THE REPUBLIC OF SOUTH AFRICA

Investor Presentation

February/March 2016

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1. Key highlights

Summary

- South Africa faces exceptionally difficult global and domestic economic conditions over the next several years
- The 2016 Budget proposals will return the public finances to a sustainable path
- The Budget sets out tax increases and spending reductions to narrow the fiscal deficit and stabilise growth of public debt, while protecting core social and economic programmes
- To expand the social wage in a sustainable manner, create jobs and reduce poverty, South Africa needs much faster rates of inclusive economic growth
- The 2016 Budget emphasises both public- and private-sector contributions to development
- Government is stepping up its partnerships with business, labour and civil society to realise the vision of the National Development Plan
- On track to carry out the reforms needed to transform the economy

2. Macro economic developments

Global growth revised down due to weak emerging market outlook

IMF Growth Projections, 2014 - 2017

Region/country Percentage	2014	2015	2016	2017	2014	2015	2016	2017
	GDP projections				CPI projections			
World	**3.4**	**3.1**	**3.4**	**3.6**	**3.5**	**3.3**	**3.4**	**3.6**
Advanced economies	**1.8**	**1.9**	**2.1**	**2.1**	**1.4**	**0.3**	**1.2**	**1.7**
United States	2.4	2.5	2.6	2.6	1.6	0.1	1.1	1.8
Euro area	0.9	1.5	1.7	1.7	0.4	0.2	1.0	1.3
United Kingdom	2.9	2.2	2.2	2.2	1.5	0.1	1.5	2.0
Japan	0.0	0.6	1.0	0.3	2.7	0.7	0.4	1.6
Emerging markets and developing economies	**4.6**	**4.0**	**4.3**	**4.7**	**5.1**	**5.6**	**5.1**	**4.9**
Brazil	0.1	-3.8	-3.5	0.0	6.3	8.9	6.3	5.2
Russia	0.6	-3.7	-1.0	1.0	7.8	15.8	8.6	7.3
India	7.3	7.3	7.5	7.5	5.9	5.4	5.5	5.4
China	7.3	6.9	6.3	6.0	2.0	1.5	1.8	2.2
Sub-Saharan Africa	**5.0**	**3.5**	**4.0**	**4.7**	**6.4**	**6.9**	**7.3**	**6.7**
South Africa	1.5	1.3	0.7	1.8	6.1	4.8	5.9	5.6
South Africa (National Treasury forecast)	*1.5*	*1.3*	*0.9*	*1.7*	*6.1*	*4.6*	*6.8*	*6.3*

Source: IMF World Economic Outlook Update, January 2016

- IMF predict world growth recovery will be 0.2 percentage points slower in 2016 due to downward revisions to growth in emerging markets
- Growth in advanced economies to drive global growth in 2016 but still uneven
- Emerging markets are not rebounding as quickly as forecast due to low commodity prices, China rebalancing and rising financial market volatility
- Sub-Saharan Africa still one of fastest growing regions – but 2016 growth revised down 0.8 percentage points
- Growth risks remain biased to the downside

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Economic outlook reflects worsening growth

- Growth reduced across the forecast period - drought, weak commodity prices, slower than expected expansion in global growth
- Investment growth lower due to weaker confidence, rand and commodity prices
- Household spending reduced by higher inflation, lower job creation
- Electricity remains a constraint on growth till 2018

RSA Growth Projections, 2012 - 2018

	2012	2013	2014	2015	2016	2017	2018
Percentage change		**Actual**		**Estimate**		**Forecast**	
Final household consumption	3.4	2.9	1.4	1.4	0.7	1.6	2.2
Final government consumption	3.4	3.3	1.9	0.4	1.2	-0.2	0.2
Gross fixed capital formation	3.6	7.6	-0.4	1.1	0.3	1.4	2.7
Gross domestic expenditure	3.9	1.4	0.6	0.1	1.1	1.7	2.2
Exports	0.1	4.6	2.6	9.5	3.0	4.6	5.2
Imports	6.0	1.8	-0.5	5.3	3.7	4.5	4.9
Real GDP growth	**2.2**	**2.2**	**1.5**	**1.3**	**0.9**	**1.7**	**2.4**
CPI inflation	5.7	5.8	6.1	4.6	6.8	6.3	5.9
Current account balance (% of GDP)	-5.0	-5.8	-5.4	-4.1	-4.0	-3.9	-3.9

Source: Reserve Bank, National Treasury

Decisive actions to accelerate growth

- Government is acting to restore confidence and support private investment
  - Encouraging private sector involvement in renewable energy and SOCs
  - InvestSA to encourage domestic and foreign investment
  - 9 Point Plan and Operation Phakisa delivering focused sector-specific strategies
- Reducing infrastructure constraints and bottle necks
  - R865 billion over MTEF to improve infrastructure
  - Reprioritised spending enhances future growth
- Improving the ease of doing business
  - Visa regulation amendments
  - Targeted small business support with municipalities
  - Project in 9 municipalities to improve regulatory processes to best practice
- Increasing policy certainty and coordination
  - Socioeconomic Impact Assessments improve engagements on new policies
  - Minerals and Petroleum Resources Development Amendment Bill likely finalised
- Enhancing labour relations and labour market stability

3. Fiscal Policy

Fiscal consolidation accelerated

Tax measures

- In 2016/17, the following tax measures have been put in place
  - R7.6 billion raised through limited fiscal drag relief,
  - R9.5 billion through increases in fuel levy and specific excise duties,
  - and R2 billion from adjustments to capital gains tax and transfer duty

Spending ceiling

- Reductions of R10 billion in 2017/18 and R15 billion in 2018/19 applied to state compensation budgets
- Moratorium placed on administrative and managerial vacancies starting in April 2016.
- Appointments considered only after departments have submitted clear human resource plans aligned with reduced compensation budgets and greater efficiency

Reprioritisation

- Reprioritisation of R31.8 billion over the MTEF period for the following
  - to support higher education, South Africa's contributions to the New Development Bank, and for a larger contingency reserve.
- Funding reprioritised away from non-essential items and compensation budgets

Consolidated fiscal deficit narrows sharply over the medium term

- Budget deficit narrows from 3.9 per cent of GDP in the current year to 2.4 per cent in 2018/19
- A primary surplus in 2016/17 for the first time since 2009 (i.e. revenue exceeds non-interest expenditure)

Consolidate budget framework, 2012/13 – 2018/19

R billion/percentage of GDP	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19
			Outcome	Revised estimate	Medium-term estimates		
Revenue	**907.6**	**1,008.1**	**1,100.0**	**1,223.1**	**1,324.3**	**1,436.7**	**1,571.6**
	27.3%	*27.9%*	*28.6%*	*30.0%*	*30.2%*	*30.2%*	*30.4%*
Non-interest expenditure	950.1	1,034.5	1,116.5	1,245.6	1,308.9	1,403.4	1,509.6
	28.6%	*28.7%*	*29.0%*	*30.6%*	*29.8%*	*29.5%*	*29.2%*
Interest payments	93.3	109.6	121.2	135.3	154.3	168.7	185.6
	2.8%	*3.0%*	*3.2%*	*3.3%*	*3.5%*	*3.6%*	*3.6%*
Expenditure	**1,043.4**	**1,144.1**	**1,237.7**	**1,380.9**	**1,463.3**	**1,572.1**	**1,695.2**
	31.4%	*31.7%*	*32.2%*	*33.9%*	*33.3%*	*33.1%*	*32.8%*
Budget balance	**-135.9**	**-136.0**	**-137.8**	**-157.9**	**-139.0**	**-135.3**	**-123.6**
	-4.1%	*-3.8%*	*-3.6%*	*-3.9%*	*-3.2%*	*-2.8%*	*-2.4%*
Primary balance	**-42.6**	**-26.4**	**-16.6**	**-22.6**	**15.4**	**33.4**	**62.0**
	-1.3%	*-0.7%*	*-0.4%*	*-0.6%*	*0.4%*	*0.7%*	*1.2%*

Source: National Treasury

Risks to the fiscal outlook remain, but government is managing them

- **Further deterioration in economic growth**
  - Decline in growth typically results in falling revenue growth, increasing the deficit and debt as a share of GDP
  - Further increases in interest rates, combined with a weaker exchange rate and rising inflation, would raise the cost of borrowing and increase the stock of debt
- **Expenditure pressures linked to inflation**
  - Rising inflation would place upward pressure on inflation-linked expenditure, including compensation, social grants and free basic services
  - Expenditure ceiling remains in place and budget execution remains excellent, with departments sticking to appropriated expenditure limits
- **Weak financial positions of several major public entities**
  - Government has acted to stabilize several state-owned enterprises
  - Future commitments of state will depend on reforms that resolve problems with governance, and may also involve private-sector participation

4. Financing of borrowing requirement

National government gross borrowing requirement and financing

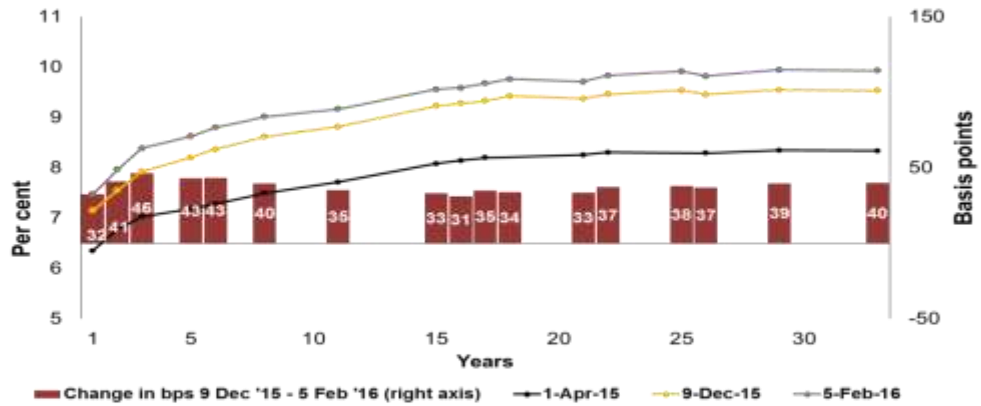
Financing of national government borrowing requirement, 2014/15 – 2018/19

	2014/15	2015/16		2016/17	2017/18	2018/19
R million	**Outcome**	**Budget**	**Revised**	**Medium-term estimates**		
Main budget balance	**-166,580**	**-173,054**	**-172,799**	**-156,342**	**-157,396**	**-151,337**
Financing						
Domestic short-term loans (net)	**9,569**	**13,000**	**13,000**	**25,000**	**33,000**	**23,000**
Treasury bills	10,011	13,000	7,557	25,000	33,000	23,000
Corporation for Public Deposits	-442	–	5,443	–	–	–
Domestic long-term loans (net)	**157,014**	**144,809**	**144,457**	**116,200**	**106,681**	**107,850**
Market loans (gross)	192,414	172,500	174,979	174,000	165,500	160,500
Loans issued for switches	-1,160	–	-2,479	–	–	–
Redemptions	-34,240	-27,691	-28,043	-57,800	-58,819	-52,650
Foreign loans (net)	**8,361**	**7,797**	**12,372**	**7,811**	**17,914**	**19,566**
Market loans (gross)	22,952	11,530	16,220	23,205	22,635	21,900
(gross)						
of loans)	-14,591	-3,733	-3,848	-15,394	-4,721	-2,334
Change in cash and other balances	**-8,364**	**7,448**	**2,970**	**7,331**	**-199**	**921**
Cash balances	-5,838	3,662	-7,655	3,230	-4,342	-3,006
Other balances	-2,526	3,786	10,625	4,101	4,143	3,927
Total	**166,580**	**173,054**	**172,799**	**156,342**	**157,396**	**151,337**

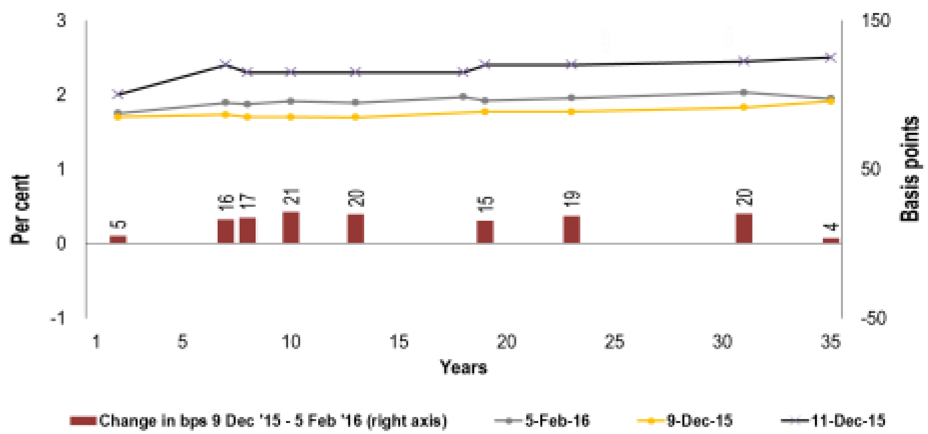
Source: National Treasury

Yield curve reflects higher risk premium

Fixed-rate bond yield curve movement



Inflation-linked bond yield curve movement



- Fixed-rate bond yields have weakened significantly since April 2015
  - commodity prices plummeted to record lows
  - constant speculation on timing and magnitude of US Fed hiking cycle
  - Chinese currency management stoked fears of a slowing Chinese economy
- Inflation-linked bond yields have continued to hold up very strongly
  - Break-even inflation rate at +7 per cent

Source: National Treasury

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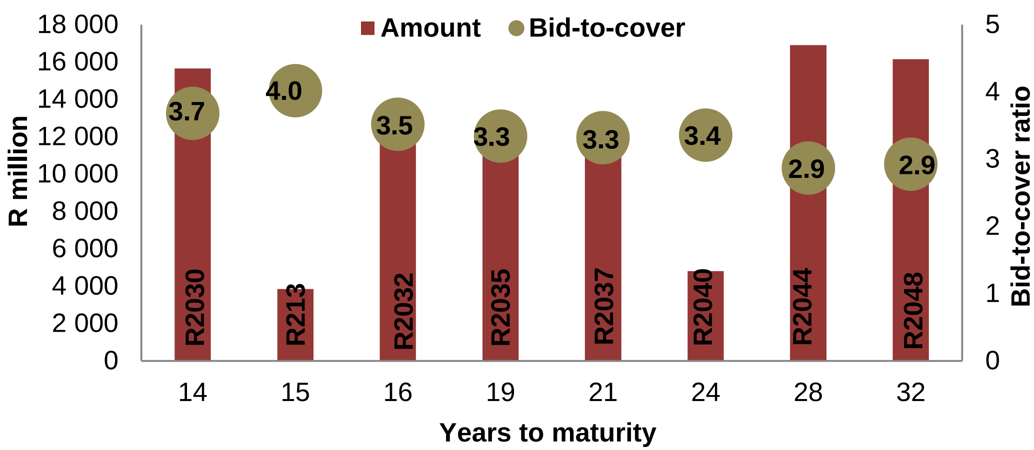
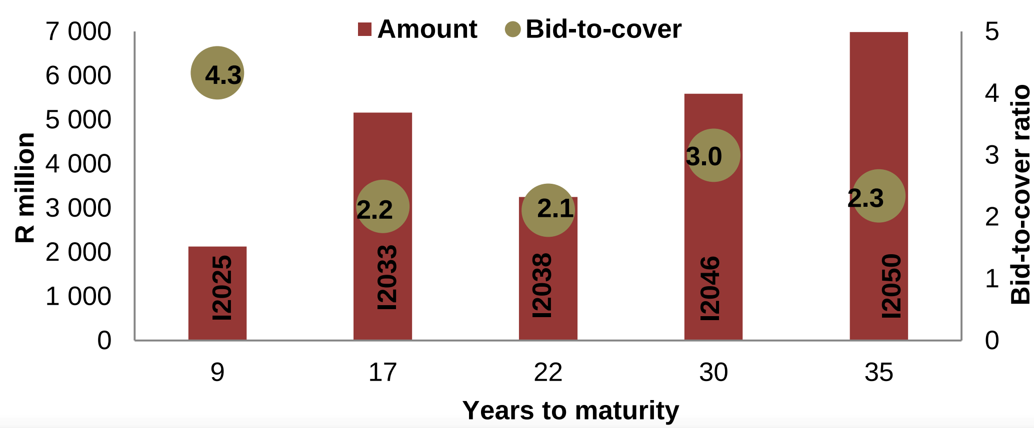
Subscription rates on government bonds remain strong

Average bid-to-cover ratio of fixed-rate bond auctions



Average bid-to-cover ratio of Inflation-linked bond auctions

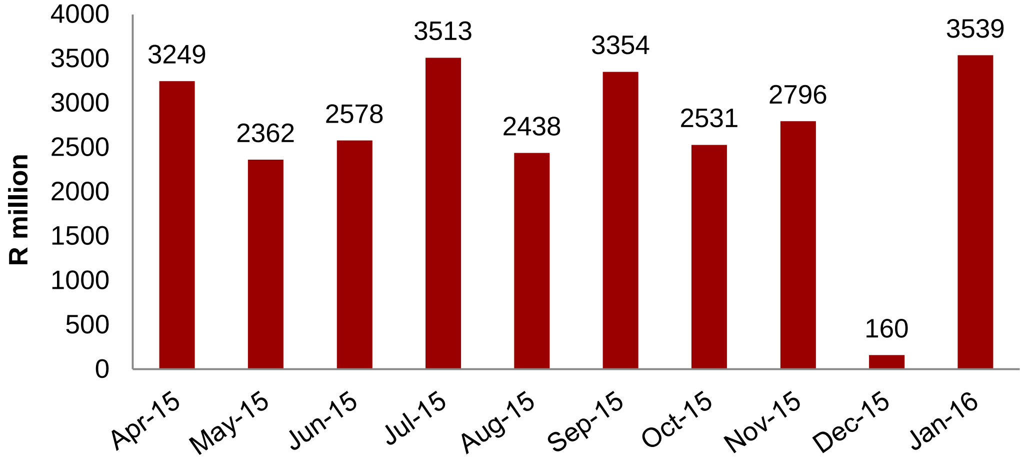


- Fixed-rate bond auctions remain well-subscribed
  - Average bid-to-cover ratios of 3.4
  - The R213 bond was 4x over-subscribed due to limited issuance
  - R2035 and R2040 bonds also in demand due to 100 per cent non-competitive auctions (non-comps)
- ILB auctions remain well subscribed
  - The I2025 bond had a high subscription rate as a result of limited issuance
  - The I2046 bond also had fair amount of appetite

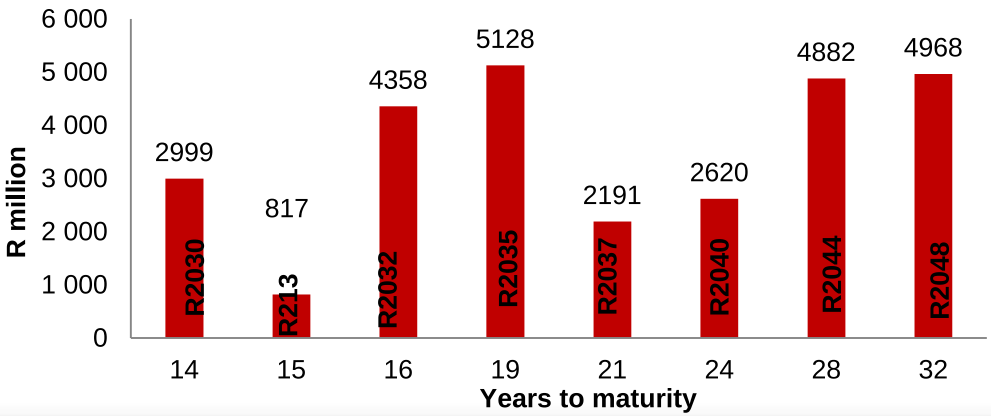
Source: National Treasury

Non-competitive auctions well taken-up

Monthly take-up of non-competitive auctions



Non-competitive auctions performance per funding instrument



- R26.5 billion raised through non-comps as at end of January 2016
- Months of July and January saw good amounts of take-up in non-comps
- New bonds allocated 100 per cent non-comps until outstanding amount reaches R10 billion
  - Non-comp participation on R2035 bond picked up aggressively in the third quarter after a relatively muted start due to market making obligation
  - R2044 and R2048 bonds have also had strong take-ups

Source: SA National Treasury

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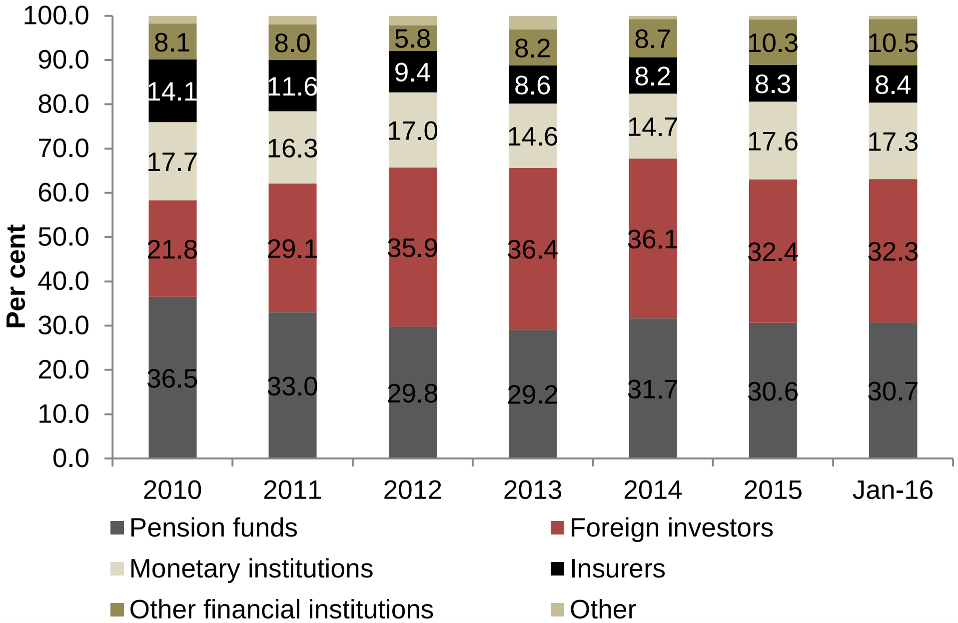
Deep capital markets enable funding of borrowing requirement

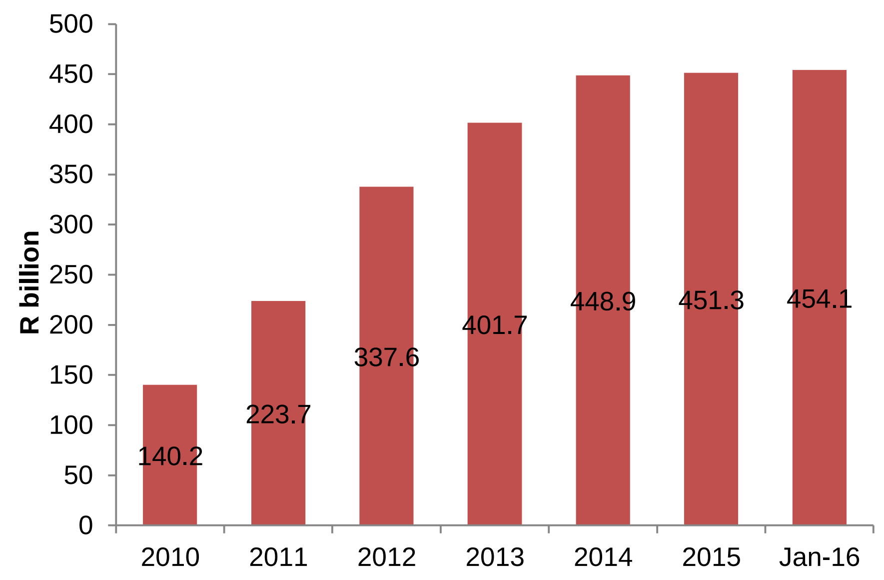
- Non-resident bond holdings as a proportion of total government domestic debt decreased from 36 per cent in 2014 to 32.4 per cent in 2015
- In absolute terms, non-resident holdings increased by a modest R1.2 billion during the year
- The was an increase in non-resident holdings of R3 billion in January 2016

Holdings of domestic government bonds (%), 2010 – Jan 2016



Source: Share Transaction Totally Electronic LTD(Strate)

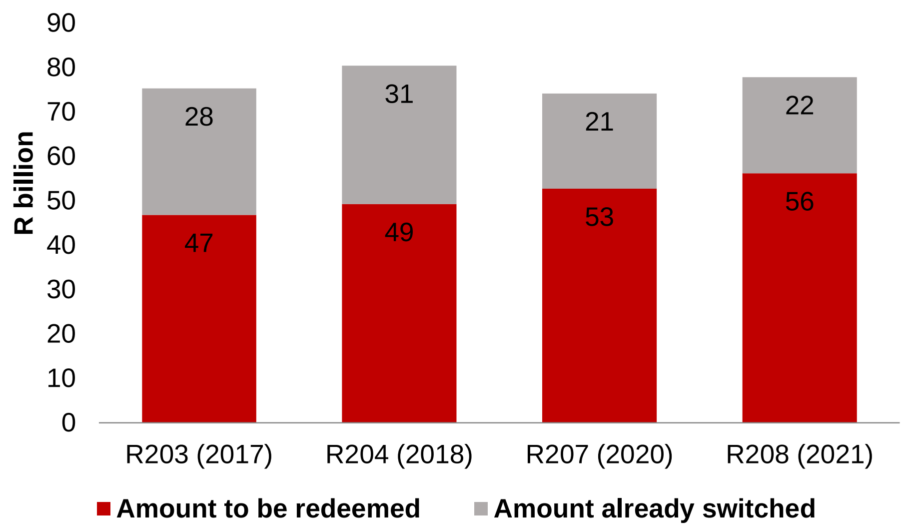
Non-residents domestic government bond holdings, 2010 – Jan 2016



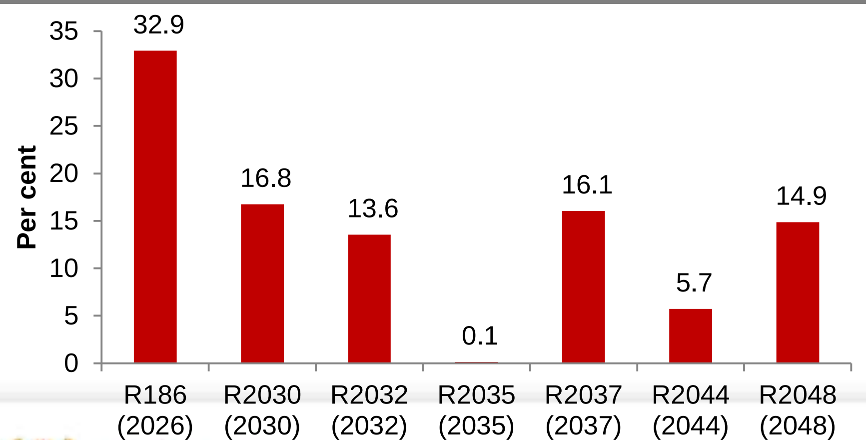
Source: Share Transaction Totally Electronic LTD(Strate)

Switch programme well received by the market

Switch auction statistics



Per cent allocation by destination bond



Source: National Treasury)

- Cash neutral basis and an all-in-price pricing method
- Bids to be submitted on a yield basis
- Be conducted at the predetermined yield for both source and destination bonds
- Conducted on an ad-hoc basis with no calendar published
- Total of R103 billion switched to date since implementation of new switch module
- Switch programme will continue in 2016/17 should market permit

5. SOCs borrowing requirement and guarantees

State-owned companies reforms in the pipeline

- An inter-ministerial committee chaired by the deputy president is overseeing implementation of reforms intended to strengthen ability of public-sector institutions to support National Development Plan outcomes

Area of reform	Description	Progress
Stabilisation	Aims to improve near-term financial and operational performance	A framework to quantify the cost of developmental activities has been developed
Coordination and collaboration	Maximization of contribution to the economy and elimination of duplication	Joint infrastructure projects are taking place in the energy, transport, mining and water sectors
Rationalisation and consolidation	Reduction of state participation in sectors where several entities operate with overlapping mandates	Currently underway with the rationalization of Broadband Infraco
Governance framework	Enactment of overarching legislation, informed by a review of the current shareholder management model	Board appointment processes will be standardized, and remuneration frameworks reviewed to ensure that compensation growth is contained and linked to efficient performance

Eskom accounts for the largest chunk of borrowing by state-owned companies (SOCs)

Borrowing Requirements , 2014/15 – 2018/19

	2014/15		2015/16	2016/17	2017/18	2018/19
R billion	**Budget**	**Outcome**	**Revised**	**Medium-term estimates**		
Domestic loans (gross)	**45.1**	**64.3**	**65.5**	**51.4**	**64.3**	**62.5**
Short-term	24.3	24.4	13.8	12.1	16.0	18.2
Long-term	20.8	39.9	51.7	39.3	48.3	44.3
Foreign loans (gross)	**38.9**	**27.2**	**42.6**	**27.8**	**32.1**	**19.3**
Long-term	38.9	27.2	42.6	27.8	32.1	19.3
Total	**84.0**	**91.5**	**108.1**	**79.2**	**96.4**	**81.8**
Percentage of total:						
Domestic loans	*53.7%*	*70.3%*	*60.6%*	*64.9%*	*66.7%*	*76.4%*
Foreign loans	*46.3%*	*29.7%*	*39.4%*	*35.1%*	*33.3%*	*23.6%*

Source: National Treasury

- The six largest state-owned companies borrowed R91 billion in 2014/15
- Eskom was the largest borrower, accounting for 71 per cent of the total funding raised by SOCs
- The depreciation of the rand against major currencies is expected to limit borrowing in foreign capital markets

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Borrowing by Development Finance Institutions lower than anticipated

Borrowing Requirements , 2014/15 – 2018/19

R billion	2014/15 Budget	2014/15 Outcome	2015/16 Revised	2016/17	2017/18	2018/19
				Medium-term estimates		
Domestic loans (gross)	**63.0**	**45.2**	**65.1**	**64.5**	**80.7**	**86.6**
Short-term	52.3	37.1	50.5	51.8	62.3	63.1
Long-term	10.7	8.1	14.6	12.7	18.4	23.5
Foreign loans (gross)	**7.4**	**6.8**	**11.1**	**18.9**	**11.2**	**12.9**
Long-term	7.4	6.8	11.1	18.9	11.2	12.9
Total	**70.4**	**52.0**	**76.2**	**83.4**	**91.9**	**99.5**
Percentage of total:						
Domestic loans	*89.5%*	*86.9%*	*85.4%*	*77.3%*	*87.8%*	*87.0%*
Foreign loans	*10.5%*	*13.1%*	*14.6%*	*22.7%*	*12.2%*	*13.0%*

Source: National Treasury

- In 2014/15, the combined borrowing of the three major development finance institutions reached R52 billion against a budgeted estimate of R70 billion
- The IDC, however, plans to raise 81 per cent of its borrowing from foreign sources in 2016/17 – a proportion that decreases to 44 per cent in 2018/19
- Borrowing in the development finance portfolio is dominated by the Land Bank, which raises mainly short-term debt

Guarantee exposure of government

Guarantee exposure to major SOCs, IPPs and PPPs, 2013/14 – 2015/16

R billion	2013/14		2014/15		2015/16	
Institution	Guarantee	Exposure	Guarantee	Exposure	Guarantee	Exposure
Total	469.4	209.6	485.1	225.9	469.5	244.6
Of which:						
Eskom	350	125.1	350	149.9	350	168.5
SANRAL	38.9	23.9	38.9	32.4	38.9	35
Denel	1.9	1.9	1.9	1.9	1.9	1.9
Development Bank of Southern Africa	29.6	25.7	12.9	4.1	14	4.5
Industrial Development Corporation	2.1	0.5	1.6	0.3	2.1	0.3
Trans-Caledon Tunnel Authority	25.7	20.5	25.6	20.8	25.6	20.6
South African Airways	7.9	5	14.4	8.4	14.4	14.4
Transnet	3.5	3.8	3.5	3.8	3.5	3.8
Land and Agricultural Bank of South Africa	3.5	1.1	6.6	2.1	6.6	5.3
South African Post Office	0	0	1.9	0.3	4.4	1.3
South African Express Airways	0.5	0.5	1.1	0.5	1.1	1.1
Independent power producers	0	0	0	0	200.2	200.2
Public-private partnerships	10.1	10.1	10.1	10.1	8.9	8.9

Source: National Treasury

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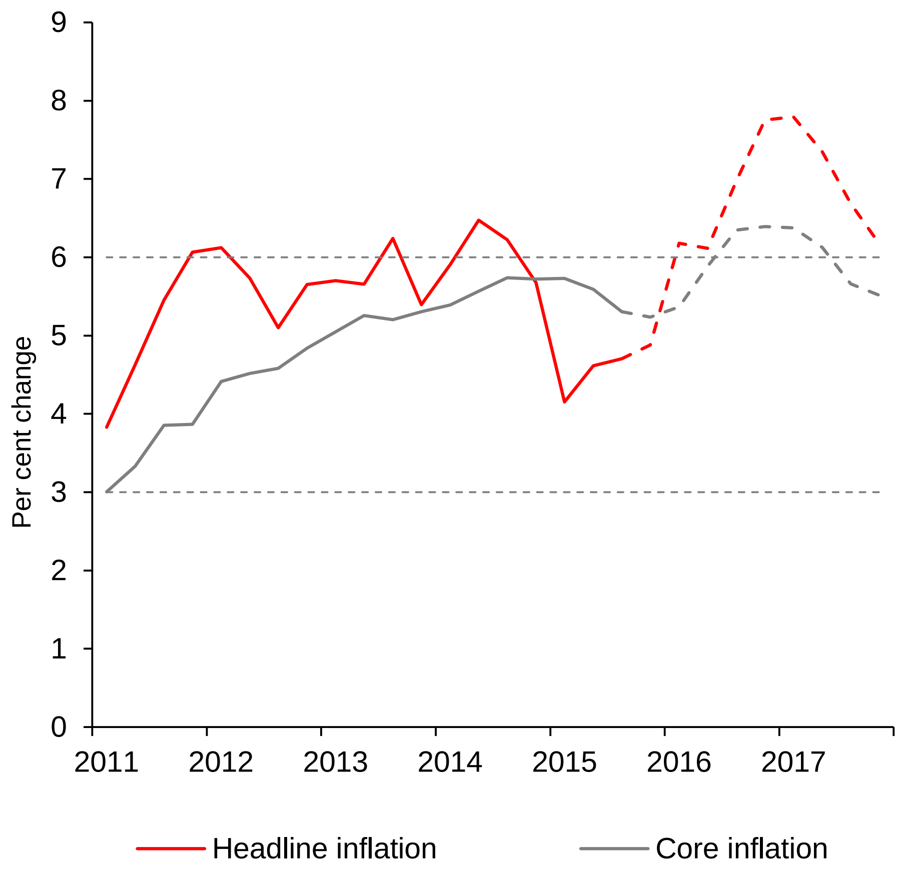
6. Monetary Policy

Inflation profile expected to breach upper limit of target

Targeted and core inflation

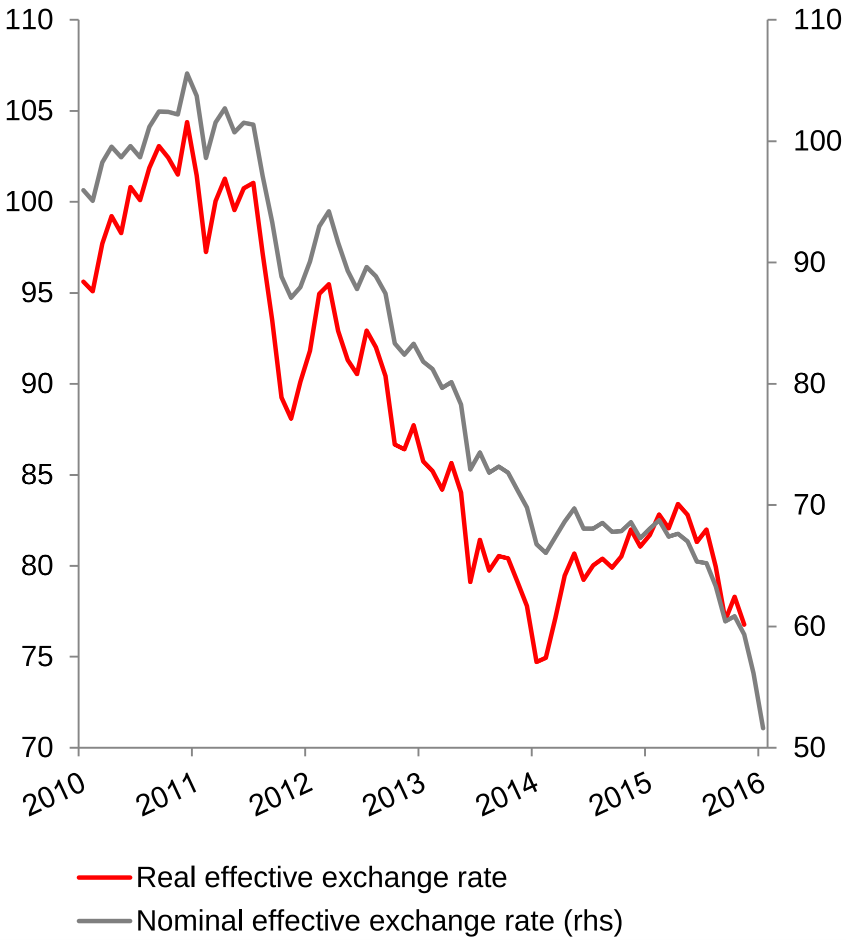


Source: Stats SA, Own calculations

- Inflation averaged 4.6 per cent for 2015. It fell to 3.9 per cent in February 2015, before increasing to 6.2 per cent in January 2016
- Low food and transport price inflation contributed to the 2015 inflation moderation
- Core inflation has been high but quite stable at between 5.1 per cent and 5.8 per cent during 2015
- Potential output has been revised down from 1.9 per cent to 1.5 per cent for 2016, and from 2.1 per cent to 1.6 per cent for 2017
- Inflation is expected to average 6.8 per cent in 2016 and 7.0 percent in 2017

ZAR exchange rate largely influenced by external factors

Effective exchange rate movement

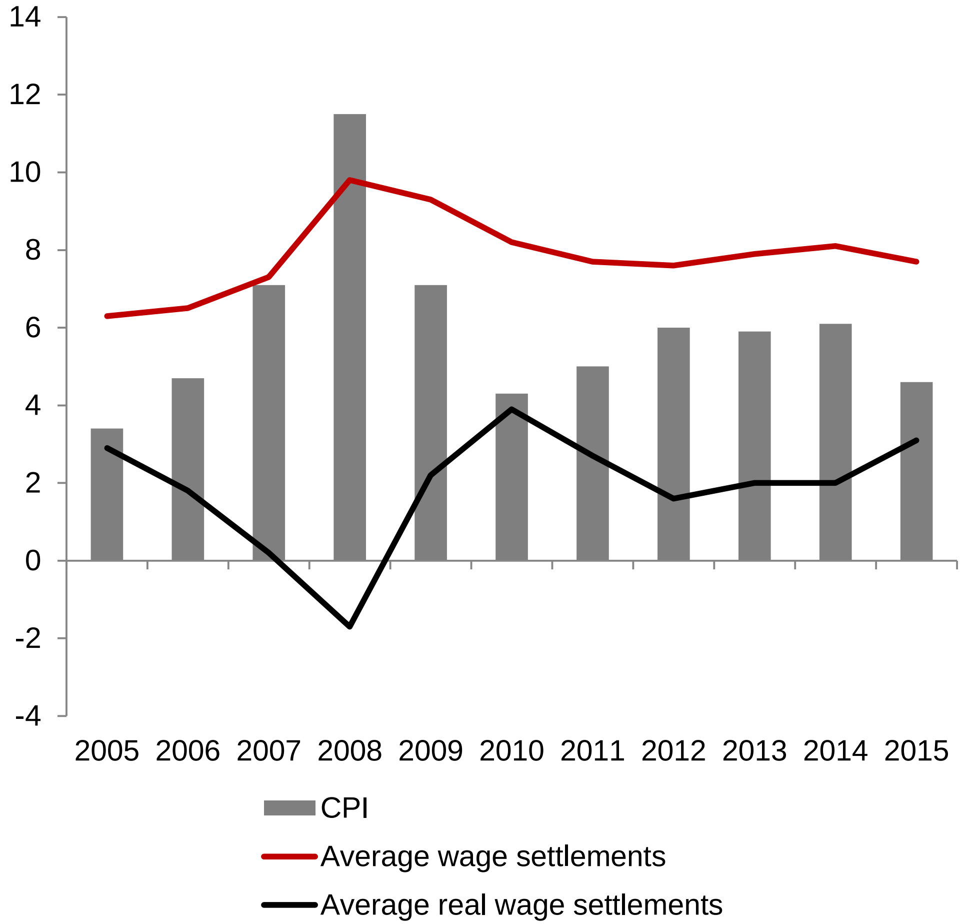


Source: Stats SA, SARB

- The exchange rate of the rand depreciated markedly since the November 2015 MPC meeting
- The slowing Chinese economy, uncertainty about the timing and pace of future US rate hikes, Euro area and Japanese QE have contributed to volatility of the rand
- Domestic factors such as the deterioration in economic prospects have also contributed to rand weakness
- The rand is expected to remain sensitive to investor sentiment, global policy and domestic economic prospects

Wage settlements and inflation expectations

Unit labour costs



Source: Stats SA, SARB, BER

- Average wage settlements contribute to the persistence of inflation at above target levels
- Inflation expectations show a marginal increase for 2016, but have deteriorated from 5.9 per cent to 6.2 per cent in 2017
- There are differences across respondent categories
- This survey was conducted before the most recent bout of rand depreciation, so the next survey may show a deterioration in inflation expectations

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