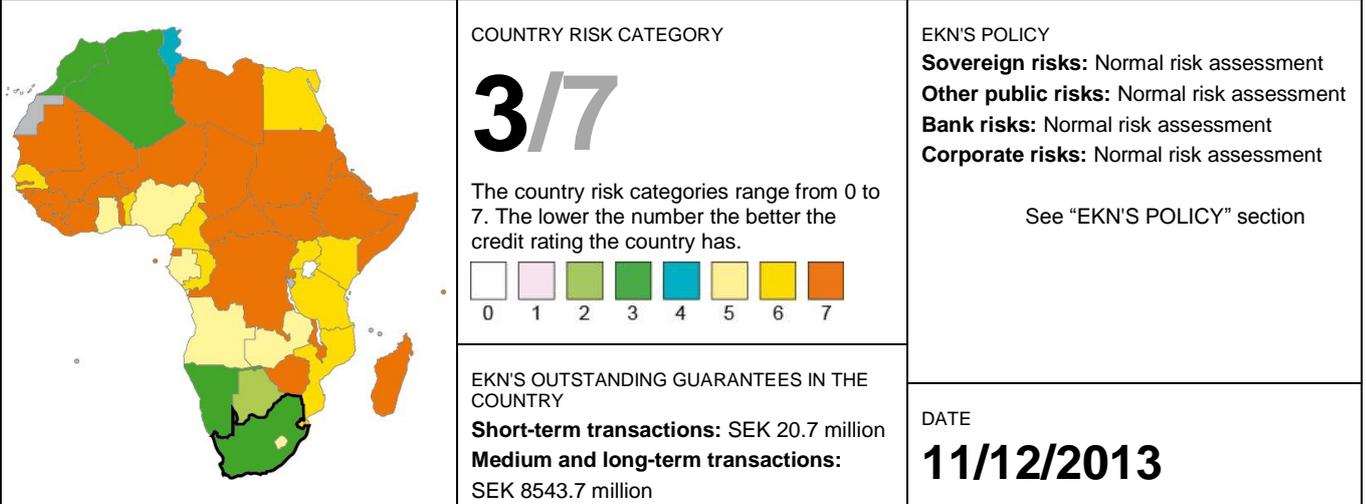


# South Africa



## Structural weaknesses slowing growth

South Africa's structural problems are preventing growth from reaching the level needed to improve living conditions for the population at large. Frustration is growing among the population and the need for political and economic reforms are becoming increasingly urgent. Unless the ANC manages to meet this challenge in the coming term, there is a risk that support for the party will erode over time. The country's public finances have been weakened by the financial crisis, but the government's economic policy is expected to continue to be responsible. A sound banking sector and a predictable business environment are further strengths which balance the somewhat subdued long-term forecast for the South African economy.

### STRENGTHS

- Stable and transparent institutions
- Responsible economic management
- Sound and well-regulated bank sector

### WEAKNESSES

- Deep structural problems of poverty, unemployment and inequality
- Social unrest and frustration among the population over the government's passivity when it comes to dealing with the structural problems
- Dependent on portfolio investment to finance the current account deficit

## POLITICS

**Political continuity to be expected**

Ever since the first democratic elections in 1994 the ANC has dominated the political arena. However, corruption scandals and frustration over the lack of decisiveness when it comes to dealing with South Africa's deep socio-economic problems have led to both a decreased turnout at elections and diminished support for the ANC. It has also provided space for a populist agenda in politics. Last summer, for example, the EFF (Economic Freedom Fighters) was founded led by the controversial Julius Malema. Malema was previously the leader of the ANC Youth League before he was thrown out of the party as he openly opposed President Zuma. EFF is aimed primarily at first-time voters. With a youth unemployment rate of 50 per cent, it is possible that they will be attracted by the EFF rhetoric. The majority of the first-time voters were born after 1994 and do not sympathize as strongly with the ANC as they have not experienced the role of the ANC in the freedom struggle.

Although both the EFF and other opposition parties are gaining ground, there is still solid support for the ANC and all indications are that they will win the next election. In light of South Africa's dependence on international capital to finance its current account deficit, it is also likely that the ANC will persist with its market-friendly policies. Political stability and continuity is therefore to be expected in the medium term.

## ECONOMY

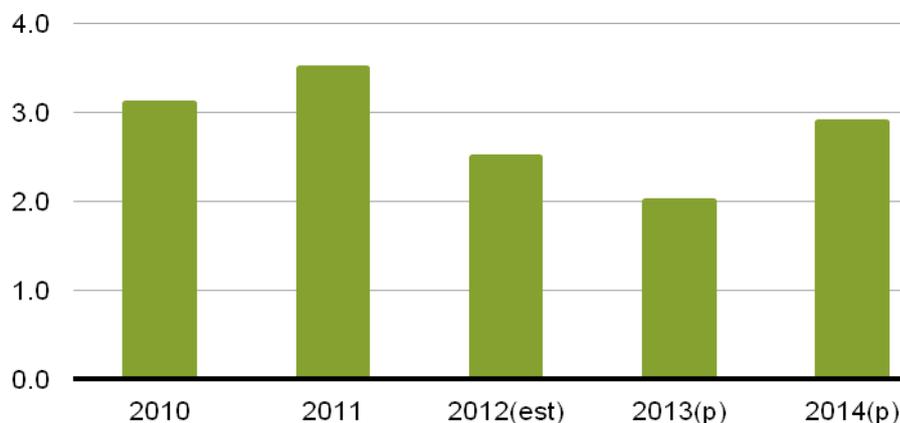
**Sound economic policies, but pressing need for reform**

South Africa maintains sound and market-oriented economic policies aimed at balance in its public finances. Several years of good economic growth have led to a significant increase in revenues and has turned South Africa into a middle-income country with a diversified economy. The economic base consists of mineral resources, but South Africa also has growing industrial and service sectors, as well as a significant financial sector.

During the financial crisis, South Africa has been able to counteract the negative effects of lower demand abroad by adopting an expansionary fiscal policy. However, this has led to a weakening of public finances which are expected to show a deficit of just over four per cent in the coming year. After the election year of 2014, the deficit is expected to decline. A rapid development of the wages of public employees, combined with a strong need for public investment, however, remains a fiscal challenge.

The South African economy is growing at about two per cent per year, which is well below its potential of 4-5 per cent. Reduced demand from the country's major trading partners, the EU and China, is a contributing factor. However, the main explanation for the weak growth is domestically generated structural problems, many of which emanate from the apartheid system. The education system is substandard and labour laws are rigid. Lack of productive employment is generating social unrest, not least demonstrated by violent strikes in the country's critical mining sector. In addition, there is a need for investment in infrastructure, particularly in transport and energy.

## GDP GROWTH, %



*Growth is expected to strengthen in 2014, but still remain below the country's potential (IMF)*

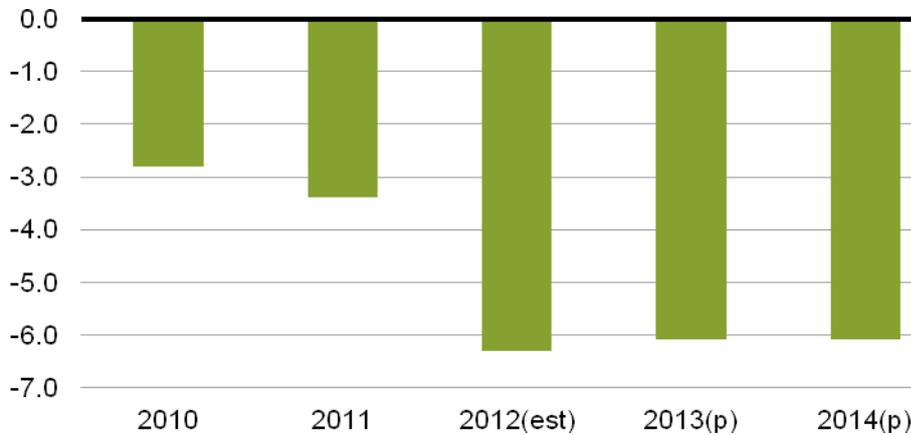
The government's main challenge therefore is to push the reform agenda forward. Some initiatives have been taken, others have been put on hold due to the elections next year. In order to realise the country's growth potential and manage its structural problems, a continued inflow of foreign investment is required that will contribute to economic policy remaining prudent. Overall, there is still a good foundation to build on with a diversified economy. However, the need for reforms is becoming increasingly acute, while the financial scope to implement them is shrinking. Therefore, the long term prognosis for the country's growth is more uncertain than before.

## BALANCE OF PAYMENTS AND DEBT ISSUES

**Low indebtedness**

South Africa's external balance is assessed overall as good. The current account deficit widened in 2012 due to weaker demand in the country's export markets, but the troubles in the mining sector are also expected to have affected exports negatively. A marginal improvement can be expected. However, South Africa has problems of low productivity, which means that exports over time are becoming more expensive relative to competing countries and export growth will be lower than in other emerging markets.

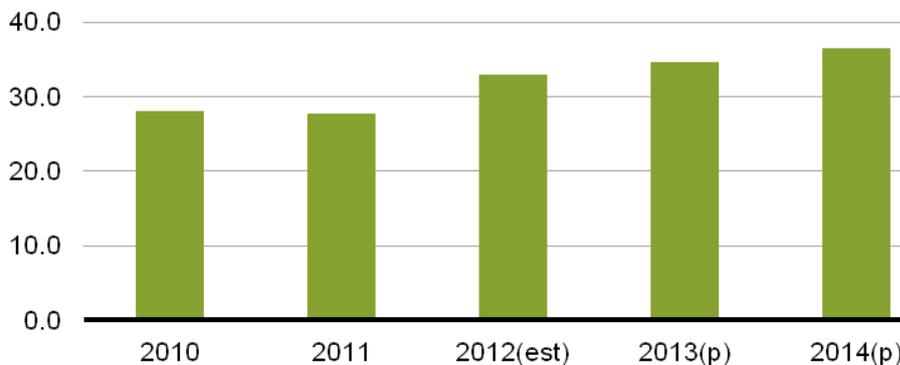
## CURRENT ACCOUNT BALANCE, % OF GDP



*The slowdown in demand from South Africa's export markets has affected the current account negatively (IMF)*

The financing of the current account deficit is a risk as it is largely made up of portfolio investment, which is more volatile than direct investment. South Africa is no longer a net lender in the capital market, after having been one for most of the 2000s. However, the moderate external debt is a strength and net debt amounts to about only six per cent of GDP. The government borrows on the domestic market and external debt is therefore expected to remain at a moderate level of around 35 per cent of GDP.

## EXTERNAL DEBT, % OF GDP



*The external debt is moderate but gradually increasing (IMF)*

## CURRENCY POLICY

**Continued volatility is to be expected**

The South African Rand has a floating rate and is sensitive to swings in the risk appetite of investors. A continued slowdown in the development of the world economy, combined with a return to a more normal US monetary policy may lead to an outflow of portfolio investments, which will put pressure on the currency. At the same time there are forces acting in the opposite direction thanks to investment in South Africa being seen as relatively attractive from a global perspective. It is therefore reason to believe that the Rand will continue to fluctuate as it had done previously.

Some currency restrictions still exist in order to protect the country against sudden capital outflows, but a liberalisation is in progress. Foreign exchange reserves are equivalent to just under four months of import cover, which is regarded as an acceptable level for South Africa, which has a relatively broad economic base. The South African currency has a high degree of convertibility and can be assessed by EKN in local currency financing transactions.

## FINANCIAL SECTOR

### **Strong banking system**

Four private banks account for almost 90 per cent of the banking sector (Standard Bank, ABSA, First Rand Bank and Nedbank). Thanks to effective banking supervision, a low dependence on external financing and a conservative approach to risk, the banking sector has only been affected to a limited extent by the financial crisis. Overall, banks are well capitalised and profitable with a low proportion of non-performing loans at about five per cent. However, as a way of increasing the proportion of the population that has access to banking services, lending to private households has risen sharply in recent years. Much of this lending has no collateral which means a risk of an increased proportion of bad loans and lower capitalisation.

## BUSINESS ENVIRONMENT

### **The region's commercial hub**

South Africa's business environment is good and the country is the region's commercial centre and the base for many international companies operating in the region. The World Bank's Doing Business Index ranks the business environment as the third best in Africa after Mauritius and Rwanda. A major contributing factor is the country's well-functioning institutions. However, the country has continuously fallen in the DBI from 32nd place in 2009 to this year's 41th place. The explanation is increased red tape when it comes to starting a business and registering a property. Additional challenges cited by companies in the region include the difficulty of recruiting skilled labour locally and the changeable nature of public regulations.

The availability of financial information is good. The South African accounting standard (SA GAAP) is equivalent to IFRS. All listed companies are required to prepare financial statements in accordance with SA GAAP as well as half-yearly accounts. SME companies must report according to IFRS SME but are not required to publish financial information.

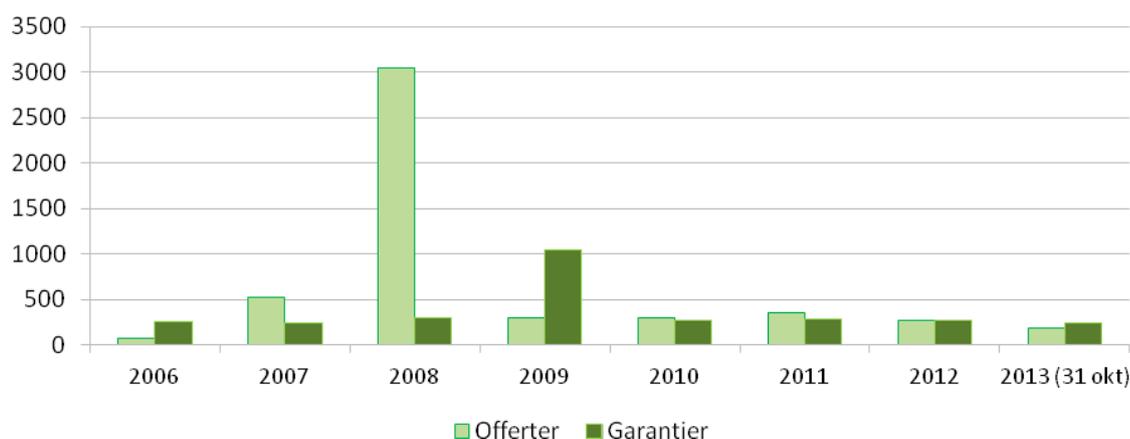
The judicial system in the country is independent, although increased political interference has been noted recently. A lack of skilled staff is causing protracted processes. In comparison with other African countries corruption is low, although it occurs in certain public institutions. However, the South African Auditor General, as well as the press and the civil society, are doing a respectable job in reporting cases of corruption within the state apparatus.

## EKN'S EXPOSURE

## JAS Gripen still dominating

EKN's outstanding guarantees were almost SEK 8.7 billion and consist almost entirely of a guarantee for the export of JAS Gripen. Other guarantees amount to over SEK 300 million and consist primarily of guarantees in the mining and transport sectors. In 2013, EKN issued 66 new guarantees equivalent to a guarantee amount of SEK 196 million. EKN sees an increase in the number of guaranteed transactions, which can be explained by the fact that South Africa serves as the region's hub where goods are re-exported to neighbouring countries in Southern Africa.

### EKN'S EXPOSURE AT DECEMBER 31 EXCLUDING JAS GRIPEN, SEK MILLION



*EKN is seeing an increase in the number of transactions, but in terms of volume, this exposure has been stable in recent years (EKN)*

## PAYMENT EXPERIENCE

## Increased difficulties in recovering claims

EKN's experience in guaranteeing transactions in South Africa is good. During the financial crisis, there were some arrears in transactions with counterparties in the mining sector. In a couple of transactions, the export company repossessed the equipment and sold it before any claim adjustment, a procedure that worked well. Claims currently total SEK 1.7 million and are divided on a handful of debtors. Most of the claims refer to problems arising as a result of the financial crisis.

EKN's experience is that increasing politicisation and on-going changes within the judicial system in the country are having a negative effect when it comes to recovering claims, and past experience also shows that recovery processes have been beset with bureaucratic difficulties. EKN's impression is that corruption is more prevalent among lower officials and in rural areas. The overall experience of claims and recovery processes in the country is therefore not univocal, but the overall impression is that it still working satisfactorily.

## EKN'S POLICY

**One of the region's best country risk categories**

Like the rest of the OECD, EKN places South Africa in country risk category 3 for both short term and long term guarantees. Next to Botswana, it is the best classification in sub-Saharan Africa. For all buyer categories, transactions are assessed on their own merits without any special restrictions or conditions.

## OFFICIAL COUNTRY DATA AND CREDIT RATINGS

OFFICIAL COUNTRY DATA	CREDIT RATING		
<b>Area:</b> 1,221,000 km <sup>2</sup> (2.7 times Sweden)		COUNTRY CEILING	SOVEREIGN RISK
<b>Population:</b> 48.6 million inhabitants (2013e)	<b>Moody's:</b>	A2	Baa1/Neg
<b>Population growth:</b> 1.7% / year (2013e)	<b>S&amp;P:</b>	A-	BBB/Stable
<b>GDP:</b> USD 402 billion in 2011 (Sweden USD 536 billion in 2011)	<b>Fitch:</b>	A-	BBB/Stable
<b>GDP/capita:</b> USD 7,972 per capita 2011 (Sweden USD 56,523 in 2011)			

## COUNTRY ANALYST



EKN's country analyst for South Africa:

Rebecka Lundgren

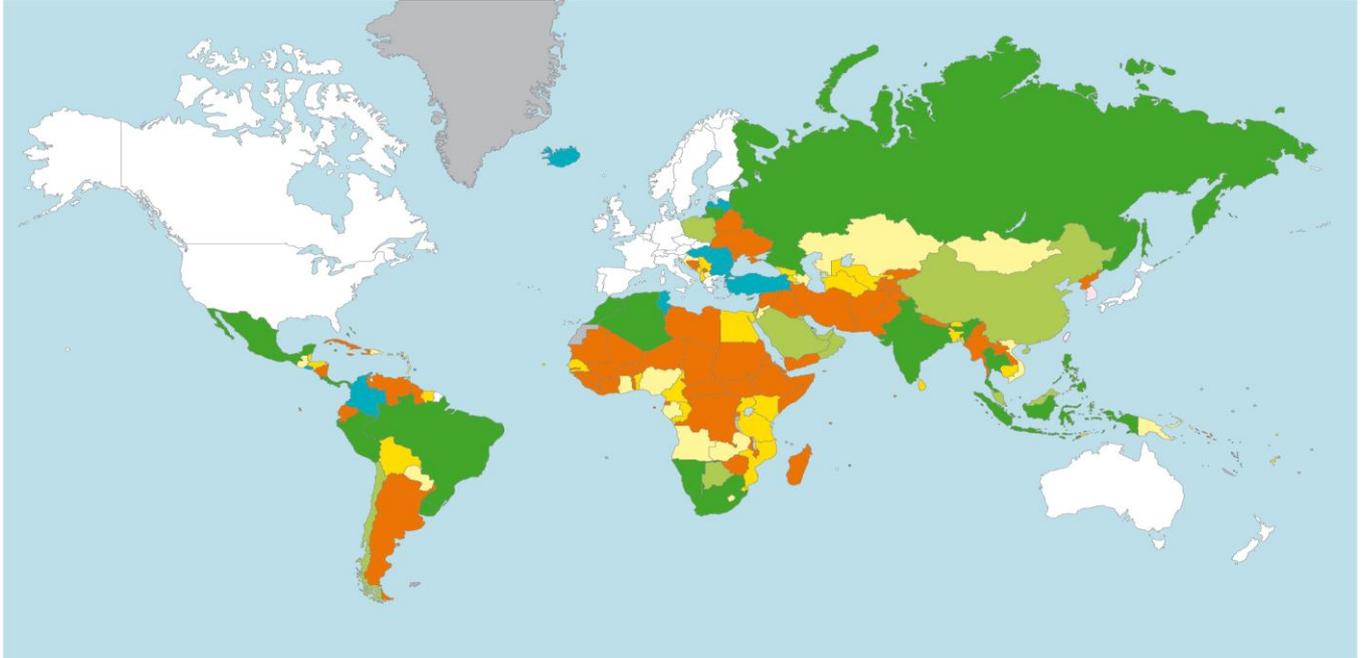
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**DISCLAIMER**

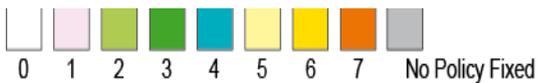
The country analysis is based on a range of sources and reflects information that is relevant to EKN at the time of publication. The responsibility for how the information is used or interpreted rests solely with the user, and EKN cannot be held responsible for any loss or damages.

## EKN'S VIEW OF THE WORLD



The country risk categories range from 0 to 7.

The lower the number the better the credit rating the country has.

**EKN – CREATING CONFIDENCE IN YOUR EXPORTS**

EKN is a government agency that supports Swedish exports and the internationalisation of Swedish industry. This we do by offering exporting companies and banks guarantees for payment and financing, together with advice on business structure and risk management. Our services provide an extra level of confidence, increased competitiveness and more opportunities for successful export transactions.

The Swedish Export Credits Guarantee Board

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