IMF Country Report No. 20/226

SOUTH AFRICA

July 2020

REQUEST FOR PURCHASE UNDER THE RAPID FINANCING INSTRUMENT—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR SOUTH AFRICA

In the context of the Request for Purchase Under the Rapid Financing Instrument (RFI), the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Chair of the Executive Board.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on July 27, following discussions that ended on July 13, with the officials of South Africa on economic developments and policies underpinning the IMF arrangement under the Rapid Facility Instrument. Based on information available at the time of these discussions, the staff report was completed on July 17.
- A **Statement by the Executive Director** for South Africa.

Letter of Intent sent to the IMF by the authorities of South Africa*

*Also included in Staff Report

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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Washington, D.C.

PRESS RELEASE

PR 20/271

IMF Executive Board Approves US$4.3 Billion in Emergency Support to South Africa to Address the COVID-19 Pandemic

FOR IMMEDIATE RELEASE

- The COVID-19 outbreak is leading to a sharp economic contraction and significant financing needs in South Africa.
- The IMF approved US$4.3 billion in emergency financial assistance under the Rapid Financing Instrument to support the authorities' efforts in addressing the challenging health situation and severe economic impact of the COVID-19 shock.
- Once the pandemic is behind, there is a pressing need to ensure debt sustainability and implement structural reforms to support the recovery and achieve sustainable and inclusive growth.

Washington, DC – July 27, 2020: The Executive Board of the International Monetary Fund (IMF) today approved South Africa's request for emergency financial assistance of SDR 3,051.2 million (US$ 4,286.5 million or 100 percent of quota) under the Rapid Financing Instrument (RFI) to meet the urgent balance of payment (BOP) needs stemming from the outbreak of the COVID-19 pandemic.

The pandemic is evolving in South Africa at a challenging time. With severe structural constraints to growth, economic activity has weakened over the last decade despite significant government spending, resulting in high unemployment, poverty, and income inequality. Like in other emerging economies, financial market volatility has increased during the pandemic, but the financial system is showing resilience.

The RFI will help fill the urgent BOP needs originating from the fiscal pressures posed by the pandemic, limit regional spillovers, and catalyze additional financing from other international financial institutions. It will complement the authorities' strong policy response to the crisis and their planned post-COVID-19 fiscal consolidation and reforms to promote growth that benefits all South Africans. The authorities have committed to manage the IMF's emergency financial assistance with full transparency and accountability.

Following the Executive Board's discussion, Mr. Geoffrey Okamoto, First Deputy Managing Director and Acting Chair, issued the following statement:

"South Africa's economy has been severely hit by the COVID-19 crisis, reporting the highest number of cases in sub-Saharan Africa. A deep economic recession is unfolding as the decline in domestic activity and disruptions in the global supply chain resulting from the COVID-19 shock have added to a pre-existing situation of structural constraints, subdued growth, and deteriorating social outcomes.

"The authorities responded swiftly to the crisis. The June *Supplementary Budget Review* presented to Parliament contains a plan to reprioritize budget appropriations toward health and mitigation spending and devote additional budgetary outlays to protect the poor, the unemployed, and the most affected businesses. The South African Reserve Bank (SARB)

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USA

took strong and timely action by lowering significantly the policy rate and ensuring adequate liquidity conditions in the financial system.

“The emergency financing under the RFI will help fill the urgent BOP needs that emerged as a result of the pandemic and thus contain the economic disruption and its regional spillovers. The RFI will also help catalyze other disbursements. The authorities’ commitment to transparently monitor and report all use of emergency funds is crucial to ensuring COVID-19-related spending reaches the targeted objectives.

“There is a pressing need to strengthen economic fundamentals and ensure debt sustainability by carrying out fiscal consolidation, improving the governance and operations of SOEs, and implementing other growth-enhancing structural reforms. The COVID-19 crisis heightens the urgency of implementing these efforts to achieve sustainable and inclusive growth. Specific reform commitments at the time of the October *Medium-Term Budget Policy Statement* will be a critical step to buttress the credibility of the reform efforts and should be followed by steadfast implementation. Efforts to preserve the central bank’s inflation mandate and proactive bank regulation and supervision, particularly for small banks, will also be important."

More information

IMF Lending Tracker (emergency financing request approved by the IMF Executive Board)
https://www.imf.org/en/Topics/imf-and-covid19/COVID-Lending-Tracker

IMF Executive Board calendar
https://www.imf.org/external/NP/SEC/bc/eng/index.aspx

INTERNATIONAL MONETARY FUND

SOUTH AFRICA

July 17, 2020

REQUEST FOR PURCHASE UNDER THE RAPID FINANCING INSTRUMENT

EXECUTIVE SUMMARY

The shock. South Africa has the highest number of COVID-19 cases in sub-Saharan Africa. To mitigate the health impact, the government introduced a lockdown with a severe bearing on domestic demand. Existing structural constraints are being exacerbated by disruptions in the global supply chain. Moreover, deteriorating global financing conditions triggered portfolio outflows, particularly at the start of the pandemic, impairing a major source of external financing. As a result, a deep recession is unfolding in an economy already experiencing protracted subdued growth and deteriorating social conditions, with high unemployment, poverty, and inequality.

Policy response. The South African Reserve Bank (SARB) took strong and timely action by lowering the policy rate and ensuring adequate liquidity conditions in the financial system. Through a supplementary budget, the government proposed a plan to reprioritize budget appropriations toward health and mitigation spending and devote additional budgetary outlays to protect the poor, the unemployed, and the most affected businesses. These actions will somewhat limit the economic contraction and its social impact but will significantly push up the budget deficit and debt, which have been under pressure due to declining revenue, and rising recurrent expenditure including transfers to weak state-owned enterprises (SOEs). Once the health crisis subsides, the authorities intend to address long-standing fiscal and structural issues to drive the recovery, boost potential growth, reverse the rising trend in public debt, and foster greater inclusion.

Request for Fund support. To help meet the urgent financing needs from COVID-19, the government has sought financing from international financial institutions (IFIs), including the African Development Bank, the BRICS New Development Bank, the IMF, and the World Bank. This financing will help contain a severe economic disruption that could also have regional spillovers. The authorities have requested a Rapid Financing Instrument (RFI) purchase of SDR 3,051.2 million, equivalent to 100 percent of quota to be used as budget finance as the pandemic has hit the economy in the absence of fiscal space. Staff supports approval of this request, which is expected to have a catalytic effect and complement the authorities' efforts to contain the health and economic impacts of the pandemic.

Approved By
D. Robinson (AFR)
B. Rother (SPR)

An IMF team comprising Ms. Ana Lucía Coronel (head, AFR), Messrs. Montfort Mlachila (senior resident representative), Ken Miyajima, Alejandro Simone, Vimal Thakoor (all AFR), and Hui Tong (SPR) held discussions with Finance Minister Tito Mboweni, Reserve Bank Governor Lesetja Kganyago, National Treasury Director General Dondo Mogajane, and other senior government officials by video conferences during June 8–21 and July 7–13, 2020. Mr. Dumisani Mahlinza and Ms. Mmatshepo Maidi (OED) participated in key discussions. Mses. Yiruo Li and Zhangrui Wang provided research support. Ms. Cecilia Prado and Mr. Hatem Alsokhebr supported the preparation of the report.

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CONTEXT

1. **The COVID-19 pandemic is evolving in South Africa at a time of rising economic vulnerabilities.** With structural constraints largely unaddressed, economic growth has remained subdued over the last decade despite significant government spending. High fiscal deficits have not materially boosted economic activity as intended while drastically lifting the debt-to-GDP ratio. Major state-owned enterprises (SOEs) have become increasingly reliant on government support due to operational and governance weaknesses. Subdued growth has exacerbated already high unemployment and poverty. Income inequality is among the highest globally. A difficult political backdrop has constrained efforts to turn around stagnating growth and rein in rising public debt.

2. **Nonetheless, South Africa has built policy buffers over the years**. The flexible exchange rate acts as an effective shock absorber; inflation is under control; the domestic banking system is sound and resilient; domestic capital markets are deep; the corporate sector includes large international players; and public debt is mostly rand denominated and has relatively long maturities.

3. **The COVID-19 crisis will significantly weaken the growth outlook**. The severe lockdown imposed to contain the spread of the infection particularly among the vulnerable population—affected by other infectious diseases or living in densely populated areas—is driving a sharp decline in domestic demand. This decline, coupled with the impact of the global downturn, is leading to a deep recession with severe social implications and negative regional spillovers through trade, remittances, finance, and revenue transfers to customs union members.

4. **Financial markets have been under stress**. Like in most other emerging economies, financial market volatility has been high amid an uncertain outlook, with government bond yields and the rand having weakened substantially in early-April before recovering somewhat. Moody's downgraded the sovereign's credit rating to sub-investment status, at the start of the outbreak in March, adding to the uneasiness and exacerbating capital outflows.

5. **The crisis prompted a strong policy response**. The South African Reserve Bank (SARB) progressively cut the policy rate significantly and maintained adequate liquidity conditions in the financial system. The government announced an economic package to mitigate the COVID-19 impact, part of which was accommodated by reassessing priorities within the FY2020/21 budget. Some public investment projects were postponed, and the lockdown allowed a reshuffling of funds toward the affected sectors, but financing needs increased amid a large revenue shortfall and tighter financing conditions.

6. **The authorities have requested Fund emergency financial assistance under the Rapid Financing Instrument (RFI)**. They seek a purchase of SDR 3,051.2 million, equivalent to 100 percent of quota. Staff assesses that South Africa qualifies for assistance to address an urgent balance of payments (BOP) needs and meets all other RFI qualification criteria and supports the request. The IMF's support will complement financing from other multilateral institutions.

RECENT ECONOMIC DEVELOPMENTS

A. Prior to COVID-19

7. **Weak economic growth and elevated fiscal deficits have rapidly worsened the public debt trajectory and eroded fiscal space**. Real GDP growth was stagnant in 2019 at 0.2 percent, following several years of subdued activity reflecting weak private investment, consumption, and productivity amid a deteriorating business environment. The budget deficit is estimated to have increased to 6.7 percent of GDP lifting debt to 64 percent of GDP in FY2019/20 (ending on March 31). One third of the deficit was driven by transfers to SOEs, mainly Eskom, the national power company, which has been facing major operational and financial difficulties. The remainder was largely due to compensation of employees, subsidies, and interest costs—the latter being the fastest growing budget item. The stock of contingent liabilities averaged 17 percent of GDP in the five fiscal years ending in FY2019/20.

8. **The monetary policy stance has been accommodative**. Inflation declined to below the mid-point of the 3–6 percent target band in 2019, although inflation expectations remained slightly higher. The rand has been floating without any SARB's intervention. Official forex reserves in 2019 were lower than adequate as measured by the Fund's reserve adequacy metrics. The external current account was moderately weaker than implied by fundamentals and desirable policies, suggesting a moderate overvaluation of real effective exchange rate in 2019.

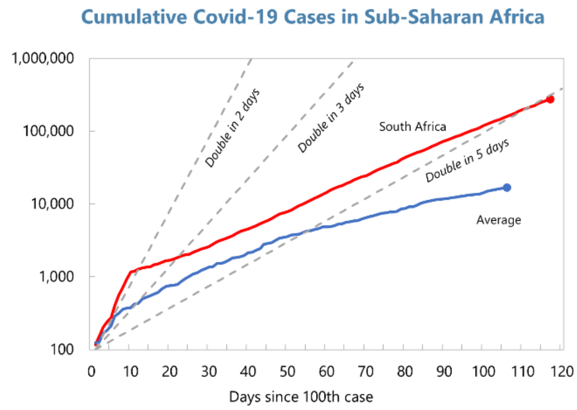
9. **The banking sector remained strong even though corporate and household balance sheets weakened**. Banks have enjoyed adequate profitability and the SARB's stress tests showed bank capital was adequate. However, banks' high interconnectedness with the broader financial system and idiosyncratic vulnerabilities in small and medium-sized banks pose risks. Among nonfinancial corporates, the interest coverage ratio weakened in several industries in the third quarter of 2019. Household finances remained under pressure, as reflected in an uptick in non-performing unsecured credit in end-2019. The *Joint IMF-World Bank Financial Sector Assessment Program* is underway.

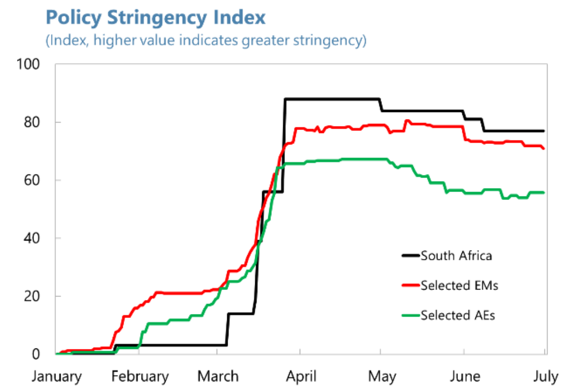
10. **Addressing structural impediments to growth has proved challenging**. Growth has been constrained by uncompetitive product and labor markets, governance weaknesses, rigid prices and wages, and inefficient state-owned industries. Some policies have aimed to increase competition, but lack of policy consensus has hindered overall progress.

B. COVID-19 Impact and Policy Response

11. **As in other countries, the authorities introduced a nationwide lockdown, which was subsequently partially eased**. The number of reported infections and deaths have risen rapidly, particularly in July, with epidemiological models predicting a peak in the third quarter. The government declared a national state of disaster, now extended through August 15, and adopted containment measures, including social distancing, travel bans, school closures, and contact tracing.

The lockdown was instituted on March 26 with only critical workers and services operating. On May 1, a phased lifting began, reducing restrictions outside metropolitan areas. On June 1, additional activities reopened, and since June 17 most restrictions on hotels, restaurants, and sporting events were lifted under strict adherence to health protocols. The banking sector and the payment system have remained operational throughout the lockdown.





Sources: Johns Hopkins Corona Virus Resource Center, Oxford COVID-19 Government Response Tracker, and IMF staff calculations.
Note: Left panel = Average of Cameroon, Cote d'Ivoire, and Ghana. Right pane = A product of an ongoing collation project of live data. Publicly available information on 17 indicators of government responses is used, including containment and closure policies (e.g., school closures and restrictions in movement), economic policies (e.g., income support to citizens or provision of foreign aid), and health system policies (e.g., the COVID-19 testing regime or emergency investments into healthcare). The index records the number and strictness of government policies. It should not be interpreted as scoring the appropriateness or effectiveness of a country's response. A higher index value does not mean a better or worse response. Selected EMs = Brazil, China, India, Indonesia, Mexico, Russia, and Turkey. Selected AEs = Germany, Japan, United Kingdom, and United States.

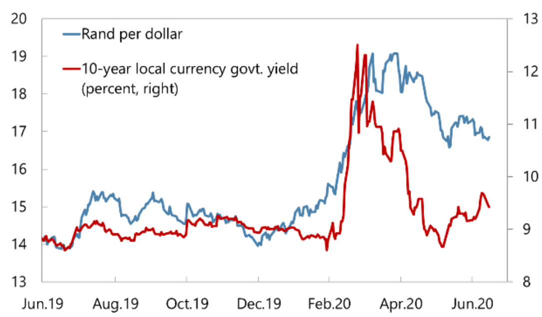
12. **Large capital outflows and asset selloffs followed the global market turmoil** (Figure 1). Net selling of local currency-denominated bonds by nonresidents has been larger than in other emerging markets, pushing up local bond yields sharply and tightening interbank market liquidity conditions. Since February's peak and through mid-July, net capital outflows (bonds and equities) exceeded 2 percent of GDP and the rand depreciated by 13 percent vis-à-vis the US dollar. The sovereign's dollar credit spread more than doubled at one point; and the rand depreciated by 31 percent in early-April, reaching its weakest level on record. Demand for foreign exchange picked up as agents either moved funds overseas or hoarded dollar liquidity domestically. Cross-border dollar funding conditions also tightened. South Africa was removed from the World Government Bond Index (WGBI) at end-April following the rating downgrade by Moody's.

Text Table 1. South Africa: Selected Macroeconomic Indicators

		2019 Article IV				2020 RFI			
		2019/20	2020/21	2021/22	2022/23	2019/20	2020/21	2021/22	2022/23
GDP growth	(percent)	0.7	0.7	1.2	1.4	-0.1	-7.7	3.4	2.0
Inflation	(percent)	4.5	5.2	5.0	5.0	4.2	2.6	4.3	4.3
Overall fiscal balance	(percent of GDP)	-6.5	-6.7	-6.7	-6.7	-6.7	-16.1	-9.5	-7.2
Public debt	(percent of GDP)	61.9	66.3	70.6	74.3	63.7	81.8	83.4	86.0

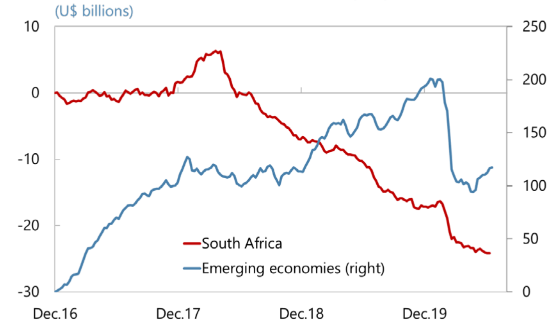
13. The authorities announced mitigating measures along three phases. The first phase is meant to preserve economic activity through immediate and targeted responses. The second phase aims at helping the economy recover by supporting investment and employment . The third phase intends to put the economy on a faster growth path and restore long-term prosperity (LOI ¶5).

South African Rand and Government Bond Yield



Source: Haver.

Cumulative Weekly Net Portfolio Inflows to South Africa and Selected Emerging Economies
(U$ billions)



Sources: IIF and IMF staff.

14. Immediate response measures in place comprise:

- **Fiscal**. Announced measures amounting to R500 billion (10.3 percent of GDP) include a bank loan guarantee scheme to help small and medium-sized enterprises (SMEs) finance operating expenses (Box 1); support to informal businesses and SMEs under stress, mainly in the tourism and hospitality sectors; cash-flow assistance through tax deferrals, holidays, and accelerated tax reimbursements; temporarily expansion of social grants to vulnerable households and distressed individuals; wage protection through the Unemployment Insurance Fund (UIF); allocations to health expenditure through a Solidarity Fund assisted by private contributions; and support to municipalities for the provision of food, basic services, and shelter for the homeless.

Text Table 2. South Africa: Announced COVID-19 Fiscal Response Package

	Billions of rand	Percent of GDP
Loan Guarantee Scheme	200	4.1
Job creation and support for SME and informal business	100	2.1
Measures for income support (tax deferrals, holidays and extensions)	70	1.4
Support to vulnerable households for 6 months	50	1.0
Wage protection (UIF)	40	0.8
Health and other frontline services	20	0.4
Support to municipalities	20	0.4
Total	**500**	**10.3**

Source: National Treasury and IMF staff calculations.

- **Monetary**. The SARB reduced the policy rate by 25 basis points in January, 100 basis points to 5.25 percent in March, 100 basis points to 4.25 percent in April, and 50 basis points to 3.75 percent in May. On March 20, the SARB announced measures to ease liquidity conditions by: (i) introducing overnight supplementary repo operations at the policy rate to support clearing banks; (ii) reducing the upper and lower interest rates of the standing facility (to lend at the repo rate and borrow at the repo rate less 200 basis points); and (iii) raising the size of the main weekly refinancing operations. On March 25, as another extraordinary measure, the SARB announced a program to purchase government bonds in the secondary market to help normalize trading liquidity and extended the main refinancing instrument maturities up to 12 months. The SARB does not consider that these emergency measures conflict with its inflation mandate. (LOI ¶8, 15)

Box 1. The COVID-19 Loan Guarantee Scheme

What is it? The scheme creates an incentive for banks to lend to SMEs that have an annual turnover of less than R300 million to help them meet some of their operational expenses. The scheme is expected to mitigate the negative economic impact of the pandemic and support financial stability. The government and commercial banks share the credit risk.

How large is it? The government initially provided a guarantee of R100 billion to the SARB with the option to increase it to R200 billion (4 percent of GDP). Since the scheme opened on May 12, the uptake has been low, potentially in response to relatively restrictive conditions (e.g., selective usage of borrowed funds). The government is working with banks on revisions to the scheme to increase the uptake and a possible expansion to non-bank lenders.

How does it work? The SARB lends to banks at the repo rate (currently 3.75 percent) plus a 0.5 percent guarantee fee. Banks in turn lend to SMEs at the repo rate plus a spread of 3.5 percent. The SARB, as the administrator of the scheme, publishes an annual report setting out the usage of the scheme and the performance (default rate) of each bank's loan portfolio.

How are losses absorbed? The net margin on the loan portfolio (estimated at 2 percentage points) is pooled as the first loss buffer. The 0.5 percentage point guarantee fee is the second loss buffer. Banks take the third loss, up to 6 percentage points of the amount loaned. The remaining losses are borne by the National Treasury. The government guarantee is recorded as a contingent liability.

- **Macro-financial**. On March 26, the SARB issued guidelines on modalities to provide debt relief to bank customers. On March 28, the liquidity coverage ratio was reduced from 100 to 80 percent; pillar 2A capital requirements were cut from 1 percent to zero; a drawdown of capital conservation buffers was allowed; and a new treatment was introduced to exempt COVID-19-related credit exposures (not defaulted) from additional capital and provisioning requirements. On April 6, the SARB issued guidance on dividends and cash bonuses distribution to encourage banks to preserve capital buffers.

- **Other**. On March 19 and 27, the authorities introduced regulations against price gouging and export control measures of goods needed for COVID-19 treatment.

Text Table 3. South Africa: Monetary Policy and Bank Regulatory Measures

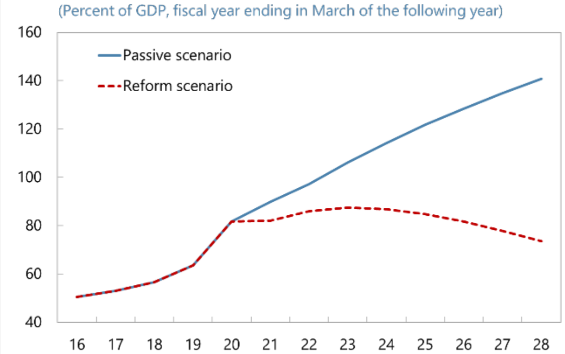
Measure	Details	Impact
Repo rate	Reduced the repo rate by 275 basis points	Reduced short-term borrowing costs
Government bond market liquidity	Started purchases of government bonds in the secondary market	Restored bond market trading liquidity
Capital requirements	Reduce the Pillar 2A capital requirement from 1 percent to zero and allowed banks to draw down the conservation buffer after consultation with the Prudential Authority	Expected to support lending
Dividends	Provide guidance on dividends and cash bonuses distribution to encourage banks to preserve capital buffers	Expected to help banks conserve capital
Liquidity coverage ratio (LCR)	Reduced LCR from 100 percent to 80 percent	Expected to support lending

Sources: National Treasure and SARB.

OUTLOOK AND RISKS

15. On June 24 the government presented a *Supplementary Budget Review* to parliament to reflect the impact of COVID-19 and state the government's economic policy intentions. The budget review contains two trajectories to illustrate the economic evolution this year and in the medium term—on current policies (passive scenario) and with the needed reforms (reform scenario). The document acknowledges that on current policies growth would be dismal, the deficit would continue to rise, and public debt would exceed 140 percent of GDP in the next seven years and would not stabilize. It then presents the reform scenario, which includes the needed fiscal consolidation and structural reforms, mentioning the general policies to attain it. The document further indicates that the forthcoming *Medium-Term Budget Policy Statement (MTBPS)*, to be presented in October, would contain the detailed measures and reforms to stabilize debt at 87 percent of GDP in FY2023/24 (debt is projected to increase from 64 percent of GDP in 2019/20 to 82 percent in FY2020/21). Staff projections and analysis in this report are based on the authorities' reform scenario, which has been endorsed by President Ramaphosa and his cabinet.

Supplementary Budget Review Debt Trajectories
(Percent of GDP, fiscal year ending in March of the following year)



Source: National Treasury.

16. Despite the sizable relief package, the pandemic will drive the economy into a deep recession in 2020, with adverse implications for the fiscal deficit and debt (Figure 2).

- **Real GDP growth** is projected to contract by 7.2 percent (compared to an expansion of 0.8 percent at the time of the 2019 Article IV consultation), after incorporating the effect of the fiscal package and liquidity injections. The sharp contraction will be driven mainly by the impact of the nationwide lockdown on all economic sectors. Investment, exports, and private consumption are set to decline, partially offset by a lower imports.

- **Inflation** is projected to undershoot the mid-point of the 3–6 percent target range in 2020 but the gap is expected to close gradually in the medium term. Headline inflation is projected at 3 percent in 2020, notwithstanding structural price rigidities and pass-through of projected rand depreciation, as a large negative output gap opens, and oil prices remain low. Inflation may prove to be stickier downward if the supply side was hit harder and the output gap was narrower than estimated.

- **The fiscal deficit and public debt** are set to rise significantly. Staff projects the consolidated government deficit to rise to about 16 percent of GDP in FY2020/21, pushing up debt by 18 percentage points of GDP.

- **The external current account deficit** is projected by staff to narrow to 1.8 percent of GDP in 2020 as domestic demand and oil prices decline. With improved terms of trade, import compression and rand depreciation, the trade surplus is set to increase. The financial account is expected to compress significantly, opening a gap to be filled by disbursements from multilaterals.

Text Table 4. South Africa: Selected Macroeconomic Indicators

		2019 Article IV				2020 RFI			
(Calendar year)		2019	2020	2021	2022	2019	2020	2021	2022
GDP growth	(percent)	0.4	0.8	1.0	1.3	0.2	-7.2	2.6	1.5
Inflation	(percent)	4.2	5.2	5.0	4.9	4.1	3.0	3.9	4.3
Overall fiscal balance	(percent of GDP)	-6.1	-6.7	-6.8	-6.8	-6.3	-13.7	-11.2	-7.9
Public debt	(percent of GDP)	60.8	65.3	69.6	73.5	62.2	78.1	82.4	85.4
Current account balance	(percent of GDP)	-3.3	-3.7	-3.7	-3.7	-3.0	-1.8	-2.1	-2.5

17. The recovery is set to start in 2021 and continue over the medium term, with inflation returning to the mid-point of the target range, and deficit and debt indicators improving. Growth would recover gradually in 2021-22 and maintain the momentum thereafter as the authorities implement substantive growth-enhancing reforms to support the necessary fiscal consolidation. The growth recovery and a rebound in oil prices would gradually lift inflation in line with inflation expectations. The fiscal deficit is set to decline to 9.5 percent of GDP in FY2021/22 once the one-off measures are phased out and average about 4½ percent in the medium term as the government implements ambitious fiscal consolidation. Public debt would peak at about 87 percent of GDP in FY2023/24 before starting to decline. As economic activity recovers and interest payments on public debt to nonresidents increase, staff projects the current account deficit to widen to an average 3.4 percent of GDP in the medium term.

18. This outlook is subject to prominent downside risks.

- ***Deteriorating health conditions.*** Should the infection spread be more severe and last longer, supply and demand would fall further, financial conditions could tighten again, and a deterioration of social conditions may ensue.

- ***Failure to implement the needed fiscal adjustment and reform.*** Should the authorities not achieve consensus to implement the envisaged reform agenda to reverse the economic stagnation of the last decade, growth and debt would follow the path in the passive scenario presented in the authorities' *Supplementary Budget Review*, posing serious threats to debt sustainability, and generating destabilizing effects such as inflation or financial repression. In particular, specific and well-defined fiscal consolidation and reform commitments in the *October MTBPS* will be a critical first step to establish the credibility of the reform efforts, followed by steadfast implementation.

- ***Adverse effects of higher domestic government borrowing.*** Increased bond issuance, particularly in the shorter end of the curve, could lead to higher domestic financing costs and greater bank purchases, likely crowding out lending.

- ***Mounting social discontent.*** Fiscal tightening and rising unemployment, if not mitigated through timely and well-targeted COVID-19 relief first, and policies that promote investment and employment later, would jeopardize growth revival and increase poverty and inequality.

- ***Materialization of contingent liabilities.*** If the government has to continue to rescue SOEs, particularly Eskom, or bear losses from the new guaranteed bank loans, additional spending pressures would emerge, posing further risks to debt sustainability. The stock of contingent liabilities would amount to about 26 percent of GDP by the end of FY2020/21 assuming the full amount of credit under the loan guarantee scheme is granted.

- ***Increasing private sector balance sheet impairments.*** Should the performance of the corporate sector turn out worse than expected, including as a result of rising financing costs, the recovery, which is anchored on private investment, would be delayed.

- ***Weakening business confidence and investor sentiment.*** If discussions and implementation of the reform scenario lacks the needed credibility, capital outflows would increase, borrowing would become more expensive, and the growth recovery would suffer.

- ***Growing bank vulnerabilities.*** Should weaknesses in small and medium-sized banks be exposed amid subdued growth and market unease, and potentially generate contagion, the financing space to support the recovery would be reduced, creating negative spillovers in the financial system.

- ***Worsening external situation.*** Deterioration in global financial conditions, increased protectionism, and intensified geopolitical tensions could add to subdued demand and undermine the recovery.

19. On the upside, steadfast implementation of reforms could allow the economy to exploit its full potential. Reform implementation would improve confidence, attract private investment, and boost growth more than expected. The debt-to-GDP ratio would improve, reducing financing requirements and costs, and creating virtuous macro-fiscal feedback loops.

POLICY DISCUSSIONS

C. Addressing the Shock

20. The *Supplementary Budget Review* appropriates health and COVID-19 mitigation spending, pushing up the FY2020/21 fiscal deficit. The supplementary budget amended the FY2020/21 budget to: (i) reprioritize resources away primarily from non-essential acquisition of goods and services and delay investment projects (about R100 billion); and (ii) provide temporary tax relief and funds to limit the impact of the recession on the most vulnerable, ensure functioning of basic services, and support the private sector's financial viability (about R155 billion). About 30 percent of the announced package (3.2 percent points of GDP) will add to the deficit, once excluding contingent liabilities and the planned spending reprioritization. The expenditure increase and a large shortfall in government revenue (as automatic stabilizers take effect when the recession squeezes income and consumption) explain the sharp increase in the deficit. In addition, only half of the announced R200 billion loan guarantee scheme is initially expected to be implemented.

Text Table 5. South Africa: Selected Fiscal Indicators

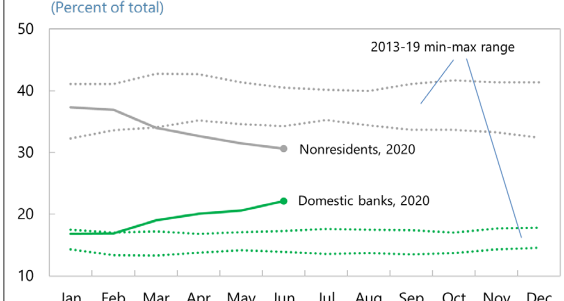
(Percent of GDP, Fiscal Year Basis)

	2019 Article IV				2020 RFI			
	2019/20	2020/21	2021/22	2022/23	2019/20	2020/21	2021/22	2022/23
Total revenue and grants	29.1	29.2	29.2	29.2	29.3	25.7	27.6	28.5
Tax revenue	25.3	25.3	25.3	25.3	25.5	21.8	23.7	24.7
Non-tax revenue	0.4	0.4	0.4	0.4	0.4	0.4	0.3	0.3
Other	3.5	3.5	3.5	3.4	3.4	3.5	3.5	3.5
Total expenditure	35.7	35.9	36.0	35.8	36.0	41.8	37.1	35.7
Current expenditure	31.2	31.4	31.6	31.6	31.7	36.5	33.2	33.1
Wages and salaries	12.2	12.1	12.0	11.8	12.3	13.1	12.3	11.7
Other goods and services	4.9	4.8	4.9	4.8	4.9	4.9	5.0	4.7
Interest	4.1	4.4	4.7	5.0	4.2	5.0	5.3	5.7
Transfers	10.0	10.0	10.0	9.9	10.3	13.5	10.7	11.0
Capital expenditure	3.2	3.2	3.3	3.3	3.1	3.2	3.0	2.3
Payment for financial assets	1.3	1.2	1.1	0.9	1.3	1.6	0.8	0.3
Contingency	0.0	0.1	0.1	0.1	0.0	0.5	0.1	0.1
Primary balance	-2.4	-2.3	-2.0	-1.6	-2.5	-11.2	-4.3	-1.5
Overall balance	-6.5	-6.7	-6.7	-6.7	-6.7	-16.1	-9.5	-7.2

21. The borrowing strategy is being recalibrated to finance the resulting budget deficit. The projected consolidated budget deficit will add significantly to the government's gross borrowing needs, which are expected to reach 25.2 percent of GDP in FY2020/21. While the cost of external issuance appears favorable, global market conditions and foreign investor appetite for local assets remain volatile. In the absence of foreign currency bond issuance, financing would entail issuance of short-term securities (mainly absorbed by domestic banks), issuance of longer-term rand-denominated bonds, drawdowns of deposits in the financial system, and borrowing from IFIs.

Holdings of South African Local Government Bonds by Nonresidents and Domestic Banks

(Percent of total)



Sources: Haver and IMF staff.

22. Fiscal policy discussions focused on optimizing the budget composition to achieve the best possible COVID-19 mitigation results in FY2020/21. Staff encouraged the authorities to target the relief to those more affected by the pandemic while reducing the pressure on the budget from less important outlays. In line with their supplementary budget, the authorities described their fiscal priorities as follows (LOI ¶13, 14):

- ***The wage bill*** has been rising at a faster pace than the cost of living due to automatic increases unrelated to productivity. Given the health emergency and benign inflation, the authorities plan to implement their policy (announced in the FY2020/21 budget) to rationalize compensation by renegotiating the final year of the current wage agreement with unions. Savings in the wage bill of about 0.7 percent of GDP facilitate the needed increase in transfers to low-income households. If the decision is overturned by the court, implementation risks would increase, as additional savings would be needed.

- ***Transfers to SOEs*** have been necessary to keep operations going. For FY2020/21, the government will have to maintain these transfers as budgeted to service debt. However, it intends to condition them to measurable progress in improving revenue generation, reducing expenses, and addressing remaining governance issues.

- ***Infrastructure spending*** will be temporarily curtailed, except for essential investments.

- ***Compensation to the unemployed and provision of social grants*** will be carried out transparently. The authorities are committed to efficiently target the temporary expansion of grants to unemployed youths in addition to existent recipients—mostly children and old adults—using the country's well-established national ID and means testing system. The authorities will ensure grants are received by legitimate beneficiaries maintaining continued transparency and accountability (LOI ¶22).

Text Table 6. South Africa: Fiscal Financing Needs and Sources
(In percent of fiscal year GDP)

	FY19/20	FY20/21	FY21/22
Gross Financing Needs Consolidated Government	14.6	25.2	20.7
National Government	15.0	24.1	20.8
Deficit	7.1	15.1	9.6
Amortization of MLT Debt	1.4	1.4	1.2
Local Currency	0.4	1.1	1.2
Foreign Currency	1.0	0.3	0.1
Amortization of ST Debt	6.6	7.7	9.9
Provinces, Local Govts, EBF deficits	-0.4	1.1	-0.1
Sources of Financing Consolidated Government	14.6	22.4	20.7
Issuance of MLT Debt	7.5	9.3	8.0
Local Currency	6.0	9.3	7.1
Foreign Currency	1.5	0.0	0.9
Issuance of ST Debt	7.3	10.7	11.0
Transactions in Asset and Liabilities	0.3	0.5	0.2
Change in Deposits and Other Balances	-0.4	2.0	1.5
Financing Gap	0.0	2.8	0.0
IMF		1.6	
World Bank		0.8	
African Development Bank		0.0	
New Development Bank		0.4	
Memo Item:			
Nominal GDP (billions of rand)	5,120	4,860	5,237

Sources: National Treasury and IMF staff estimates.

23. External financing requirements have increased. In 2020, net portfolio and other investment are set to be negative and net FDI inflows negligible. To offset the ensuing gap, banks and non-banks would draw on their external assets, official forex reserves would decline in line with the use of government forex deposits, and IFI financing will fill the remaining needs. The RFI purchase would cover 39.9 percent of the external financing needs arising from the shock.

Text Table 7. South Africa: External Financing Needs
(Billions of US dollars)

	2019	2020	2021
Balance on current account	-10.6	-5.1	-6.6
Balance on goods and services	1.8	6.8	7.1
Trade balance	2.7	9.3	7.3
Balance on income	-9.9	-9.2	-11.4
Balance of transfer	-2.5	-2.7	-2.3
Balance on financial account	10.0	-5.4	4.5
FDI	1.5	0.0	0.3
Portfolio Investment	9.1	-4.8	4.3
Other Investment	-0.3	-0.4	0.2
Derivatives	-0.3	-0.2	-0.3
Overall balance (including E&Os)	1.8	-10.5	-2.1
Financing	-1.8	10.5	2.1
RFI	...	4.2	0.0
Percent of Financing	...	39.9	0.0
FX reserves drawdown	-1.8	3.0	2.1
Other Sources	...	3.3	0.0
World Bank	...	2.0	0.0
New Development Bank	...	1.0	0.0
AfDB	...	0.3	0.0
Other prospective sources	...	0.0	0.0

Source: IMF staff calculations.

24. The SARB's emergency measures have helped stabilize domestic liquidity and market conditions but risks should be closely monitored. Progressive monetary easing and regulatory forbearance are expected to encourage bank lending, even though overall private sector credit is anticipated to weaken considerably. The SARB's purchases of government bonds in the secondary market have helped ease pressure on their yields and supported the private sector's absorption of government debt. The SARB has emphasized that such purchases are only designed to stabilize disorderly market liquidity conditions and can neither address the structural constraints to growth nor should they be allowed to jeopardize attainment of the inflation objective. Staff recommends continuing to transparently communicate the temporary nature of these operations to maintain investor confidence and avoid potential risks to the inflation mandate.

25. The financial system is expected to cushion the impact of the recession by drawing down existing buffers. Supported by the SARB's liquidity injections, banks generally have ample cash. Deposits from corporates and asset managers have increased, even though maturities have shortened on heightened risk aversion. The SARB is supervising the execution of banks' capital restoration plans and risk disclosure. Staff advises closely monitoring bank liquidity conditions following the reduction in the minimum requirements. It also recommends the SARB encouraging banks to timely recognize all defaulted restructured exposures (from a regulatory capital and IFRS9 perspective) and preserve capital buffers against deteriorating asset quality and regulatory forbearance. Staff recommends ensuring the loan guarantee scheme assists the intended beneficiaries while limiting their adverse impact on bank balance sheets and the government's contingent liabilities.

26. Smaller banks need more supervisory attention. Some of these banks have witnessed large declines in liquidity ratios, including a small public bank, the Land Bank, which has had difficulties in meeting its debt obligations. Small banks, with generally less diversified business models and low profitability, are more susceptible to weaker economic activity. On the positive side, they have higher capital ratios than larger banks and have been taking measures to improve profitability, including selective capital allocation, proactive credit collection strategies, and careful management of their cost base. COVID-19 is likely to affect these plans and calls for increased monitoring and supervision, and for the introduction of a comprehensive resolution regime as a key element of contingency planning.

D. Preparing the Recovery

27. The government is confident that the plan to mitigate the pandemic's economic impact will be effective, albeit costly, and will lay the foundations for a durable recovery. The authorities' reform scenario embeds actions to boost private investment and address BOP difficulties, by accelerating reforms to reignite growth, employment creation, and inclusion (LOI ¶16). The authorities also intend to sustain and deepen initiatives to prevent state capture and corruption and safeguard the independence and integrity of key institutions (LOI ¶19). Regarding labor market reforms, staff reiterated its advice to ease the regulatory burden faced by firms regarding flexibility in hiring and firing and address the constraints posed by collective bargaining. More generally, staff recommended deepening structural reform implementation to raise per-capita growth in the medium term and benefit all South Africans.

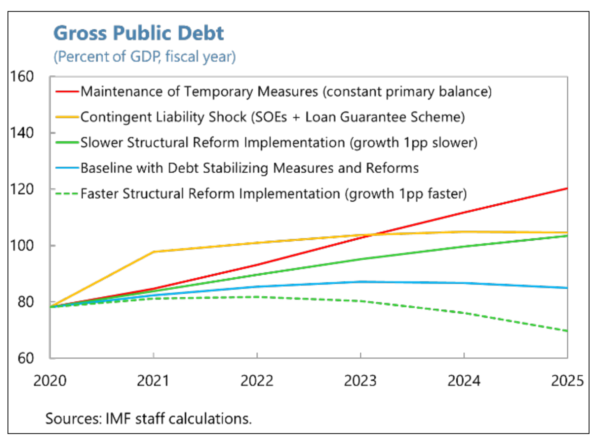
28. The authorities intend to advance near-term policy action in line with some of the decisions announced in President Ramaphosa's *2020 State of the Nation Address*

- Expediting allocation of broadband spectrum to increase competition in *telecommunications* and reduce the cost of data and developing digitalization to further boost financial inclusion.
- Finalizing the *mining* legislation (mining charter) to reduce investor uncertainty.
- Providing clarity on land reform to allow for higher contribution of *agriculture* to growth, and encourage investments supporting a green recovery.
- Injecting greater predictability as regards power availability and creating investment opportunities in the *electricity* sector by accelerating the implementation of Eskom's operational and financial turnaround plan (LOI ¶17).
- Opening the *transport* industry (ports and railways) to the private sector to boost efficiency.
- Increasing competition in *retail* by supporting the entry of SMEs across the value chain.

29. Improving the business environment will also require determined efforts to strengthen the public sector's balance sheet once the immediate emergency is behind. Staff recommended a gradual and growth-friendly but sizable reduction of the consolidated government deficit. This consolidation will require implementation of fiscal measures of about 5–5½ percent of GDP over the next five years, which alongside the impact of the growth recovery would allow the deficit to decline to average levels of about 4½ percent of GDP in the medium term. Needed measures include limiting increases in recurrent expenditure, mainly compensation, transfers to SOEs, and ill-targeted subsidies, while pursuing a recovery of productive public investment and protecting outlays for health and education and well-targeted social assistance. The authorities intend to pursue policies to that end. They will let the temporary relief package lapse as the pandemic subsides; make permanent some of the COVID-19 related cuts in non-essential outlays; and take any additional measures to restore fiscal and debt sustainability in line with their reform scenario. With this purpose, the authorities intend to move to a zero-based budgeting method as a way of taking a fresh perspective and repositioning spending in line with the post-COVID-19 reality (LOI ¶14).

30. Staff highlighted the potential for materialization of downside risks and the need to have contingency plans in place. Should the pandemic produce further economic damage or other risks to the outlook materialize, post-COVID-19 fiscal consolidation would need to be larger and reforms deeper, given the absence of fiscal space and the high debt level. The authorities are confident that the planned expenditure streamlining will be complemented by enhanced tax revenue from the economic recovery aided by better tax administration (including leveraging anti-money laundering tools to investigate tax crimes) and other measures. Staff called for a reduction in tax incentives once increased private sector activity takes place encouraged by the reforms. The authorities indicated that the budget includes additional COVID-19-related allocations to the contingency reserve to address additional needs that may emerge.

31. Debt sustainability critically hinges on sustained implementation of policies to address underlying fiscal and structural weaknesses. The intended reduction in the fiscal deficit and reform implementation are expected to boost the medium-term growth potential—and put debt on a downward trajectory. Nonetheless, debt sustainability is subject to considerable risks posed by the large gross financing requirements, significant contingent liabilities, and implementation risks of the ambitious reform scenario. The authorities intend to seek consensus for the introduction of a fiscal rule to target a debt objective and complement the existing primary expenditure ceiling, thus adapting the fiscal framework to the now critical debt reduction objective. Attracting more private investment to lift its contribution to growth from its anemic pre-COVID-19 level (0.1 percentage points in 2019) is critical to jumpstarting economic growth and job creation. Reviving growth requires steadfast reform implementation.



32. Preserving price and financial stability will remain the SARB's key objective. The SARB has demonstrated its willingness and capacity to do so during past episodes of market stress, such as the global financial crisis. As the economy recovers and inflation moves up to the mid-point of the target band, the monetary expansion is expected to be wound down gradually. The SARB will continue to let the flexible exchange rate act as the first line of defense and leverage the range of emergency tools used recently to maintain adequate domestic liquidity conditions and financial stability, paying due attention to their potential inflationary impact.

THE RAPID FINANCING INSTRUMENT

33. South Africa's urgent BOP needs justifies the RFI purchase. By adding pressures to the capital account, COVID-19 has exacerbated the BOP difficulties. With real GDP growth turning deeply negative, the fiscal position will further deteriorate. While the flexible rand is helping absorb the shock and subdued inflation provides the SARB with room for maneuver, RFI resources will contribute to fill the urgent BOP needs originating from the fiscal pressures posed by the pandemic and could prevent a possible erosion of official forex reserves. The RFI purchase will also limit regional spillovers and catalyze additional IFI financing (LOI ¶3). An upper credit tranche (UCT) Fund supported program is not necessary, because the BOP gap is expected to close within a year as the immediate impact of COVID-19 subsides and the authorities implement the intended policies.

34. South Africa's capacity to repay the Fund is adequate. The RFI purchase and other COVID-19-related disbursements will increase the already high debt-to-GDP ratio. However, the authorities intend to gradually stabilize and turn around the debt trajectory in the medium term. While adding about 1.5 percent of GDP to the current debt stock ratio, the RFI amortization will not increase debt service obligations in a material way.

35. The authorities will ensure that resources from the RFI are used transparently (LOI ¶22). South Africa boasts a strong public financial management system and is a leader in budget transparency. The public procurement system has been revamped to address the weaknesses that facilitate state capture. The digital procurement platform allows for transparency in the dissemination of procurement announcements and allocated contracts, monitoring of contract allocation, and assessment of awarded companies' financial status as well as their ultimate beneficiaries. Against this background, the authorities will transparently plan, use, monitor, and report all COVID-19-related spending to ensure it reaches the targeted objectives, notably by:

- Regularly publishing the execution of COVID-19-related expenditures vis-à-vis the adjustment budget by type of spending.
- Auditing all COVID-19-related expenditure, including ex-post evaluation of delivery, within 12 months and publishing the audit report on the Auditor General's website.
- Publicly disseminating all COVID-19-related procurement contracts and allocation (with details about awarded companies and their beneficial owners).

36. The authorities will meet their commitments under the IMF's safeguards policy (LOI ¶21). They will undergo a safeguards assessment of the SARB. The authorities will also provide staff with the SARB's audit reports and authorize the SARB's external auditors to hold discussions with staff. Since the funds will be used for budget support, the authorities have established a memorandum of understanding between the National Treasury and the SARB that clarifies the responsibilities to timely service the financial obligations to the IMF.

STAFF APPRAISAL

37. South Africa's economy has been severely hit by the COVID-19 crisis. As other countries, the nation had to adopt costly emergency measures and opt for an extensive lockdown to mitigate the impact of the pandemic. The health crisis is causing human suffering and financial distress. The domestic economic disruption, falling external demand, and overall financial market uncertainty have triggered a severe contraction in business activity and are expected to create a deep recession this year, with a full recovery only expected in the medium term. The acute decline in consumption and investment, alongside the need for fiscal support, will result in a sharp, albeit temporary, deterioration in domestic revenue mobilization and an increase in public expenditure.

38. The authorities' policy response to the crisis has been timely and comprehensive. The SARB's upfront action to soothe liquidity conditions and temporarily provide regulatory relief contributed to the stabilization of financial markets. The government's sizable package rightly identifies the sectors in need of relief, including the health sector, and targets assistance to the poor, the unemployed, and SMEs that do not have alternative sources of financing. The package has been generally well received by the population, and its implementation will provide some respite to the most affected companies and individuals. It is important that the temporary nature of these measures be respected and that the related contingent liabilities be carefully managed to limit undue effects on the medium-term fiscal position and growth outlook. Proactive bank regulation and supervision, particularly for small banks, is also crucial.

39. The way forward remains challenging. COVID-19 has already exacerbated economic vulnerabilities built over the last decade, particularly on the real economy and the fiscal position. It has significantly increased the debt level and the service burden. Once COVID-19 is behind, there is a pressing need to restore economic fundamentals by consolidating the fiscal position and streamlining SOE operations. These actions could usefully be complemented by introducing an explicit debt target. Increasing the medium-term growth potential requires higher private investment, which in turn necessitates improved governance, lower entry barriers to product markets, and a more flexible labor market to support job creation, and achieve sustainable and inclusive growth. Fiscal consolidation and growth-enhancing structural reforms will be crucial to reversing the current upward debt trajectory. Substantial uncertainty remains, and with it significant downside risks as to how and when both global conditions and the South African economy will emerge from the pandemic. Should these risks materialize, the fiscal consolidation and structural reform efforts would have to be larger.

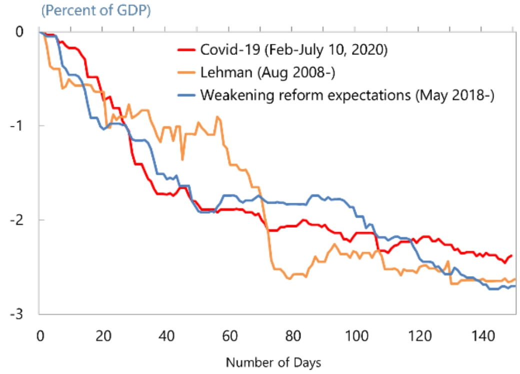
40. The COVID-19 crisis heightens the urgency of advancing these efforts and effective implementation will be key. The *Supplementary Budget Review* presented to parliament on June 24, outlines a medium-term reform scenario establishing the fiscal path necessary to keep debt sustainable, which has been endorsed by the cabinet. However, critical elements of the fiscal effort should be specified soon and concrete policies to attain the reform scenario should be announced expeditiously to garner credibility. Approval by parliament of these policies at the time of the October *MTBPS* and their steadfast implementation will be crucial to allow South Africa to benefit from higher economic growth. This will in turn boost confidence and help the country regain its investment grade status over time. Even more importantly, high growth, well-targeted social protection, a lean and efficient public sector, and dynamic entrepreneurship are the only combination to create employment, fight poverty and reduce inequality in South Africa.

41. Against this backdrop, an IMF purchase under the RFI in the amount of SDR 3,051.2 million (100 percent of quota) is warranted. Alongside the authorities' measures to deal with the shock and their intended policies to redress the fiscal position and implement reforms, the RFI will help address the urgent BOP needs that has emerged from COVID-19. While risks to the outlook are substantial, South Africa's capacity to repay the Fund is adequate. The RFI will provide the government with urgently needed financing to address the health and social implications of the economic downturn; avoid a severe economic disruption while giving time to the authorities to advance longstanding reforms; limit regional spillovers; and play a catalytic role as the authorities engage with other IFIs.

Figure 1. South Africa: Macro-Financial Effects of COVID-19

Nonresidents sold local currency-denominated bonds and equities…

Cumulative Net Portfolio Outflows
(Percent of GDP)

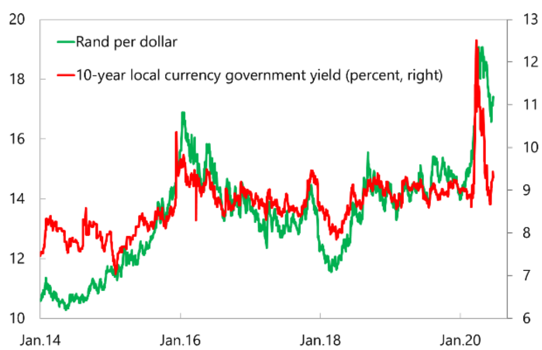


…and public sector external funding cost jumped.

Public Sector External Credit Spreads
(Basis points, 5 year CDS)

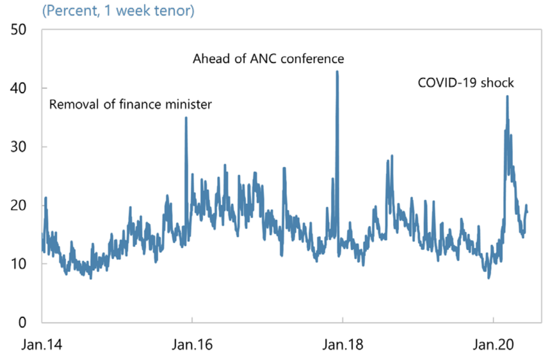
The rand weakened to a record level, while government bond trading liquidity thinned and yields soared…

South African Rand and Local Government Bond Yield



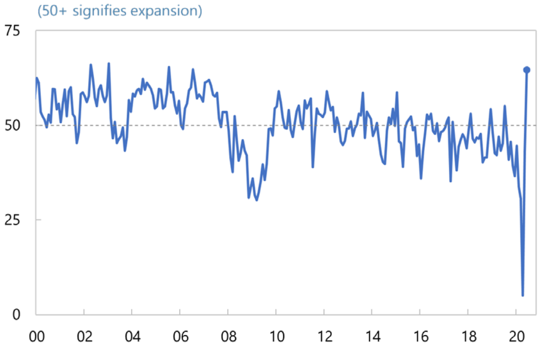
…as rand volatility surged.

Implied Dollar-Rand Volatility
(Percent, 1 week tenor)



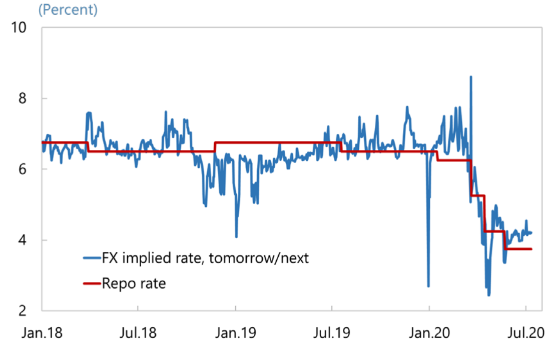
Business activity plummeted amid a national lockdown…

Manufacturing Business Activity PMI
(50+ signifies expansion)



…prompting a policy response, including rate cuts and liquidity support.

Repo and FX-Implied Rates
(Percent)

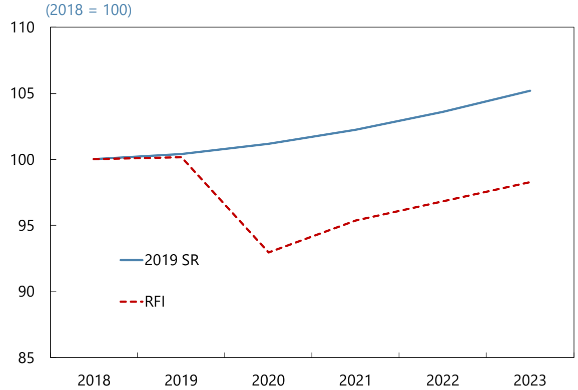


Sources: Bloomberg LP, Haver Analytics, IIF, and IMF staff calculations.

Figure 2. South Africa: Macroeconomic Effects of COVID-19

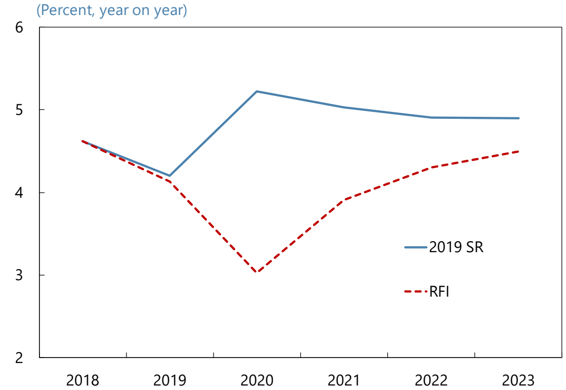
COVID-19 is expected to drive a sharp economic contraction…

Real GDP
(2018 = 100)



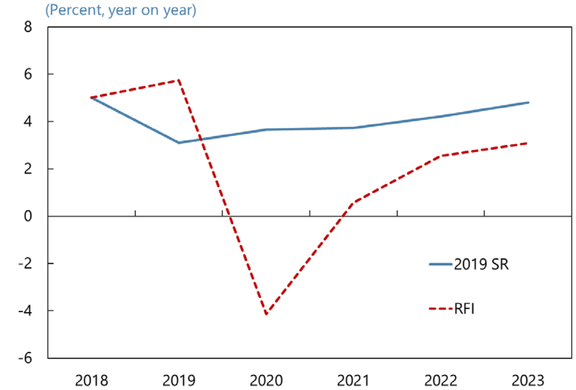
…. with inflation initially further undershooting the mid-point of the 3–6 percent target range…

Headline Inflation
(Percent, year on year)



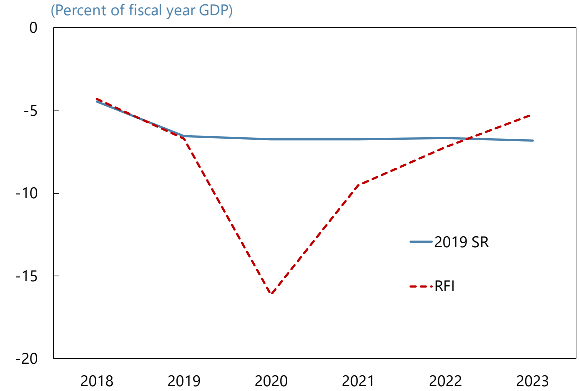
…bank lending to the private sector contracting strongly…

Bank Lending to the Private Sector
(Percent, year on year)



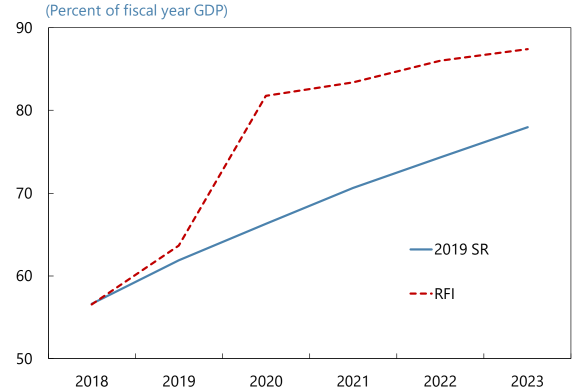
…and the fiscal deficit worsening.

Overall Fiscal Deficit
(Percent of fiscal year GDP)



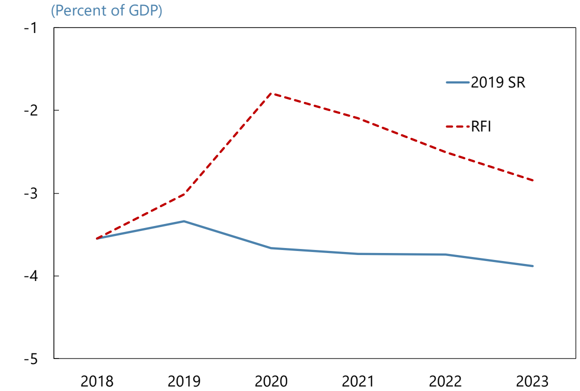
As a result, the trajectory of public debt as a share of GDP is projected to worsen…

Public Debt
(Percent of fiscal year GDP)



…while the current account deficit is expected to narrow as imports decline.

External Current Account Deficit
(Percent of GDP)



Sources: South African authorities, and IMF staff estimates.

Note: SR = Staff Report, RFI = Rapid Financing Instrument.

Table 1. South Africa: Selected Economic Indicators, 2017–23

	2017	2018	2019	2020	2021	2022	2023
				Est.		Proj.	
National income and prices (annual percentage change unless otherwise indicated)							
Real GDP	1.4	0.8	0.2	-7.2	2.6	1.5	1.5
Real GDP per capita	-0.1	-0.7	-1.3	-8.6	1.1	0.0	0.0
Real domestic demand	1.9	0.9	0.6	-8.1	3.2	1.9	1.7
GDP deflator	5.3	3.9	4.1	3.0	3.9	4.3	4.5
CPI (annual average)	5.3	4.6	4.1	3.0	3.9	4.3	4.5
CPI (end of period)	4.7	4.9	3.7	2.4	4.3	4.3	4.5
Labor market (annual percentage change unless otherwise indicated)							
Unemployment rate (percent of labor force, annual average)	27.5	27.1	28.7	36.4	36.1	36.6	37.1
Unit labor costs (formal nonagricultural)	5.1	4.6	4.1	3.0	3.9	4.3	4.5
Savings and Investment (percent of GDP)							
Gross national saving	16.3	14.4	14.6	12.7	12.9	12.7	12.4
Public (incl. public enterprises)	1.3	1.1	0.9	-5.5	-3.8	-1.8	-0.4
Private	14.9	13.2	13.7	18.2	16.7	14.5	12.8
Investment (including inventories)	18.8	17.9	17.6	14.5	15.0	15.2	15.2
Public (incl. public enterprises)	6.3	5.7	5.4	5.1	4.9	4.2	3.9
Private	12.5	12.5	12.5	9.9	10.5	11.5	11.8
Fiscal position (percent of GDP unless otherwise indicated) 1/							
Revenue, including grants 2/	28.2	29.0	29.1	27.2	26.8	28.2	28.7
Expenditure and net lending	32.6	33.2	35.3	40.9	37.9	36.1	34.5
Overall balance	-4.4	-4.1	-6.3	-13.7	-11.2	-7.9	-5.8
Primary balance	-0.8	-0.3	-2.1	-8.9	-6.0	-2.3	0.2
Structural balance (percent of potential GDP)	-3.8	-3.5	-4.8	-9.0	-8.0	-6.1	-4.6
Gross government debt 3/	53.0	56.7	62.2	78.1	82.4	85.4	87.1
Government bond yield (10-year and over, percent) 4/	9.2	9.4	9.0	10.0	...	...	...
Money and credit (annual percentage change unless otherwise indicated)							
Broad money	6.4	5.6	6.1	1.9	4.6	4.9	5.2
Credit to the private sector	4.3	5.5	5.5	-4.6	0.6	2.7	3.3
Repo rate (percent, end-period) 5/	6.8	6.8	6.5	4.1	...	...	...
3-month Treasury bill interest rate (percent) 4/	7.3	7.2	7.1	5.7	...	...	...
Balance of payments (annual percentage change unless otherwise indicated)							
Current account balance (billions of U.S. dollars)	-8.9	-13.1	-10.6	-5.1	-6.6	-8.6	-10.3
percent of GDP	-2.5	-3.5	-3.0	-1.8	-2.1	-2.5	-2.8
Exports growth (volume)	-0.7	2.6	-2.5	-12.3	9.1	7.4	2.3
Imports growth (volume)	1.0	3.3	-0.5	-15.0	10.9	8.2	2.8
Terms of trade	4.5	-2.6	2.6	3.4	1.0	-0.6	-0.3
Overall balance (percent of GDP)	0.5	0.2	0.5	-3.7	-0.6	0.2	0.4
Gross reserves (billions of U.S. dollars)	50.7	51.6	55.1	52.1	50.0	50.8	52.4
in percent of ARA (w/o CFMs)	63.1	72.1	75.5	71.4	68.6	69.7	71.9
in percent of ARA (w/ CFMs)	69.0	78.8	83.1	78.6	75.5	76.7	79.2
Total external debt (percent of GDP)	49.6	46.8	50.4	55.3	52.0	49.0	47.9
Nominal effective exchange rate (period average) 4/	9.9	-0.1	-5.2	-10.0	...	...	...
Real effective exchange rate (period average) 6/	12.8	1.8	-1.9	-4.3	...	...	...
Exchange rate (Rand/U.S. dollar, end-period) 5/	12.3	14.4	14.0	17.5	...	...	...

Sources: South African Reserve Bank, National Treasury, Haver, Bloomberg, World Bank, and Fund staff estimates and projections.

1/ Consolidated government as defined in the budget unless otherwise indicated.

2/ Revenue excludes "transactions in assets and liabilities" classified as part of revenue in budget documents. This item represents proceeds from the sales of assets, realized valuation gains from holding of foreign currency deposits, and other conceptually similar items, which are not classified as revenue by the IMF's Government Finance Statistics Manual 2014.

3/ Central government.

4/ January-May 2020 average.

5/ As of May 2020.

6/ January-March 2020 average.

Table 2. South Africa: Consolidated Government Operations,[1] FY 2016/17–2022/23

	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
				Est.		Proj.	
				(In billions of rand)			
Total revenue and grants	1,267	1,332	1,431	1,501	1,248	1,444	1,588
Tax revenue	1,105	1,161	1,239	1,305	1,058	1,242	1,375
Non-tax revenue 2/	15.0	16.3	21.4	22.9	18.0	18.1	18.9
Provinces, social security, and other entities	148	155	170	172	172	184	194
Total expenditure	1,443	1,542	1,643	1,844	2,033	1,943	1,990
Current expenditure	1,285	1,372	1,484	1,622	1,775	1,738	1,842
Wages and salaries	512	548	585	629	638	645	653
Other goods and services	218	221	235	252	240	259	260
Interest	157	173	192	215	242	276	318
Transfers	399	430	472	526	655	558	611
Capital expenditure	149	150	143	156	156	156	128
Payment for financial assets	8.5	20.3	15.7	65.2	76.6	44.1	14.3
Contingency	0.0	0.0	0.0	0.0	24.6	5.0	5.0
Primary balance	-18.7	-37.1	-19.6	-127.9	-542.9	-222.8	-83.2
Overall balance	-175	-210	-212	-343	-785	-498	-402
Financing	175	210	212	343	785	498	402
Local Currency Debt (net)	157	204	184	314	547	371	371
Foreign Currency Debt (net)	36.4	29.8	26.2	27.5	119.8	40.5	38.0
Official Creditors	0.0	0.0	0.0	0.0	134.5	0.0	0.0
Commercial Creditors	36.4	29.8	26.2	27.5	-14.7	40.5	38.0
Transactions in Assets and Liabilities	18.2	19.5	14.5	15.2	23.1	7.9	4.8
Use of cash and other balances	-36.8	-43.5	-12.7	-13.7	95.3	79.1	-11.8
Structural primary balance	-3.9	-11.2	11.2	-41.3	-306.0	-85.9	-11.9
Gross government debt	2,233	2,490	2,788	3,261	3,976	4,368	4,791
				(In percent of GDP)			
Total revenue and grants	28.7	28.3	29.0	29.3	25.7	27.6	28.5
Tax revenue	25.0	24.7	25.1	25.5	21.8	23.7	24.7
Non-tax revenue	0.3	0.3	0.4	0.4	0.4	0.3	0.3
Provinces, social security, and other entities	3.3	3.3	3.5	3.4	3.5	3.5	3.5
Total expenditure	32.6	32.8	33.3	36.0	41.8	37.1	35.7
Current expenditure	29.1	29.2	30.1	31.7	36.5	33.2	33.1
Wages and salaries	11.6	11.7	11.9	12.3	13.1	12.3	11.7
Other goods and services	4.9	4.7	4.8	4.9	4.9	5.0	4.7
Interest	3.5	3.7	3.9	4.2	5.0	5.3	5.7
Transfers	9.0	9.1	9.6	10.3	13.5	10.7	11.0
Capital expenditure	3.4	3.2	2.9	3.1	3.2	3.0	2.3
Payment for financial assets	0.2	0.4	0.3	1.3	1.6	0.8	0.3
Contingency	0.0	0.0	0.0	0.0	0.5	0.1	0.1
Primary balance	-0.4	-0.8	-0.4	-2.5	-11.2	-4.3	-1.5
Overall balance	-4.0	-4.5	-4.3	-6.7	-16.1	-9.5	-7.2
Financing	4.0	4.5	4.3	6.7	16.1	9.5	7.2
Local Currency Debt (net)	3.6	4.3	3.7	6.1	11.2	7.1	6.7
Foreign Currency Debt (net)	0.8	0.6	0.5	0.5	2.5	0.8	0.7
Official Creditors	0.0	0.0	0.0	0.0	2.8	0.0	0.0
Commercial Creditors	0.8	0.6	0.5	0.5	-0.3	0.8	0.7
Transactions in Assets and Liabilities	0.4	0.4	0.3	0.3	0.5	0.2	0.1
Use of cash and other balances	-0.8	-0.9	-0.3	-0.3	2.0	1.5	-0.2
Structural primary balance (percent of potential GDP)	-0.1	-0.2	0.2	-0.8	-6.3	-1.6	-0.2
Gross government debt 3/	50.5	52.9	56.5	63.7	81.8	83.4	86.0
Memorandum items:							
National budget primary balance (percent of GDP)	-0.9	-1.4	-1.3	-3.1	-10.2	-4.6	-2.0
National budget overall balance (percent of GDP)	-4.2	-4.9	-5.0	-7.1	-15.1	-9.6	-7.5
Fiscal year GDP (billions of rand)	4,420	4,702	4,931	5,120	4,860	5,237	5,571
Fiscal year real GDP growth (percent)	0.8	1.6	0.4	-0.1	-7.7	3.4	2.0
Fiscal year GDP Deflator growth (in percent)	6.2	4.8	4.4	3.9	2.8	4.2	4.3
Fiscal year nominal GDP growth (percent)	7.1	6.4	4.9	3.8	-5.1	7.7	6.4
Contingent Liabilities (percent of GDP) 4/	15.2	15.7	17.3	19.1	25.6	...	...

Sources: South African National Treasury and Fund staff estimates and projections.

1/ Data are on a fiscal year basis (April 1-March 31) and are based on the June 24, 2020 Supplementary Budget Review. Consolidated government corresponds to the national government, social security funds, provincial governments, and some public entities. Local governments are only partially captured through the transfers sent to them by national government.

2/ Non-tax revenue excludes transactions in financial assets and liabilities. These transactions are classified as a domestic financing item given that they involve primarily revenues associated with realized exchange rate valuation gains from the holding of foreign currency deposits and other conceptually similar smaller items.

3/ Covers only national government debt.

4/ Contingent Liabilities are sourced from Table 11 of the Statistical Annex of the 2020 *Budget Review*. For FY 2020/21, the 200 billion rand loan guarantees that are expected to be provided in the context of the COVID-19 fiscal support package were added to the total contingent liabilities in the 2020 *Budget Review.*

Table 3. South Africa: Balance of Payments, 2017–23

	2017	2018	2019	2020	2021	2022	2023
				Est.		Proj.	
				(In billions of US dollars)			
Balance on current account	-8.9	-13.1	-10.6	-5.1	-6.6	-8.6	-10.3
Balance on goods and services	4.5	1.3	1.8	6.8	7.1	6.4	5.9
Exports of goods and services	104	110	105	87	99	108	113
Imports of goods and services	-99	-109	-103	-80	-91	-102	-107
Balance on income	-10.5	-11.6	-9.9	-9.2	-11.4	-13.3	-14.6
Income receipts	6.1	7.3	8.1	0.6	0.3	0.3	0.2
Income payments	-16.6	-18.9	-18.0	-9.8	-11.7	-13.7	-14.8
Balance on transfers	-2.9	-2.7	-2.5	-2.7	-2.3	-1.7	-1.5
Capital flows (including errors and omissions)	10.8	13.9	12.4	-5.4	4.6	9.4	11.9
Balance on capital and financial account	10.2	11.5	10.0	-5.4	4.6	9.4	11.9
Balance on capital account	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Balance on financial account	10.2	11.5	10.0	-5.4	4.5	9.4	11.9
Direct investment	-5.4	1.4	1.5	0.0	0.3	0.8	1.6
Liabilities	2.0	5.4	4.6	2.6	3.1	3.8	4.7
Assets	-7.4	-4.1	-3.1	-2.5	-2.8	-3.0	-3.1
Portfolio investment	16.5	2.5	9.1	-4.8	4.3	6.9	8.0
Liabilities	20.9	6.8	6.1	-4.0	4.3	6.9	8.0
Assets	-4.4	-4.3	3.0	-0.9	0.0	0.0	0.0
Financial derivatives	-0.3	0.5	-0.3	-0.2	-0.3	-0.3	-0.3
Liabilities	-17.1	-16.5	-11.3	-9.5	-10.5	-11.4	-11.8
Assets	16.8	17.0	11.0	9.3	10.2	11.1	11.5
Other investment	-0.6	7.1	-0.3	-0.4	0.2	1.9	2.6
Liabilities	4.6	8.7	-0.7	-1.0	-0.4	1.3	1.9
Assets	-5.3	-1.6	0.4	0.6	0.6	0.6	0.6
Errors and omissions	0.6	2.4	2.4	0.0	0.0	0.0	0.0
Overall balance of payments	1.9	0.9	1.8	-10.5	-2.1	0.8	1.6
IFI disbursements				7.5			
FX reserves drawdown	-1.9	-0.9	-1.8	3.0	2.1	-0.8	-1.6
Gross reserves (end of period)	50.7	51.6	55.1	52.1	50.0	50.8	52.4
				(In percent of GDP)			
Balance on current account	-2.5	-3.5	-3.0	-1.8	-2.1	-2.5	-2.8
Balance on goods and services	1.3	0.3	0.5	2.4	2.2	1.8	1.6
Balance on goods	1.4	0.5	0.8	3.3	2.3	1.8	1.5
Balance on services	-0.1	-0.2	-0.3	-0.9	-0.1	0.0	0.1
Exports of goods and services	29.6	29.9	29.9	30.6	31.0	31.1	31.0
Imports of goods and services	-28.3	-29.6	-29.4	-28.2	-28.8	-29.3	-29.3
Balance on income	-3.0	-3.2	-2.8	-3.2	-3.6	-3.8	-4.0
Balance on transfers	-0.8	-0.7	-0.7	-1.0	-0.7	-0.5	-0.4
Capital flows (including errors and omissions)	3.1	3.8	3.5	-1.9	1.4	2.7	3.3
Balance on capital and financial account	2.9	3.1	2.8	-1.9	1.4	2.7	3.3
Balance on capital account	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Balance on financial account	2.9	3.1	2.8	-1.9	1.4	2.7	3.3
Direct investment	-1.5	0.4	0.4	0.0	0.1	0.2	0.4
Portfolio investment	4.7	0.7	2.6	-1.7	1.4	2.0	2.2
Financial derivatives	-0.1	0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Other investment	-0.2	1.9	-0.1	-0.1	0.1	0.5	0.7
Errors and omissions	0.2	0.7	0.7	0.0	0.0	0.0	0.0
Overall balance of payments	0.5	0.2	0.5	-3.7	-0.6	0.2	0.4
Gross reserves (end of period)	14.5	14.0	15.7	18.3	15.7	14.6	14.4
in months of next year's imports	5.6	6.0	8.2	6.8	5.9	5.7	5.6
Memorandum items:							
Total external debt	49.6	46.8	50.4	55.3	52.0	48.8	47.6
International investment position (net)	9.1	13.3	7.9	...	...	...	...
GDP at current prices (US$ billion)	349	368	351	284	318	347	364

Sources: South African Reserve Bank and Fund staff estimates and projections.

Table 4. South Africa: Financial Corporations, 2017–23

	2017	2018	2019	2020	2021	2022	2023
				Est.		Proj.	
				(In billions of rand)			
Central Bank							
Net foreign assets	585	700	737	834	767	772	806
Net domestic assets	-329	-431	-455	-504	-444	-435	-450
Domestic claims	-313	-399	-413	-467	-410	-405	-423
Central government (net)	-382	-474	-517	-572	-515	-509	-528
State and local government	0.4	0.3	0.3	0.3	0.3	0.3	0.3
Public nonfinancial corporations	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Private sector	0.3	0.3	1.1	1.1	1.1	1.1	1.1
Other depository corporations	62	68	96	97	97	97	97
Other financial corporations	5.0	5.0	5.0	5.0	5.0	5.0	5.0
Other items net	-15.3	-31.6	-40.6	-37.1	-33.6	-30.1	-26.6
Monetary base	257	269	282	330	323	337	356
Other Depository Corporations							
Net foreign assets	113	60	105	174	191	200	207
Net domestic assets	3,127	3,356	3,526	3,482	3,653	3,832	4,030
Domestic claims	4,183	4,467	4,749	4,791	4,987	5,213	5,451
Central government (net)	433	484	525	752	880	969	1,045
State and local government	18.8	20.9	23.0	22.0	23.4	24.8	26.3
Public nonfinancial corporations	76.1	71.3	77.1	81.2	84.4	87.4	90.5
Private sector	3,051	3,204	3,388	3,230	3,249	3,336	3,445
of which loans and securities	2,948	3,111	3,281	3,128	3,146	3,231	3,336
Central Bank	145	147	159	152	162	172	182
Other financial corporations	459	541	577	552	589	624	662
Other items net	-1,055	-1,111	-1,224	-1,309	-1,335	-1,382	-1,421
Depository Corporations							
Net foreign assets	699	760	841	1,008	958	973	1,013
Net domestic assets	2,660	2,787	2,922	2,829	3,054	3,236	3,414
Domestic claims	3,662	3,853	4,081	4,074	4,318	4,539	4,749
Central government (net)	50	10	9	181	365	460	518
State and local government	19.2	21.3	23.3	22.3	23.7	25.1	26.6
Public nonfinancial corporations	77.1	72.3	78.1	82.2	85	88	91
Private sector	3,052	3,204	3,389	3,231	3,250	3,337	3,446
of which loans and securities	2,948	3,111	3,281	3,128	3,146	3,231	3,336
Other financial corporations	464	546	582	557	594	629	667
Other items net	-1,002	-1,066	-1,159	-1,246	-1,264	-1,303	-1,334
Broad money	3,359	3,547	3,764	3,837	4,012	4,209	4,428

Sources: International Financial Statistics, South African Reserve Bank, and IMF staff estimates.

Table 4. South Africa: Financial Corporations, 2017–23 (concluded)

	2017	2018	2019	2020	2021	2022	2023
				Est.		Proj.	
				(In billions of rand)			
Other Financial Corporations							
Net foreign assets	831	835	986	1,035	1,073	1,094	1,105
Net domestic assets	4,092	3,939	3,987	3,974	4,193	4,430	4,699
Domestic claims	6,372	6,230	6,407	6,387	6,727	7,086	7,489
Central government (net)	947	1,028	1,130	1,284	1,515	1,687	1,814
State and local government	15.1	16.2	16.9	17.0	17.8	18.7	19.7
Public nonfinancial corporations	420	420	512	590	650	708	766
Private sector	3,811	3,560	3,423	3,160	3,141	3,200	3,342
of which loans and securities	877	926	977	901	896	913	953
Central Bank	11.2	9.1	9.5	9.6	10.1	10.6	11.1
Other Depository Corporations	1,167	1,196	1,317	1,326	1,394	1,462	1,537
Other items net	-2,280	-2,290	-2,420	-2,413	-2,534	-2,657	-2,790
Non-liquid liabilities	4,923	4,774	4,974	5,009	5,266	5,524	5,805
Financial Corporations							
Net foreign assets	1,530	1,595	1,828	2,043	2,030	2,067	2,119
Net domestic assets	5,692	5,666	5,699	5,568	5,947	6,293	6,661
Domestic claims	8,392	8,332	8,580	8,568	9,047	9,524	10,023
Central government (net)	997	1,038	1,138	1,465	1,880	2,146	2,332
State and local government	34.3	37.4	40.1	39.3	41.6	43.8	46.3
Public nonfinancial corporations	498	493	590	672	735	796	857
Private sector	6,863	6,764	6,812	6,392	6,390	6,537	6,788
of which loans and securities	3,825	4,037	4,257	4,030	4,042	4,144	4,289
Other items net	-2,700	-2,666	-2,882	-3,000	-3,100	-3,230	-3,362
Liabilities	7,222	7,261	7,526	7,611	7,977	8,361	8,780
Liquid	2,166	2,316	2,407	2,456	2,566	2,691	2,830
Nonliquid	5,056	4,945	5,119	5,155	5,411	5,669	5,950
Memorandum items:							
Central Bank (billions of US dollar)							
Net foreign reserves	47.5	48.7	52.5	49.9	47.8	48.6	50.2
Central gov. FX deposits	9.0	8.7	10.1	7.5	5.4	5.3	5.9
Year-on-year growth (percent)							
Monetary base	7.0	4.6	4.9	16.9	-2.0	4.4	5.7
Broad money	6.4	5.6	6.1	1.9	4.6	4.9	5.2
Claims on private sector							
Dep. Corp.	5.1	5.0	5.8	-4.6	0.6	2.7	3.3
Dep. Corp., loans and securities	4.3	5.5	5.5	-4.6	0.6	2.7	3.3
Fin. Corp.	9.5	-1.4	0.7	-6.2	0.0	2.3	3.8
Fin. Corp., loans and securities	4.3	5.5	5.5	-5.3	0.3	2.5	3.5
Broad money multiplier (ratio)	13.1	13.2	13.3	11.6	12.4	12.5	12.4
Claims on public sector (percent of total assets)							
Other Depository Corporations							
Central government	10.8	11.5	12.0	14.8	16.1	17.0	17.6
Public nonfinancials	1.4	1.3	1.3	1.3	1.3	1.3	1.3
Other Financial Corporations							
Central government	13.6	13.8	14.3	15.8	17.4	18.3	18.7
Public nonfinancials	4.8	4.5	5.2	6.0	6.3	6.5	6.7

Sources: International Financial Statistics, South African Reserve Bank, and IMF staff estimates.

Table 5. South Africa: Medium-Term Macroeconomic Framework, 2017–25

	2017	2018	2019	2020	2021	2022	2023	2024	2025
				Est.			Proj.		
National income and prices (annual percentage change)									
Real GDP	1.4	0.8	0.2	-7.2	2.6	1.5	1.5	2.1	2.3
CPI (annual average)	5.3	4.6	4.1	3.0	3.9	4.3	4.5	4.5	4.5
Output gap (percent of potential real GDP)	-0.2	-0.3	-0.4	-7.0	-4.6	-3.2	-2.1	-0.7	0.0
Labor market (annual percentage change)									
Unemployment rate (percent of labor force, annual average)	27.5	27.1	28.7	36.4	36.1	36.6	37.1	37.2	37.2
Savings and Investment (percent of GDP)									
Gross national saving	16.3	14.4	14.6	12.7	12.9	12.7	12.4	12.2	12.5
Public (incl. public enterprises)	1.3	1.1	0.9	-5.5	-3.8	-1.8	-0.4	0.9	2.2
Private	14.9	13.2	13.7	18.2	16.7	14.5	12.8	11.4	10.3
Investment (including inventories)	18.8	17.9	17.6	14.5	15.0	15.2	15.2	15.5	15.9
Public (incl. public enterprises)	6.3	5.7	5.4	5.1	4.9	4.2	3.9	3.8	3.8
Private	12.5	12.5	12.5	9.9	10.5	11.5	11.8	12.1	12.4
Fiscal position (percent of GDP) 1/									
Revenue, including grants	28.2	29.0	29.1	27.2	26.8	28.2	28.7	29.1	29.5
Expenditure and net lending	32.6	33.2	35.3	40.9	37.9	36.1	34.5	33.4	32.5
Overall balance	-4.4	-4.1	-6.3	-13.7	-11.2	-7.9	-5.8	-4.3	-3.1
Primary balance	-0.8	-0.3	-2.1	-8.9	-6.0	-2.3	0.2	1.8	3.2
Gross government debt 2/	53.0	56.7	62.2	78.1	82.4	85.4	87.1	86.8	85.0
Balance of payments (percent of GDP unless otherwise indicated)									
Exports of Goods and Services (volume, annual percentage change)	-0.7	2.6	-2.5	-12.3	9.1	7.4	2.3	3.5	4.4
Imports of Goods and Services (volume, annual percentage change)	1.0	3.3	-0.5	-15.0	10.9	8.2	2.8	3.7	4.2
Current account balance (billions of U.S. dollars)	-8.9	-13.1	-10.6	-5.1	-6.6	-8.6	-10.3	-12.4	-13.9
percent of GDP	-2.5	-3.5	-3.0	-1.8	-2.1	-2.5	-2.8	-3.2	-3.4
Overall balance	0.5	0.2	0.5	-3.7	-0.6	0.2	0.4	0.2	0.2
Gross reserves (billions of U.S. dollars)	50.7	51.6	55.1	52.1	50.0	50.8	52.4	53.2	53.9
percent of short-term debt (residual maturity)	93.7	89.2	99.7	101.0	90.3	82.2	85.0	82.6	81.4
Total external debt	49.6	46.8	50.4	55.3	52.0	49.0	47.9	46.7	46.6

Sources: Haver, South African National Treasury, World Bank, and Fund staff estimates and projections.

1/ Consolidated government unless otherwise indicated.

2/ National government.

Table 6. South Africa: Indicators of Capacity to Repay the IMF, 2020–25[1]

	2020	2021	2022	2023	2024	2025
IMF obligations based on existing credit (in millions of SDRs)						
Principal	0.0	0.0	0.0	0.0	0.0	0.0
SDR Charges and Assessments	0.1	0.3	0.3	0.3	0.3	0.3
IMF obligations based on prospective credit (in millions of SDRs)						
Principal	0.0	0.0	0.0	381.4	1525.6	1144.2
Charges and interest	24.0	32.9	33.0	32.9	22.4	6.0
Total IMF obligations based on existing and prospective credit						
In millions of SDRs	24.1	33.2	33.2	414.6	1548.2	1150.4
In millions of U.S. dollars	17.4	23.9	23.9	296.9	1106.1	818.8
In percent of GDP	0.0	0.0	0.0	0.1	0.3	0.2
In percent of exports of goods and services	0.0	0.0	0.0	0.4	1.3	0.9
In percent of government revenue	0.0	0.0	0.0	0.3	1.0	0.7
In percent of gross international reserves	0.0	0.1	0.1	0.8	2.9	2.1
In percent of IMF quota	0.8	1.1	1.1	13.6	50.7	37.7
IMF credit outstanding (end of period)						
In millions of SDRs	3051.2	3051.2	3051.2	2669.8	1144.2	0.0
In millions of U.S. dollars	4214.5	4233.6	4248.2	3727.3	1601.6	0.0
In percent of GDP	1.5	1.3	1.2	1.0	0.4	0.0
In percent of exports of goods and services	4.8	4.3	3.9	3.3	1.4	0.0
In percent of government revenue	5.8	4.8	4.2	3.5	1.4	0.0
In percent of gross international reserves	5.9	6.1	6.0	5.1	2.2	0.0
In percent of IMF quota	100.0	100.0	100.0	87.5	37.5	0.0
Memorandum items (in millions of U.S. dollars)						
Nominal GDP	284,201	317,888	347,317	363,844	385,702	407,682
Exports of goods and services	87,026	98,553	108,009	112,657	117,907	124,749
Government revenue	72,987	88,615	100,529	106,520	114,705	122,549
Gross international reserves	52,056	50,002	50,804	52,421	53,216	53,878
IMF quota	3051.2	3051.2	3051.2	3051.2	3051.2	3051.2
SDRs per U.S. dollars	0.72	0.72	0.72	0.72	0.71	0.71

Sources: South African authorities, and IMF staff estimates and projections.

1/ Assumes RFI disbursement in July 2020.

Table 7. South Africa: Financial Soundness Indicators, 2017–20

	2017	2018	2019	2020 [1/]
		(Percent)		
Capital adequacy				
Regulatory capital to risk weighted assets	16.3	16.1	16.6	15.8
of which Tier 1 capital	15.4	14.9	15.6	14.9
Capital to total assets	8.8	8.4	8.5	7.5
Asset quality				
Nonperforming loans to total of loans	2.8	3.7	3.9	4.0
Nonperforming loans net of provisions to capital	13.6	17.8	18.1	21.1
Earnings, profitability, and efficiency				
Return on assets	1.7	1.7	1.5	1.4
Return on equity	20.0	19.8	17.6	16.6
Interest margin to gross income	50.7	50.0	53.3	53.2
Trading income to total income	7.8	6.7	4.7	8.1
Non-interest expenses to gross income	54.9	52.8	53.6	60.4
Personnel expenses to non-interest expenses	48.1	51.9	44.4	45.1
Liquidity				
Liquid assets to total assets	15.1	15.6	15.0	15.9
Liquid assets to short-term liabilities	30.0	31.1	30.2	31.8
Customer deposits to total loans	55.9	55.7	57.4	57.6
Exposure to FX risk				
Net open FX position to capital	0.1	0.7	0.9	0.0
Foreign-currency-denominated loans to total loans	8.9	9.4	8.3	11.2
Foreign-currency-denominated liabilities total liabilities	6.6	8.0	7.4	8.7
Sectoral distribution of loans and advances				
Residents	89.5	89.3	90.0	86.3
Central Bank and other financial corporations	13.5	15.7	15.2	14.4
General government	0.5	0.5	0.6	0.6
Nonfinancial corporations	35.4	34.0	34.0	33.3
Households	40.1	39.1	40.2	38.1
Nonresidents	10.5	10.7	10.0	13.7
Derivatives				
Gross asset position in financial derivatives to capital	60.2	41.9	51.2	117.0
Gross liability position in financial derivatives to capital	59.3	42.9	49.3	122.7
Real Estate Market				
Residential real estate price growth [2/]	4.2	3.8	3.5	2.6
Residential real estate loans to total loans	25.0	24.0	24.2	22.8
Commercial real estate loans to total loans	7.6	7.5	8.0	7.6
Household debt				
Household debt to GDP	42.3	43.3	43.8	…
Household debt to disposable income	71.2	72.7	73.0	…
Household debt service to disposable income	9.1	9.3	9.4	…

Sources: Financial Soundness Indicators Database, Haver, and IMF staff calculations.

[1/] As of March, 2020

[2/] As of April, 2020.

Table 8. South Africa: Gross External Financing Requirements and Sources, 2017–23

	2017	2018	2019	2020	2021	2022	2023
			(In billions of US dollars)				
Gross external financing requirements	48.9	67.2	68.5	60.3	58.2	63.9	72.1
Current account deficit	8.9	13.1	10.6	5.1	6.6	8.6	10.3
Short-term debt at remaining maturity	40.0	54.2	57.9	55.2	51.6	55.3	61.8
Short-term debt at original maturity	37.2	40.9	47.9	44.4	41.5	47.3	52.4
MLT amortization	2.8	13.3	10.0	10.8	10.0	8.1	9.5
Sources of Financing							
FX reserves drawdown	-1.9	-0.9	-1.8	3.0	2.1	-0.8	-1.6
FDI (net)	-5.4	1.4	1.5	0.0	0.3	0.8	1.6
New borrowing and debt rollover	56.2	66.8	68.8	49.8	55.8	63.9	72.1
Short-term debt	40.9	47.9	44.4	41.5	47.3	52.4	54.8
Long-term debt	15.3	18.9	24.4	8.3	8.6	11.5	17.3
Other sources (including IFI)	0.0	0.0	0.0	7.5	0.0	0.0	0.0
RFI	0.0	0.0	0.0	4.2	0.0	0.0	0.0
			(In percent of GDP)				
Gross external financing requirements	14.0	18.3	19.5	21.2	18.3	18.4	19.8
Current account deficit	2.5	3.5	3.0	1.8	2.1	2.5	2.8
Short-term debt at remaining maturity	11.5	14.7	16.5	19.4	16.2	15.9	17.0
Short-term debt at original maturity	10.6	11.1	13.6	15.6	13.1	13.6	14.4
MLT amortization	0.8	3.6	2.8	3.8	3.2	2.3	2.6
Sources of Financing							
FX reserves drawdown	-0.5	-0.2	-0.5	1.1	0.6	-0.2	-0.4
FDI (net)	-1.5	0.4	0.4	0.0	0.1	0.2	0.4
New borrowing and debt rollover	16.1	18.1	19.6	17.5	17.6	18.4	19.8
Short-term debt	11.7	13.0	12.6	14.6	14.9	15.1	15.1
Long-term debt	4.4	5.1	6.9	2.9	2.7	3.3	4.7
Other sources (including IFI)	0.0	0.0	0.0	2.6	0.0	0.0	0.0
RFI	0.0	0.0	0.0	1.5	0.0	0.0	0.0

Annex I. Public Debt Sustainability Analysis[1]

The COVID-19 crisis has significantly increased South Africa's government debt and debt service obligations. Public debt was already high before the crisis due to persistent weak growth, high fiscal deficits, and the materialization of contingent liabilities from SOEs. It is now projected to peak at 87 percent of GDP in FY2023/24, and gradually decline as relief measures are phased out, and fiscal consolidation and structural reforms take hold. Gross financing needs are projected to average 19.3 percent of GDP during 2020–25 and start falling from 2021. The outlook is subject to significant downside risks posed by the uncertain nature of the pandemic and the global recovery; increased contingent liabilities; and implementation risks to fiscal consolidation and reform. Although risks are mitigated by the rand denomination and average long maturities of debt and a deep local institutional investor base, debt sustainability critically hinges on sustained implementation of policies to address underlying fiscal and structural weaknesses.

A. Context

1. **Public debt, gross financing needs (GFNs), and contingent liabilities have expanded in the context of the COVID-19 crisis**. While revenue had been recovering before the crisis, it will be negatively affected by the pandemic. Current expenditure had drifted up and is further pressured by the emergency. Declining revenue and spending pressures are pushing up the national government deficit increasing public debt to an estimated 82 percent of GDP in FY2020/21. In parallel, GFNs are set to increase from 11.5 percentage points of GDP FY2015/16 to about 24 percent of GDP in FY2020/21. The stock of contingent liabilities averaged 17 percent of GDP in the past five years and are projected at 26 percent of GDP in FY20/21. Almost 25 percent of the increase is explained by SOE loan guarantees, reflecting their persistent cash deficits and inability to borrow on the strength of their balance sheets, and 45 percent reflects a new loan guarantee scheme to support enterprises during the pandemic.

B. Baseline Projections

2. **The debt-to-GDP ratio is projected to rise to about 87 percent of GDP and start to decline gradually from 2024** (Figure A1.3). The debt trajectory would deteriorate markedly in the short term as the deep recession in 2020 and the package of measures to respond to COVID-19 result in an unprecedented national government deficit level. However, the deficit is expected to decline significantly in FY2021/22 as the temporary fiscal support unwinds and the economy starts to recover. In the medium term, a considerable deficit reduction is anticipated owing to the automatic revenue stabilizers as growth picks up; the permanent nature of some of the spending

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[1] For methodology, see: "Staff Guidance Note for Public Debt Sustainability Analysis in Market-Access Countries", IMF Policy Paper, May 6, 2013 and "Modernizing the Framework for Fiscal Policy and Public Debt Sustainability Analysis", SM/11/211.

rationalization in FY2020/21; the subsequent fiscal consolidation; and the impact of structural reforms on growth.

3. Given adverse initial conditions, GFNs are expected to remain sizable during the projection period as high deficits persist. GFNs are anticipated to exceed 16 percent of GDP, on average, in 2021–25 despite the favorable maturity and currency structure of the debt (Figure A1.3) and are projected to be met by domestic financing sources (primarily non-bank financial institutions), non-residents, and resources from IFIs.

Box A1.1. Staff Assumptions Underlying the Debt Sustainability Analysis

Data Coverage

Consistent with the debt coverage used by the authorities, calculations are based on the national government's main budget (central government). While this methodology excludes provincial governments, social security funds, and extra-budgetary institutions, these entities are not allowed to incur debt. Even though municipalities can borrow, most provincial and municipal expenditure is funded through transfers from the national government and is thus already captured to a considerable extent. However, the DSA also excludes SOEs, whose indebtedness has increased rapidly in recent years.

Macroeconomic Assumptions

Real GDP growth is projected to decline by 7.2percent in 2020 (compared to growth of 0.2 percent in 2019) as the pandemic impacts an already weak economy through: (i) a severe lockdown; (ii) an external demand shock; and (ii) a tightening of financial conditions as appetite for emerging market risk fell. Growth is projected to bounce back in 2021-22 as these effects subside and the output gap starts to close. Thereafter, growth would gradually increase to about 2.3 percent in 2025 as structural reforms reinvigorate economic activity. The GDP deflator is expected to average 4.1 percent in 2020–25.

Fiscal Assumptions

Debt projections include stock-flow adjustments to capture discounts on new issuance of existing benchmark bonds as well as valuation effects on inflation-linked and foreign currency denominated debt. The primary deficit is projected to be broadly in balance in 2023 and be in surplus in 2024. The intended fiscal consolidation is predicated on an expenditure-to-GDP downward trajectory driven by: (i) phasing out of emergency measures; (ii) wage containment action; (ii) tight control over goods and services expenditure; (iii) rationalization of transfers to public entities; and (iv) reduction in financial assistance to SOEs, especially Eskom. In addition, revenue is projected to recover gradually as growth recuperates and improvements in tax administration and tax policy measures take hold.

4. The debt outlook is subject to downside risks:

- ***Growth over-projection***. Given the uncertainty, the impact of the crisis could potentially be higher than expected, thus making growth projections optimistic and posing an upside risk to debt-to-GDP forecasts. Growth forecasting errors in the past have been on the optimistic side but usually within the interquartile range (Figure A1.2).

- ***Underestimated primary balance***. Upward pressure on the primary balance could stem from lower-than-anticipated revenue collection and/or higher-than-expected spending pressures including because of a prolonged pandemic and challenging wage negotiations. Primary balance projections have not been systematically biased (Figure A1.2).

- ***Higher interest rates***. Higher borrowing costs may arise from declines in EM risk appetite and/or increased risk perceptions derived from the credibility of the growth enhancing strategy, particularly if delays occur.

- ***Larger contingent liabilities***. Weak SOE and SME balance sheets could trigger further government support or lead to calls of guarantees on loans.

5. **Specific characteristics of the government debt mitigate risks**. These relate to the debt composition and maturity, with low shares in foreign currency (10 percent in 2019), short term instruments (11 percent in 2019), and an average term to maturity of about 12 years.

C. Scenario Analysis

6. **The analysis illustrates the sensitivity with which an individual or a combination of shocks can affect the public debt and GFNs projected paths on the downside and the upside** (Figures A1.4, A1.5 and A1.6).

- ***Persistent low growth scenario***. If growth were permanently lower than in the baseline by 1 percentage point on average during 2021–25, the debt-to-GDP ratio would reach about 104 percent of GDP in 2025. This scenario factors in the adverse impact of lower tax revenue elasticities and higher interest rates as well as the denominator effects of lower GDP.

- ***Primary balance shock scenario***. If the primary balance improved more gradually than in the baseline, deviating by a cumulative 11 percent of GDP during the medium term, the projected debt level would surpass 96 percent of GDP in 2025. The debt-to-GDP ratio would almost reach 89 percent if a temporary shock to growth with a magnitude of one-standard-deviation were to materialize in 2021 and 2022.

- ***Combined macro-fiscal shocks scenario***. A combination of standard shocks to growth and interest rates—a primary balance shock (temporary deterioration equivalent to one half of the 10-year historical standard deviation), and an exchange rate shock (consistent with the maximum movement over the past 10 years and an exchange rate pass-through of 0.25)—would result in an increase in the debt-to-GDP ratio to about 104 percent by 2025 and higher gross financing needs by about 8 percentage points of GDP by 2025.

- ***Contingent liability shock scenario***. Should all remaining SOE and loan guarantee scheme liabilities be called, debt would rise to about 105 percent of GDP by 2025. This scenario underscores both the direct risks posed by contingent liabilities to the fiscal outlook and the indirect risks posed by the impact on investor confidence and borrowing costs.

- ***Faster implementation of structural reforms***. This scenario assumes that growth becomes permanently higher than in the baseline by 1 percentage point on average during 2020–25 due to deeper reform implementation. In such a case, the debt-to-GDP ratio would return to below 70 percent of GDP in 2025 and gross financing needs would be below 15 percent of GDP in 2023. This scenario factors in the favorable impact of higher tax revenue elasticities and lower interest rates as well as the denominator effects of higher GDP on spending.

7. The heat map summarizes the risk assessment of South Africa's debt and GFNs (Figure A1.1).[2] All shock scenarios for the debt level and gross financing needs flash red given the already high debt starting point in the baseline. Mitigating factors are the large domestic institutional investor base, the low share of foreign currency, and the low share of short-term debt. However, South Africa's high bond spreads, which have been slightly below 600 basis points on average in the last three months, elevated external financing requirements, and relatively high share of debt held by non-residents add to the risks.

8. The fan charts highlight the importance of adopting decisive policies to reduce downside risks and the probability of debt distress (Figure A1.6, middle panel). Under a scenario in which downside shocks are predominant, debt-to-GDP ratio reaches 93 percent of GDP by 2025 (using the upper end of the 75th–90th percentile fan chart). Conversely, if shocks are symmetric to both up and downsides, which could be triggered for example by somewhat faster progress in structural reforms, the probability of the debt exceeding the same high level is reduced and the probability of better than baseline outcomes increases significantly.

[2] The framework uses indicative thresholds of 70 percent of GDP for debt and 15 percent of GDP for gross financing needs, benchmarks beyond which a country is reported as facing high risk, leading to a yellow color in the heat map if benchmarks are exceeded in a stress scenario and a red color if they are exceeded in the baseline. The benchmarks are based on a cross-country early-warning exercise of EMs that have experienced episodes of debt distress. Debt distress events are defined as default to commercial or official creditors, restructuring and rescheduling events, or IMF financing.

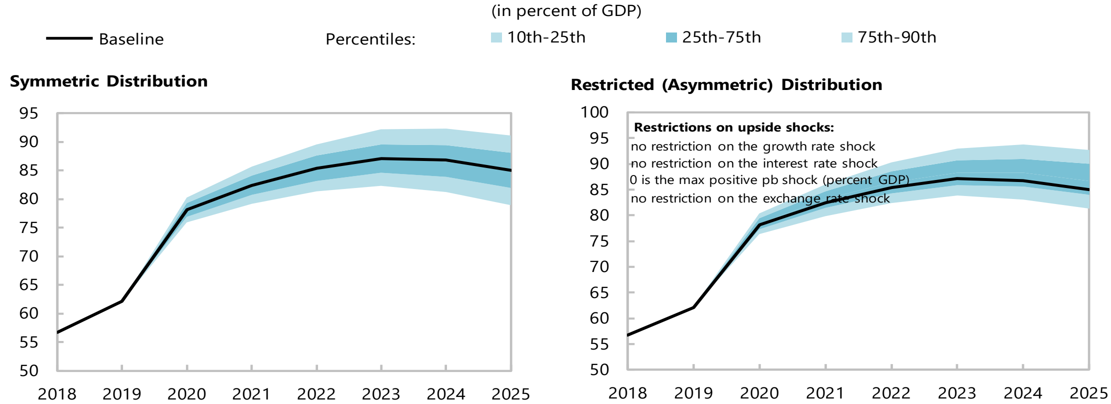
Figure A1.1. South Africa Public DSA Risk Assessment

Heat Map

Debt level 1/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock /6	Persistently Low Growth
Gross financing needs 2/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock /6	Persistently Low Growth
Debt profile 3/	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt	

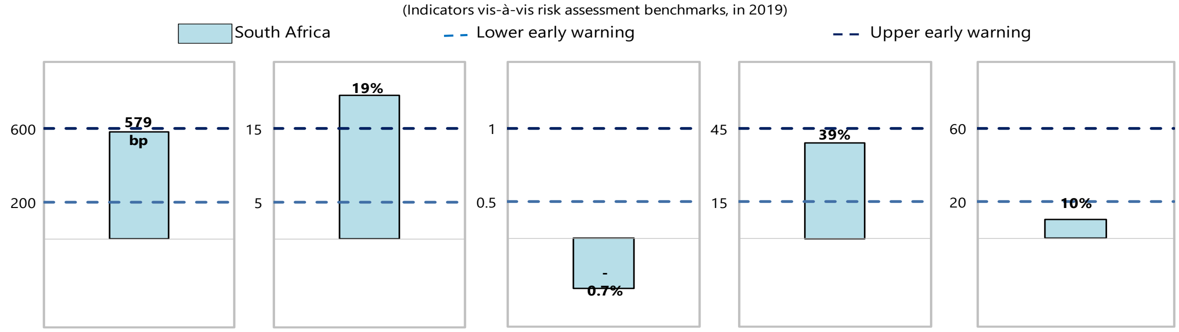
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2019)



Bond spread (in basis points) 4/

External Financing Requirement (in percent of GDP) 5/

Annual Change in Short-Term Public Debt (in percent of total)

Public Debt Held by Non-Residents (in percent of total)

Public Debt in Foreign Currency (in percent of total)

Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 70% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 15% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.

Lower and upper risk-assessment benchmarks are:

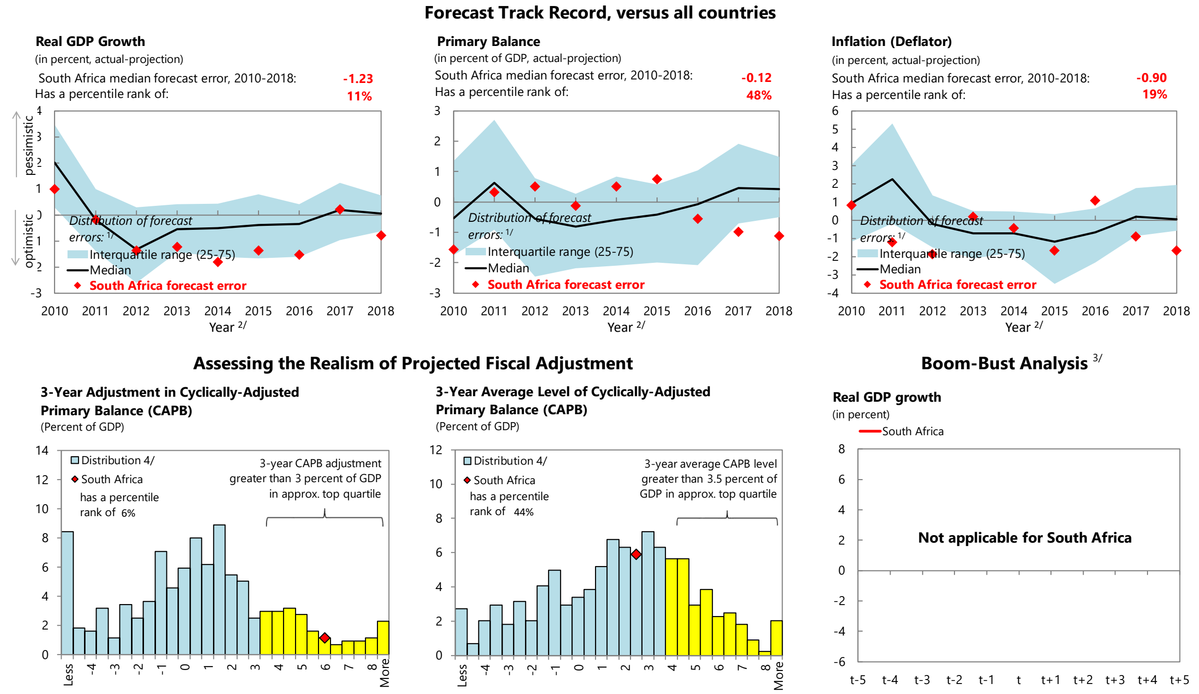
200 and 600 basis points for bond spreads; 5 and 15 percent of GDP for external financing requirement; 0.5 and 1 percent for change in the share of short-term debt; 15 and 45 percent for the public debt held by non-residents; and 20 and 60 percent for the share of foreign-currency denominated debt.

4/ Long-term bond spread over U.S. bonds, an average over the last 3 months, 14-Apr-20 through 13-Jul-20.

5/ The external financing requirement is defined for the economy as a whole (including the private sector). More specifically, it is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

6/ The contingent liability shock scenario included in the heat map entails the calling of all remaining SOE loan guarantees plus the contingent liabilities of the loan guarantee fund. The standard financial sector contingent liability shock usually in the heat map is not triggered in the case of South Africa because the three year cumulative increase of the credit-to-GDP or loan-to-deposit ratio do not exceed the corresponding thresholds (i.e. 15 percent of GDP for the credit to GDP ratio and 1.5 loan-to-deposit ratio).

Figure A1.2. South Africa Public DSA – Realism of Baseline Assumptions



Source : IMF Staff.

1/ Plotted distribution includes all countries, percentile rank refers to all countries.

2/ Projections made in the spring WEO vintage of the preceding year.

3/ Not applicable for South Africa, as it meets neither the positive output gap criterion nor the private credit growth criterion.

4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Figure A1.3 South Africa Public Sector Debt Sustainability Analysis (DSA) – Baseline Scenario

(In percent of GDP unless otherwise indicated)

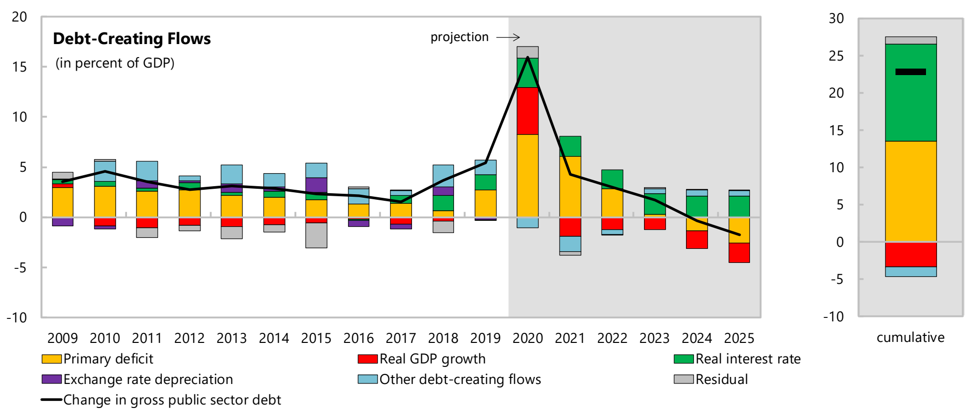
Debt, Economic and Market Indicators [1/]

	Actual			Projections					
	2009-2017 [2/]	2018	2019	2020	2021	2022	2023	2024	2025
Nominal gross public debt	43.2	56.7	62.2	78.1	82.4	85.4	87.1	86.8	85.0
Public gross financing needs	10.7	11.6	14.7	21.5	21.2	20.7	19.0	17.2	16.2
Real GDP growth (in percent)	1.6	0.8	0.2	-7.2	2.6	1.5	1.5	2.1	2.3
Inflation (GDP deflator, in percent)	6.1	3.9	4.1	3.0	3.9	4.3	4.5	4.5	4.5
Nominal GDP growth (in percent)	7.8	4.7	4.2	-4.3	6.6	5.9	6.1	6.7	6.9
Effective interest rate (in percent) [4/]	7.5	7.0	7.0	7.2	6.8	6.8	7.1	7.2	7.2

As of July 13, 2020		
Sovereign Spreads		
EMBIG (bp) 3/		526
5Y CDS (bp)		316
Ratings	Foreign	Local
Moody's	Ba1	Ba1
S&Ps	BB-	BB
Fitch	BB	BB

Contribution to Changes in Public Debt

	Actual			Projections							
	2009-2017	2018	2019	2020	2021	2022	2023	2024	2025	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	2.9	3.7	5.4	16.0	4.3	3.0	1.7	-0.3	-1.8	22.9	
Identified debt-creating flows	3.5	4.8	5.5	14.8	4.7	3.1	1.6	-0.4	-1.8	22.0	
Primary deficit	2.2	0.6	2.7	8.3	6.0	2.8	0.3	-1.4	-2.6	13.5	0.8
Primary (noninterest) revenue and grants	24.2	25.6	25.7	23.6	23.3	24.7	25.3	25.8	26.2	148.9	
Primary (noninterest) expenditure	26.4	26.3	28.4	31.9	29.3	27.5	25.6	24.5	23.6	162.4	
Automatic debt dynamics [5/]	0.0	2.0	1.3	7.6	0.1	0.7	0.8	0.4	0.2	9.8	
Interest rate/growth differential [6/]	-0.1	1.2	1.5	7.6	0.1	0.7	0.8	0.4	0.2	9.8	
Of which: real interest rate	0.5	1.6	1.6	2.9	2.0	1.9	2.0	2.1	2.1	13.1	
Of which: real GDP growth	-0.6	-0.4	-0.1	4.7	-1.9	-1.2	-1.2	-1.7	-1.9	-3.3	
Exchange rate depreciation [7/]	0.1	0.8	-0.1	…	…	…	…	…	…	…	
Other identified debt-creating flows	1.3	2.2	1.4	-1.0	-1.5	-0.5	0.5	0.6	0.6	-1.3	
Privatization/Drawdown of Deposits	0.5	0.5	0.7	-0.1	-2.3	-0.6	-0.1	-0.1	0.0	-3.1	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Stock-Flow adjustment	0.8	1.7	0.7	-1.0	0.8	0.1	0.6	0.7	0.6	1.8	
Residual, including asset changes [8/]	-0.5	-1.1	0.0	1.2	-0.4	-0.1	0.1	0.1	0.1	0.9	



Source: IMF staff.

1/ Public sector is defined as central government.

2/ Based on available data.

3/ Long-term bond spread over U.S. bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as [(r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as r - π (1+g) and the real growth contribution as -g.

7/ The exchange rate contribution is derived from the numerator in footnote 5 as ae(1+r).

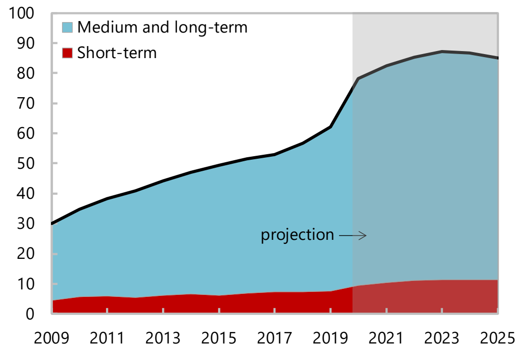
8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

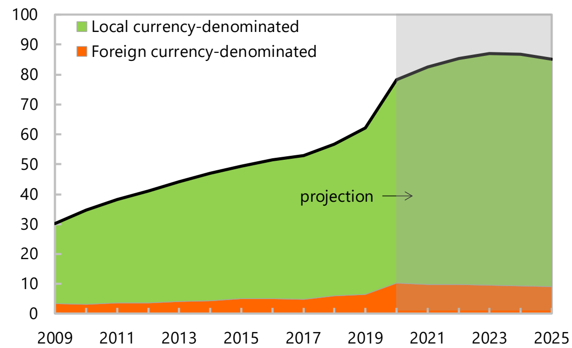
Figure A1.4 South Africa Public DSA – Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

By Maturity
(in percent of GDP)



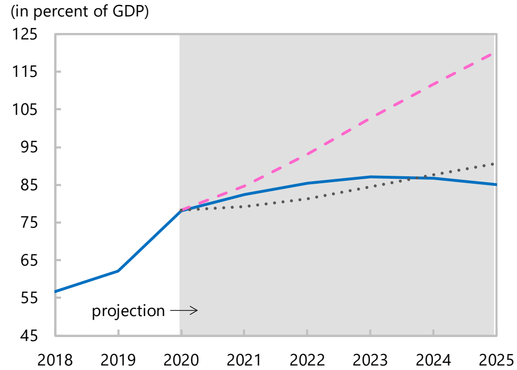
By Currency
(in percent of GDP)



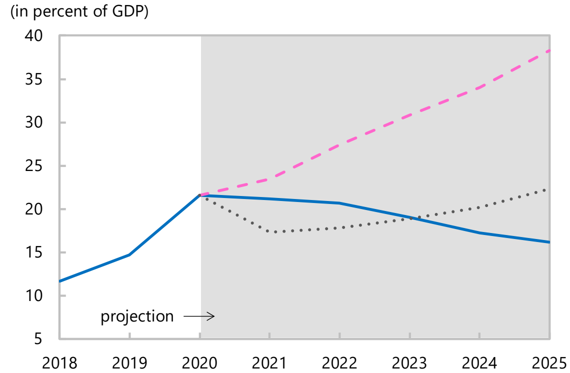
Alternative Scenarios

Baseline Historical Constant Primary Balance

Gross Public Debt
(in percent of GDP)



Public Gross Financing Needs
(in percent of GDP)



Underlying Assumptions
(in percent)

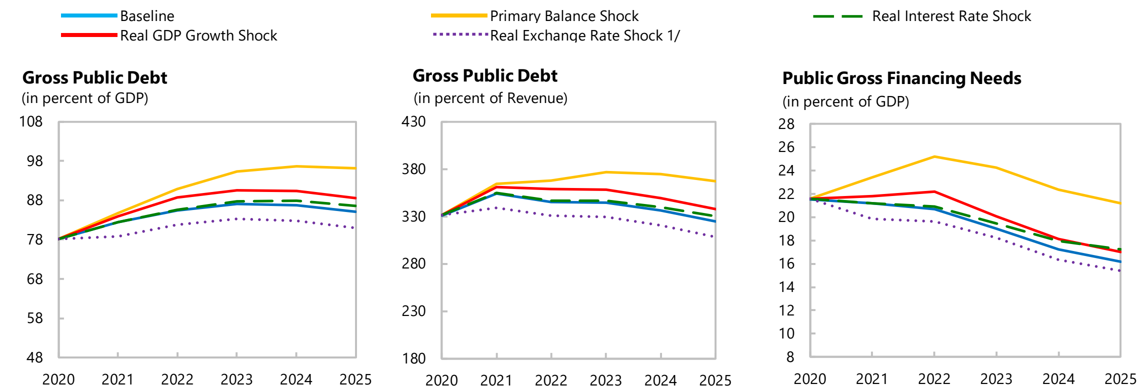
Baseline Scenario	2020	2021	2022	2023	2024	2025
Real GDP growth	-7.2	2.6	1.5	1.5	2.1	2.3
Inflation	3.0	3.9	4.3	4.5	4.5	4.5
Primary Balance	-8.3	-6.0	-2.8	-0.3	1.4	2.6
Effective interest rate	7.2	6.8	6.8	7.1	7.2	7.2
Constant Primary Balance Scenario						
Real GDP growth	-7.2	2.6	1.5	1.5	2.1	2.3
Inflation	3.0	3.9	4.3	4.5	4.5	4.5
Primary Balance	-8.3	-8.3	-8.3	-8.3	-8.3	-8.3
Effective interest rate	7.2	6.8	6.8	6.9	6.8	6.6

Historical Scenario	2020	2021	2022	2023	2024	2025
Real GDP growth	-7.2	1.7	1.7	1.7	1.7	1.7
Inflation	3.0	3.9	4.3	4.5	4.5	4.5
Primary Balance	-8.3	-2.0	-2.0	-2.0	-2.0	-2.0
Effective interest rate	7.2	6.8	6.9	7.0	6.9	6.6

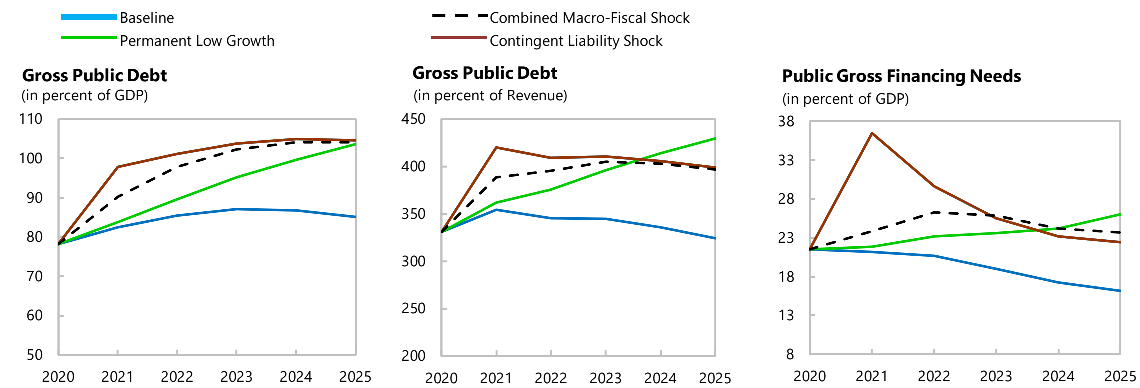
Source: IMF staff.

Figure A1.5 South Africa Public DSA – Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions
(in percent)

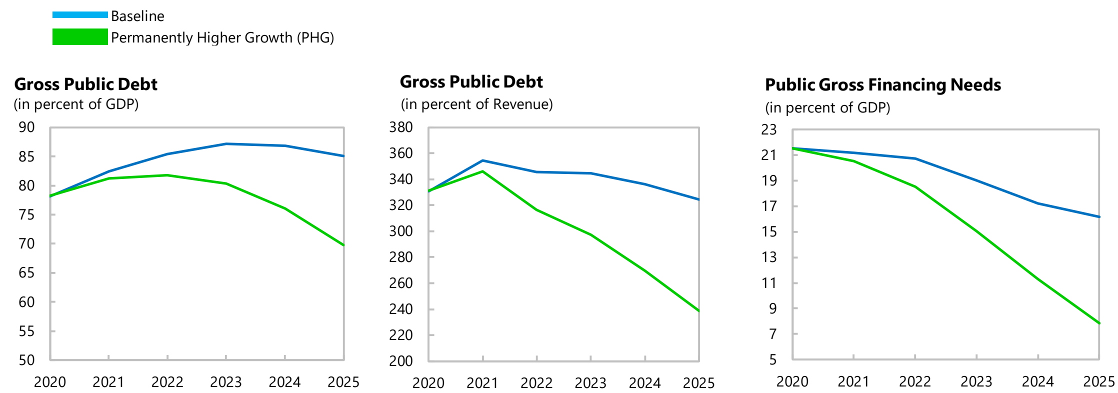
	2020	2021	2022	2023	2024	2025
Primary Balance Shock						
Real GDP growth	-7.2	2.6	1.5	1.5	2.1	2.3
Inflation	3.0	3.9	4.3	4.5	4.5	4.5
Primary balance	-8.3	-8.3	-6.0	-2.8	-0.3	1.4
Effective interest rate	7.2	6.8	6.8	7.1	7.2	7.3
Real Interest Rate Shock						
Real GDP growth	-7.2	2.6	1.5	1.5	2.1	2.3
Inflation	3.0	3.9	4.3	4.5	4.5	4.5
Primary balance	-8.3	-6.0	-2.8	-0.3	1.4	2.6
Effective interest rate	7.2	6.8	7.1	7.5	7.8	7.9
Combined Shock						
Real GDP growth	-7.2	1.5	0.5	1.5	2.1	2.3
Inflation	3.0	3.6	4.0	4.5	4.5	4.5
Primary balance	-8.3	-8.3	-6.0	-2.8	-0.3	1.4
Effective interest rate	7.2	7.0	6.9	7.3	7.5	7.6

	2020	2021	2022	2023	2024	2025
Real GDP Growth Shock						
Real GDP growth	-7.2	1.5	0.5	1.5	2.1	2.3
Inflation	3.0	3.6	4.0	4.5	4.5	4.5
Primary balance	-8.3	-6.5	-3.6	-0.3	1.4	2.6
Effective interest rate	7.2	6.8	6.8	7.1	7.2	7.2
Real Exchange Rate Shock						
Real GDP growth	-7.2	2.6	1.5	1.5	2.1	2.3
Inflation	3.0	15.5	4.3	4.5	4.5	4.5
Primary balance	-8.3	-6.0	-2.8	-0.3	1.4	2.6
Effective interest rate	7.2	7.0	6.7	6.9	7.1	7.1
Contingent Liability Shock						
Real GDP growth	-7.2	2.6	1.5	1.5	2.1	2.3
Inflation	3.0	3.9	4.3	4.5	4.5	4.5
Primary balance	-8.3	-21.3	-2.8	-0.3	1.4	2.6
Effective interest rate	7.2	6.8	7.1	8.0	8.5	8.7

Source: IMF staff.

Figure A1.6 South Africa Public DSA – Upside Risks Stress Tests

Additional Stress Tests



Underlying Assumptions

(in percent)

Baseline	2019	2020	2021	2022	2023	2024
Real GDP growth	-7.2	2.6	1.5	1.5	2.1	2.3
Inflation	3.0	3.9	4.3	4.5	4.5	4.5
Primary balance	-8.3	-6.0	-2.8	-0.3	1.4	2.6
Effective interest rate	7.2	6.8	6.8	7.1	7.2	7.2

PHG	2019	2020	2021	2022	2023	2024
Real GDP growth	-7.2	3.6	2.5	2.5	3.1	3.3
Inflation	3.0	3.9	4.3	4.5	4.5	4.5
Primary balance	-8.3	-5.6	-1.2	2.2	4.7	6.7
Effective interest rate	7.2	6.8	6.9	7.2	7.5	7.6

Source: IMF staff.

Appendix I. Letter of Intent

Pretoria, South Africa
July 15, 2020

Ms. Kristalina Georgieva
Managing Director
International Monetary Fund (IMF)
Washington, D.C. 20431

Dear Ms. Georgieva,

1. On behalf of the Government of South Africa, we hereby request approval of financial support from the IMF under the Rapid Financing Instrument (RFI) in an amount of SDR 3,051.2 million (100 percent of quota) to mitigate the adverse economic impact of COVID-19. We request that, upon approval by the IMF's Executive Board, the full amount be made immediately available to the National Treasury account at the South African Reserve Bank (SARB) as budget support.

2. South Africa has been hit hard by COVID-19. With its rapid spread and the adverse economic impact of a strict lockdown, the economy is under severe stress. Preliminary data show a marked decline in economic activity during the lockdown, with a nascent recovery underway. We expect output to fall drastically in 2020 and take more than three years to recover to pre-crisis levels. Unemployment will exceed 30 percent. Formal sector job losses are expected to exceed one million.

3. Prolonged weakness in the South African economy would have negative spillovers to the sub-Saharan African region, in particular in the southern part of the continent. South Africa remains a key contributor to the region's GDP. Trade in goods and services and remittances from regional workers employed in South Africa would also be at risk. At the same time, a drag in South Africa's investments in neighboring economies would jeopardize regional integration.

4. The crisis has adversely affected domestic market liquidity conditions and financial asset prices amid global market turmoil and fears that the pandemic would weigh heavily on growth and public finances. The country experienced sizable portfolio outflows in March, both in absolute terms and relative to emerging market peers. The sovereign credit downgrade by Moody's at end-March, which led to South Africa's exclusion from the World Government Bond Index, further exacerbated losses. These developments contributed to a significant depreciation of the rand, which fell more than 30 percent against the US dollar this year through early-April. The real effective exchange rate declined 16 percent in the first five months of 2020, one of the largest depreciations among large, liquid emerging markets. Domestic bond market yields rose sharply. Despite portfolio flows having

broadly stabilized since May, valuations of domestic financial assets, including the exchange rate, remain weak, resulting in challenging financing conditions for the public and private sectors.

5. We decided to implement a strong relief package amounting to R500 billion or more than 10 percent of GDP in response to the crisis. It is part of a set of interventions divided into three phases. In the first phase, we have reprioritized disaster relief already allocated in the budget towards the health sector; phase two relates to the fiscal support package; while the third phase will take place over the medium term and will be directed toward structural reforms to achieve higher and more durable economic growth. Given the profound uncertainty around the evolution of the pandemic and health-related conditions, it is likely that these phases will overlap.

6. As part of the relief package, we are implementing measures that include support to vulnerable groups through six-month top-ups of social security grants, food security, and other forms of distress relief; temporary employment relief support through the unemployment insurance fund; additions to health services; funding for municipal services such as cleaning, sanitizing and provision of clean water to poor and rural communities; school sanitization and preparedness; support to small businesses and workers and to critical public entities; and tax deferral measures and payment holidays. We have also launched a credit guarantee scheme for small and medium-sized firms. The scheme will be implemented in phases, over a minimum of 2 years. The SARB will provide the initial funding, but the fiscus will ultimately backstop and guarantee credits for an initial amount of R100 billion, up to a limit of R200 billion.

7. The direct impact of the fiscal package on the consolidated budget amounts to R185 billion while R101 billion of existing expenditure commitments will be reprioritized and shifted towards COVID-19-related interventions. The rest of the spending will be financed through the use of cash balances and borrowing from multilateral institutions (around US$7–7.5 billion).

8. The SARB has progressively cut the policy rate and provided liquidity to the financial sector and domestic markets. The Monetary Policy Committee (MPC) has cut rates by 275 basis points so far in 2020, taking the repo rate to 3.75 percent, its lowest level on record. In real terms, the policy rate is now negative, and well below the estimated real neutral rate of about 2 percent. In addition, the SARB has sought to support financial market functioning by: (1) expanding liquidity provision to banks through new lending facilities; (2) providing finance for the credit-guarantee scheme to support SMEs; (3) purchasing government bonds on the secondary market to ensure orderly market functioning; and (4) releasing capital buffers and relaxing provisioning requirements for banks, to keep credit flowing to the real economy.

9. Despite these efforts, GDP is projected to contract by over 7 percent in 2020. The growth projection is premised on a gradual relaxation of the restrictions associated with the lockdown. The peak in the infection rate is expected for end of 2020Q3, while the steepest economic contraction is forecast to occur in 2020Q2. Even after the relaxation of lockdown restrictions, the recovery of investment, exports and imports is expected to be gradual. Growth is forecast at 2.6 percent and 1.5 percent in 2021 and 2022, respectively.

10. Notwithstanding the sharp depreciation of the rand against the US dollar since January, inflationary pressures are projected to remain well contained given the widening negative output gap, weak wage pressures, and lower oil prices. Annual average headline CPI inflation is consequently expected to gradually return to the midpoint of the target band during 2020–22.

11. As a result of COVID-19-related pressures on the budget, the external position is under stress. Despite import compression, the current account deficit is projected to be around 1.8 percent of GDP in 2020 due to large net income payments. However, with the increase in capital outflows, higher financing costs, and additional spending required to support households and firms through the crisis, the government borrowing needs over the upcoming months will be substantial. While exchange rate flexibility helps mitigate balance of payments pressures, a temporary external financing need of about US$10.5 billion is likely to emerge in 2020. We intend to cover this need through the use of reserves and financing from IFIs, including the African Development Bank, the BRICS New Development Bank, the IMF and the World Bank.

12. COVID-19 has put significant pressure on the budget. The FY2020/21 budget deficit was 6.8 percent of GDP. However, the large economic downturn has led to substantial revisions of the fiscal indicators. Our estimates indicate that revenue will be lower by around R304 billion (or 6.3 percent of GDP) compared to the budget. Given that immediate spending adjustments are not prudent in the midst of a deep recession, the massive revenue losses, alongside the stimulus spending, imply that the national government deficit is now estimated at around 14.6 percent of GDP in FY2020/21. In addition to financing this deficit, the government may face increasing contingent liabilities, mainly from deteriorating finances in state-owned enterprises (SOEs).

13. The supplementary budget review submitted to parliament on June 24, 2020 sought approval of the COVID-19 relief package. This budget presented a medium-term stabilization scenario that will be the basis for the October Medium-Term Budget Policy Statement (MTBPS) baseline projections. This scenario reflects our decision to implement the needed measures to achieve debt stabilization. To this end not only will the temporary relief measures be phased out as the pandemic wanes, but some of the expenditure cuts implemented to make room for the relief measures will either become permanent or be replaced by other cuts.

14. From FY2021/22 onwards, once the impact of the pandemic subsides, we will take action to reverse the upward trajectory of the public debt-to GDP ratio. To facilitate this effort, we are open to introducing a debt ceiling in addition to the nominal spending ceiling currently in place. The October MTBPS and the process leading up to the February 2021 budget will propose fiscal consolidation measures that will allow public debt to decline after peaking at 87.4 percent of GDP in FY2023/24. The implementation of zero-based budgeting for national and provincial departments will reduce dependency on previous budgets and pursue a better alignment between revenue and expenditure. We intend to take measures that include further reductions in the wage-to GDP ratio, rationalization of transfers to SOEs, and streamlining of subsidies. The reform package seeks to place expenditure levels on a more sustainable footing while improving its composition. On the revenue side, we intend to help revenue recover by strengthening enforcement to enhance tax compliance, alongside other revenue measures. Moreover, our support to SOEs will be strictly

conditional on meeting key performance indicators to improve their operational and financial health so as to reduce its need over time. This process has been initiated with Eskom and will be extended to all SOEs.

15. The SARB will preserve its inflation objective and aim to anchor inflation expectations around the mid-point of the 3-6 percent target range. Based on the underlying economic conditions, there will be adjustments in the policy stance to ensure inflation does not accelerate above the 4.5 percent midpoint of the target range on a sustained basis. The SARB's active balance sheet policies will be unwound over time, in line with the planned transition of the monetary policy implementation framework, which was premised on a money market liquidity shortage before the crisis. The SARB will also ensure soundness of the financial system. Bank regulatory allowances will be reversed, in time, as conditions normalize. SARB measures have been conceived as temporary interventions for a crisis, which will be most intense this year and fade over the medium term.

16. In addition to fiscal consolidation, debt stabilization will require removing structural constraints to growth. To this end, we will implement reforms as articulated in our document entitled *Economic Transformation, Inclusive Growth, and Competitiveness: Towards an Economic Strategy for South Africa. These reforms* focus on (1) modernizing and reforming network industries (such as electricity, road, rail, ports and telecommunications) so that lower costs and increased efficiency can improve business competitiveness; (2) re-orienting trade policies and pursuing greater regional integration to boost exports, employment and innovation; (3) lowering barriers to entry to make it easier for businesses to start, grow, and compete; and (4) supporting labor-intensive sectors such as tourism and agriculture to achieve more inclusive growth.

17. Addressing Eskom's problems is key to restoring reliable electricity supply, building confidence, and lessening the burden on the fiscus. In the near-term the focus is on: (1) improving the fleet's efficiency to reduce risks of load shedding; (2) stabilizing Eskom's financial situation by spending wisely on procurement and compensation and enhancing revenue collection from municipalities; and (3) continuing to encourage private sector participation in the sector. The planned unbundling will enable greater efficiencies in the electricity sector and reduce fiscal risk posed by Eskom.

18. Given that COVID-19 has destroyed some productive capacity, deep reforms are needed in product markets to remove barriers to domestic and foreign investment, followed by reforms to support job-rich growth. South African firms need to innovate, move to greener technologies, raise productivity, and seek out export markets. We intend to encourage firm entry to improve competition; leverage public-private partnerships in a fiscally responsible way to boost market access; and reduce regulatory obstacles to investment in all sectors. We intend to raise employment-creation by revamping the skills framework, giving firms greater ability to hire labor and undertaking education reforms to make it easier for first time workers to find a job.

19. On governance, meaningful reforms are being implemented in the South African Revenue Service, the Public Investment Corporation, and other institutions. New leadership has been appointed in various public entities; policies and procedures are being reviewed; and prosecution

agencies have been given additional capacity to investigate and hold wrong-doers accountable. New procurement legislation, aimed at consolidating rules and management of the public procurement system within one framework, is set to be presented to parliament during the current fiscal year.

20. South Africa does not have outstanding credit from the IMF and its capacity to repay the RFI purchase is adequate. We intend to meet our financial obligations to the IMF on a timely basis. External and public debt sustainability indicators will not change significantly as a result of the RFI purchase, and we will take any necessary measures to maintain debt sustainability.

21. The SARB will undergo a safeguards assessment as soon as feasible. We will provide Fund staff with the SARB's audit reports and authorize IMF staff to engage with external auditors as needed. We have put in place a memorandum of understanding between the SARB and the National Treasury that clarifies the responsibilities for timely servicing of the financial obligations to the IMF.

22. Moreover, in line with the Public Financial Management Act, we are committed to transparently plan, use, monitor and report all COVID-19 related spending to ensure it reaches the targeted objectives, by: (1) publishing on a regular basis the execution of COVID-19-related expenditures, auditing such expenditure, including ex-post valuation of delivery, within 12 months of the end of the fiscal year, to be performed by the Auditor General and publishing the findings; and (2) publicly disseminating all COVID-19-related procurement contracts and allocation (with details about awarded companies and their beneficial owners).

23. We do not intend to introduce or intensify exchange and trade restrictions and other measures or policies that would compound South Africa's balance of payments difficulties.

24. We agree to the publication of all the documents submitted to the Executive Board in relation to this request.

Sincerely yours,

/s/	/s/
Tito Titus Mboweni	Lesetja Kganyago
Minister of Finance	Governor, South African Reserve Bank

Statement by Mr. Dumisani Hebert Mahlinza and Ms. Mmatshepo Maidi on South Africa July 27, 2020

The South African authorities thank management and staff for their timely response to the request for emergency financing under the Rapid Financing Instrument (RFI) to address urgent financing needs created by the COVID-19 pandemic. They consider the RFI critical to catalyzing additional resources from development partners.

The shock generated by the COVID-19 pandemic and the ensuing health response has led to a large contraction in GDP, which has worsened South Africa's growth trajectory. At the same time, the combination of higher risk aversion towards emerging markets and the downgrading of South Africa's sovereign credit rating to sub-investment grade triggered substantial portfolio outflows. As a result, a sizeable financing gap has emerged, in an environment of rising debt service costs, weak growth and high global uncertainty.

To help address the urgent financing needs, the authorities request a purchase under the RFI in the amount of SDR3,051.2 million, equivalent to 100 percent of quota. Given the large financing gap, the authorities have also secured emergency financing from the New Development Bank and from the African Development Bank and plan to seek additional funding from other development partners.

The authorities are committed to the effective and transparent use of COVID-19-related resources, building on their strong public financial management system and commitment to transparency. They have also revamped their public procurement system to address weaknesses. In this context, they will regularly publish the execution of COVID-19 related expenditures; publish all COVID-19-related procurement contracts and details of beneficiary owners; and audit all COVID-19 related expenditures, including undertaking an ex-post evaluation of delivery. The South African Reserve Bank (SARB) will also undergo a safeguard assessment in line with the Fund requirement.

Pre-COVID-19 Economic Performance

Notwithstanding structural constraints that have resulted in subdued growth, unemployment, poverty and inequality, the authorities have continued to adhere to sound macroeconomic policies, supported by a flexible exchange rate and an effective inflation targeting regime. The sound domestic banking system and deep capital markets along with a largely rand denominated public debt profile, has facilitated the economy's resilience.

Economic performance in 2019 remained sluggish, with the economy growing by 0.2 percent largely constrained by electricity shortages and other structural challenges. The fiscal position continued to weaken, with the budget deficit increasing to 6.7 percent of GDP. The monetary policy stance remained accommodative as inflation declined to levels below the mid-point of the target band.

As part of ongoing efforts to improve policy implementation, the authorities have continued to build consensus around key policy positions throughout the year. Going forward they will continue to refine the details of their strong reform strategy.

Impact of the COVID-19 Pandemic

Since the first registered COVID-19 case on March 9, 2020, the number of cases in South Africa has risen to 394 948, as of July 22, 2020. The rate of infection is expected to peak in the third quarter of 2020. Taking into account the spillovers from the global downturn and the implementation of domestic containment measures since March 2020, economic activity continues to be curtailed.

While severe pandemic outcomes have been prevented by early implementation of containment measures, GDP growth is projected to contract by 7.2 percent in 2020, with significant spillover effects on neighboring economies. On the fiscal front, a domestic revenue shortfall of over R300 billion is forecast, while spending on health and support to vulnerable households and businesses has increased. As a result, the fiscal deficit is projected to widen from 6.8 per cent, projected in February 2020, to 14.6 percent of GDP in FY 2020/21. Consequently, the ratio of public debt to GDP is projected to rise from 63.5 percent in FY2019/20 to 81.8 percent in FY2020/21. On the social front, the pandemic will increase unemployment, which is already at 30.1 percent at the end of the first quarter while formal sector job losses from the pandemic are expected to exceed one million.

Policy Responses to the Pandemic

Recognizing the potential adverse impact of the pandemic, the authorities took early action to contain the spread of the virus and ensure the adequacy of the health system. The government declared a national state of disaster towards end-March and subsequently instituted a national lockdown, with the temporary closure of schools and all non-essential businesses. In parallel, the authorities enhanced testing and treatment facilities. At the same time, they established a COVID-19 National Command Council to promote public awareness and provide COVID-19 updates.

To mitigate the impact of the pandemic, the authorities have designed a three-phase intervention approach which prioritizes disaster relief in the first stage, fiscal support in the second phase and, a focus on structural reforms in the third phase. In this respect, they are implementing a broad fiscal relief package amounting to R500 billion (10.3 percent of GDP) to support healthcare spending and cushion the impact of the crisis on the most vulnerable households and businesses. Additional allocations towards public health at the national, provincial, and local government spheres are also being made. The package includes funding for a large temporary increase in social grants as well as funding for the Social Relief of

Distress grant for the most destitute. Further, additional funding has been availed for unemployment insurance payments. Other measures include tax deferral and payment holidays.

A loan guarantee scheme amounting to R200 billion has been set up to assist businesses with the financing of recurrent expenses such as salaries, rents, lease agreements and contracts with suppliers. The Scheme is administered by the SARB and is guaranteed by the National Treasury. To date, uptake on this scheme is estimated at R11.7 billion, which is slower than anticipated. After a review, changes have been made to the Scheme, including adding a 'business restart' option and clarifying the criteria under which banks should lend.

The SARB's response to the COVID-19 pandemic has been timely and appropriate to the scale of the shock. Specifically, the Monetary Policy Committee has reduced the policy rate by 275 basis points, between March and July, taking the repo to 3.50 percent, its lowest level on record. Further, the SARB has provided a range of additional lending instruments to ensure banks have sufficient liquidity and has conducted government bond purchases in the secondary market to restore the smooth functioning of the market. In both these cases, the volumes of liquidity provided have tapered off as conditions have normalized.

To uphold its financial stability mandate, the SARB continues to monitor activity in the banking and financial sectors and has upgraded its supervisory capacity to effectively deal with elevated stress in the system. Capital and liquidity buffers, built up during more normal times, have been temporarily reduced, giving banks more scope to extend credit to the real economy. The SARB has also provided regulatory guidance for dealing with borrowers who would be able to meet their debt obligations but for the COVID-19 shock, which will help contain the negative balance sheet effects of the crisis. In addition, the SARB has encouraged banks to forgo dividend payments to conserve capital, and further enhance bank resilience.

Post-crisis Measures

Once the pandemic subsides, the authorities aim to return to a sustainable fiscal position. To demonstrate their commitment to this objective, a special Adjustments Budget was tabled in Parliament on June 24, 2020, outlining an active scenario, which will be the basis for the Medium-Term Budget Policy Statement (MTBPS) baseline projections. The October 2020 MTBPS will propose fiscal consolidation measures that will allow public debt to stabilize in FY2023/24. To this end, the temporary relief measures implemented in response to the pandemic will be phased out as the pandemic wanes and some expenditure cuts will become permanent. In addition, the authorities intend to move to a zero-based budgeting framework to rebalance and streamline spending. Further, the authorities are committed to reducing government guarantees as part of an effort to maintain prudent levels of debt and contingent liabilities. In this regard, they will closely monitor contingent liabilities in line with guarantee reporting guidelines for national departments and state-owned enterprises.

In line with the "Economic Transformation, Inclusive Growth, and Competitiveness: Towards an Economic Strategy for South Africa" paper, the authorities will implement key structural reforms. In this respect, they will rationalize transfers to SOEs and streamline subsidies. In particular, support to SOEs will be strictly conditioned on meeting key performance indicators to improve their operational and financial health. In addition, they will further strengthen governance and accountability of SOEs by reviewing policies and procedures.

To remove structural constraints to growth, the authorities plan to modernize and reform network industries including transport, energy, water, and telecommunications as well as implement deep reforms in product markets to remove barriers to domestic and foreign investment, followed by reforms to support job-rich growth. They consider addressing Eskom's problems as essential to restoring reliable electricity supply, building confidence and reducing the burden on the fiscus. In the near-term, the focus will be on improving efficiency to reduce risks of load shedding, stabilizing Eskom's financial situation and encouraging private sector participation. In the telecommunications sector, the authorities will expedite the allocation of broadband to increase competition and reduce the cost of data and developing digitalization.

Conclusion

The authorities remain committed to implementing prudent policies and structural reforms to further entrench macroeconomic stability and avert a larger crisis. To this end, they will steadfastly implement reforms to foster sustainable and inclusive growth as the crisis abates. Our authorities appreciate the continued support from the Fund and other development partners in tackling the COVID-19 pandemic. As such, they look forward to the Executive Directors' support to their request for emergency financing under the RFI to sustain their efforts to mitigate the impact of the pandemic on all South Africans.