a number of positives over this period:

- In 1994 total GDP was at $136bn – now $400tbn
- Inflation for 14 years to 1994 averaged 14% pa, while inflation from 1994 to 2012 averaged 6% pa
- Gross gold and reserves were $3bn, but are now $50bn
- The JSE market capitalisation was $101bn. Now touching $950bn
- Social grants have increased from 2.4 million to 16.1 million recipients

**INFLATION**

The South Africa Reserve Bank (SARB) inflation target is between 3 and 6%. The recorded inflation for the past 2 years is set out below.

**GDP SIZE AND GROWTH**

GDP Annual Growth Rate in South Africa is reported by Statistics South Africa. GDP Annual Growth Rate in South Africa averaged 3.19% from 1994 until 2013.

**WORLD RANKINGS**

| Economy | Ease of Doing Business Rank | Starting a Business | Getting Credit | Protecting Investors | Paying Taxes | Trading Across Borders |
|---|---|---|---|---|---|---|
| South Africa | 41 | 64 | 28 | 10 | 24 | 106 |
| Russian Federation | 92 | 88 | 109 | 115 | 56 | 157 |
| China | 96 | 158 | 73 | 98 | 120 | 74 |
| Philippines | 108 | 170 | 86 | 128 | 131 | 42 |
| Brazil | 116 | 123 | 109 | 80 | 159 | 124 |
| India | 134 | 179 | 28 | 34 | 158 | 132 |

Table from 2014 Doing Business Report, which lists the ranking obtained by the BRICS countries and the Philippines on specific areas.

In the 2013/14 World Economic Forum's Global Competitiveness index, South Africa was ranked as the 53rd most competitive country out of 148 surveyed, making it the second highest ranked country in Africa after Mauritius (45th) [Source: World Economic Forum, Latest publication date: September 2013].

The Doing Business Project provides objective measures of business regulation and their enforcement across 189 economies and selected cities at the subnational and regional level. In the 2014 Doing Business Report, South Africa obtained an overall ranking of 41st out of 189 economies.

Furthermore, South Africa ranked very favourably on specific areas such as ease of doing business, starting a business, getting credit and protecting investors, when compared to other BRICS countries and the Philippines.

## INTEREST RATES

The prime interest rate is the benchmark interest rate in South Africa and is reported by the South African Reserve Bank (SARB). The Prime Interest Rate in South Africa averaged 18.07% from 1994 until 2014, reaching an all-time high of 25.5% in June of 1998 and a record low of 5% in July of 2012. In South Africa, the interest rates decisions are taken by the South African Reserve Bank's Monetary Policy Committee (MPC).

## FOREIGN EXCHANGE CONTROL

Control is exercised through the Financial Surveillance Department ("FinSurv") of the South African Reserve Bank and through Authorised Dealers in foreign exchange at commercial and merchant banks. No South African resident company, close corporation or trust may acquire foreign assets or incur foreign liabilities without FinSurv approval. For purposes of the exchange control regulations, a non-resident is a natural person or legal entity whose normal place of residence, domicile or registration is outside the Common Monetary Area (CMA) – South Africa, Namibia, Swaziland and Lesotho.

## ACCOUNTING PRINCIPLES / FINANCIAL STATEMENTS – IFRS

Financial statements must be prepared annually. Certain companies are required to have their financial statements audited and other companies must have their financial statements independently reviewed, in terms of the Companies Act of 2008.

## BUSINESS ENTITIES

Companies are classified as profit or non-profit companies. The Companies Act of 2008 distinguishes between four types of profit companies:

- public company
- private company
- personal liability company
- state-owned company

A branch of a foreign company is required to register as an external company with the Companies and Intellectual Property Commission (CIPC) and is not subject to Dividends Withholding Tax (DWT).

Companies may be formed or acquired in South Africa.

## TAXATION

The Source of income tax law in South Africa is the Income Tax Act No.58 of 1962. Compliance with South Africa tax legislation is undertaken by the South African Revenue Services (SARS). South Africa has concluded more than 70 tax treaties at present.

**TAXABLE INCOME**

Income tax is imposed on a taxpayer's profits, which consist of business/trading income, passive income and capital gains. Expenses incurred in the production of income may be deducted in computing taxable income.

**CAPITAL GAINS**

66.6% (33.3% in the case of individuals) of capital gains are included in taxable income and taxed at the normal income tax rate. However, gains on the sale of substantial foreign shareholdings are exempt if certain conditions are satisfied.

**TAX RATE**

Companies are liable for income tax at a flat rate of 28% on taxable income. The rate on branches was reduced from 33% to 28% on 01 March 2012.

**TAX LOSSES**

Trading losses may be carried forward indefinitely. Assessed losses fall away if the company does not trade in a particular year of assessment.

**BUSINESS PROCESS SERVICES INCENTIVE (BPS)**

The BPS, effective for the period 1 January 2011 to 31 March 2014, replaced the Business Process Outsourcing and Offshoring incentive which came to an end on 31 March 2011. The objective is to attract investment and create employment in South Africa through offshore activities. The "base" incentive offers a three-year operational expenditure (OPEX) grant. In addition to this grant a "graduated" bonus incentive is offered for greater job creation.

**EMPLOYMENT TAX INCENTIVE (ETI)**

The ETI is an incentive aimed at encouraging employers to hire young and less experienced work seekers and was implemented with effect from 1 January 2014. It reduces the cost to employers of hiring young South Africans aged 18 – 29, earning less than R6,000 per month, through a cost-sharing mechanism with government. Currently, excess amounts can be set off against future PAYE liabilities. To enhance this incentive, SARS is developing a mechanism to reimburse firms in instances where the incentive exceeds PAYE payable. The refund system will become effective during the fourth quarter of 2014.

## OTHER INCENTIVES

Other incentives include a preferential corporate tax rate for small business corporations; an R&D deduction; depreciation allowances; urban development and infrastructure development allowances; public private partnerships grants; environmental expenditure deductions; a carbon-reducing exemption; oil and gas income tax incentives; renewable energy related allowances and a film allowance.

## DIVIDENDS WITHHOLDING TAX (DWT)

Dividends paid to individuals, trusts and foreign persons are subject to a 15% withholding tax (subject to the provisions of any applicable tax treaty e.g. UK – 5%, USA – 5%).

## WITHHOLDING TAX ON INTEREST

With effect from 1 January 2015 interest paid to non-residents, to the extent that the amount is regarded as having been received or accrued from a source in the Republic, subject to certain exemptions (e.g. any bank, national, provincial or local government; or in respect of listed debt), will be subject to a final withholding tax at a rate of 15% (subject to the provisions of applicable tax treaties).

## WITHHOLDING TAX ON ROYALTIES

Royalties paid to non-residents, to the extent that the amount is regarded as having been received or accrued from a source in the Republic, are subject to a final withholding tax at a rate of 12% (15% with effect from 1 January 2015), subject to the provisions of applicable tax treaties.

## OTHER WITHHOLDING TAXES

Any person who purchases immovable property in the Republic from a non-resident, must withhold from the amount that person must pay to the non-resident a withholding tax equal to:

a) 5% if the non-resident is an individual;

b) 7.5% if the non-resident is a company; and

c) 10% if the non-resident is a trust.

A final withholding tax of 15% is withheld on gross payments to non-resident entertainers and sportspersons who earn income in South Africa.

With effect from 1 January 2016 service fees paid to or for the benefit of any non-resident will be subject to a final withholding tax at a rate of 15%, but only to the extent that the amount is regarded as having been received by or accrued to that non-resident from a source within the Republic and subject to the provisions of applicable tax treaties. “Service fees” means any amount that is received or accrued in respect of technical, managerial and consultancy services but does not include services incidental to the imparting of or the undertaking to impart any scientific, technical, industrial or commercial knowledge or information, or the rendering of or the undertaking to render any assistance or service in connection with the application or utilisation of such knowledge or information.

**EMPLOYEES TAX: PAY AS YOU EARN (PAYE)**

Employees' tax is the tax withheld by an employer from an employee's remuneration. The amount of employees' tax is calculated in accordance with tax tables issued by SARS and is paid to SARS by the employer. Directors of companies and members of close corporations are also regarded as employees for this purpose.

**SKILLS DEVELOPMENT LEVY (SDL)**

SDL is a payroll tax on employers with annual payroll costs above ZAR 500,000 and is based on 1% of payroll. The levy entitles employers to claim the cost of training employees from relevant Sector Education and Training Academies (SETA), in certain instances.

**UNEMPLOYMENT INSURANCE FUND (UIF)**

UIF is a social security tax on employers and employees, with both contributing the equivalent of 1% each of an employee's gross income (up to a capped amount) to the Unemployment Insurance Fund.

**TRANSFER PRICING**

Transfer pricing legislation requires a South African taxpayer to follow arm's length principles in transactions with connected persons outside South Africa. Changes to the transfer pricing rules that apply as from 01 April 2012 shifts the responsibility for adjusting prices to arm's length from the tax authorities to the taxpayer.

**THIN CAPITALISATION**

Thin capitalisation provisions limit the deduction of interest payable by South African companies on debt provided by a non-resident connected person in relation to the South African borrower or a non-resident connected person entitled to participate, directly or indirectly, in not less than 25% of the company's equity. As from 01 April 2012, the thin capitalisation rules merged into the general transfer pricing rules and the "safe-harbour" 3:1 ratio no longer applies. The main test for the thin capitalisation purposes is to assess the commercial terms and conditions of an agreement concluded between independent parties as compared to the terms and conditions concluded between a South African taxpayer and a non-resident connected person.

**CONTROLLED FOREIGN COMPANIES (CFC)**

Under the CFC rules, an amount equal to the net income earned by a CFC in relation to a South African resident is subject to tax in the hands of the South African resident unless an exemption applies. A CFC is a foreign company in which one or more South African residents hold, directly or indirectly, more than 50% of the participation or voting rights of the company. Tax paid in the foreign country may generally be offset against the South African tax payable.

**TAX YEAR-END**

The tax year-end is the same as the corporation's accounting year-end. Companies are required to file their income tax returns annually, within 12 months of the company's financial year-end.

**PROVISIONAL TAX**

Advance payments of tax must be made twice a year, based on estimates of the final tax amount, the first during the first six months of the company's financial year and the second before the end of the year. Where the provisional tax payments are less than the final tax liability, an additional payment of provisional tax must be made within six months after the end of the tax year. Penalties and interest are imposed for failure to comply. Where the taxable income is greater than R1 million, the second provisional tax estimate must be greater than 80% of the final tax payable. Any shortfall will be subject to a penalty.

**VALUE ADDED TAX (VAT)**

VAT is levied on the sale of goods and the provision of services at a standard rate of 14%; certain transactions are zero-rated or exempt. VAT vendors are entitled to input VAT credits of the VAT paid on the acquisition of goods or services for enterprise purposes.

A vendor making standard or zero-rated supplies of more than R 1 million per year is obliged to register. Vendors below the R1m threshold may elect to register as a VAT vendor voluntarily.

VAT returns must generally be submitted every two months, but businesses with an annual turnover in excess of ZAR 30 million must submit monthly returns. Returns must be submitted within 25 days after the end of the tax period. Full payment must accompany the return.

**BLACK ECONOMIC EMPOWERMENT AND AFFIRMATIVE ACTION**

Black Economic Empowerment (BEE) is a programme which promotes the accelerated integration of black people into the South African economy. Compliance is voluntary.