



Economic Review and Outlook

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Outlook



Introduction: the downward trend in SA's growth since ...

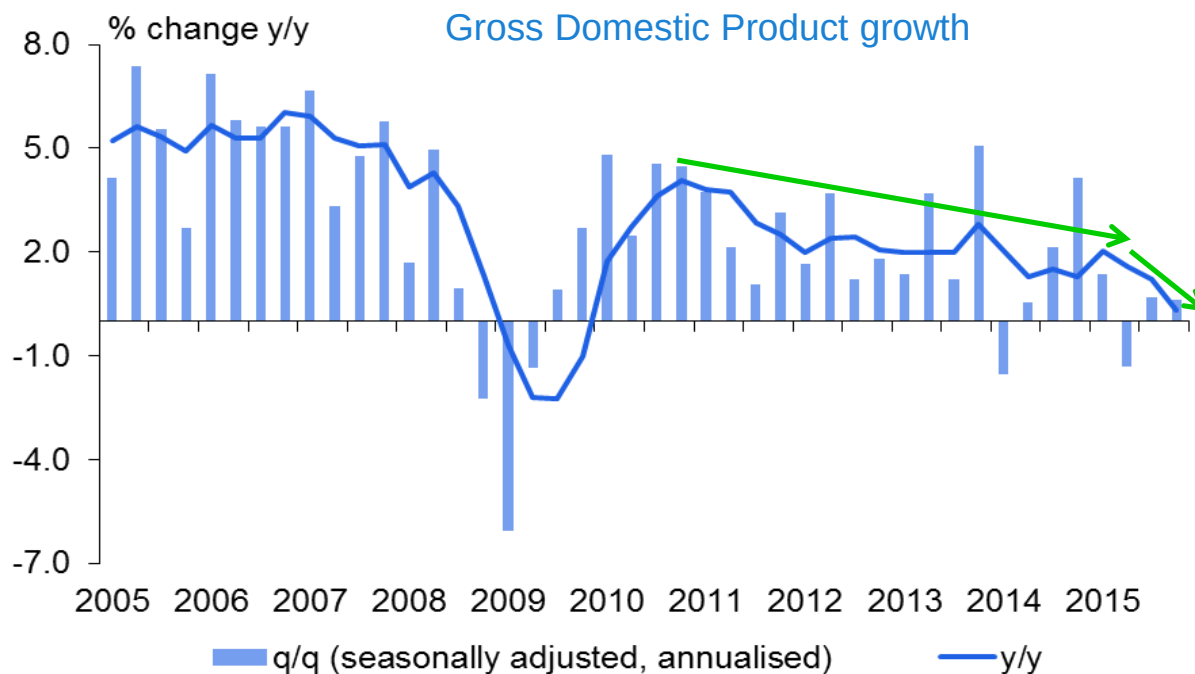


- The slump in the commodity cycle has intensified in Q1.16, along with the weak performance of key trading partners (notably China), while domestically the most severe drought in twenty five years is occurring, causing SA to face another difficult year of low economic growth.
- Cyclical issues aside however, South Africa remains institutionally sound, with solid ratings from the World Economic Forum's Global Competitiveness Survey, as the strength of its auditing and reporting standards are ranked first, and the regulation of its securities exchange (JSE) second in the world.
- The soundness of SA's banking sector is ranked eighth, with deep, liquid sophisticated markets and consistent, sound budgetary policies that allow South Africa to be a key contributor to the global bond market. SA sovereign credit ratings are still investment grade.
- The International Budget Partnership's latest Open Budget Index ranks SA third among 88 countries, after only New Zealand and Sweden. However, from 2011 SA has seen credit rating downgrades on the deterioration in its economic growth, and some fiscal slippage as the ratios also deteriorated, although very recently a more conservative Budget was seen under the new Finance Minister.

Expected case forecasts, real % growth y/y Investec	2015	2016	2017	2018	2019	2020
GDP (%)	1.3	0.7	1.4	1.5	2.2	2.5

... 2011, has accelerated recently ...

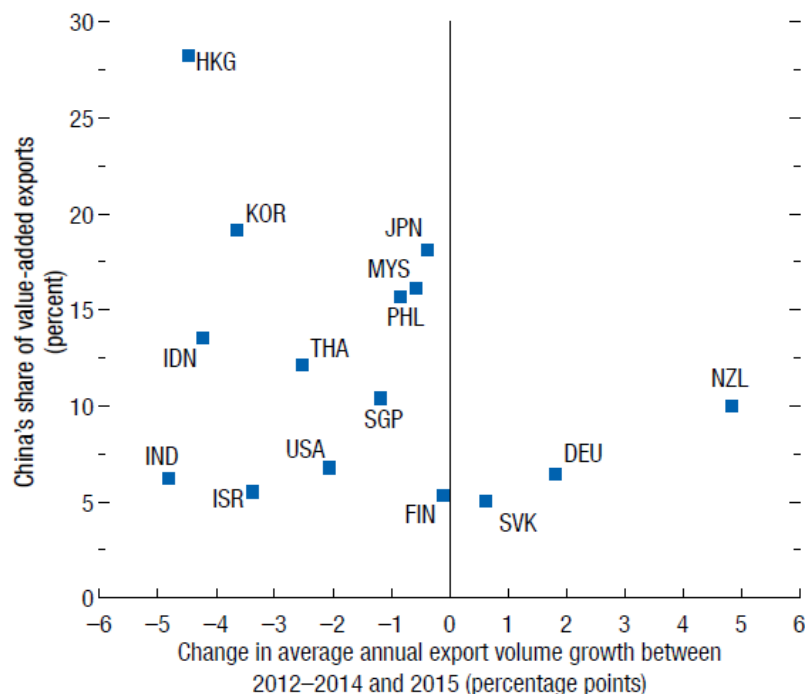
- The unsupportive global environment for a commodity exporter risks the South African economy stalling this year, if not entering a technical recession, along with the global economic slowdown. The major rating agencies are currently assessing SA's growth outlook.
- Structural improvements would see the SADC economic giant reap faster growth, and so an improved ability to reduce unemployment and inequality, and eliminate poverty.
- The advent of 2016 has heralded a closer working relationship between government and business, which if successful, would allow sustained faster growth and so a more rapid progression of upward social mobility, as occurred in earlier years of SA's democracy.



...as the slowdown in global trade growth, led by China, ...

- The global slowdown has had a major impact on SA as countries more exposed to China have seen a greater contraction in the value of their exports (IMF).
- China's imports of services are rising while imports of commodities decline. "China is a major importer across a range of commodities, especially metals, for which it accounted for about 40 percent of total global demand in 2014. China's investment slowdown has had a significant impact on the demand for and prices of those commodities closely related to investment activities - indeed, metal prices have fallen steadily since early 2011 (by almost 60 percent on average)."IMF

Countries where China accounts for a relatively high share of value-added exports tended to experience weaker export growth in 2015, but with some exceptions.



GDP Growth (Annualized semiannual percent change) Emerging Market and Developing Economies

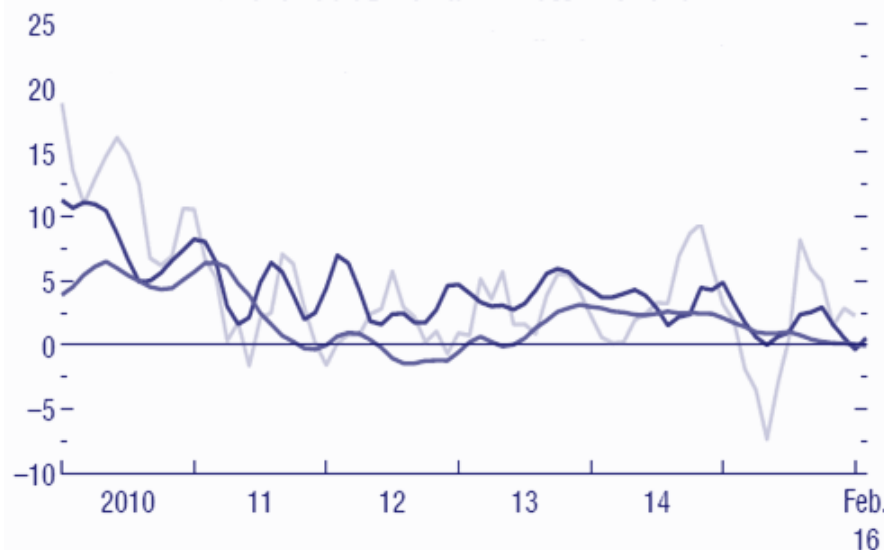


Source: "World Economic Outlook", IMF, April 2016

... has translated through into a weak domestic environment, ...

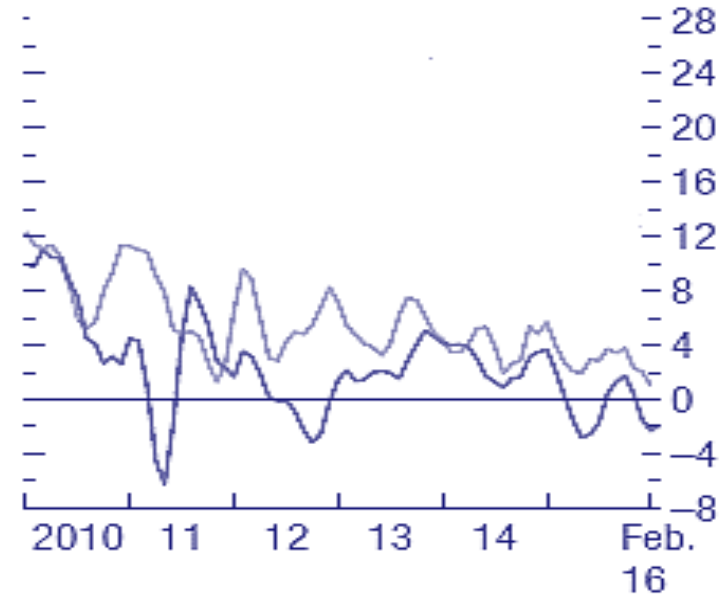
- “Consecutive downgrades of future economic prospects carry the risk of a world economy that reaches stalling speed and falls into widespread secular stagnation.”
- “Extreme flooding and drought from the current El Nino is worsening poverty and displacement in a range of emerging markets and low-income developing countries.”
- The IMF has revised down its global growth forecasts (3.2% y/y 2016), citing that “demand, notably investment demand, remains weak worldwide, but especially in commodity exporters, whose terms of trade have collapsed.”IMF

World Trade, Industrial Production, and Manufacturing PMI (Three-month moving average; annualized percent change, unless noted otherwise)



— Manufacturing PMI (deviations from 50)
— Industrial production
— World trade volumes

Industrial Production (Three-month moving average; annualized percent change)



— Advanced economies
— Emerging market economies
Source: “World Economic Outlook”, IMF, April 2016

... and the IMF has revised its forecasts down again.

IMF: The Global Outlook in summary (% y/y).

		Projections		Difference from January 2016 WEO Update ¹		Difference from October 2015 WEO ¹	
	2015	2016	2017	2016	2017	2016	2017
World Output	3.1	3.2	3.5	-0.2	-0.1	-0.4	-0.3
Advanced Economies	1.9	1.9	2.0	-0.2	-0.1	-0.3	-0.2
United States	2.4	2.4	2.5	-0.2	-0.1	-0.4	-0.3
Euro Area	1.6	1.5	1.6	-0.2	-0.1	-0.1	-0.1
Germany	1.5	1.5	1.6	-0.2	-0.1	-0.1	0.1
France	1.1	1.1	1.3	-0.2	-0.2	-0.4	-0.3
Italy	0.8	1.0	1.1	-0.3	-0.1	-0.3	-0.1
Spain	3.2	2.6	2.3	-0.1	0.0	0.1	0.1
Japan	0.5	0.5	-0.1	-0.5	-0.4	-0.5	-0.5
United Kingdom	2.2	1.9	2.2	-0.3	0.0	-0.3	0.0
Canada	1.2	1.5	1.9	-0.2	-0.2	-0.2	-0.5
Other Advanced Economies ²	2.0	2.1	2.4	-0.3	-0.4	-0.6	-0.5
Emerging Market and Developing Economies	4.0	4.1	4.6	-0.2	-0.1	-0.4	-0.3
Commonwealth of Independent States	-2.8	-1.1	1.3	-1.1	-0.4	-1.6	-0.7
Russia	-3.7	-1.8	0.8	-0.8	-0.2	-1.2	-0.2
Excluding Russia	-0.6	0.9	2.3	-1.4	-0.9	-1.9	-1.7
Emerging and Developing Asia	6.6	6.4	6.3	0.1	0.1	0.0	0.0
China	6.9	6.5	6.2	0.2	0.2	0.2	0.2
India ³	7.3	7.5	7.5	0.0	0.0	0.0	0.0
ASEAN-5 ⁴	4.7	4.8	5.1	0.0	0.0	-0.1	-0.2
Emerging and Developing Europe	3.5	3.5	3.3	0.4	-0.1	0.5	-0.1
Latin America and the Caribbean	-0.1	-0.5	1.5	-0.2	-0.1	-1.3	-0.8
Brazil	-3.8	-3.8	0.0	-0.3	0.0	-2.8	-2.3
Mexico	2.5	2.4	2.6	-0.2	-0.3	-0.4	-0.5
Middle East, North Africa, Afghanistan and Pakistan	2.5	3.1	3.5	-0.5	-0.1	-0.8	-0.6
Saudi Arabia	3.4	3.0	4.0	-1.0	-0.7	-1.3	-0.9
Sub-Saharan Africa	3.4	3.0	4.0	-1.0	-0.7	-1.3	-0.9
Nigeria	2.7	2.3	3.5	-1.8	-0.7	-2.0	-1.0
South Africa	1.3	0.6	1.2	-0.1	-0.6	-0.7	-0.9

Note: Real effective exchange rates are assumed to remain constant at the levels prevailing during February 2-March 1, 2016. Economies are listed on the basis of economic size. The aggregated quarterly data are seasonally adjusted. ¹Difference based on rounded figure for the current, January 2016 WEO Update and October 2015 WEO forecasts. ²Excludes the G7 (Canada, France, Germany, Italy, Japan, United Kingdom, United States) and euro area countries. ³For India, data and forecasts are presented on a fiscal year basis and GDP from 2011 onward is based on GDP at market prices with fiscal year 2011/12 as a base year. ⁴Indonesia, Malaysia, Philippines, Thailand, Vietnam

Source: IMF, WEO April 2016

We have revised our growth forecasts down since January 2016.

- Weak economic conditions are likely to persist in South Africa in 2016, with a further moderation in household consumption expenditure growth likely as consumer confidence is depressed, employment growth in the private sector low and interest rates and taxes increase. Globally, weak demand (secular stagnation) is negatively impacting SA's industrial and export sectors.
- Insufficient financial support for the agriculture sector (which is hamstrung by the drought) will threaten future food security, has already lifted inflation, will negatively impact the current account and, under the new monetary policy paradigm, result in higher interest rates.

Expected case forecasts, real % y/y Investec	2015	2016	2017	2018	2019	2020
GDP (%)	1.3	0.7	1.4	1.5	2.2	2.5
HCE (%)	1.6	0.8	1.0	1.6	2.0	1.9
GCE (%)	0.3	0.5	-0.3	0.2	0.5	0.6
GFCF (%)	1.4	-0.7	2.2	5.1	7.1	6.3
GFCF as a % GDP	20.8	20.5	20.6	21.4	22.4	23.2
GDE (%)	0.3	1.3	-4.5	-1.7	-2.8	-4.7
Export (%)	9.0	4.9	5.7	6.9	8.0	8.2
Imports (%)	5.7	5.1	5.5	8.2	7.1	8.5
Balance: Current Account (sa) - % GDP	-4.9	-5.4	-5.4	-5.6	-5.5	-5.5
Consumer Inflation (Av: %)	4.6	6.3	5.4	5.6	5.4	5.3
Prime Overdraft Rate (year-end: %)	9.75	11.00	11.50	11.50	11.50	11.50
Rand/USD	12.76	14.87	13.84	12.48	11.49	12.15

Country credit ratings



S&P	Fitch	Moody's	Rating
BBB+	BBB+	Baa1	
Mexico (stable) Spain (stable)	Mexico (stable) Spain (stable)	Ireland (Positive)	
BBB	BBB	Baa2	
		South Africa (negative) Greece (stable) Spain (stable)	Investment grade
BBB-	BBB-	Baa3	
India (stable) South Africa (negative)	India (stable) Turkey (stable) Russia (negative) South Africa (negative)	India (positive) Turkey (negative)	Sub investment grade (speculative)
BB+	BB+	Ba1	
Turkey (negative) Russia (negative)	Brazil (negative)	Russia (stable)	
BB	BB	Ba2	
Brazil (negative)		Brazil (negative)	Speculative grade
B-	B-	B3	
Greece (Stable)			

Exchange rate



Exchange rates:

- Concerns over the loss of investment grade rating, along with the negative market impact of the replacement of previous Finance Minister Nhlanhla Nene by temporary Finance Minister van Rooyen, drove the domestic currency to elevated risk-aversion levels.
- Despite the appointment soon thereafter of Pravin Gordhan to the Finance Minister role, the rand went into the mid-January global debt, commodities and equities market rout severely weakened, reaching a historic low of close to R17.00/USD.
- The mid-January rout occurred on growing fears of global recession as the commodity cycle, global trade volumes and world economic growth slumped lower. Both the ECB and the Fed subsequently then issued dovish monetary policy statements, with the USD then weakening, and EM and key commodity currencies strengthening as global risk aversion subsided substantially.

Base line case currency forecasts: likelihood dwindles as political risk rises

	Q1.16	Q2.16	Q3.16	Q4.16	Q1.17	Q2.17	Q3.17	Q4.17
USD/ZAR (Av)	15.82	15.00	14.45	14.20	14.30	14.00	13.70	13.35
GBP/ZAR (Av)	22.59	21.90	21.53	21.58	21.88	21.42	20.96	20.43
EUR/ZAR (Av)	17.44	16.65	15.90	15.98	16.59	16.38	16.30	16.02
ZAR/JPY (Av)	7.20	7.40	7.68	7.89	7.83	7.93	8.10	8.24
GBP/USD (Av)	1.43	1.46	1.49	1.52	1.53	1.53	1.53	1.53
EUR/USD (Av)	1.10	1.11	1.10	1.13	1.16	1.17	1.19	1.20
USD/JPY (Av)	115	111	111	112	112	111	111	110

Source: Investec, SARB

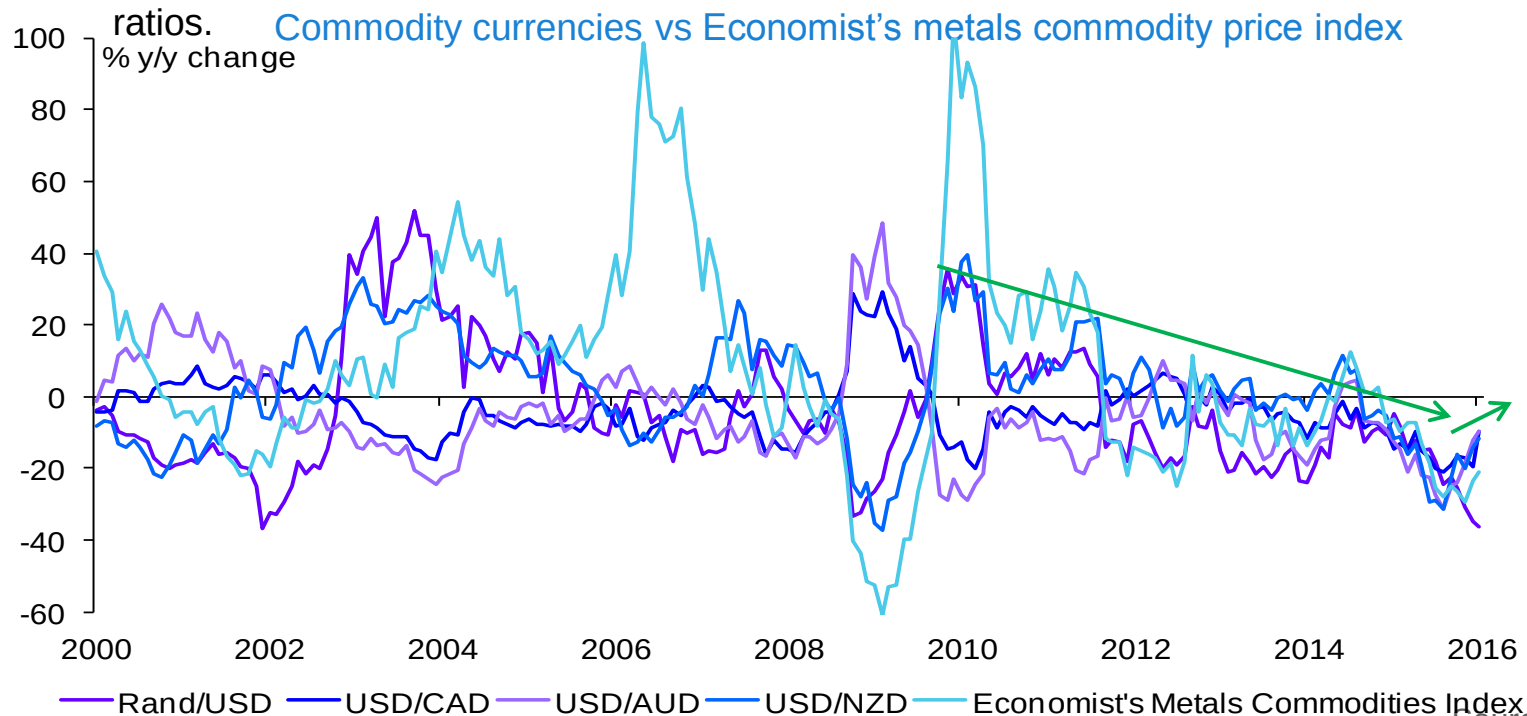
Scenarios for SA:

		Q1.16	Q2.16	Q3.16	Q4.16	Q1.17	Q2.17	Q3.17	Q4.17
Scenario 1:	Rand/USD (average)	15.80	15.00	14.45	14.20	14.30	14.00	13.70	13.35
Base line	Repo rate (end rate)	7.00	7.00	7.25	7.50	7.75	7.75	8.00	8.00
case 40%	The rand is expected to strengthen back toward PPP (reach PPP by 2020) as sedate pace of global monetary policy normalisation is factored in. Economic growth remains weak as the commodity super cycle is over, with trend growth only reached domestically by 2019 on modestly strengthening global demand (back to trend). Structural constraints (infrastructure, inflexible labour market, increasing state intervention and state control of the economy, fiscal constraints, deindustrialisation) hold SA back from achieving a faster economic growth rate. S&P downgrades SA one notch on the local currency sovereign debt front.								
Scenario 2:	Rand/USD (average)	15.80	17.30	18.90	19.30	18.60	17.50	16.40	16.20
Down case	Repo rate (end rate)	7.00	7.50	8.00	8.50	8.50	9.00	9.00	10.00
40%	Intensification of commodity slump, domestic and global rapid, sharp interest rate hikes. All credit ratings of SA's sovereign foreign currency long-term debt downgraded to sub-investment grade. Global economic slowdown worsens, commodity slump intensifies (SA recession), and/or persistent schedule 3 load shedding, prolonged drought, substantial rand weakness, significant strike action in private sector. CPI demand-led inflation subdued by recession, commodity price slump, pass through from rand weakness suppressed as consumer affordability suppressed.								
Scenario 3:	Rand/USD (average)	15.80	18.50	19.60	20.40	21.50	22.60	23.50	24.70
Extreme	Repo rate (end rate)	7.00	8.00	9.00	9.50	10.50	11.00	12.00	13.00
down case	SA's credit rating drops to speculative grade (local and foreign currency from all agencies) on ongoing fiscal problems leading to sovereign debt default, resulting in sovereign debt restructure and haircuts on sovereign debt. Loss of private sector property rights under state custodianship. Sub-investment credit rating sees some primary delistings from the JSE, partial debt default, haircuts included in this scenario. Substantial recession (depression), global economy falls into recession, commodity cycle in depression, civil unrest, persistent load-shedding.								
19%									
Scenario 4:	Rand/USD (average)	15.79	13.80	11.30	10.60	9.50	8.70	8.20	8.00
Up case	Repo rate (end rate)	7.00	6.50	6.00	5.75	5.50	5.00	4.50	4.50
1%	Fast, sustainable economic growth of 5.0-7.0% y/y plus as SA cuts interest rates in line with other commodity exporters, provides fiscal stimulation to productive industries and focuses on economic growth first. Global demand recovers and moves above trend. Fiscal consolidation, SA credit ratings stabilise as risk of bankruptcy recedes leading to decline in the probability of the extreme down case. Alternatively, QE4 in US as stimulus to markets occurs following major terrorist attack, with EM currency strength and lower interest rates in SA, but growth still lags. Ratings stabilise.								

Source: Investec

Commodity prices are a key influencer of the domestic currency ...

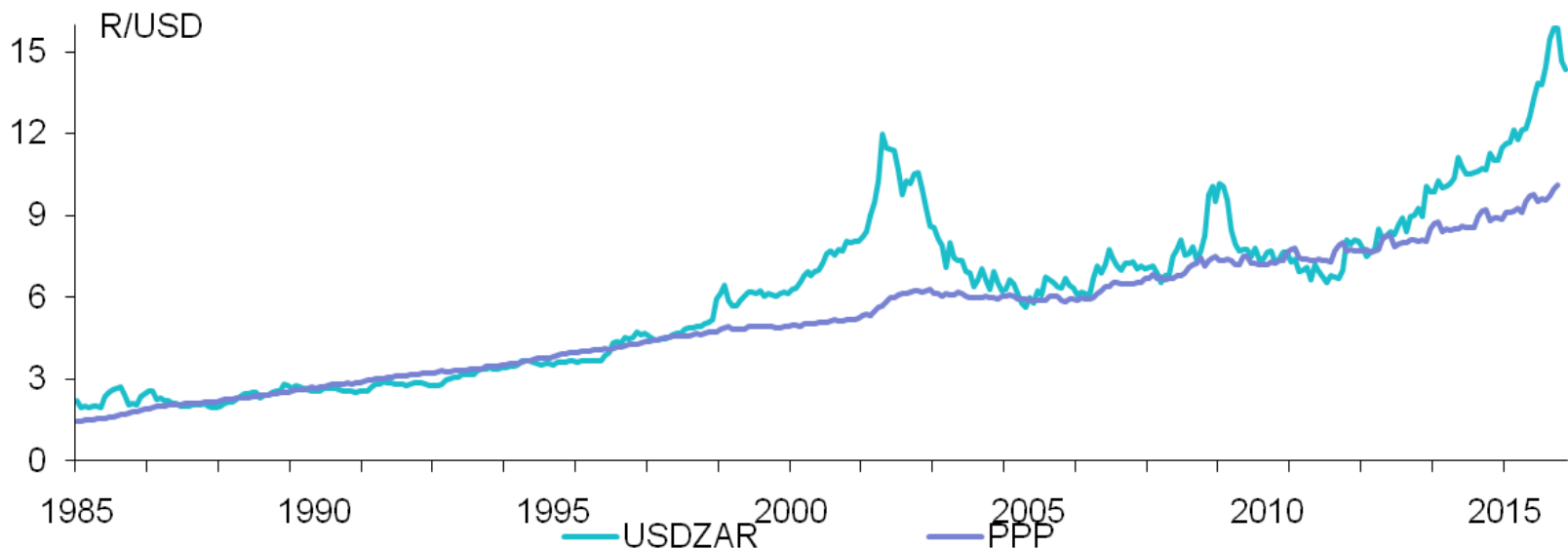
- The reduction in risk aversion from the second half of January became more marked over March and April, with foreigners purchasing R23.0bn worth of SA debt on a net basis in those two months (foreigners purchased US\$62.7bn net in EM portfolio assets in the same period).
- The domestic currency turned the corner with other EM currencies. However, over May, a debt sell-off occurred, with the rand depreciating on domestic economic growth concerns, fears of credit rating downgrades and expectations of higher interest rates in the US.
- SA's extreme economic weakness risks it receiving a sub-investment grade rating, along with heightened political risk. In particular, the credit rating agencies are reassessing SA's creditworthiness in terms of its downward economic growth trajectory and rising government debt



... along with political risk and ...

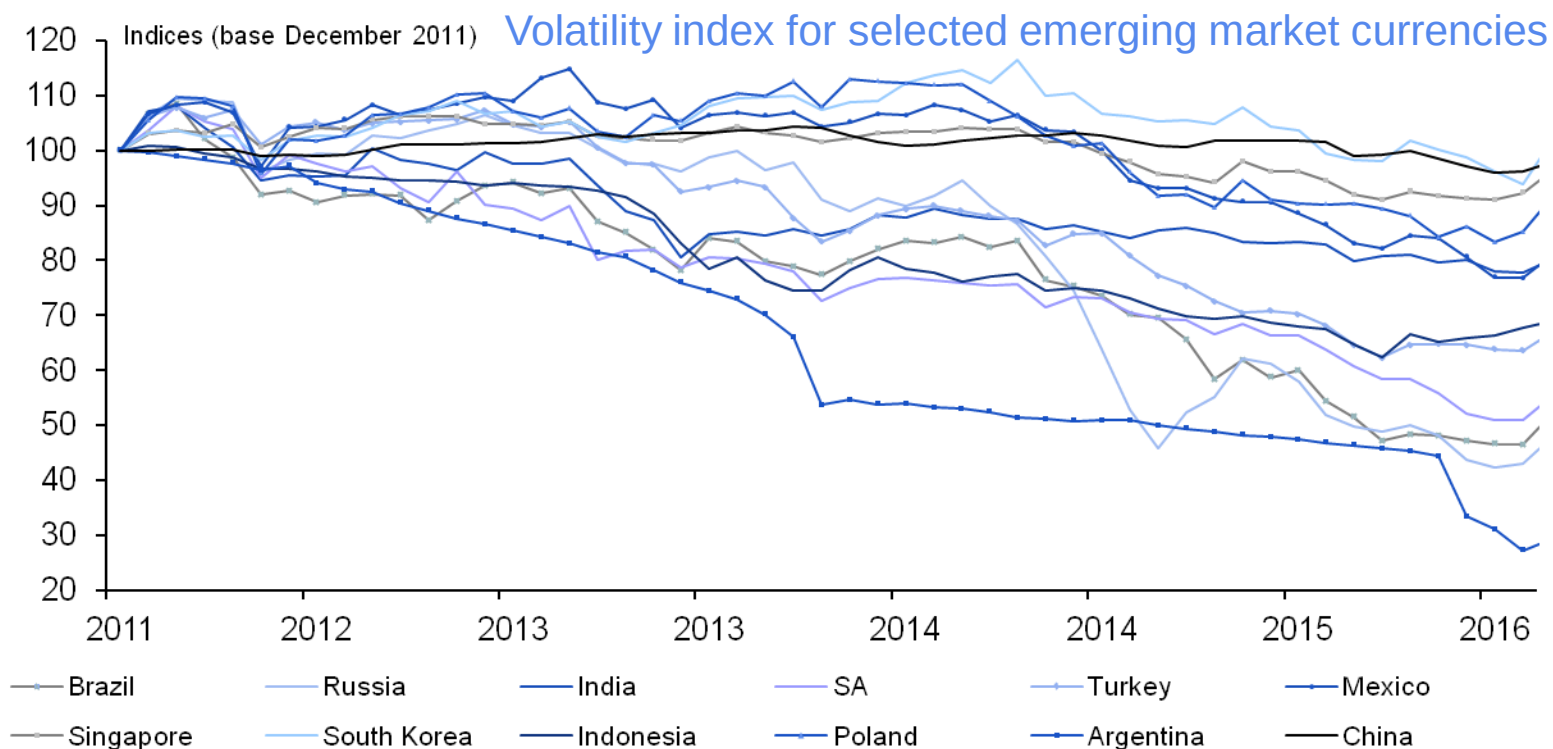
- From 2011 SA has seen credit rating downgrades from Standard & Poor's (S&P) on the deterioration in economic growth, and fiscal slippage.
- This year a more conservative Budget was seen under the new Finance Minister, Pravin Gordhan, although concern was evidenced over the achievement of the budget in later years.
- Political risk, specifically the concern that the Finance Minister, Pravin Gordhan, could be arrested has recently weakened the rand, as the perceived consequent risk of SA seeing its benchmark rating (sovereign foreign currency long-term rating) fall to sub-investment grade has been seen to increase.

Purchasing Power Parity value of the rand vs USD



... global risk aversion.

- S&P is due to deliver its credit rating decision on 3rd June, and the negative outlook it has SA on means the sovereign could be downgraded to sub-investment grade. While the baseline case sees sub-investment grade avoided this year, the down case does not.
- The most recent rand weakness has been escalating on the concern SA will lose its investment grade rating from S&P, as the removal of Finance Minister Gordhan is seen as weakening the move to achieve fiscal consolidation.
- The likelihood of the down case will increase unless it is formally announced that there will definitely be no arrest of the Finance Minister Gordhan, and that he will remain in his role.



Source: Investec, I-Net Bridge

Down case: recession



Down case currency forecasts								
	Q1.16	Q2.16	Q3.16	Q4.16	Q1.17	Q2.17	Q3.17	Q4.17
USD/ZAR (Av)	15.80	17.30	18.90	19.30	18.60	17.50	16.40	16.20
GBP/ZAR (Av)	22.59	25.26	28.16	29.34	28.46	26.78	25.09	24.79
EUR/ZAR (Av)	17.44	19.20	20.79	21.71	21.58	20.48	19.52	19.44
ZAR/JPY (Av)	7.30	6.42	5.87	5.80	6.02	6.34	6.77	6.79

Down case forecasts, real % growth y/y	2015	2016	2017	2018	2019	2020
GDP (%)	0.2	-1.9	-0.4	2.0	2.4	2.5
HCE (%)	1.0	0.8	1.2	1.7	2.4	2.9
GCE (%)	-0.3	-0.3	1.0	0.8	0.8	1.8
GFCF (%)	0.4	-2.5	3.2	3.3	4.8	5.0
Export (goods & non-factor services) - %	4.9	-2.0	2.2	6.4	6.3	8.2
Imports (goods & non-factor services) - %	3.6	5.4	7.8	9.1	5.6	9.7
Balance: Current Account (sa) - % GDP	-4.1	-2.5	-6.0	-5.9	-5.6	-5.3
Consumer Inflation (Av: %)	4.6	3.4	4.7	5.2	5.0	5.3
Prime Overdraft Rate (year-end: %)	6.25	8.50	10.00	10.50	10.75	10.75
Interest rate (R186), long-term (year-end: %)	8.60	10.50	12.00	13.50	14.00	12.22
Rand/USD	12.76	18.53	16.53	15.63	14.43	12.46

Extreme down case: failed state



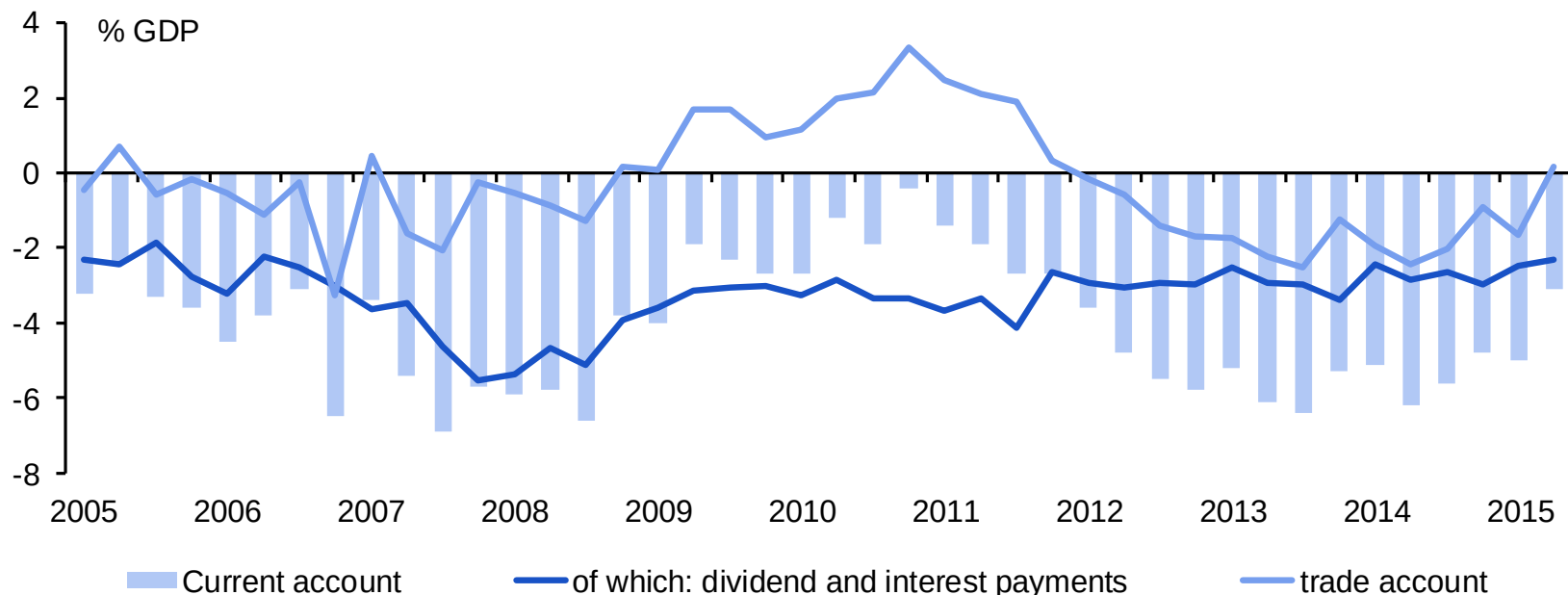
Extreme down case currency forecasts								
	Q1.16	Q2.16	Q3.16	Q4.16	Q1.17	Q2.17	Q3.17	Q4.17
USD/ZAR (Av)	15.80	18.50	19.60	20.40	21.50	22.60	23.50	24.70
GBP/ZAR (Av)	22.59	27.01	29.20	31.01	32.90	34.58	35.96	37.79
EUR/ZAR (Av)	17.44	20.54	21.56	22.95	24.94	26.44	27.97	29.64
ZAR/JPY (Av)	7.30	6.00	5.66	5.49	5.21	4.91	4.72	4.45

Extreme Down case forecasts, real % growth y/y	2015	2016	2017	2018	2019	2020
GDP (%)	1.3	-1.6	-5.5	-2.4	0.6	2.1
HCE (%)	1.5	0.5	-2.2	-2.6	-1.1	1.8
GCE (%)	0.2	-0.4	-0.1	-0.3	-1.9	-3.8
GFCF (%)	0.8	-2.2	-5.1	-6.9	0.4	6.4
Export (goods & non-factor services) - %	8.9	-0.9	3.2	18.0	18.3	14.5
Imports (goods & non-factor services) - %	5.6	5.2	8.9	12.0	12.0	12.0
Balance: Current Account (sa) - % GDP	-4.1	-6.6	-8.4	-8.2	-7.9	-7.6
Consumer Inflation (Av: %)	4.6	8.9	9.8	9.4	8.7	8.3
Prime Overdraft Rate (year-end: %)	6.25	9.50	13.00	18.00	16.50	14.00
Interest rate (R186), long-term (year-end: %)	8.60	13.30	16.60	23.00	20.5	15.00
Rand/USD	12.76	20.00	24.15	26.45	27.65	28.60

-SA's current account is chiefly influenced by dividend and coupon payments to foreign investors.

- Foreign purchases of bonds and equities contribute to funding the current account deficit via a capital account surplus.
- The current account deficit in turn consists considerably of dividend and coupon payments to foreigners holding SA bonds and equities.
- An improvement in SA's trade balance would reduce the CAD (current account deficit), but there remains the risk of further slowdown in demand from China and rand weakness in SA.
- Oil and petroleum products are SA's largest commodity import, constituting close to 20% of total merchandise imports.

Current account deficit chiefly composed of dividend and coupon payments to foreigners



Source: SA Reserve Bank

Inflation



Inflation: moderating



- The fall in the petrol price in late 2014 and early 2015 created a low base effect, without which the outcome for CPI inflation in Q1.16 would have been closer to 5.5% y/y, instead of 6.5% y/y.
- The oil price has risen recently to US\$47.5/bbl, we continue to expect the oil price to average around US\$40-45/bbl this year, with an upside risk.
- The drought has pushed up food prices, and the lag between maize prices and CPI inflation means ongoing, significant food price inflation increases for the consumer, even though retailers are limiting pass through on weak consumer affordability.
- The latest data shows food price inflation rose to 9.8% y/y as unprocessed food price inflation jumped to 12.5% y/y from 10.4% y/y as a consequence of the drought. Meat prices rose by another 1% y/y, fruit and vegetable price inflation both were 18.7% y/y and the bread and cereals category saw a jump in price inflation to 13.3% from 10.6% y/y.
- We expect consumer food price inflation in double digits this year, placing upward pressure on CPI.

Forecasts	2014	2015	2016	2017	2018	2019	2020
Consumer Inflation (Av: %)	6.1	4.6	6.3	5.4	5.6	5.4	5.3
(year-end: %)	5.3	5.2	6.2	5.5	6.0	5.4	5.1
Producer Inflation (Av: %)	7.4	3.6	7.7	4.8	5.8	5.6	5.1
(year-end: %)	5.8	4.8	7.3	5.4	6.0	5.4	4.7

Interest rate



Interest rates:



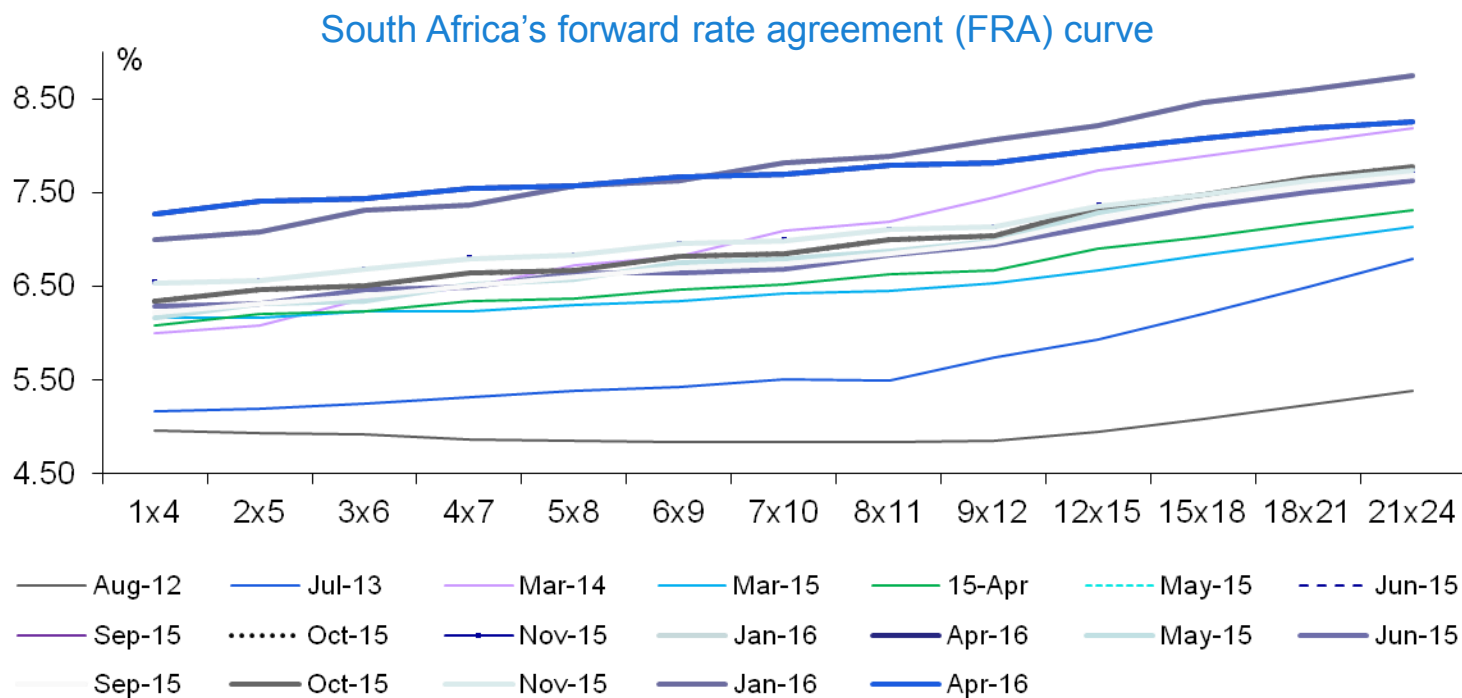
- South Africa has now hiked interest rates by 2.00% in the current upwards interest rate cycle (which began in 2014), where the rand has depreciated from R10.63/USD, R14.42/EUR and R17.37/GBP to R14.39/USD, R16.22/EUR and R20.63/GBP.
- A 50bp hike was delivered in January and a 25bp hike in March from the MPC, and while a tailing down in hawkishness could be expected with an unchanged outcome in May, particularly given the rand's substantial pull back, the SARB is instead still very hawkish.
- While the risk of recession is real for SA this year, the SARB is following a different monetary policy paradigm than in 2009, when it cut interest rates despite CPI inflation peaking at 13.00%, food price inflation in double digits and material rand weakness, with the economy also at risk of recession (one quarter of contraction had occurred already).
- The very hawkish nature of the SARB this time around leads us to believe that further interest rate hikes will occur this year, of at least 75bp; a 25bp hike in May, another 25bp in July, and a third hike in September of the same magnitude. While we continue to believe the SARB should pause, it seems more likely they will hike interest rates further this year.

Forecasts									
	Q1.16	Q2.16	Q3.16	Q4.16	Q1.17	Q2.17	2016	2017	2018
Repo Rate (year-end: %)	7.00	7.00	7.25	7.50	7.75	7.75	7.50	8.00	8.00
Prime Overdraft Rate (year-end: %)	10.50	10.50	10.75	11.00	11.25	11.25	11.00	11.50	11.50
SA rand bond (Gov10 yr, year-end: %)	9.37	9.68	10.00	9.90	10.30	10.25	9.90	10.20	10.00

Source: Investec

... further interest rate hikes are likely, ...

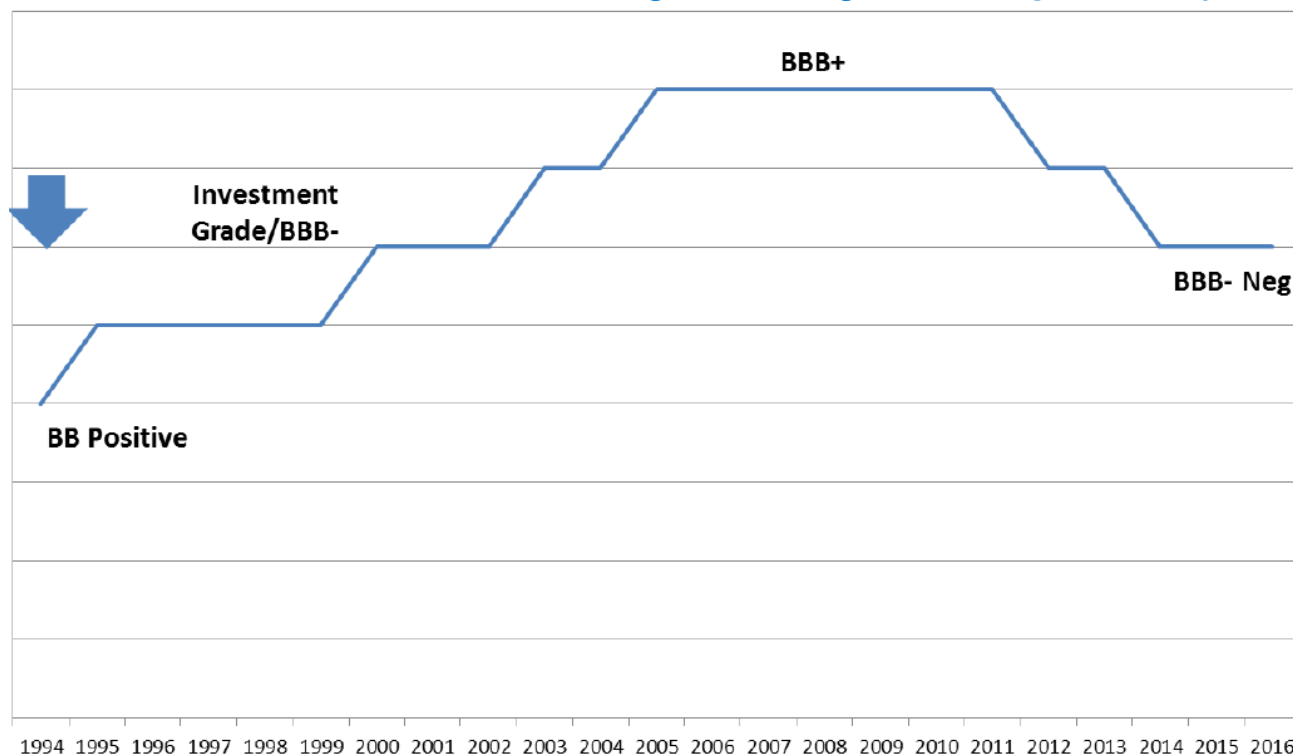
- The SARB currently has a substantially higher CPI inflation forecast than ourselves at 7.0% y/y in 2017, but their figures are volatile.
- The 2016 GDP growth outlook will likely be closer to 1.0% y/y than 2.0% y/y as the SARB reaffirmed its commitment to further interest rate hikes (upward interest rate cycle to remain in place).
- The SARB leaves no room for doubt that it intends hiking interest rates at the expense of economic growth.
- It could hike at subsequent MPC meetings.



... as are credit rating downgrades ...

- We continue to believe that the next move from Standard & Poor's (and next rating agency move) will be a downgrade on the local currency front (currently BBB+, to BBB) not on the hard currency front (now BBB-), to bring greater alignment between the two.
- This could occur at the June 2016 review, but does not deliver a sub-investment grade outcome.
- We believe that unless South Africa enters the down case, we will not see a sub-investment grade rating delivered this year from any of the agencies.

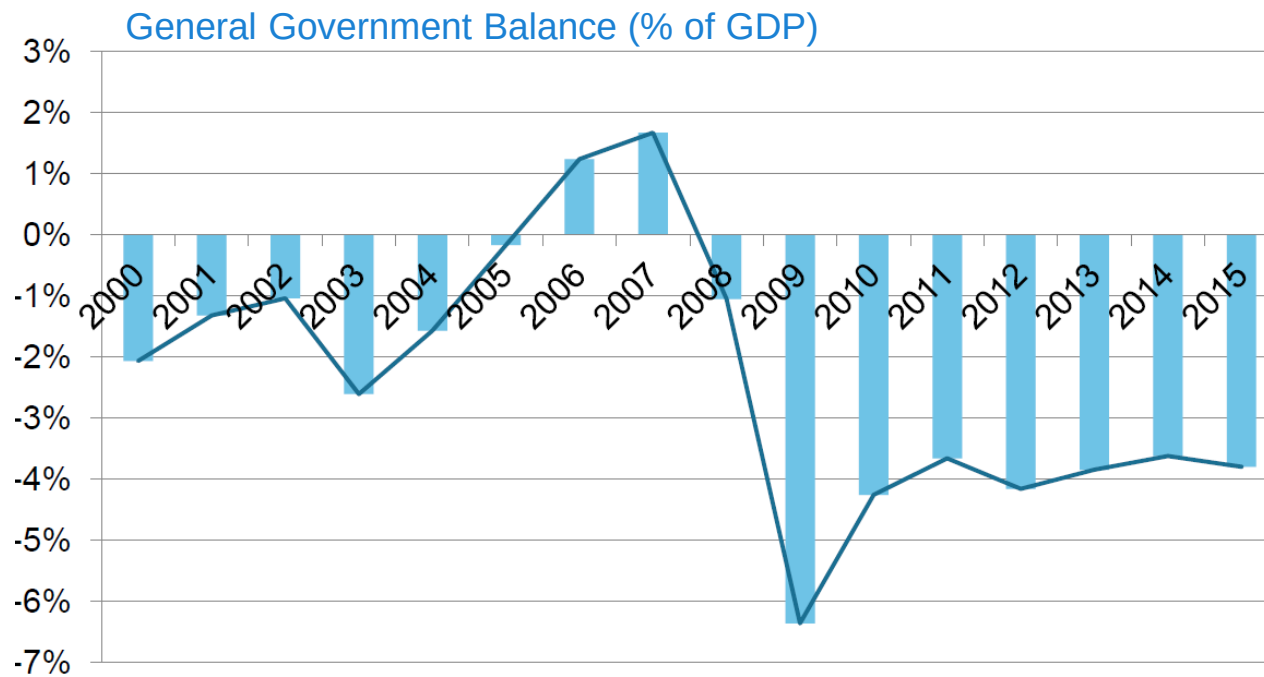
Standard & Poor's credit rating on SA long-term foreign currency sovereign debt



Source: Standard and Poor's

... which would raise borrowing costs, ...

- We have low economic growth forecast out to 2020 on the expected downgrade, and weakness or at best stability despite FOMC more dovish, and higher interest rates.
- SA could see its local currency rating revised lower to BBB- next year at the earliest (from our expectation that it will drop to BBB this year) if economic growth continues around 1.0% y/y or deteriorates further. First the local currency rating would be placed on a negative outlook however.
- From a hard (foreign) currency rating perspective, SA is at risk of falling into the sub-investment grade category, as the outlook is negative, and while it is not impossible this could be delivered in June, we continue to believe it is less likely than the local currency alignment (downgrade) .



... currently South Africa is still rated investment grade.

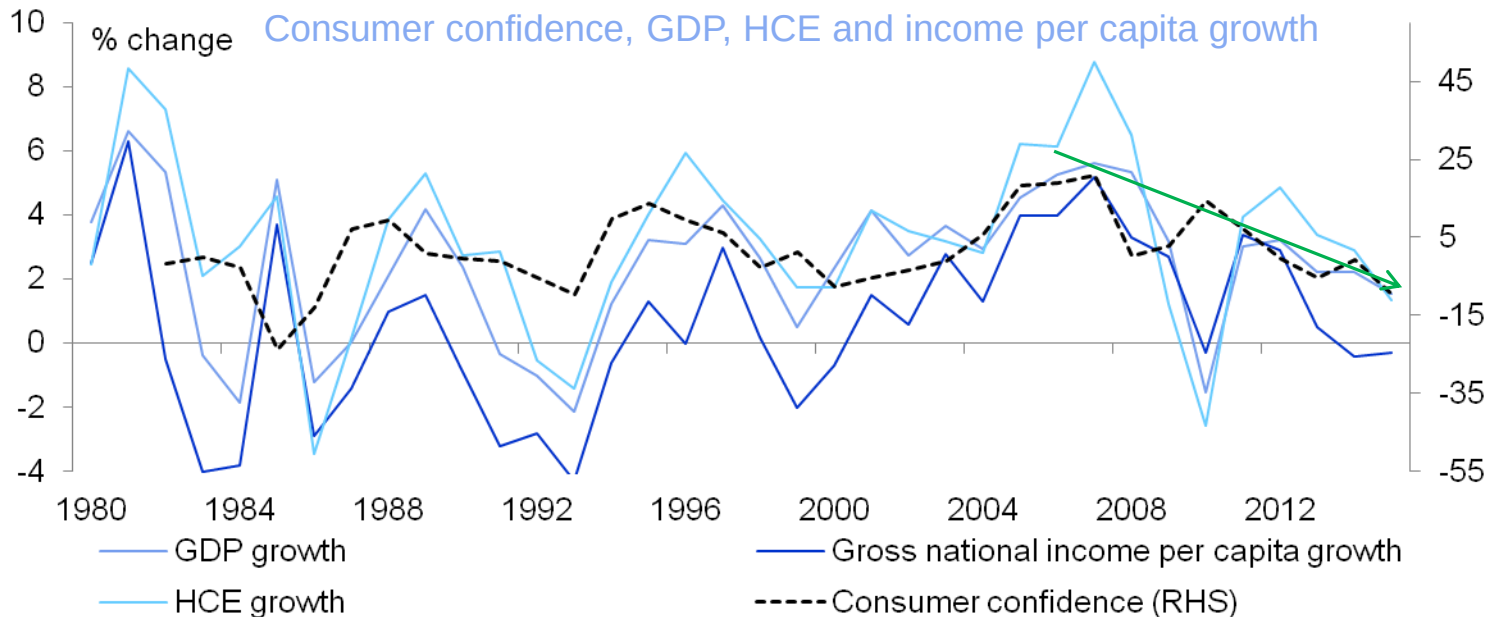
- 
- Strong, capable world class private business sector
 - Prudent monetary policy
 - Sound banking sector
 - Fiscal policy battling against headwinds
 - Well managed JSE and strong foreign interest in SA listed equities
 - Incubated a large number of companies to large scale, international level
 - SA part of global automotive supply chain
 - Mineral rich, endowed country, potential significant gas and oil reserves
 - World-class private sector education and private sector healthcare
 - Tourism opportunity for employment, particularly as SA is a youthful population

Consumer health



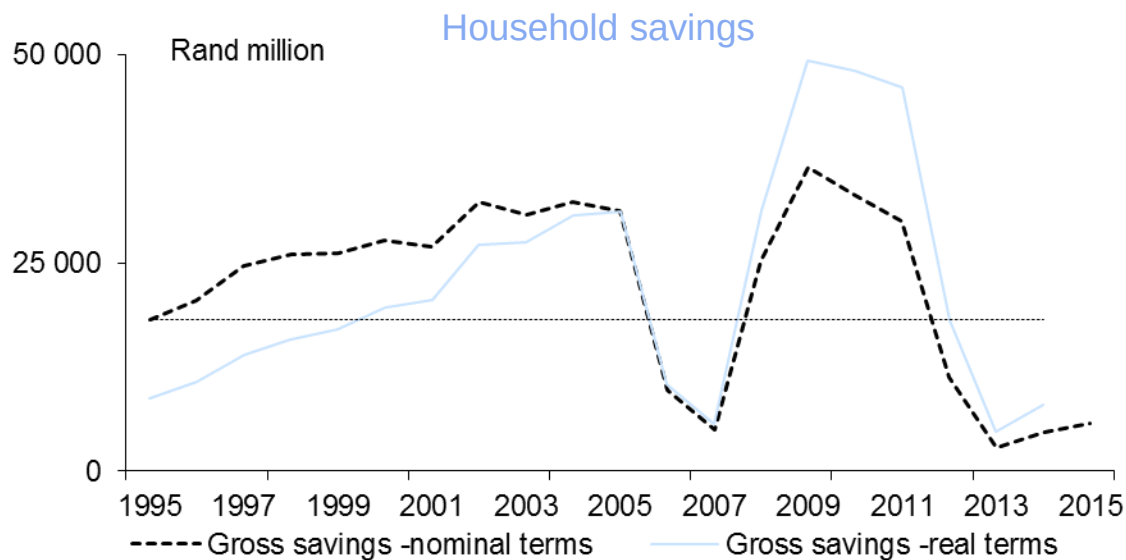
SA consumer: is evidencing financial vulnerability ...

- Consumers' ability to spend is constrained by higher interest rates and taxes, falling real incomes per capita and rising unemployment, as well as high indebtedness and modest credit extension to the household sector.
- The collapse in consumer confidence bodes ill for GDP growth this year, due to its strong correlation with HCE (household consumption expenditure), as HCE consists of two thirds of GDP growth.



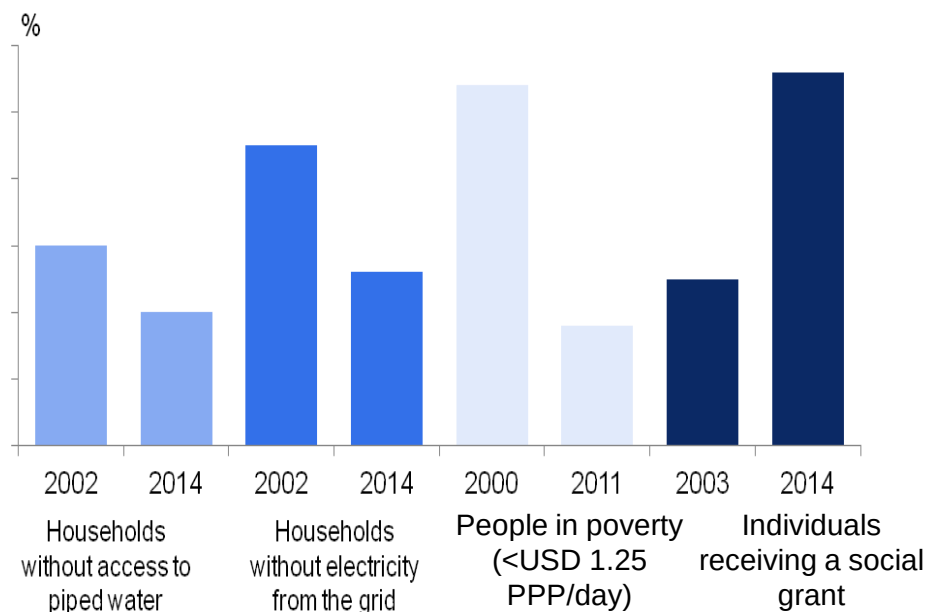
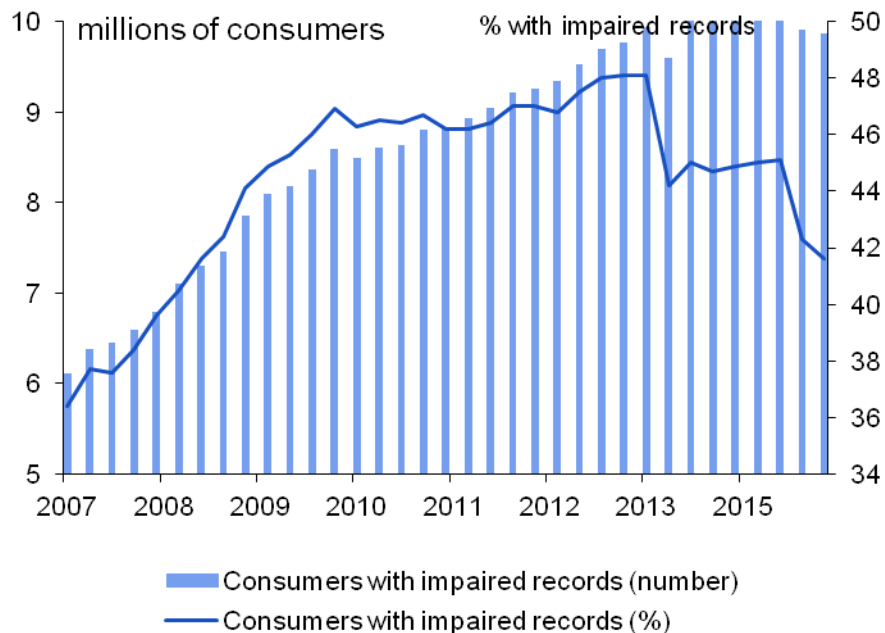
Expected case forecasts, real % growth y/y Investec	2015	2016	2017	2018	2019	2020
HCE (%)	1.6	0.8	1.0	1.6	2.0	1.9
GCE (%)	0.3	0.5	-0.3	0.2	0.5	0.6

... impairments are elevated (excluding savings amnesty), savings are low ...



Consumers with impaired credit records

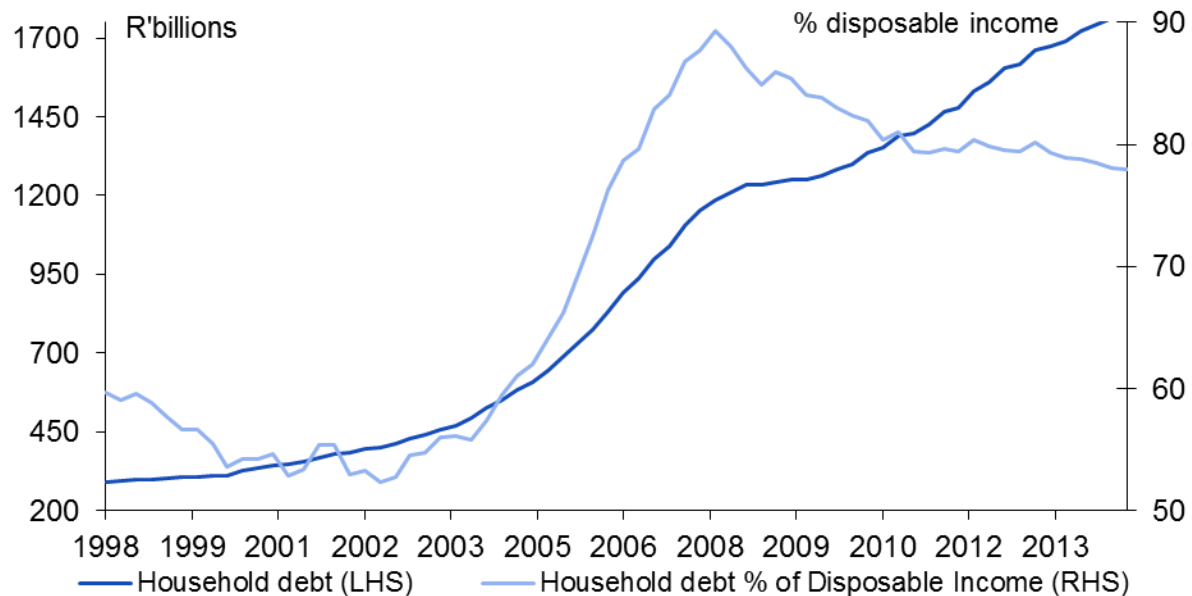
Social progress has been impressive



... real disposable income growth is still on a downward trend, indebtedness is high.



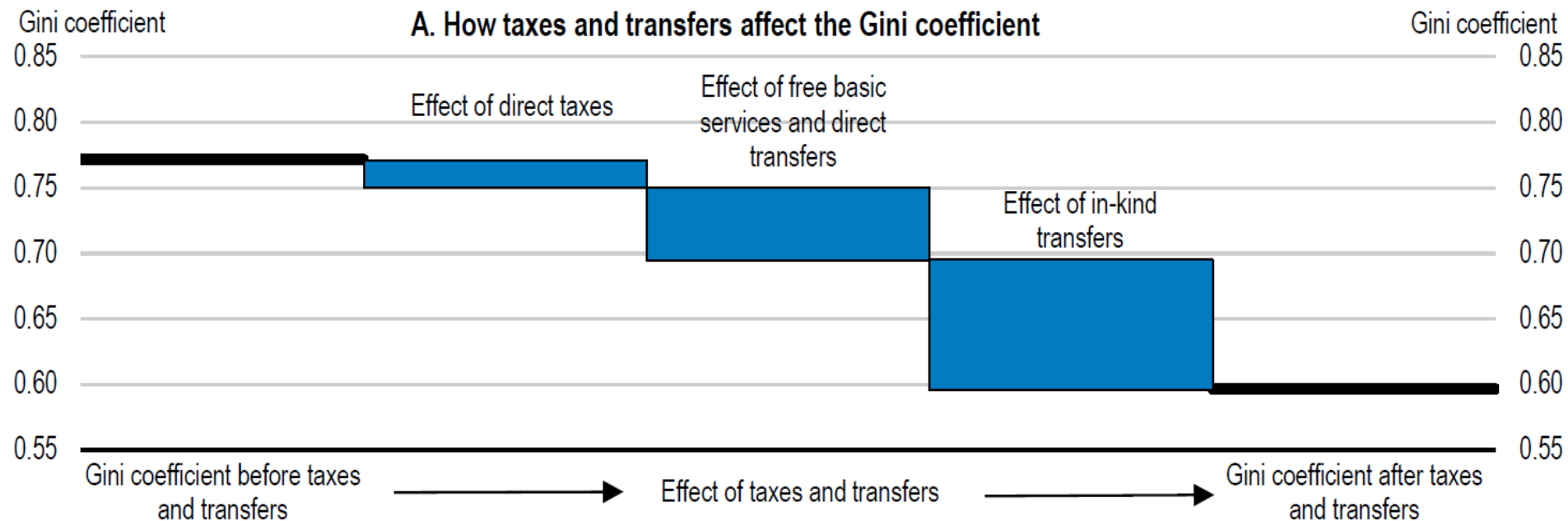
Household debt (R'bn, nominal) and household debt % disposable income



Both the OECD and the World bank recognise social mobility in ...

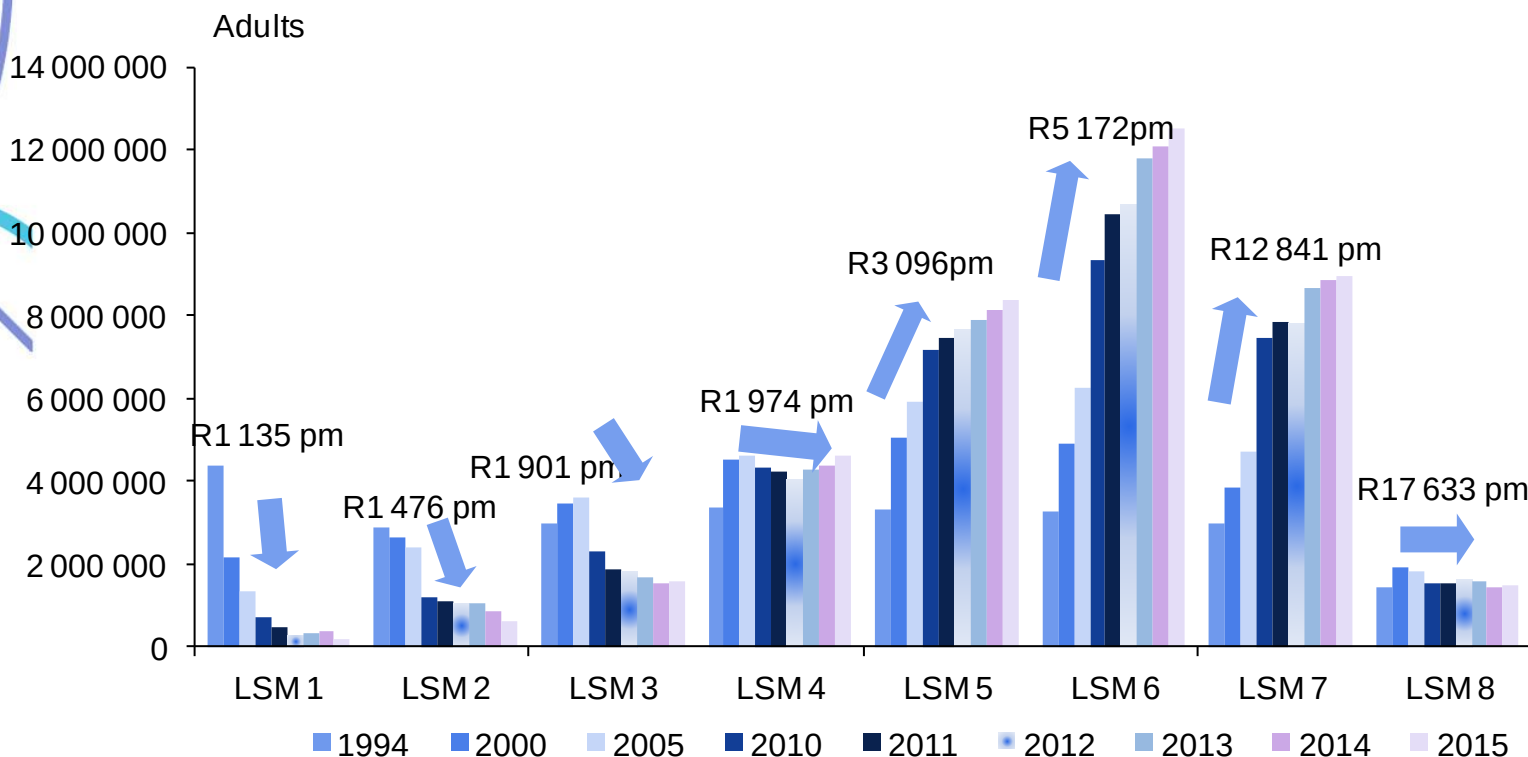
- “Since 1994 South Africa has made great progress in reducing absolute poverty by rolling out social grants for pensioners, the disabled and children.
- Access to education, housing, water, electricity and other services has been greatly broadened. As a result, well-being has increased substantially.
- Social progress has been achieved with redistributive grants and wide access to key public services, notably education, health, housing, water, sanitation and electricity. These services account for 60% of government spending”, OECD, Economic Surveys, South Africa, July 2015
- A World Bank survey shows “South Africa now ranks at the top in terms of the scale of redistribution” .

Social benefits reach many people



... SA persists since 1994, but ...

Living Standard Measures in South Africa



LSM 1 Radio, minimal access to services
 LSM 3 above plus TV, DVD/video player, electricity
 LSM 5 above plus magazines, books, lottery tickets
 LSM 7 above plus DSTv, motor vehicles, internet,
 LSM 9 above, higher income

LSM 2 above plus stove, water on plot
 LSM 4 above plus Hi-fi, flush toilet, fridge, electric hotplate, newspaper
 LSM 6 above plus cell phones, cinema
 LSM 8, above plus full ownership of durables full access to services
 LSM 10 above, higher income

Source: Eighty 20, AMPS. Availability of historical data is limited

... the number of tax payers funding the social wage is still small.

- In the Budget marked fiscal consolidation aimed at avoiding sub-investment sovereign credit ratings occurred as current expenditure plans were cut , but the budget was also supportive of the weak economic environment as tax increases were limited.
- Individuals shoulder the bulk of the tax burden in South Africa (34%), with VAT bringing in 26% of tax revenue and corporates 20%.

Fiscal consolidation is probable for SA if the budget is maintained, which is a positive outcome, with lower than previously projected deficit figures and a stabilisation of debt over the medium term.

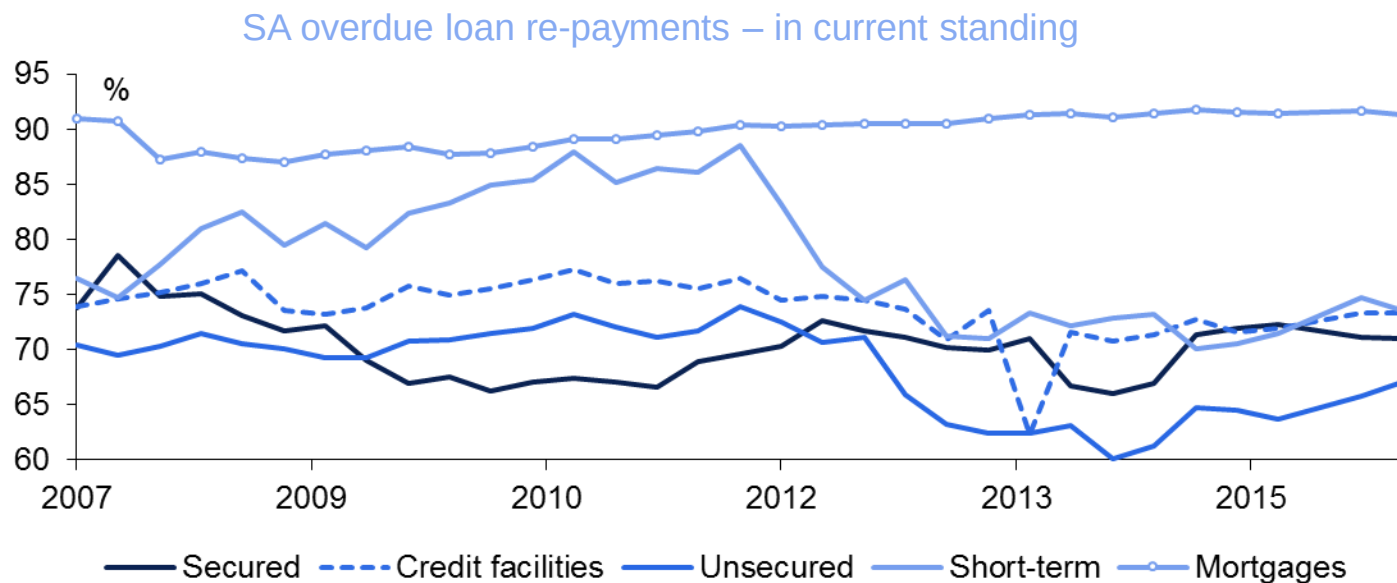
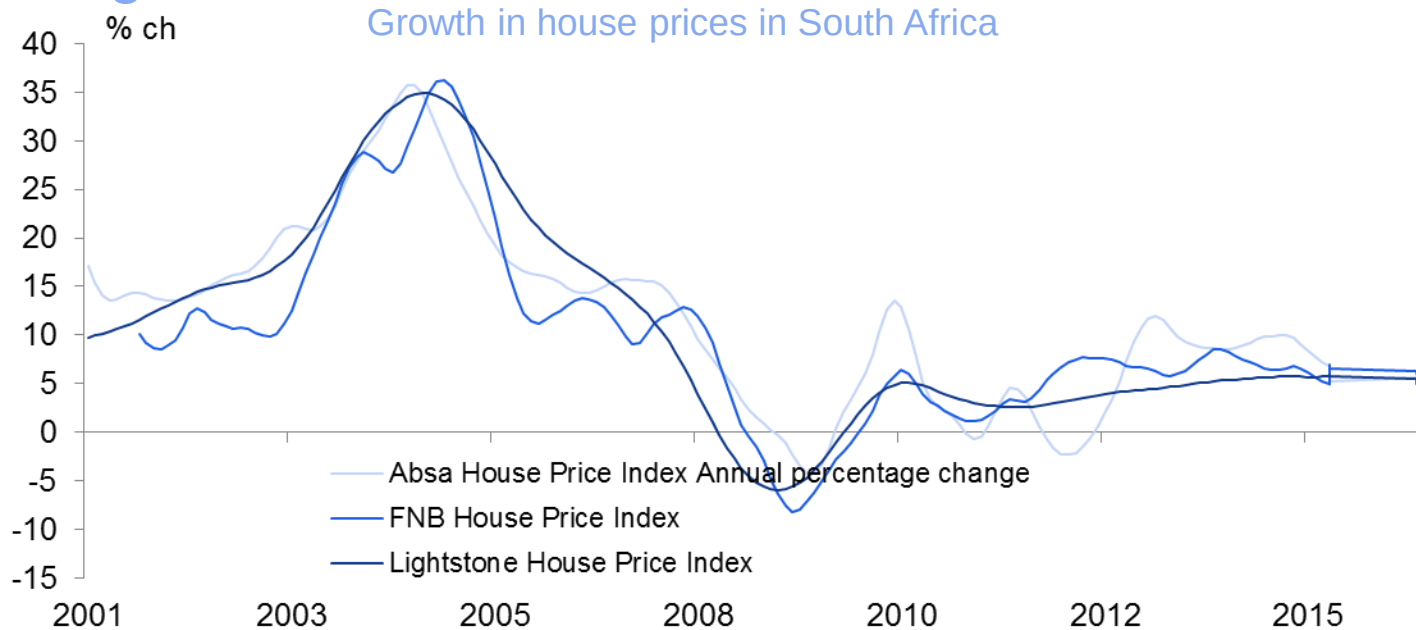
Estimates of individual tax payers and taxable income, 2016/17

Taxable bracket	Registered individuals		Taxable income		Income tax payable before relief		Income tax and medical tax credits relief		Income tax payable after rate increase	
	Number	%	R bn	%	R bn	%	Rbn	%	R bn	%
0 – R70 000 ¹	6 619 854		178.2		-		-		-	
R70 001 – R150 000	2 583 046	36.3	271.9	12.5	12.6	2.8	0.6	9.1	12.0	2.7
R150 001 – R250 000	1 733 463	24.4	338.8	15.6	35.7	8.0	1.2	17.7	34.5	7.8
R250 001 – R350 000	1 071 798	15.1	317.9	14.6	49.5	11.1	1.3	20.0	48.2	10.9
R350 001 – R500 000	800 990	11.3	330.7	15.2	66.1	14.8	1.5	22.5	64.6	14.6
R500 001 – R750 000	497 722	7.0	300.7	13.9	75.9	17.0	1.1	16.3	74.9	17.0
R750 001 – R1 000 000	197 813	2.8	169.8	7.8	50.3	11.2	0.4	6.6	49.9	11.3
R1 000 001 – R1 500 000	136 782	1.9	163.4	7.5	53.6	12.0	0.3	4.6	53.3	12.1
R1 500 001+	94 578	1.3	276.5	12.7	104.0	23.2	0.2	3.2	103.8	23.5
Total	7 116 192	100.0	2 170	100.0	447.6	100.0	6.6	100.0	441.0	100.0
Grand total	13 736 046		2 348		447.6		6.6		441.0	

Source: Budget 2016

1. Registered individuals with taxable income below the income-tax threshold

House price growth is modest with little evidence of an asset bubble.



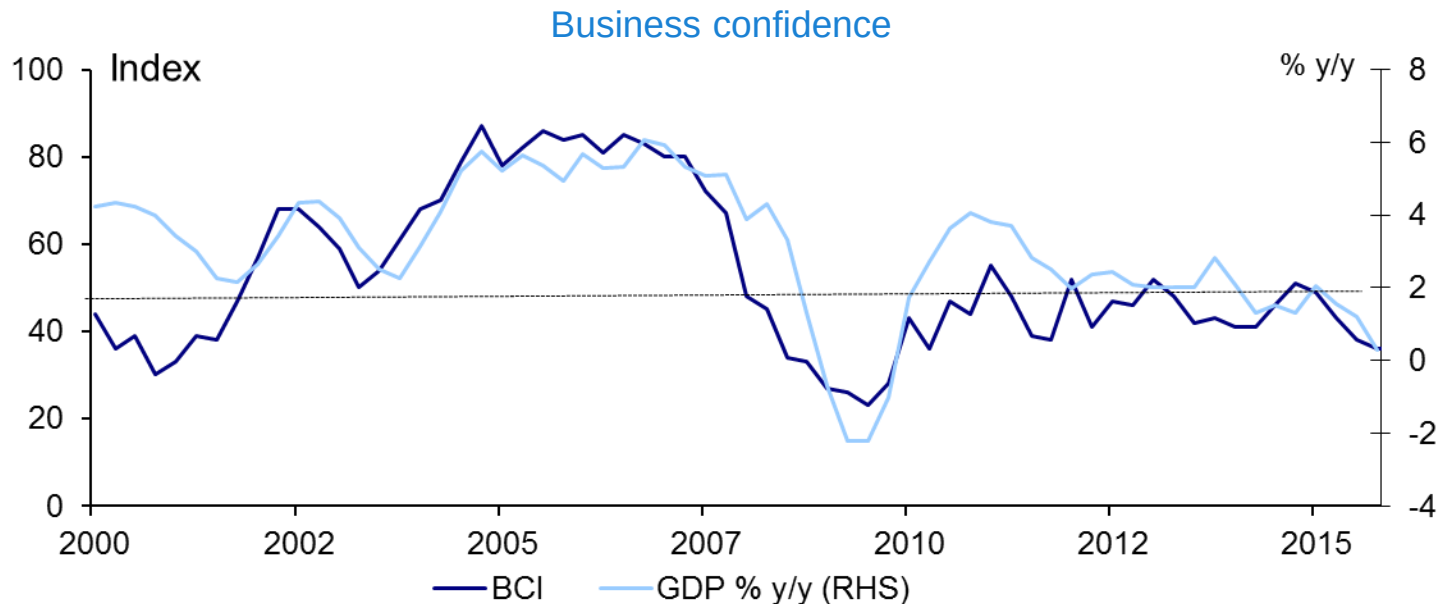


Domestic Gross Fixed Investment and industrial production



Fixed investment: is weak.

- Business confidence gives a good leading indication of the likelihood of expansion or contraction (recession) in the economy, and so the impact on private sector employment and fixed investment.
- Q1.16's outcome signals GDP in the first quarter will likely be weak, close to stalling – the BCI reading proved accurate for Q4.15 GDP which came close to stalling (below 0.2% q/q, seasonally adjusted).



Expected case forecasts, real % growth y/y Investec	2015	2016	2017	2018	2019	2020
GFCF (%)	1.4	-0.7	2.2	5.1	7.1	6.3
GFCF as a % GDP	20.8	20.5	20.6	21.4	22.4	23.2

Major capex projects in the next five years

Announced date	Project Name	Company Name	Estimated value (m)	Estimated completion date
Apr 2012	Transnet's Market Demand Strategy (MDS) – Railway projects	Transnet	300 000	Apr 2020
Apr 2011	Passenger Rail Agency of SA (Prasa) rolling stock fleet-renewal programme	Passenger Rail Agency of South Africa	151 500	Dec 2030
Feb 2007	Project Kusile (formerly called Bravo)	Eskom	141 500	Jun 2021
Feb 2006	Medupi project (previously known as Alpha and Charlie)	Eskom	125 000	Aug 2017
Aug 2000	Spoornet's capital renewal programme	Spoornet	54 000	Jun 2020
Jun 2013	Renewable Energy Independent Power Producer Procurement Programme (REIPPP) – third round	Department of Energy	44 400	Jun 2016
Feb 2006	Ingula pumped storage scheme project (previously known as Braamhoek pumped-storage scheme)	Eskom	25 900	Jul 2017
Aug 1996	Coega Industrial Development Zone (IDZ)	Portnet	25 200	Dec 2030
Oct 2013	Savana City Mixed-use Development	Basil Read and Old Mutual's housing Impact Fund of SA	24 000	Dec 2023
Apr 2015	The Department of Energy (DoE) fourth Renewable Energy Independent Power Producer Procurement Programme (REIPPPP)	Department of Energy (DoE)	23 000	Dec 2018

Major capex projects in the next five years

Announced date	Project Name	Company Name	Estimated value (m)	Estimated completion date
Mar 2013	Venetia underground diamond mine	De Beers Consolidated Mines South Africa (DBCM)	20 000	Dec 2021
May 2012	Umzimvubu water resources development project	Department of Water Affairs (DWA)	20 000	Jan 2018
Sep 2009	Waterfall City Mixed-Development project ⁶	Sanlam	17 500	Dec 2016
May 2008	Limpopo water supply programme	Department of Water Affairs and Forestry and 23 mining	16 100	Dec 2016
Mar 2007	Anglo Coal South Africa expansion	Anglo Coal South Africa	15 000	Dec 2023
Aug 2011	Lesotho Highlands Water Project – Phase 2	Department of Water Affairs	12 000	Aug 2020
Feb 2012	Greenfield Railway project	Transnet and Swazi rail	12 000	Dec 2016
Apr 2011	New Largo coal mine project	Anglo American, through its subsidiary, Anglo American Inyosi Coal	11 650	Jan 2017
Feb 2008	Impala no. 17 shaft – Rustenburg	Implats	11 100	Dec 2021
Jun 2012	Royal Bafokeng Platinum and Anglo American Platinum's Bafokeng Rasimone Platinum Mine North Shaft Merensky Phase 3	Platinum and Anglo American Platinum	11 010	Aug 2017

Major capex projects in the next five years

Announc ed date	Project Name	Company Name	Estimated value (m)	Estimated completion date
Feb 2009	The Cradle City project	Amari Land	11 000	Dec 2039
Mar 2015	Wind farm projects, Northern Cape – Round 3 of the DoE’s Renewable Energy Independent Power Producer Procurement Programme (REIPPPP)	Mainstream Renewable Power	9 000	Dec 2018
May 2008	Lufhereng housing development	Lufhereng development (joint initiative between the City of Johannesburg and the Gauteng Department of Housing)	9 600	Jul 2017
Jul 2009	Fisantekraal housing project	Basil Read, in association with Garden Cities	9 500	Dec 2020
Jul 2013	Department of Energy (DoE) peaker projects	Department of Energy	9 551	Dec 2016
Mar 2015	Palabora Copper’s Lift 2 project	Bauba Platinum	9 300	Dec 2033
May 2012	The Square Kilometre Array (SKA) project – Phase 1	Department of Science and Technology	8 900	Dec 2023
Sep 2008	Cape Town Bus Rapid Transmit (BRT)	City of Cape Town	8 680	Dec 2020
Aug 2007	South Deep Gold mine expansion	Gold Fields	8 500	Oct 2016
Mar 2008	Prison projects	Department of Correctional Services	8 000	Dec 2017
Jun 2007	Project Hoefyster	Arscor/Denel	8 000	Dec 2017
Aug 2015	Gamsberg sinc mine	Vedanta Resources	8 700	Mar 2018
Sep 2005	Argonaut project	DRD Gold	8 000	Mar 2017
Jun 2007	Project Hoefyster	Arm Scor/Denel	8 000	Dec 2017

Major capex projects in the next five years

Announced date	Project Name	Company Name	Estimated value (m)	Estimated completion date
Apr 2015	Cell C Long-term Evolution infrastructure programme	Cell C	8 000	Apr 2018
Apr 2007	Wesizwe Platinum's Bakubung Platinum-Group Metals Mine Project (formerly known as the Ledig Frischgewaar platinum project)	Wesizwe Platinum Limited	7 900	Apr 2018
Apr 2008	Doornkuil mixed-use development	50:50 joint venture between Basil Read Development and the Old Mutual investment Group SA (Omigsa)	7 800	Feb 2017
Oct 2008	Styldrift 1 expansion project	Royal Bafokeng Platinum and Anglo American Platinum	7 500	Mar 2019
Jan 2015	Department of Higher Education and Training's development plan	The Department of Higher Education and Training's (DHET's) Steyn City Properties	6 500	Dec 2017
Jan 2015	Department of Higher Education and Training's development plan	The Department of Higher Education and Training's (DHET's)	7 100	Dec 2018
Oct 2018	Menlyn Maine City Precinct	Ice Finance, Equity Estates, GP Property Investment Holdings, Nedbank and ABS Bank	7 000	Dec 2016
Jul 2013	City Power Capital Expenditure Investment	City Power	6 700	Dec 2016
Mar 2015	Steyn City Lifestyle Resort	Steyn City Properties	6 500	Dec 2017
Oct 2015	BMW Rosslyn plant upgrade	BMW	6000	Jun 2019
Jun 2010	Telkom mobile network roll-out	Telkom	6 000	Dec 2016

Major capex projects in the next five years

Announc ed date	Project Name	Company Name	Estimated value (m)	Estimated completion date
May 2009	Cornubia Mixed-use development – Phase 1	Tongaat Hulett Developments and the eThekweni municipality	5 100	Dec 2017
Sep 2005	Zimbali (All Projects)	Moreland Development & IFA (International Financial Advisers)	5 000	Jun 2021
Mar 2002	Alice Quarry – Eastern Cape	Alice Quarry	5 000	May 2022
Sep 2015	Maluti-A-Phofung special economic zone	Free State Development Corporation	3 800	Dec 2016
Apr 2013	BP Capital Investment plan	BP Southern Africa	4 700	Jun 2018
Nov 2015	VWSA's investment plan	VWSA	4 500	Dec 2017
Aug 2012	Boikarabelo coal project	Resource Generation (ResGen)	4 500	Jul 2018
Oct 2010	Crossways Farm Village	CMAI Property Development	4 300	Dec 2017
Jun 2015	Vaal River City development project	Gauteng provincial government and the River City Development Company	4 000	Dec 2020
Nov 2006	Bridge City shopping and residential centre development	Joint venture between Moreland and eThekweni municipality	4 000	Dec 2019
Aug 2013	Scatec Solar photovoltaic (PV) power projects	Scatec Solar, through its joint venture company, Scatec Solar	3 955	Dec 2016

Major capex projects in the next five years

Announced date	Project Name	Company Name	Estimated value (m)	Estimated completion date
Jan 2011	Passenger Rail agency of SA (Prasa) rail signalling system	Passenger Rail Agency of SA	3 700	Dec 2018
Aug 2006	Boschendal redevelopment plan, Western Cape	Boschendal Property Company	3 800	Dec 2016
Jun 2014	Exxaro Belfast coal mine	Exxaro Resources	3 800	Dec 2017
Sep 2009	Mall of Africa – part of Waterfall City Mixed-Development project	Sanlam	3 500	Dec 2016
May 2013	Amakhala Emoyeni (Phase 1)	Department of Energy	3 475	Jun 2016
Nov 2005	IDC Titanium Project	Government and the IDC	3 280	Jun 2019
May 2008	The Houghton development project	Asvid Holdings	3 000	Dec 2018
Aug 2011	Rustenburg rapid transport project – Phase 1	Department of Transport	3 000	Mar 2016
Nov 2013	Shanghai Zendai Property – mixed use development	Shanghai Zendai Property	3 000	Dec 2017
May 2009	Eastern Cape roads repair project	Eastern cape Department of Roads and Transport	3 000	Mar 2019
Feb 2015	Masingita City	Township realtors (S) Pty Ltd	3 000	Dec 2018
Mar 2015	Ngqura liquid-bulk terminal storage	Oil tanking Grindrod Calulo Holdings	2 900	Mar 2019
Jun 2014	Royal Bafokeng Platinum housing development	Royal Bafokeng Platinum's (RBPlat's)	2 800	Dec 2020

Moving forward



The private sector is well regarded globally, ...



- Financial market development: 12th out of 140 countries
 - 1st Financing through local equity market
 - 2nd Regulation of securities exchanges
 - 6th Availability of financial services
 - 8th Soundness of banks
 - 21st Affordability of financial services
 - 32nd Ease of access to loans
 - 47th Venture capital availability
 - 63rd Legal rights index
- Market size: 29th out of 140 countries
 - 27th Domestic market size index
 - 29th GDP (PPP\$ billions)
 - 36th Foreign market size index
 - 94th Exports as a percentage of GDP



- Business sophistication: 33rd out of 140 countries

- 24th Extent of marketing
- 26th Willingness to delegate authority
- 31st Control of international distribution
- 33rd State of cluster development
- 38th Local supplier quality
- 39th Production process sophistication
- 51st Local supplier quantity
- 56th Value chain breadth
- 70th Nature of competitive advantage

- Innovation: 38th out of 140 countries

- 31st University-industry collaboration in R&D
- 32nd Company spending on R&D
- 32nd Capacity for innovation
- 33rd Quality of scientific research institutions
- 46th PCT patents, applications/million pop.
- 106th Availability of scientists and engineers
- 119th Gov't procurement of advanced tech products

... with a number of competitive strengths ...



- Goods market efficiency: 38th out of 140 countries (institutions)
 - 13th Effectiveness of anti-monopoly policy
 - 32nd Total tax rate, % profits
 - 40th Effect of taxation on incentives to invest
 - 43rd Intensity of local competition
 - 46th Extent of market dominance
- Technological readiness: 50th out of 140 countries
 - 19th Int'l Internet bandwidth, kb/s per user
 - 28th Firm-level technology absorption
 - 41st Availability of latest technologies
 - 63rd Mobile-broadband subscriptions/100 pop.
 - 64th FDI and technology transfer
 - 71st Individuals using Internet, %
 - 93rd Fixed-broadband internet subscriptions/100 pop.

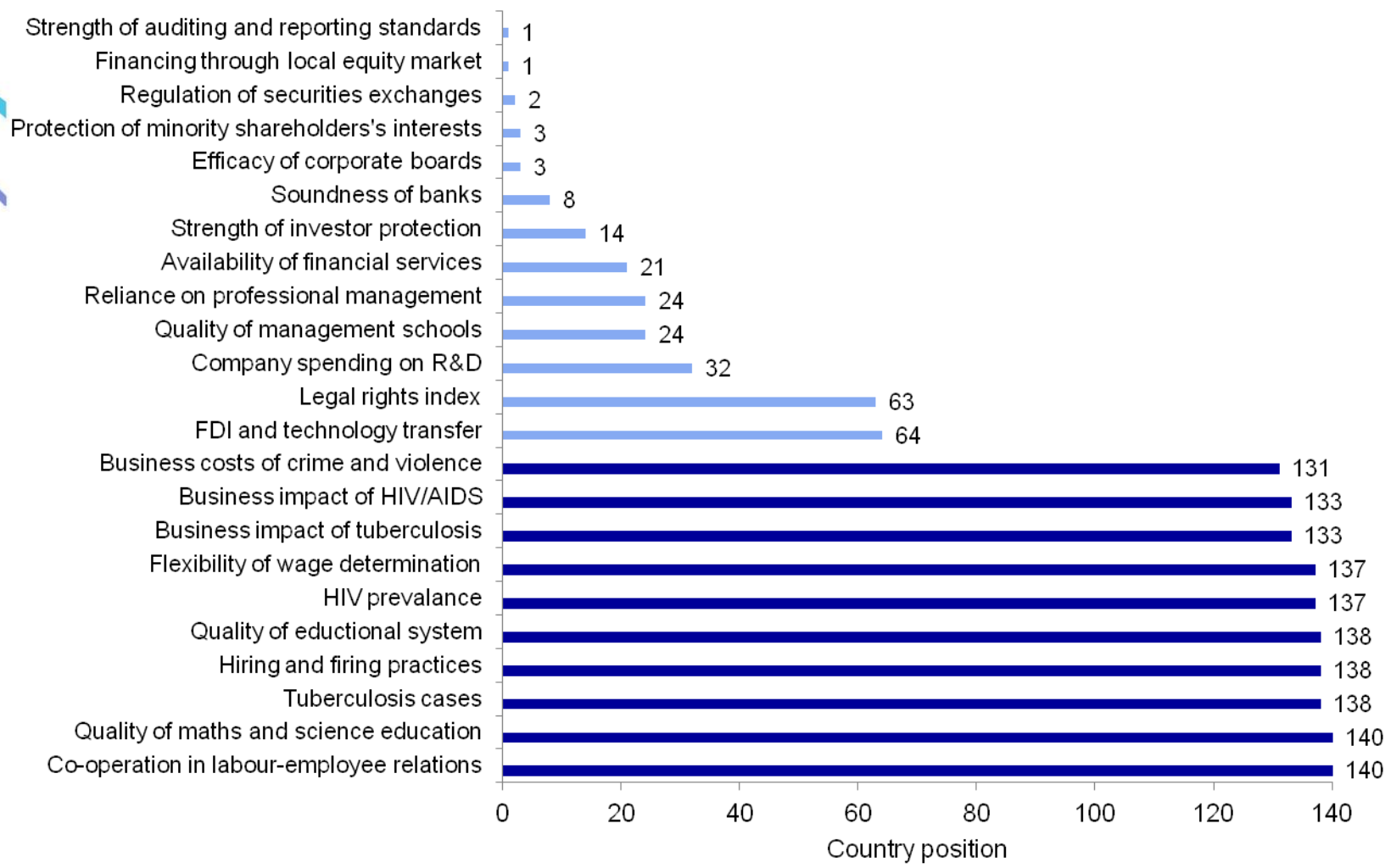


- **Governance: 38th out of 140 countries (institutions)**
 - 1st Strength of auditing and reporting standards, and for regulation of securities exchange
 - 3rd Protection of borrowers/lenders legal rights and of minority shareholders interests
 - 3rd Efficacy of corporate boards, 14th strength of investor protection
 - 98^h Public trust in politicians, 94th diversion of public funds
 - 105th Favouritism of government officials, 120th burden of government regulations
- **Infrastructure: 68th out of 140 countries**
 - 59th Quality of overall infrastructure
 - 14th Quality of air transport infrastructure
 - 116th Quality of electricity supply
- **Human Development: 126th out of 140 countries (health education)**
 - 127th Life expectancy years
 - 127th Quality of primary education
 - 138th Quality of education system
 - 140th Quality of math and science education

... is weak on a global comparison basis, as is labour market efficiency, ...

- In contrast to the well performing private sector, public sector service delivery remains very poor on a global comparison scale.

South Africa's 2013 rankings: top sectors (blue) vs bottom (dark blue)



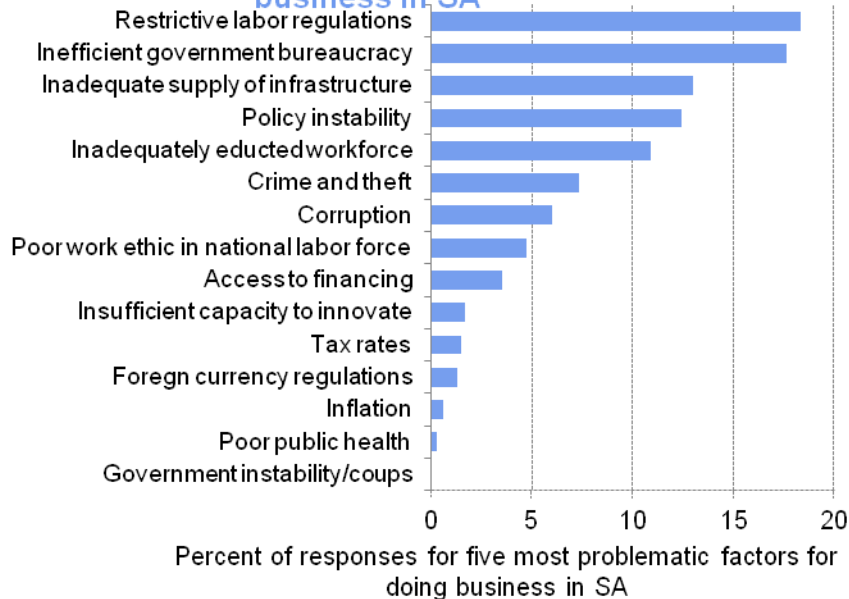


- Higher education and training: 83rd out of 140 countries (institutions)
 - 12th Secondary education enrolment, gross %
 - 19th Extent of staff training
 - 24th Quality of management schools
 - 41st Availability of specialized training services
 - 93rd Tertiary education enrolment, gross %
 - 119th Internet access in schools
 - 138th Quality of the education system
 - 140th Quality of math and science education
- Labour market efficiency: 107th out of 140 countries
 - 24th Reliance on professional management
 - 29th Redundancy costs, weeks of salary
 - 30th Effect of taxation on incentives to work
 - 46th Country capacity to attract talent
 - 61st Country capacity to retain talent
 - 86th Women in labour force, ratio to men
 - 127th Pay and productivity
 - 137th Flexibility of wage determination
 - 138th Hiring and firing practices
 - 140th Cooperation in labour-employer relations

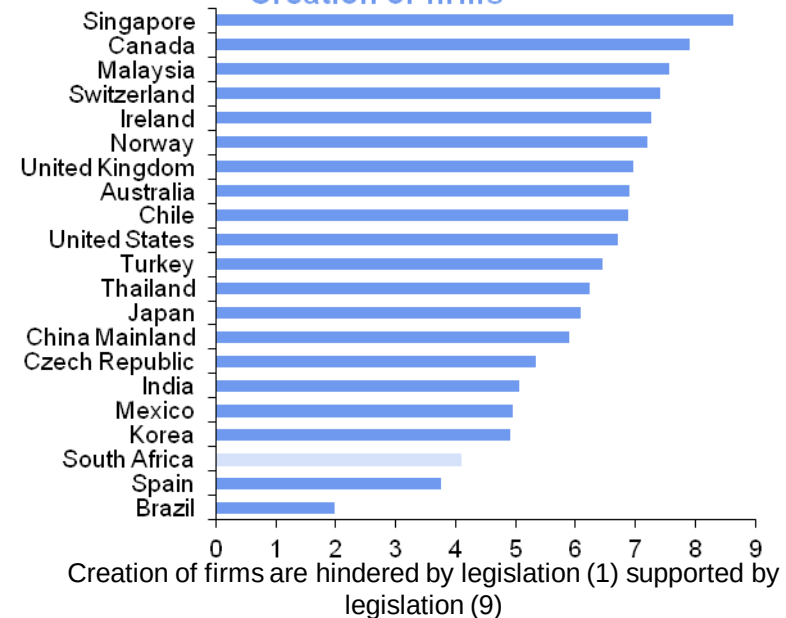
The eight point plan with government and business working together, ...

- Uniting behind a cohesive narrative and plan;
- Over-delivery on fiscal consolidation;
- Businesses accept an increase in the marginal tax rates for wealthy individuals;
- More effective management of state-owned enterprises, by appointing, for example, professionals to their boards;
- Accelerated public private-partnerships;
- A review of legislative implementation to ensure consistency and certainty;
- Ensuring that labour legislation contributes to inclusive growth, especially of the youth;
- The appointment of a standing anti-corruption committee to combat graft in both the public and private sectors.

The most problematic factors for doing business in SA

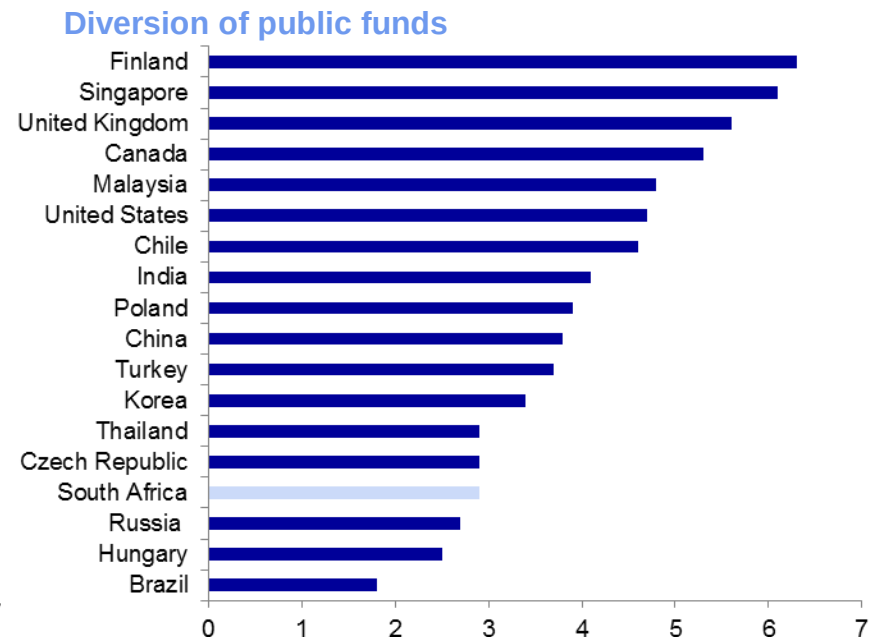
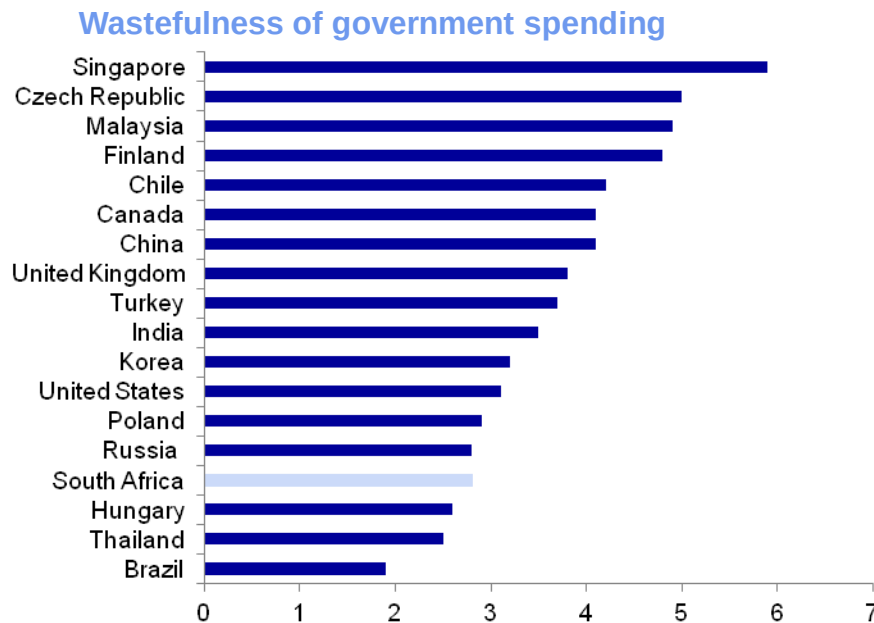


Creation of firms



... if fully implemented could eventually reverse ...

- The World Bank adds that the “NDP lists several critical factors for its successful implementation; focused leadership that provides policy consistency; ownership of the plan by all formations of society, strong institutional capacity at technical and managerial levels, efficiency in all areas of government spending including management of the public service wage bill and making resources available for other priorities, and prioritization and clarity on levels of responsibility and accountability at every sphere of government as well as a common understanding of the roles of business, labor and civil society.”
- However, the World Bank says the political crisis in SA has kept business confidence in SA low (and the rand weak). Weak business/investor confidence is a major impediment to faster economic growth and investment in SA, and SA’s doing business ranking is slipping.



Source: IMD World Competitiveness Yearbook 2015/Global Competitiveness Report 2015/16

... the downward trend in SA's growth, leading to faster, sustained growth ...

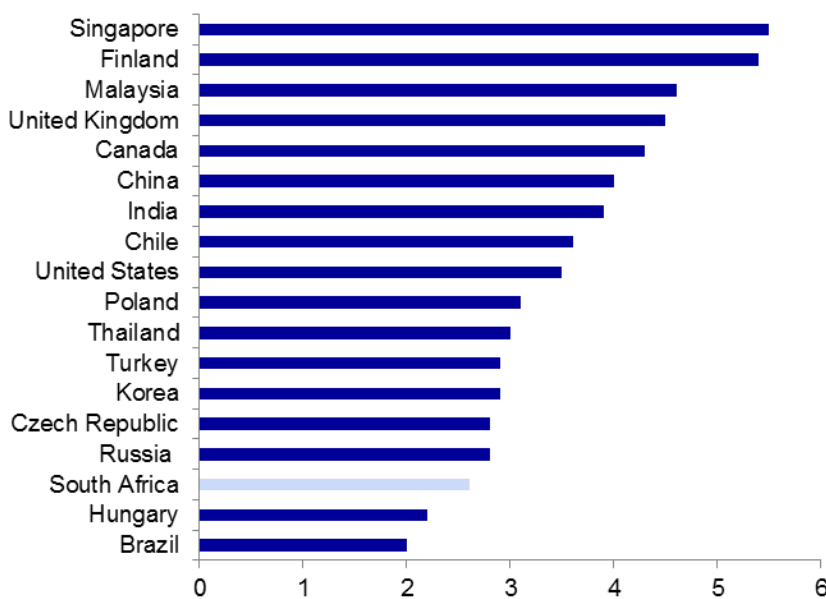
- Creation of new businesses is critical for sustained faster economic growth.
- The World Bank highlights that “(e)conomies around the world have taken steps making it easier to start a business—streamlining procedures by setting up a one-stop shop, making procedures simpler or faster by introducing technology and reducing or eliminating minimum capital requirements.”
- “Globally, South Africa stands at 120 in the ranking of 189 economies on the ease of starting a business “, slipping down from 113 in 2015 on high costs, long delays or bottlenecks reflected in a large number of procedures.

Topics	DB 2016 Rank	DB 2015 Rank	Change in Rank
Starting a Business	120	113	↓ -7
Dealing with Construction Permits	90	82	↓ -8
Getting Electricity	168	168	No change
Registering Property	101	97	↓ -4
Getting Credit	59	52	↓ -7
Protecting Minority investors	14	12	↓ -2
Paying Taxes	20	19	↓ -1
Trading Across Borders	130	130	No change
Enforcing Contracts	119	117	↓ -2
Resolving Insolvency	41	38	↓ -3
Doing Business 2016	Doing Business 2015	Change in Rank	
73	69	-4	↓

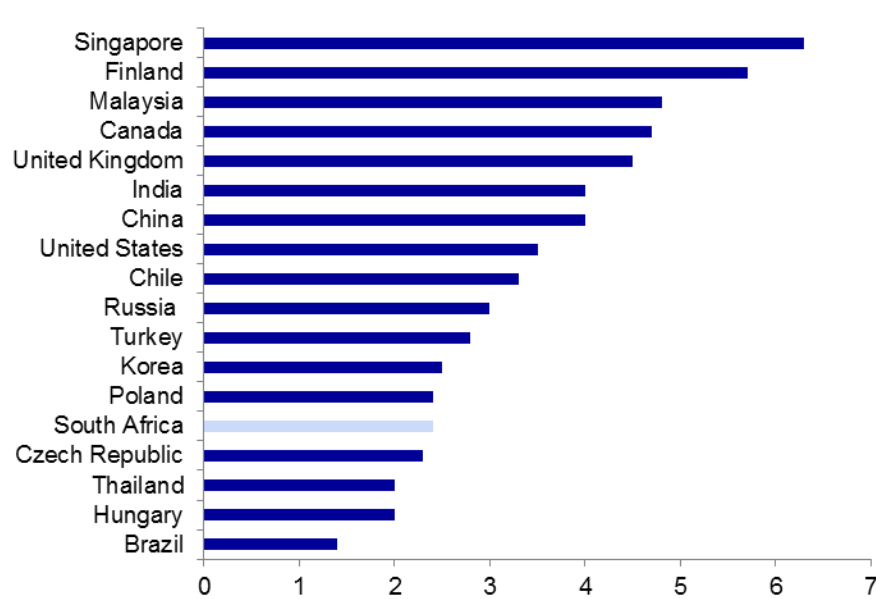
... and so allow SA's credit ratings to stabilise, and even eventually improve.

- The IMF highlights that “(i)n emerging market and developing economies, policymakers should reduce macroeconomic and financial vulnerabilities and rebuild resilience, including by implementing productivity enhancing reforms.”
- “In some commodity exporters, ... financial strains may limit the room to implement a gradual adjustment (to “durably lower commodity revenues and new, more diverse growth models”).”
- On SA the IMF highlights elevated policy uncertainty as key reason for expected slower growth.
- SA needs to strengthen its property rights to increase business confidence and so growth.

Favouritism in decisions of government officials



Public trust in politicians



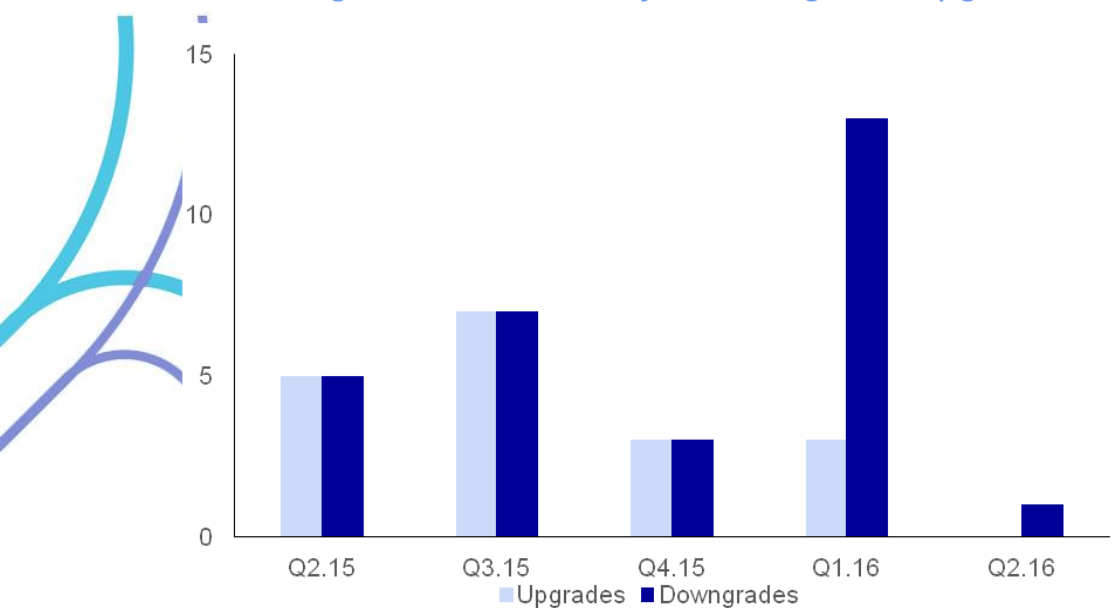
To what extent do government officials show favouritism to well-connected firms and individuals when deciding upon policies and contracts? (1) always show favouritism (7) never show favouritism

Credit rating outlook

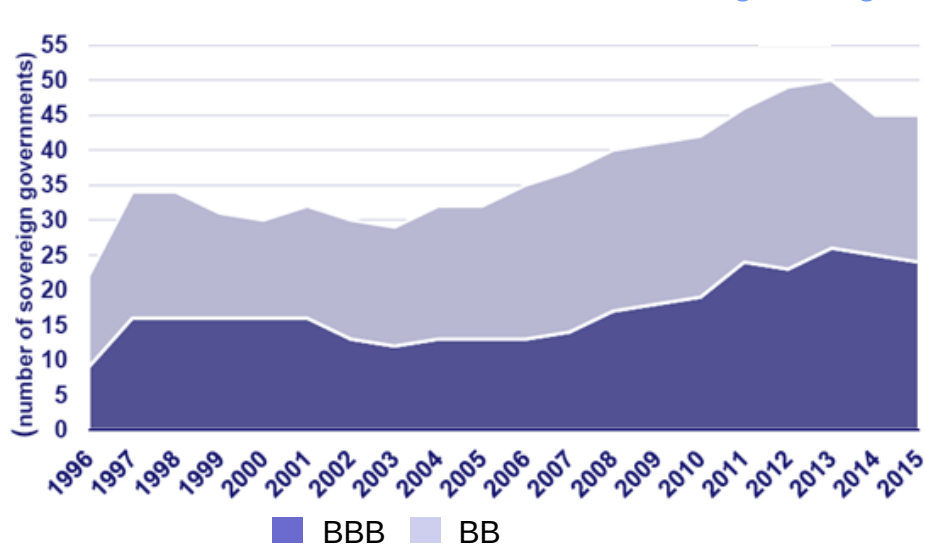


Globally S&P shows more downgrades are occurring than upgrades...

More downgrades are currently occurring than upgrades



Growth and distribution of BBB/BB sovereign ratings



Sovereigns currently rated	
BBB	BB
Colombia	Bahrain
Iceland	Brazil
India	Bulgaria
Italy	Costa Rica
Kazakhstan	Croatia
Mexico	Cyprus
Morocco	Guatemala
Panama	Hungary
Peru	Indonesia
Philippines	Portugal
Poland	Russia
Romania	Serbia
South Africa	Turkey
Spain	Vietnam
Thailand	Azerbaijan
Uruguay	Bangladesh
Andorra	Bolivia
Aruba	Dominican Republic
The Bahamas	Georgia
Turks and Caicos Islands	Jordan
Malta	Macedonia
Montserrat	Paraguay
Oman	Suriname

Outlook:

- 
- We continue to believe that the next move from Standard & Poor's (and next rating agency move) will be a downgrade on the local currency front (currently BBB+, to BBB) not on the hard currency front (now BBB-), to bring greater alignment between the two.
 - This could occur at the June 2016 review, but does not deliver a sub-investment grade outcome.
 - We believe that unless South Africa enters the down case, we will not see a sub-investment grade rating delivered this year from any of the agencies.
 - We have low economic growth forecast out to 2020 on the expected downgrade, rand weakness or at best stability despite FOMC more dovish, and higher interest rates.
 - SA could see its local currency rating revised lower to BBB- next year at the earliest (from our expectation that it will drop to BBB this year) if economic growth continues around 1.0% y/y or deteriorates further. First the local currency rating would be placed on a negative outlook however.
 - From a hard (foreign) currency rating perspective, SA is at risk of falling into the sub-investment grade category, as the outlook is negative, and while it is not impossible this could be delivered in June, we continue to believe it is less likely than the local currency alignment (downgrade) .

Our down case is a loss of the foreign currency sovereign investment grade ...

- 
- South Africa continues to approach the down case as the global commodity slump intensifies, while domestically interest rate hikes have been quite rapid, even though globally monetary policy is dovish, as the global economic slowdown has been seen to worsen.
 - On the positive side, strike action in the private sector has waned in SA, while load shedding is reduced and additional electricity capacity has come on line. The drought has worsened however, increasing the risk of recession, with the industrial sector already in recession.
 - The rand has seen substantial weakness, both on concern over credit rating downgrades and as EM currencies weakened earlier in the year, although recently EM currencies saw some strength.

Down case forecasts, real % growth y/y		2015	2016	2017	2018	2019	2020
GDP (%)		0.2	-1.9	-0.4	2.0	2.4	2.5
HCE (%)		1.0	0.8	1.2	1.7	2.4	2.9
GCE (%)		-0.3	-0.3	1.0	0.8	0.8	1.8
GFCF (%)		0.4	-2.5	3.2	3.3	4.8	5.0
Export (goods & non-factor services) - %		4.9	-2.0	2.2	6.4	6.3	8.2
Imports (goods & non-factor services) - %		3.6	5.4	7.8	9.1	5.6	9.7
Balance: Current Account (sa) - % GDP		-4.1	-2.5	-6.0	-5.9	-5.6	-5.3
Consumer Inflation (Av: %)		4.6	3.4	4.7	5.2	5.0	5.3
Prime Overdraft Rate (year-end: %)		6.25	8.50	10.00	10.50	10.75	10.75
Interest rate (R186), long-term (year-end: %)		8.60	10.50	12.00	13.50	14.00	12.22
Rand/USD		12.76	18.53	16.53	15.63	14.43	12.46

SOURCE: INVESTEC

... as SA's hard currency rating falls to speculative grade, ...



- Global risk aversion has always impacted the rand very substantially as it is a highly liquid, heavily traded currency, with up to a US\$25bn daily turnover recorded. However, the risk of SA seeing its benchmark rating (sovereign foreign currency long-term rating) fall to sub-investment grade (as it is currently on the last rung of investment grade) has materially weakened the rand.
- Countries which do not have investment grade ratings have higher borrowing costs, which would also complicate SA's fiscal consolidation, should it occur as long-term interest rates rise.
- The SA Reserve Bank estimates that “a downgrade below investment grade is likely to increase short-term rates by 80 basis points. Long-term bond yields would be expected to move more, rising by 104 basis points.”
- “As countries move from the investment grade region into the speculative zone, costs do not rise in a linear trend. Instead, the curve steepens. This indicates that markets attribute less significance to variations within the investment grade space than they do beyond it”.
- Under speculative grade (down case) SA enters recession, for five quarters, rand weakness, interest rates are higher than in expected case.
- The rating agencies have estimated it takes about seven years to regain investment grade rating once it has been lost.

... the extreme down case sees a loss of both the foreign currency and local investment grade sovereign ratings.



- The scenario sees the global economy falls into recession (and SA depression which is ten or more quarters of negative growth), with the commodity cycle falling substantially further.
- Domestically, unfettered populism occurs resulting in government overspending and slow economic growth leading to sovereign debt default, resulting in sovereign debt restructure and haircuts on sovereign debt, and civil unrest. Complete loss of private sector property rights under state custodianship, this process is already underway in part.
- All of SA's credit rating drop to speculative grade, some primary delistings from the JSE occur.

Extreme Down case forecasts, real % growth y/y		2015	2016	2017	2018	2019	2020
GDP (%)		1.3	-1.6	-5.5	-2.4	0.6	2.1
HCE (%)		1.5	0.5	-2.2	-2.6	-1.1	1.8
GCE (%)		0.2	-0.4	-0.1	-0.3	-1.9	-3.8
GFCF (%)		0.8	-2.2	-5.1	-6.9	0.4	6.4
Export (goods & non-factor services) - %		8.9	-0.9	3.2	18.0	18.3	14.5
Imports (goods & non-factor services) - %		5.6	5.2	8.9	12.0	12.0	12.0
Balance: Current Account (sa) - % GDP		-4.1	-6.6	-8.4	-8.2	-7.9	-7.6
Consumer Inflation (Av: %)		4.6	8.9	9.8	9.4	8.7	8.3
Prime Overdraft Rate (year-end: %)		6.25	9.50	13.00	18.00	16.50	14.00
Interest rate (R186), long-term (year-end: %)		8.60	13.30	16.60	23.00	20.5	15.00
Rand/USD		12.76	20.00	24.15	26.45	27.65	28.60

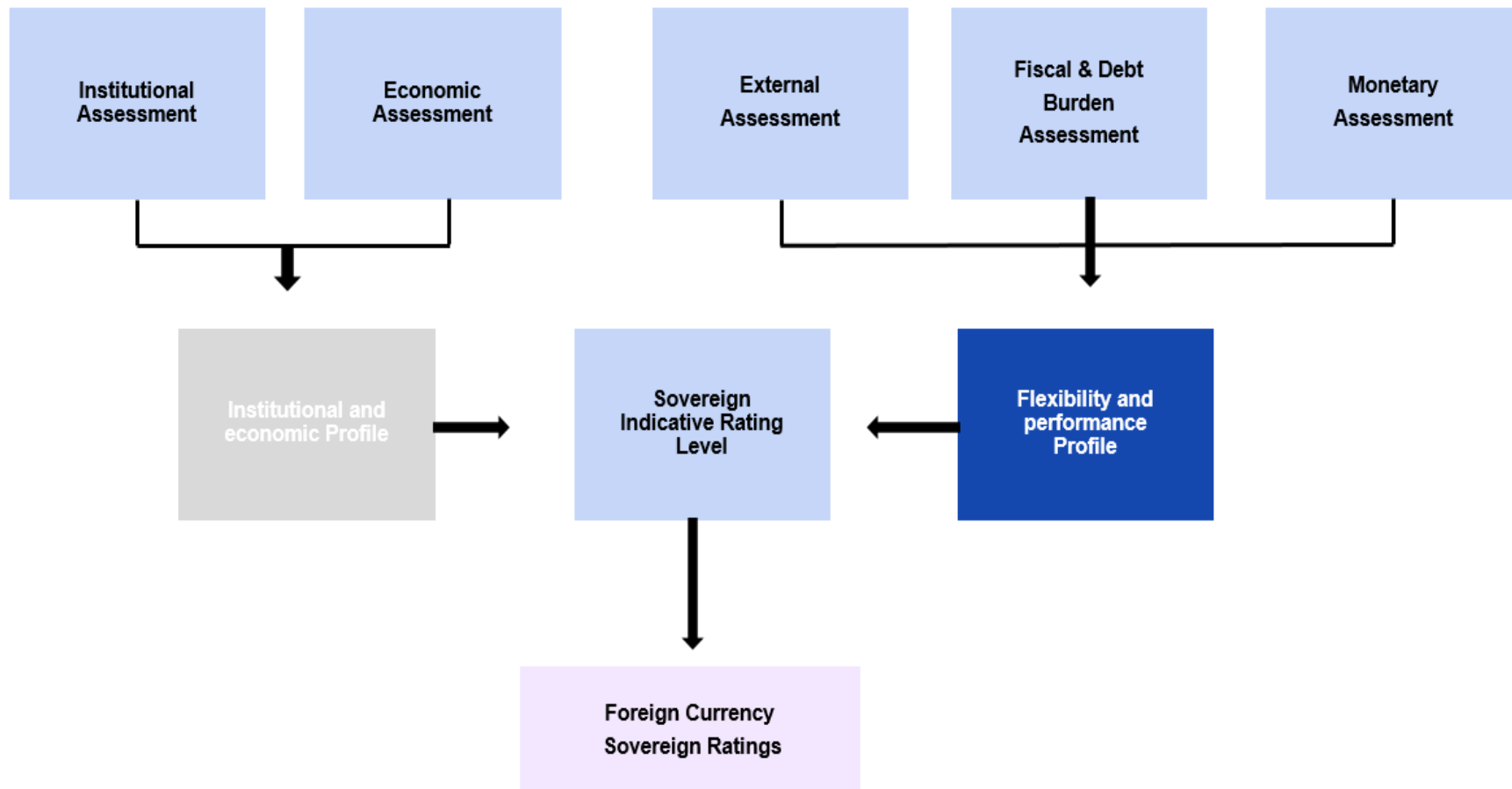
Source: Investec

What could improve South Africa's credit ratings? ...

Triggers for outlook revision to stable

- Policy implementation that lifts business confidence and private sector investment, and so ultimately results in higher GDP growth

Transparent Framework For Sovereign Ratings

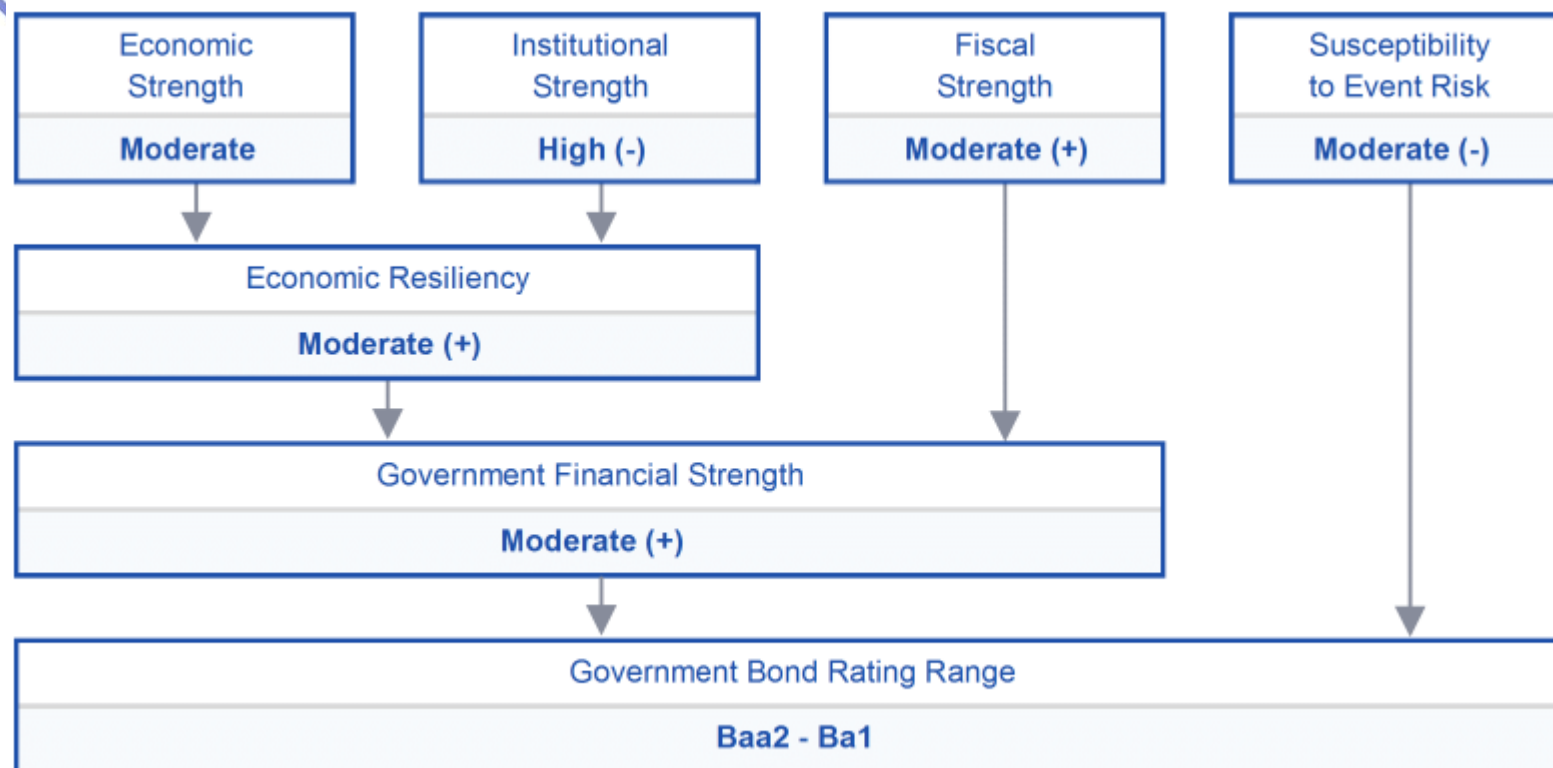


What could improve South Africa's credit ratings? ...

Factors that Could Lead to Confirmation of the Rating at the Current Level

- Maintain spending restraint,
- Succeed in the delivery of planned structural reforms,
- Achieve the fiscal consolidation envisioned in the 2016/17 Budget Review,
- And thereby reverse the deterioration in key credit metrics witnessed in the past few years.

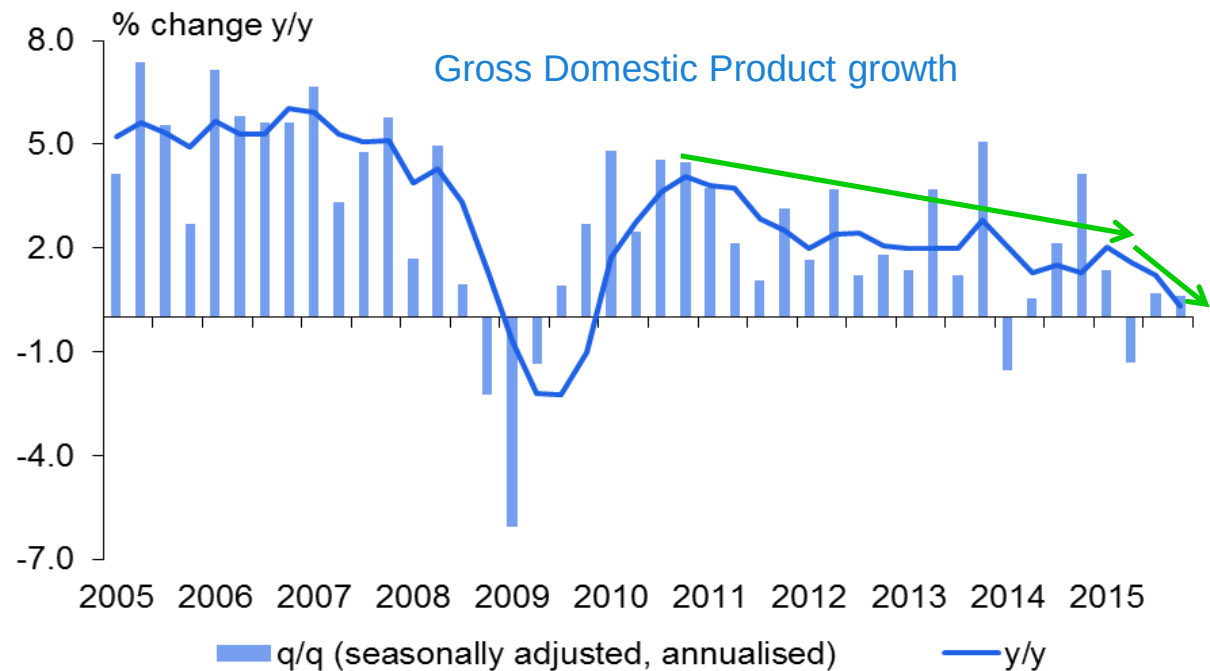
South Africa's sovereign rating are dominated by four factors



Appendix



The credit rating agencies are reacting to the material downward trend in SA's growth since 2011, which has accelerated recently, ...



Rating History		
Date	Long-term Foreign Currency	Long-term Local Currency
4 Dec 2015	BBB-	BBB
10 Jan 2013	BBB	BBB+
25 Aug 2005	BBB+	A
2 May 2003	BBB	A-
27 Jun 2000	BBB-	BBB+
19 May 2000	BB+	BBB+
5 Jun 1996	BB	BBB
22 Sep 1994	BB	-

... as have a number of other forecasters.



South Africa Economic Forecast Summary, 2016-17 % of change, volume (2010 prices) – Standard & Poor’s	2014	2015	2016	2017
GDP	1.5	1.3	0.8	1.8
Real private consumption	1.4	1.6	1.0	1.6
Real fixed investment	(0.4)	1.4	0.3	1.9
Real exports of goods and services	2.6	9.0	2.3	4.3
Real imports of goods and services	(0.5)	5.7	3.0	5.0
Inflation (annual average, %)	6.1	4.6	6.5	6.0
Unemployment rate (%)	25.1	25.4	25.5	25.9

Macroeconomic performance and projections National Treasury	2014	2015	2016	2017	2018
GDP (%)	1.5	1.3	0.9	1.7	2.4
HCE (%)	1.4	1.4	0.7	1.6	2.2
GCE (%)	1.9	0.4	1.2	-0.2	0.2
GFCF (%)	-0.4	1.1	0.3	1.4	2.7
GDE (%)	0.6	0.1	1.1	1.7	2.2
Export (%)	2.6	9.5	3.0	4.6	5.2
Imports (%)	-0.5	5.3	3.7	4.5	4.9
Consumer Inflation (Av: %)	6.1	4.6	6.8	6.3	5.9

A number of factors underpin SA's current ratings, ...

Moody's Baa2 (equivalent to BBB)

- 
- Complementary monetary, fiscal and exchange-rate framework;
 - Moderate external exposure that reduces vulnerabilities to exchange-rate volatility and a persistent current account deficit;
 - Abundant natural resources;
 - A deep and sophisticated financial market and a well-capitalized and regulated banking system;
 - Dominant role in the African economy.

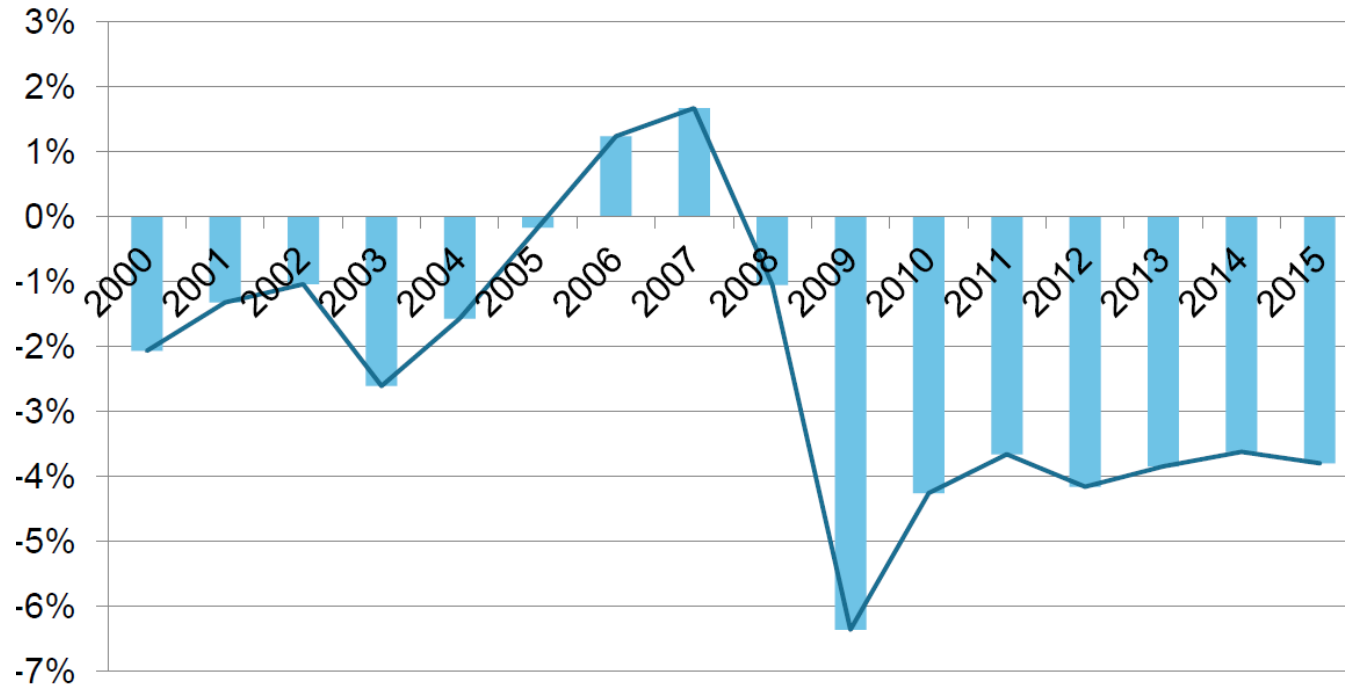
Fitch BBB-

- Foreign-currency debt and deposit dollarisation are low, reducing the exposure to exchange rate shocks. The floating currency helps absorb shocks to external demand.
- The banking system is strong, with a banking system indicator of 'bbb'. Financing flexibility is supported by deep, local markets.
- Government debt is largely denominated in local currency (90%), and government bonds have a long maturity of 13.8 years, limiting exchange rate and rollover risk. The central government has deposits equivalent to 5.3% of GDP.
- South Africa scores better than the 'BBB' range median on the World Bank's governance indicators. It benefits particularly from strong fiscal and monetary institutions.
- The country has a wealth of natural resources, including gold, platinum, palladium, diamonds, coal and iron. However, dependence on minerals adds to the volatility of export earnings.

... post the global financial crisis SA's fiscal consolidation has been slow ...



General Government Balance (% of GDP)



Risks To Fiscal Consolidation (S&P)

- GDP growth may impact on tax revenue collections
- Rising exposures to state owned entities with weak balance sheets
- Rising debt servicing costs as domestic interest rates increase

... along with its macroeconomic rankings.



- 2016

- Macroeconomic environment: 85th out of 140 countries

- 94th Government budget balance, % GDP
- 75th General government debt, % GDP
- 101st Gross national savings, % GDP
- 108th Inflation, annual % change
- 51st Country credit rating, 0-100 (best)

- 2008

- Macroeconomic environment: 50th out of 131 countries

- 48th Government budget balance, % GDP
- 49th General government debt, % GDP
- 103rd Gross national savings, % GDP
- 70th Inflation, annual % change
- 43rd Interest rate spread

South Arica's sovereign rating's negative outlook means there is ...

External Factors

- Weak external demand
- Low commodity prices

Domestic factors

- Electricity supply constraints
- Labour issues in the real sectors
- Weak business confidence (low private sector investment)
- Policy implementation challenges

Risks to fiscal consolidation

- Low GDP growth may impact on tax revenue collections
- Rising exposures to state owned entities with weak balance sheets
- Rising debt servicing costs as domestic interest rates increase

Rating Pressures

- Lower GDP growth
- SOEs risks and overall reduction in fiscal flexibility
- Increase in external imbalances

... pressure for further downgrades.



Moody's Baa2 (equivalent to BBB)

- stabilizing the public finances amidst slow growth;
- weak labor productivity exacerbated by deteriorating terms of trade;
- low national savings rate;
- high unemployment and wide income disparities that add to social tensions.

Fitch BBB-

- General government debt is high, and is expected to peak at 52.4% of GDP in 2017.
- The current account is sizeable, at a forecast 4.3% of GDP in 2015, and net external debt, projected at 12.2% of GDP at end-2015, is above the peer median.
- GDP per capita is below the 'BBB' range median, but above the 'BB' median. The country has one of the most unequal income distributions in the world, as shown by a Gini coefficient of 0.65 in 2011 and only 42.6% of the working-age population have a job.
- Inflation is high, at close to the upper end of the South African Reserve Bank's target range of 6%.
- GDP growth has averaged 2.1% in the five years to 2015, compared with a peer median of 3%. Growth is held back by electricity shortages, fractious labour relations, skill mismatches in the labour force and slow progress in improving the business environment.

Country credit ratings: the A tier



S&P	Fitch	Moody's	Rating
AAA	AAA	Aaa	Investment grade
Germany (stable)	Germany (stable)	Germany (stable)	
Canada (stable)	Canada (stable)	Canada (stable)	
UK (negative)	US (stable)	US (stable)	
Australia (stable)	Australia (stable)	Australia (stable)	Investment grade
AA+	AA+	Aa1	
US (stable)	UK (stable)	UK (stable)	
AA	AA	Aa2	
France (negative)	France (stable)	France (stable)	Investment grade
AA-	AA-	Aa3	
China (stable)		China (negative)	
Chile (stable)		Chile (stable)	
A+	A+	A1	Investment grade
Ireland (stable)	China (stable)		
Japan (stable)	Chile (stable)	Japan (stable)	
A	A	A2	
	Japan (stable)		Investment grade
	Ireland (stable)		
A-	A-	A3	
		Mexico (stable)	



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