CareEdge Global assigns Long Term Foreign Currency Rating of BB (Unsolicited) to the Republic of South Africa

Credit Profile
South Africa's credit profile primarily reflects its weak economic structure as well fiscal profile. These challenges, however, are offset by the country's comfortable external position and a good track record of monetary policy management.

The government's key priorities are to implement reforms in key economic sectors, such as logistics and power, and to achieve fiscal consolidation, which may both be challenging and time-consuming. CareEdge will observe for progress in these focus areas.

Strengths
- Adequate external profile supported by stable foreign direct investment (FDI) and a positive net international investment position (NIIP)
- Strong regulatory environment with supportive institutions
- Highly developed financial sector

Weaknesses
- Low economic growth rates primarily on account of structural constraints
- Weak fiscal profile on account of low revenue base, lack of flexibility on the expenditure side
- Inefficient state-owned enterprise (SOE) management

Key Monitorables
- Commitment to implementation of structural reforms to improve growth potential
- Progress on enhancing efficiencies of SOEs
- Potential impact of contingent liabilities on government finances
- Timelines for exiting Financial Action Task Force (FATF) grey list

Key Rating Drivers

Economic Structure & Resilience
The economy is constrained by a rigid labour market, large income inequality, electricity shortages and high logistics costs. As a result, the growth is low, significantly below potential and expected to be around 1.3% of GDP over the next 3-4 years. Reforms are currently underway with the associated state-owned enterprises (SOEs)- Eskom for power generation, distribution and transmission, and Transnet for logistics. Meaningful progress towards efficiency can enable the economy to aspire for better growth prospects over the medium-term horizon. These challenges are balanced by a well-diversified economy with the presence of a competitive financial services sector and a sizeable mining industry.

Fiscal Strength

Government finances face multiple challenges, including a low revenue base and a lack of flexibility on the expenditure side. These are partly a reflection of the weak economic structure, coupled with an expanding wage bill (35% of total expenditure in 2023) and high interest-to-revenue ratio (15% in 2023). General government debt-to-GDP is high at 74% in 2023 and is projected to increase over the medium term, reaching 78% by 2025. Borrowing requirements are projected to increase from 5% of GDP in FY22/23 to around 8.1% in FY23/24, reflective of the ZAR 253 billion debt (4% of GDP) bailout of Eskom, upcoming redemptions and financing of the fiscal deficit.

The government plans to draw down 25% of the profit from the South African Reserve Banks (SARB) gold and foreign exchange contingency reserve account (USD 28 billion in 2024) to reduce borrowing needs over the next three years. This approach will help repay debt and improve public finance management. Contingent liabilities of SOEs, are currently estimated at around 10% of GDP (FY23/24). The government notes that the financial health of several SOEs have deteriorated and will continue to pose a risk to the fiscal outlook.

External Position & Linkages

The current account deficit-to-GDP (CAD) widened to around 1.6% for 2023, from 0.5% in 2022, due to an easing of commodity prices, weakening terms of trade, and lower exports due to logistics constraints. Nonetheless, in 2024, the trade balance has been in surplus territory, which could be sustained, as steadier electricity supply and improved logistics could boost exports. In addition, the world economy is expected to fare better as easing monetary policy globally lifts demand, and China's stimulus and interventions start to translate into firmer activity. Import volumes may also remain subdued for longer based on subdued domestic demand.

The CAD is mostly funded through stable net FDIs, and partly by portfolio inflows. While a reliance on portfolio inflows could expose the country to vulnerabilities, South Africa has a good net international investment position (NIIP) of around 29% of GDP (2023). The recent entry on the Financial Action Task Force's (FATF's) grey list (February 2024), due to weakness in policies relating to anti-money laundering and financial terrorism, could impact financial inflows. However, due to the National Treasury's ongoing exercise to strengthen the financial system, the country is expected to exit this list by 2025, which will mitigate this risk.

Monetary & Financial Stability

South Africa adheres to a floating exchange rate; however, the South African Reserve Bank (SARB) may intervene in the foreign exchange market to smooth out volatility of the exchange rate. The SARB shows strong adherence to its inflation and financial stability mandate, with an inflation target band of between 3-6%. Inflation eased to 5.9% in 2023 from 6.9% in 2022 and is expected to decline to 4.9% and 4.5% in 2024 and 2025 (the mid-point of the SARBs target band) respectively.

The banking sector health is comfortable with manageable non-performing loans of around 5% (2023) of total loans, assets of more than 100% of GDP, and good capital levels. The five largest banks in the country hold over 90% of total assets.

South Africa's financial sector is also highly developed within the African region. Large institutional investors (pension funds, insurers and mutual funds) have assets of more than 200% of GDP.

Institutions & Quality of Governance

The country has robust institutions such as the National Treasury and the SARB. However, systemic corruption, particularly within SOEs have weakened overall governance. The country has also seen sporadic protests due to socioeconomic discontent, which have the potential to threaten social stability.

For the first time since its democracy, a coalition government, the Government of National Unity (GNU) was elected in May 2024. The GNU highlights a nine-point agenda, with an aim to prioritise structural reforms, and address basic infrastructure, service delivery shortfalls and weak investments. The agenda indicates that South Africa remains on course to achieve the desired policy outcomes under the previous administration, which broadly favour both the economic and fiscal outlook. However, a key risk will be navigating coalition politics.

South Africa – Select Indicators									
	Unit	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024 F**	**2025 F**
Economic Indicators									
Nominal GDP	USD Billion	405.1	389.2	338.2	420.0	405.1	377.7	373.2	384.8
GDP Per Capita (Constant-PPP)	USD	13,850	13,689	12,690	13,171	13,321	13,200	13,116	13,075
Real GDP Growth	%	1.6	0.3	-6.0	4.7	1.9	0.6	0.9	1.2
GFCF/ GDP	%	15.9	15.5	13.8	13.2	14.2	15.2	-	-
Gross Domestic Savings/ GDP	%	16.7	16.3	16.9	18.8	17.3	15.6	-	-
Exports (G&S)/GDP	%	27.5	27.2	27.5	31.1	33.5	33.0	-	-
Working-Age (15-64) Population (% Share in Total)	%	65.5	65.3	65.3	65.4	65.6	65.8	66.1	66.3
Old-Age (65+) Population (% Share in Total)	%	5.9	6.0	6.0	6.0	5.9	5.9	5.9	6.0
Fiscal Indicators – General Government									
Fiscal Balance/ GDP	%	-3.7	-4.7	-9.6	-5.5	-4.3	-6.0	-6.1	-6.3
Revenue/ GDP	%	26.4	26.7	25.0	27.1	27.7	27.0	27.1	27.1
Expenditure/ GDP	%	30.2	31.4	34.6	32.6	32.0	32.9	33.2	33.5
GG Gross Debt/ GDP	%	51.5	56.1	68.9	68.8	71.1	73.9	75.4	77.9
GG External Debt (by Creditor)/ GG Gross Debt	%	29.6	29.8	26.4	25.5	24.4	23.8	-	-
Interest/ Revenue	%	11.1	11.6	13.5	13.0	13.5	15.0	-	-
External Indicators									
Current Account Balance/ GDP	%	-2.9	-2.6	1.9	3.7	-0.5	-1.6	-1.8	-1.9
FDI, Net Inflows/ GDP	%	1.4	1.3	0.9	9.7	2.3	1.4	-	-
Outstanding FII Liabilities/ GDP	%	57.6	63.9	67.1	49.6	48.3	47.4	-	-
NIIP/ GDP	%	11.1	8.0	33.2	24.4	18.9	29.0	-	-
Foreign Exchange Reserves	USD Billion	51.6	55.1	55.5	58.1	61.0	60.2	58.6	57.6
Import Cover	Months	4.7	5.1	7.2	5.4	4.4	5.3	-	-
External Debt/GDP	%	42.6	47.6	50.4	38.2	40.6	41.9	-	-
Monetary and Financial Indicators									
CPI Inflation	%	4.6	4.1	3.3	4.6	6.9	5.9	4.9	4.5
Exchange Rate (Average)	LC per USD	13.3	14.5	16.4	14.8	16.4	18.5	-	-
Non-Performing Loans/ Total Gross Loans	%	3.7	3.9	5.2	4.5	4.5	5.4	-	-
Private debt, loans and debt securities/ GDP	%	72.2	72.6	73.3	66.2	67.2	-	-	-

Sources: International Monetary Fund, World Bank, Bank for International Settlements, National Sources, CareEdge Global

Note: F - Forecast; PPP – Purchasing Power Parity; GFCF – Gross Fixed Capital Formation; Exports (G&S) – Exports of Goods and Services; GG – General Government; FDI – Foreign Direct Investment; FII – Foreign Institutional Investment; NIIP – Net International Investment Position; Data refers to fiscal/calendar year and actual/estimate as reported by the source; Where general government data is unavailable, central government data is used; Latest available data for 2023

Rating History

Instrument	Type	Rating	Date
Issuer Rating	Long Term Foreign Currency (Unsolicited)	BB	October 3, 2024

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Criteria Applied

CareEdge Sovereign Rating Methodology

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