5

Asset and liability management

Overview

Over the past three years, public debt has risen to support infrastructure investment, and to fund economic and social priorities. Over the medium term, the fiscal stance will stabilise the growth of debt and maintain long-term sustainability, ensuring that debt and debt-service costs do not crowd out productive expenditure.

Borrowing requirement has risen in the wake of the 2009 recession

In 2012/13, government's net borrowing requirement is expected to reach R168.8 billion, up from R152.7 billion in 2011/12, while state-owned entities will borrow an estimated R76.9 billion to fund their capital expenditure programmes. Development finance institutions will borrow a projected R13.9 billion to meet developmental funding commitments. After increasing in line with budget deficits, government's net debt stock is expected to peak at 38.5 per cent of GDP in 2014/15. As the fiscal position improves over time, debt and debt-service costs will stabilise.

Owing to prudent macroeconomic policies, and deep and liquid capital markets, the state is able to finance its borrowing requirement mainly in the domestic market. Government's debt instruments remain attractive to global investors, as demonstrated by a successful US$1.5 billion global bond issue in January 2012. Global investors increased their holdings of South African domestic bonds from 12.8 per cent in 2008 to 29.1 per cent in 2011.

Global investors increased their holdings of South African bonds during 2011

State-owned entities and development finance institutions will continue to invest and fund infrastructure development that promotes long-term growth. Government will ensure that these institutions remain financially stable, and facilitate cost-effective funding, enabling them to deliver on their mandates.

Reports on debt management will complement investor road shows and new website

As part of its commitment to transparency, the National Treasury will begin publishing yearly reports on South Africa's public debt management. The first such report will be produced by end-June 2012, complementing regular domestic and international road shows and the recent launch of an investor relations website.

This chapter reviews debt market developments and the debt management strategy, outlines borrowing and financing trends, and discusses the role of state-owned entities and development finance institutions.

Key medium-term indicators

- Net borrowing requirement of R168.8 billion in 2012/13, decreasing to R140.9 billion in 2014/15.
- Annual Treasury bill net issuance of R22 billion over the medium term.
- Two new fixed-income and three new inflation-linked domestic bonds.
- Borrowing of US$3 billion in the international capital market over the medium term.
- Switches (exchanges) in domestic and foreign bonds.
- Net loan debt of 36 per cent of GDP in 2012/13, increasing to 38.5 per cent (R1.5 trillion) in 2014/15.
- Debt-service costs peak at 2.8 per cent of GDP in 2013/14 and decline thereafter.

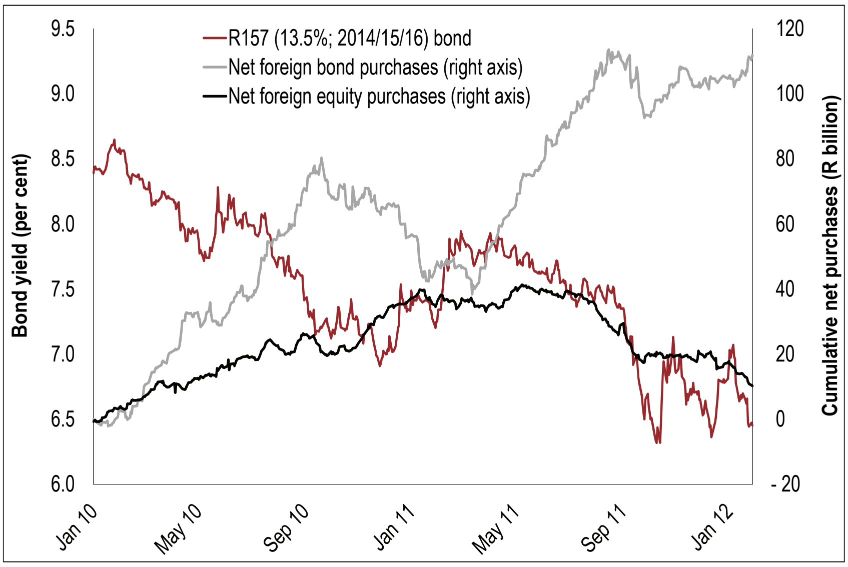
Developments in South Africa's debt markets

Domestic bond market

Domestic bond market benefited from asset reallocation towards higher-yielding emerging markets

Over the past year concerns about the continuing European debt and banking crises intensified, contributing to shifts in capital flows. While there was a "flight to safety" toward some developed countries, South Africa's bond market benefited from asset reallocation towards higher-yielding emerging markets. Net bond purchases by foreign investors reached R48 billion for the year (2010: R56 billion). In contrast, equity purchases recorded a net foreign outflow.

Figure 5.1 Bond yields and cumulative net bond and equity purchases by non-residents, 2010 – 2012



Source: Bloomberg

Weekly bond issuances of R3 billion in 2011 were matched by increased appetite for government debt, leading to a robust performance of the fixed-income market. The BEASSA All Bond Index increased by 8.8 per cent during 2011, compared with the JSE Equity All Share Index (up 2.6 per cent for the year) and cash (STeFI, 5.7 per cent).

Strong growth in appetite for government debt in 2011 outpaced performances of equities and cash

The Johannesburg Stock Exchange registered an increase of 23.7 per cent in annual bond turnover in 2011, reaching a record high of R20.9 trillion. The bond market is becoming an increasingly important source of funding for the private sector. During 2011, net issuance by corporations increased by R4 billion to R49 billion, with financial corporations responsible for the largest proportion of this issuance.

Outstanding municipal bonds increased from R11.6 billion in 2010 to R13.2 billion in 2011. Johannesburg, which accounts for 60 per cent of this market, issued R850 million in new debt and Ekurhuleni issued R800 million in new debt. Turnover in municipal debt, however, decreased by R6.9 billion to R17.1 billion.

Outstanding municipal bonds grew to R13.2 billion in 2011, but turnover decreased

During 2011, the domestic bond yield curve steepened, with the long end more than 50 basis points higher. Increased demand for inflation-linked bonds, together with higher-yielding long rates, suggests an expectation of higher inflation over the long term.

Domestic money market

During 2011, the Treasury bill rates were anchored by the monetary policy stance. The Reserve Bank kept the repurchase (repo) rate unchanged at 5.5 per cent.

Reserve Bank kept repo rate unchanged in 2011

International bond market

Emerging and developing economies were affected by higher risk aversion during 2011. Sovereign bond spreads and credit default swaps for emerging markets as a group continued to widen throughout the year.

Emerging markets issued sovereign debt in excess of US$20 billion at the beginning of 2012. South Africa also issued a 12-year, US$1.5 billion note. After two years of low and negative issuance in rand-denominated debt issued in Europe (Eurorand bonds) and Japan (Uridashi bonds), net issuances reached R7 billion and R10 billion respectively in 2011.

Managing the debt portfolio

Recent events in Europe have highlighted how large, poorly structured debt portfolios can make governments more vulnerable to financial and economic shocks. Government's debt management strategies are designed to ensure fiscal sustainability.

The primary aim of the debt management strategy is to meet the financing requirements of the public sector at the lowest possible cost. This is done within prudent risk levels and in support of government's broader economic policies. The principles of openness, transparency and predictability support this goal. Government works to develop the country's capital markets, maintains benchmark bonds, and actively manages the maturity structure and composition of debt.

Strategy is to meet the financing requirements of the public sector at the lowest possible cost

Diversifying funding instruments and benchmarking risk

Introduction of Islamic bonds (sukuk) under consideration

In recent years, to develop the domestic bond market and broaden the investor base, government expanded its portfolio from mainly Treasury bills and fixed-income bonds to include inflation-linked bonds, floating-rate notes and retail bonds. The introduction of Islamic bonds (sukuk) is now under consideration. The Treasury bill portfolio has been expanded from 91-day and 182-day bills to include 273-day and 364-day bills. Retail bonds were first issued in 2004 to bolster South African savings, and now consist of fixed- and inflation-linked bonds.

Government's risk management framework sets benchmarks for:

- Debt composition, limiting foreign debt to 20 per cent of total debt.
- The composition of domestic debt at 70 per cent fixed and 30 per cent non-fixed to reduce risks associated with interest rate increases and inflation.
- Smoothing the maturity structure – the schedule of debt repayments – to manage refinancing risk.

Government reduced the share of foreign debt to 5.4 per cent of total net debt in 2011/12

Financing in international capital markets is intended to meet government's foreign currency commitments, broadening the investor base and establishing benchmarks for state-owned entities to borrow. This strategy reduced the share of foreign debt as a proportion of total net debt from 19.9 per cent in 2007/08 to 5.4 per cent in 2011/12, reaching 2.9 per cent in 2014/15. Low levels of foreign debt reduce currency risk and contribute to the sustainability of the public finances.

Sovereign rating outlook

Persistent uncertainty in the global economy and the European debt crisis have increased pressure on credit rating agencies to communicate their ratings in a manner that reflects the changing environment.

From January 2011 to December 2011, 171 countries had their ratings reviewed by the major rating agencies (Moody's Investor Services, Standard & Poor's, Fitch Ratings, and Ratings and Investment Information Inc.). Of these, 31 countries were upgraded and 55 were downgraded; the ratings of 60 were affirmed; 21 were placed on credit watch; and 4 were assigned ratings for the first time.

South Africa has not been immune to this changing environment. Moody's Investor Services and Fitch Ratings have revised the outlook for South Africa from stable to negative, while affirming the country's long-term foreign currency ratings. The agencies report that the country's rating outlook could be affected negatively in the event of a serious deterioration in the fiscal position, citing lower-than-expected growth and high unemployment among their concerns.

South Africa's prudent macroeconomic policies, fiscal guidelines, debt management policies and sound constitutional institutions support a positive long-term rating outlook.

Domestic debt consists of fixed-income bonds and non-fixed rate debt instruments (short-term loans, floating-rate notes and inflation-linked bonds). Non-fixed rate debt increased from 26.3 per cent in 2007/08 to 36.3 per cent in 2011/12. Since the onset of the global crisis, government has increased the issuance of Treasury bills and inflation-linked bonds to finance the large borrowing requirement, resulting in a deviation from the 30 per cent risk guidelines. As the fiscal outlook improves, reliance on non-fixed rate debt will be reduced to the benchmark.

To improve the tradability of bonds and achieve a liquidity premium requires that large benchmark bonds are created at key maturities across the yield curve. To reduce near-term exposure to refinancing risk government will continue to exchange maturing bonds before due date for longer-dated bonds, in what is referred to as switch auctions or exchanges.

Consolidated borrowing and financing

Consolidated borrowing will increase to R152.3 billion in 2012/13 and decline to R120 billion in 2014/15

The consolidated government borrowing requirement includes the financing requirements of national and provincial government, the social security funds and national extra-budgetary institutions.

Consolidated borrowing in 2012/13 will increase to R152.3 billion before declining to R120 billion in 2014/15. The consolidated borrowing requirement is lower than that of the national government – mainly because of large investments held by the social security funds and capital reserves held by extra-budgetary institutions, which constitute prefunding for infrastructure investment. Extra-budgetary institutions also raise loans to finance large-scale infrastructure investment. These include the South African National Roads Agency Limited (SANRAL) and Trans-Caledon Tunnel Authority (TCTA) project loans, which amount to about R16.5 billion over the medium term.

Table 5.1 Financing of consolidated government net borrowing requirement, 2008/09 – 2014/15

	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15
R billion		Actual		Estimate		Medium-term estimates	
Budget balance[1]	**-25.0**	**-159.6**	**-116.7**	**-142.3**	**-153.5**	**-143.3**	**-121.5**
Extraordinary receipts and payments	3.9	5.8	2.2	3.9	1.2	1.5	1.5
Net borrowing requirement	**-21.1**	**-153.8**	**-114.5**	**-138.4**	**-152.3**	**-141.8**	**-120.0**
Domestic loans	45.9	177.1	176.6	169.5	151.1	157.5	141.3
Foreign loans	-3.7	23.9	4.7	4.4	-7.7	-5.0	-2.7
Change in cash and other balances[2]	-21.1	-47.1	-66.8	-35.5	8.9	-10.7	-18.6
Financing	**21.1**	**153.8**	**114.5**	**138.4**	**152.3**	**141.8**	**120.0**

1. A negative number reflects a deficit

2. A negative change indicates an increase in cash balances

National borrowing requirement

Net borrowing requirement of R168.8 billion in 2012/13

The net borrowing requirement for 2010/11, the revised estimate for 2011/12 and estimates for the medium term are set out in Table 5.2. In 2011/12, the net borrowing requirement is expected to amount to R152.7 billion, increasing to R168.8 billion in 2012/13 before declining to R140.9 billion in 2014/15.

Table 5.2 National government net borrowing requirement, 2010/11 – 2014/15

R million	2010/11 Outcome	2011/12 Budget	2011/12 Revised	2012/13	2013/14	2014/15
				Medium-term estimates		
National budget balance[1]	**-135 403**	**-159 066**	**-156 648**	**-170 025**	**-159 536**	**-142 358**
Extraordinary receipts	**3 010**	**1 350**	**4 435**	**1 200**	**1 500**	**1 500**
Premiums on bond transactions[2]	1 690	1 300	3 500	1 200	1 500	1 500
Special dividends	362	–	–	–	–	–
Saambou Bank curatorship	20	–	30	–	–	–
Revaluation profits on foreign currency transactions[3]	87	–	660	–	–	–
Liquidation of SASRIA investment	150	50	228	–	–	–
Equalisation Fund account transfer	700	–	–	–	–	–
Other[4]	1	–	17	–	–	–
Extraordinary payments	**-839**	**-150**	**-530**	**-24**	**–**	**–**
Premiums on loan transactions[2]	-227	–	–	–	–	–
Revaluation losses on foreign currency transactions[3]	-439	–	-384	–	–	–
Defrayal of GFECRA losses[5]	-173	-150	-146	-24	–	–
Borrowing requirement	**-133 232**	**-157 866**	**-152 743**	**-168 849**	**-158 036**	**-140 858**

1. A negative number reflects a deficit
2. Premiums received or incurred on new loan issues, bond switch and buy-back transactions
3. Revaluation profits or losses on government's foreign exchange deposits at the Reserve Bank when used to meet government's foreign currency commitments
4. Mainly penalties on early withdrawal of retail bonds
5. Realised losses on the Gold and Foreign Exchange Contingency Reserve Account

Extraordinary receipts and payments

Extraordinary receipts of R4.4 billion include R3.5 billion premiums on bond transactions

A total of R4.4 billion in extraordinary receipts is expected in 2011/12, consisting of premiums of R3.5 billion on bond transactions, proceeds of R228 million from government's liquidation of its investments in the South African Special Risk Insurance Association, revaluation profits of R660 million on foreign currency transactions and cash owed to government from the curatorship of Saambou Bank of R30 million. Over the medium term, premiums of R4.2 billion on bond transactions are projected.

Extraordinary payments of R530 million are expected in 2011/12. These consist of losses on the Gold and Foreign Exchange Contingency Reserve Account of R146 million and revaluation losses of R384 million on foreign currency transactions. In 2012/13 provision is made for losses of R24 million on the Gold and Foreign Exchange Contingency Reserve Account.

Where public enterprises hold assets not associated with service delivery, sale or reprioritisation of funds may be considered

Government is reviewing its substantial investments in enterprises and public entities. Some of these enterprises and entities hold cash, excess financial reserves or assets that are not associated with public-service delivery. Where such resources can be more productively applied to finance policy priorities, the sale of such assets, or the return of surplus funds to the fiscus, will be considered.

Financing the national borrowing requirement

Table 5.3 provides information on the funding of government's net borrowing requirement for 2010/11, revised estimates for 2011/12 and projections for the medium term.

Table 5.3 Financing of national government net borrowing requirement[1], 2010/11 – 2014/15

	2010/11	2011/12		2012/13	2013/14	2014/15
R million	Outcome	Budget	Revised	Medium-term estimates		
Domestic short-term loans (net)	**34 893**	**22 000**	**20 828**	**22 000**	**22 000**	**20 000**
Treasury bills	21 610	22 000	20 828	22 000	22 000	20 000
Corporation for public deposits	13 283	–	–	–	–	–
Domestic long-term loans (net)	**136 850**	**135 367**	**139 925**	**119 998**	**130 353**	**114 259**
Market loans	150 386	150 400	155 400	151 367	151 054	142 277
Redemptions[2]	-13 536	-15 033	-15 475	-31 369	-20 701	-28 018
Foreign loans (net)	**2 839**	**4 999**	**9 546**	**-7 492**	**-3 564**	**-305**
Market loans	5 151	7 150	12 025	4 035	10 590	7 320
Arms procurement loan agreements	470	1 009	985	183	25	–
Redemptions (including revaluation of loans)[3]	-2 782	-3 160	-3 464	-11 710	-14 179	-7 625
Change in cash and other balances[4]	**-41 350**	**-4 500**	**-17 556**	**34 343**	**9 247**	**6 904**
Cash balances	-48 456	-8 100	-21 156	30 743	5 647	3 304
Other balances[5]	7 106	3 600	3 600	3 600	3 600	3 600
Financing	**133 232**	**157 866**	**152 743**	**168 849**	**158 036**	**140 858**

1. A longer time series is presented in Table 1 of Annexure B
2. Domestic loan redemption figures are net of anticipated switches, reducing redemptions by R15 billion in 2013/14 and R34 billion in 2014/15
3. Foreign loan redemptions in 2014/15 are net of anticipated switches, reducing redemptions by R2.4 billion
4. A negative change indicates an increase in cash balances
5. Mainly surrenders of unspent money requested in previous financial years and late requests with regard to expenditure committed in previous years

The net borrowing requirement excludes loan redemptions – the repurchase of bonds at or before maturity – which also need to be financed. Scheduled loan redemptions are set out in Table 5.4. Loan redemptions in 2011/12 amount to R18.9 billion – R746 million higher than anticipated, mainly due to redemption of foreign loans at weaker-than-forecasted exchange rates and higher retail bond redemptions. Loan redemptions are projected to reach R35.6 billion in 2014/15.

Table 5.4 Loan redemptions, 2010/11 – 2014/15

	2010/11	2011/12		2012/13	2013/14	2014/15
R million	Outcome	Budget	Revised	Medium-term estimates		
Domestic loans	**13 536**	**15 033**	**15 475**	**31 369**	**20 701**	**28 018**
Foreign loans	**2 782**	**3 160**	**3 464**	**11 710**	**14 179**	**7 625**
Principal	2 439	2 998	2 982	14 030	13 530	6 940
Revaluation[1]	343	162	482	-2 320	649	685
Total	**16 318**	**18 193**	**18 939**	**43 079**	**34 880**	**35 643**
Excludes switch auctions:						
Domestic	–	–	–	–	*15 000*	*34 000*
Foreign	–	–	–	–	–	*2 438*

1. Forward estimates are based on projections of exchange rates

Domestic short-term loans

Domestic short-terms loans increased by R20.8 billion in 2011/12

Short-term borrowing consists of Treasury bill issuance and borrowing of surplus cash from the broader public sector through the Corporation for Public Deposits. In 2011/12, Treasury bill issuance increased by R20.8 billion to R157 billion. Demand for Treasury bills remained strong, with auctions on average oversubscribed by 2.3 times. Of the total amount of Treasury bills issued, 76 per cent is held by South Africa's commercial banks, and 1 per cent is held by international investors. Over the medium term, Treasury bill net issuance is expected to average R22 billion a year, concentrated in longer-dated maturities.

Table 5.5 Treasury bill issuance, 2011/12 – 2012/13

Maturity	2011/12			2012/13		2011/12	2012/13
R million	Opening balance	Net change	Closing balance	Net change	Closing balance	Weekly auction estimates	
91-day	49 725	-1 007	48 718	1 007	49 725	3 825	3 825
182-day	27 950	7 930	35 880	3 510	39 390	1 380	1 515
273-day	34 125	4 095	38 220	5 850	44 070	980	1 130
364-day	24 350	9 810	34 160	11 633	45 793	660	880
Total	**136 150**	**20 828**	**156 978**	**22 000**	**178 978**	**6 845**	**7 350**

Domestic long-term loans

Domestic long-term loan issuance amounts to R155.4 billion in 2011/12. Fixed-income bond issuance was concentrated in the longer maturities.

Table 5.6 Domestic long-term market loan issuance, 2011/12

As of 31 January 2012 R million	Cash value	Average yield %	Outstanding value
Fixed-income[1]	**92 842**	**8.31**	
R206 (7.5%; 2014)	4	6.96	31 861
R203 (8.25%; 2017)	13 033	7.71	77 241
R204 (8%; 2018)	8 267	8.09	72 975
R207 (7.25%; 2020)	11 565	8.16	86 080
R208 (6.75%; 2021)	15 258	8.29	77 627
R186 (10.5%; 2025/26/27)	11 094	8.47	95 709
R213 (7%; 2031)	10 217	8.78	25 264
R209 (6.25%; 2036)	8 225	8.67	52 067
R214 (6.5%; 2041)	11 046	8.79	23 740
Retail	4 133	7.47	11 517
Inflation-linked[2]	**32 807**	**2.51**	
R211 (2.5%; 2017)	102	1.29	19 141
R212 (2.75%; 2022)	7 832	2.45	22 723
R210 (2.6%; 2028)	7 546	2.56	27 276
R202 (3.45%; 2033)	17 247	2.53	55 611
Retail	80	1.51	223
Total	**125 649**		

1. Includes non-competitive auction allocations of R14 billion
2. Outstanding value is revaluated using the relevant reference inflation rate

Fixed-income bond issuance was concentrated in longer maturities during 2011/12

Bonds with a maturity of more than 12 years constitute 43.7 per cent of total fixed-income bond issuance. Over the next two years, domestic long-term loan issuance will average R151.2 billion, decreasing to R142.3 billion in 2014/15. It is anticipated that current weekly auction levels in domestic bonds will be broadly maintained in 2012/13.

The non-competitive auctions in domestic fixed-income bonds, which provide primary dealers a 48-hour option of taking up an additional 30 per cent of their allocation at the auction clearing yield, will remain a source of funding.

To create benchmark bonds and smooth the maturity structure, government will introduce five new bonds in 2012/13.

Table 5.7 New domestic bonds, 2012/13

Fixed-income		Inflation-linked	
Bond code	Maturity date	Bond code	Maturity date
R2023	28 February 2023	RI2025	31 January 2025
R2048[1]	28 February 2047	RI2038	31 January 2038
	28 February 2048		
	28 February 2049	RI2050[1]	31 December 2049
			31 December 2050
			31 December 2051

1. Bond of which the maturity value is split equally over three years

The two fixed-income bonds will have 11-year and 36-year maturities, and the three inflation-linked bonds will have 13-year, 26-year and 39-year maturities. To improve liquidity and manage refinancing risk, government will re-introduce bonds with the maturity split over three years, similar to the current R157 and R186 benchmark bonds.

Switch auction programme will continue to reduce refinancing risk

Government will continue with its switch auction programme in which short-term bonds are exchanged for longer-dated bonds. Over the past two years, this programme has reduced the maturity value of the R205 bond maturing on 31 March 2012 by R7.5 billion to R270 million and the revalued amount of the R189 bond maturing 31 March 2013 by R30.4 billion to R27.2 billion. Over the medium term, switch auctions to reduce the maturity value of the R206 (7.5 per cent; 2014) and R201 (8.75 per cent; 2014) bonds will be announced and switches (exchanges) in foreign bonds will also be considered.

Retail bonds worth R12.1 billion account for 1.1 per cent of total debt and aim to increase savings

Retail bonds amount to R12.1 billion or 1.1 per cent of total debt. During 2011/12, investments in retail bonds amounted to R4.6 billion, of which R1.3 billion were reinvestments of maturing bonds and capitalised interest. More retail bond products are under consideration.

Foreign loans

Despite challenging market conditions, government successfully issued a 30-year US$750 million bond in March 2011 and a 12-year US$1.5 billion bond in January 2012. The 30-year bond provides an ultra-long global benchmark for state-owned entities.

Global borrowing to maintain benchmarks in major currencies and meet foreign currency commitments

Over the medium term, government intends to borrow about US$3 billion in global markets to maintain benchmarks in major currencies and meet part of its foreign currency commitments. The balance of these commitments will be met from foreign currency bank balances and purchases of foreign currency in the domestic market. To diversify funding options, government is considering entering the sukuk market. Banking institutions have been invited to submit proposals on advisory services for the structuring and issuing of such bonds.

Drawdowns on the arms procurement loan agreements in 2012/13 amount to R183 million, with final drawdowns of R25 million in 2013/14.

Cash balances

Table 5.8 shows the projected change in government's cash balances over the medium term. Government's total cash consists of deposits in rands and in foreign currency held with commercial banks and the Reserve Bank.

Table 5.8 Change in cash balances, 2011/12 – 2014/15

	2011/12		2012/13	2013/14	2014/15
R million	**Budget**	**Revised**	**Medium-term estimates**		
Rand currency					
Opening balance	**109 053**	**111 413**	**129 425**	**109 060**	**103 413**
Cash utilised for domestic funding	-6 896	18 012	-20 365	-5 647	-1 256
Closing balance	**102 157**	**129 425**	**109 060**	**103 413**	**102 157**
Of which:					
Tax and loan accounts	*35 000*	*62 268*	*41 903*	*36 256*	*35 000*
Sterilisation deposits	*67 157*	*67 157*	*67 157*	*67 157*	*67 157*
Change in cash balance[1] (opening less closing balance)	**6 896**	**-18 012**	**20 365**	**5 647**	**1 256**
Foreign currency[2]					
Opening balance	**57 241**	**62 143**	**65 287**	**54 909**	**54 909**
Domestic foreign exchange purchases	22 285	3 444	8 352	13 917	9 034
International borrowing	8 159	13 010	4 218	10 615	7 320
Cash utilised for foreign funding	-15 448	-13 310	-22 948	-24 532	-18 402
Closing balance	**72 237**	**65 287**	**54 909**	**54 909**	**52 861**
US$ equivalent	*10 064*	*8 881*	*7 624*	*7 624*	*7 335*
Change in cash balance[1] (opening less closing balance)	**-14 996**	**-3 144**	**10 378**	**-**	**2 048**
Total change in cash balances[1]	**-8 100**	**-21 156**	**30 743**	**5 647**	**3 304**
Total closing cash balance	**174 394**	**194 712**	**163 969**	**158 322**	**155 018**

1. A negative value indicates an increase in cash balances and a positive value indicates that cash is utilised to finance part of the borrowing requirement

2. Rand values at which foreign currency was purchased or borrowed

The foreign exchange deposits with the Reserve Bank are made from money borrowed in the international markets and from purchases of foreign currency in the local market. It is expected that total foreign currency balances will decrease to US$7.3 billion over the medium term.

A portion of cash will be used to finance part of the gross borrowing requirement

Total cash with the Reserve Bank and commercial banks will reach a high of R194.7 billion in 2011/12, declining to R155 billion in 2014/15 as cash is used to finance part of the gross borrowing requirement.

The losses and profits on the foreign exchange activities of the Reserve Bank are accounted for on the Gold and Foreign Exchange Contingency Reserve Account. The balance on this account is split into transactions with a cash flow and non-cash flow (valuation) impact. Due to a weaker currency, the balance of valuation gains and losses increased to a net R78.3 billion as of 31 December 2011, R59.9 billion higher than a year earlier.

Debt-service costs

Debt-service costs are influenced by the volume of debt, new borrowing and market variables such as interest, inflation and exchange rates. Table 5.9 summarises trends and projections to 2014/15. Debt-service costs as a percentage of GDP are expected to peak in 2013/14.

Table 5.9 National government debt-service costs, 2010/11 – 2014/15

	2010/11	2011/12		2012/13	2013/14	2014/15
R million	**Outcome**	**Budget**	**Revised**	**Medium-term estimates**		
Domestic	60 812	70 797	70 550	82 563	94 578	103 103
Short-term loans	8 732	9 661	9 826	10 864	13 983	15 569
Long-term loans	52 080	61 136	60 724	71 699	80 595	87 534
Foreign	5 415	5 782	6 095	6 825	6 228	5 936
Total	**66 227**	**76 579**	**76 645**	**89 388**	**100 806**	**109 039**
As percentage of:						
GDP	*2.4*	*2.6*	*2.6*	*2.7*	*2.8*	*2.7*
Expenditure	*8.2*	*9.4*	*8.6*	*9.2*	*9.6*	*9.6*
Revenue	*9.9*	*11.9*	*10.4*	*11.2*	*11.3*	*10.9*

Government's debt portfolio

Total loan debt

Net loan debt consists of total domestic and foreign debt, less cash balances. Net loan debt is expected to be R1 trillion by the end of 2011/12, or 33.3 per cent of GDP, increasing to 36 per cent of GDP in 2012/13 and reaching 38.5 per cent of GDP in 2014/15.

Table 5.10 Total national government debt, 2008/09 – 2014/15

	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15
R billion		**Outcome**		**Estimate**	**Medium-term estimates**		
Domestic debt							
Gross loan debt[1]	529.7	705.5	892.7	1 072.9	1 247.4	1 430.6	1 595.6
Cash balances	-101.3	-106.6	-111.4	-129.4	-109.1	-103.4	-102.2
Net loan debt[2]	428.4	598.9	781.3	943.5	1 138.3	1 327.2	1 493.4
Foreign debt							
Gross loan debt[1]	97.3	99.5	97.9	129.5	107.5	97.6	99.3
Cash balances[3]	–	-25.3	-60.4	-75.5	-56.4	-54.1	-55.0
Net loan debt[2]	97.3	74.2	37.5	54.0	51.1	43.5	44.3
Total gross loan debt	**627.0**	**805.0**	**990.6**	**1 202.4**	**1 354.9**	**1 528.2**	**1 694.9**
Total net loan debt	**525.7**	**673.1**	**818.8**	**997.5**	**1 189.4**	**1 370.7**	**1 537.7**
As percentage of GDP:							
Total gross loan debt	*27.2*	*33.0*	*36.0*	*40.1*	*41.0*	*42.2*	*42.4*
Total net loan debt	*22.8*	*27.6*	*29.7*	*33.3*	*36.0*	*37.8*	*38.5*
Foreign debt as percentage of:							
Gross loan debt	*15.5*	*12.4*	*9.9*	*10.8*	*7.9*	*6.4*	*5.9*
Net loan debt	*18.5*	*11.0*	*4.6*	*5.4*	*4.3*	*3.2*	*2.9*

1. Forward estimates are based on projections of exchange and inflation rates
2. Net loan debt is calculated with due account of the cash balances of the National Revenue Fund (bank balances of government's accounts with the Reserve Bank and commercial banks)
3. Foreign currency deposits revaluated at forward estimates of exchange rates

Composition of government loan debt

Table 5.11 presents the maturity distribution of the domestic bond portfolio. The average term-to-maturity of government bonds – the time between when a bond is issued and when it is repaid – is expected to reach 10.9 years in 2011/12. This compares favourably to Germany, Canada, Japan, France, Italy (about six years) and the UK (13 years). The longer the average term-to-maturity, the lower the refinancing risk.

Bond maturity profile compares favourably with other countries

Table 5.11 Maturity distribution of domestic marketable bonds, 2009/10 – 2011/12

Percentage of total	Portfolio[1]		2011/12 Estimates	
Years	2009/10	2010/11	Funding[2]	Portfolio[1]
0 – 3	5.7	11.6	–	13.3
3 – 7	31.5	25.3	16.4	24.6
7 – 10	24.4	18.9	28.2	21.9
10 – 19	29.6	31.3	23.3	24.3
Longer than 19	8.8	12.9	32.1	15.9
Weighted average years to maturity	*10.1*	*10.4*	*15.3*	*10.9*

1. The total bond portfolio as at the end of the period
2. Bond issuances for the fiscal year

Table 5.12 shows the composition of domestic debt by various funding instruments, which are broadly categorised as bonds and Treasury bills. Treasury bills as a percentage of the total domestic portfolio increased from 12.3 per cent in 2008/09 to 15.9 per cent in 2011/12. The non-fixed rate debt component of the domestic portfolio will increase from 29.6 per cent in 2008/09 to 36.3 per cent in 2011/12. Over time, government will return the debt portfolio to the optimal risk ratio.

Table 5.12 Composition of domestic debt by instrument, 2008/09 – 2014/15

End of period	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15
R billion		Outcome		Estimate		Medium-term estimates	
Short-term loans	**65.0**	**114.8**	**149.6**	**170.4**	**192.4**	**214.4**	**234.4**
Shorter than 91-days[1]	–	0.3	13.5	13.5	13.5	13.5	13.5
91-days	37.7	48.2	49.7	48.7	49.7	49.7	49.7
182-days	13.8	24.3	28.0	35.9	39.4	43.2	46.2
273-days	12.9	27.8	34.1	38.2	44.0	50.1	55.6
364-days	0.6	14.2	24.3	34.1	45.8	57.9	69.4
Long-term loans	**464.7**	**590.7**	**743.1**	**902.5**	**1 055.0**	**1 216.2**	**1 361.2**
Fixed-income	369.0	445.7	553.9	670.3	798.6	907.7	998.9
Inflation-linked[2]	83.9	130.4	170.8	219.0	242.4	293.2	343.2
Retail	1.7	4.6	9.5	12.1	12.9	14.2	18.0
Floating rate	7.8	7.8	7.8	–	–	–	–
Zero coupon	2.1	2.1	1.0	1.0	1.0	1.0	1.0
Other[3]	0.2	0.1	0.1	0.1	0.1	0.1	0.1
Total	**529.7**	**705.5**	**892.7**	**1 072.9**	**1 247.4**	**1 430.6**	**1 595.6**
As percentage of total domestic debt:							
Short-term loans	*12.3*	*16.3*	*16.8*	*15.9*	*15.4*	*15.0*	*14.7*
Non-fixed rate debt	*29.6*	*35.9*	*36.8*	*36.3*	*34.9*	*35.5*	*36.2*

1. Mainly borrowing from the Corporation for Public Deposits
2. Includes revaluation as a result of changes in inflation rates
3. Loan levies, former regional authorities and Namibian debt

The consolidated maturity schedule of total government and state-owned entities' debt as of 31 December 2011 shows that 63.1 per cent of total debt will mature within the next 10 years.

As shown in Table 5.13, non-residents' holdings as a percentage of total domestic government bonds increased to 29.1 per cent in 2011 from 21.8 per cent the previous year.

Table 5.13 Ownership of domestic government bonds, 2007 – 2011

Percentage of total	2007	2008	2009	2010	2011
Pension funds	47.2	43.9	39.9	36.5	33.0
Foreign investors	10.6	12.8	13.8	21.8	29.1
Monetary institutions	16.5	18.0	18.3	17.7	16.3
Insurers	11.6	13.7	12.4	14.1	11.6
Other financial institutions	12.2	10.2	13.2	8.1	8.0
Other	1.9	1.4	2.4	1.8	2.0

Source: Share Transactions Totally Electronic Ltd. (STRATE)

Provisions and contingent liabilities

Projections for provisions and contingent liabilities are shown in Table 5.14. Provisions are liabilities for which the payment date or amount is uncertain.

Table 5.14 Composition of provisions and contingent liabilities[1], 2010/11 – 2014/15

End of period R billion	2010/11 Outcome	2011/12 Estimate	2012/13 Medium-term estimates	2013/14	2014/15
Net loan debt	**818.8**	**997.5**	**1 189.4**	**1 370.7**	**1 537.7**
Provisions	**74.4**	**94.4**	**97.2**	**92.8**	**94.8**
Special drawing rights	0.8	0.8	0.8	0.8	0.8
International Monetary Fund[2]	40.5	40.5	40.5	40.5	40.5
International Bank for Reconstruction and Development[2]	10.4	11.6	12.3	10.8	11.2
Multilateral Investment Guarantee Agency[2]	0.1	0.1	0.1	0.1	0.1
African Development Bank[2]	7.5	25.8	27.3	23.8	24.7
Development Bank of Southern Africa Limited[3]	4.8	4.8	4.8	4.8	4.8
Government employees leave credits	10.3	10.8	11.4	12.0	12.7
Contingent liabilities	**288.6**	**310.8**	**338.9**	**352.6**	**358.9**
Guarantees	149.6	170.1	198.6	217.3	228.2
Post-retirement medical assistance	56.0	56.0	56.0	56.0	56.0
Road Accident Fund	47.6	49.2	47.5	44.6	40.7
Government Employees Pension Funds	–	–	–	–	–
Claims against government departments	20.6	20.6	20.6	20.6	20.6
Export Credit Insurance Corporation of SA Limited	9.6	9.6	10.7	8.2	6.9
Unemployment Insurance Fund	3.3	3.4	3.6	4.0	4.6
Other[4]	1.9	1.9	1.9	1.9	1.9
Total	**1 181.8**	**1 402.7**	**1 625.5**	**1 816.1**	**1 991.4**
Total as percentage of GDP	*42.9*	*46.8*	*49.2*	*50.1*	*49.8*

1. Medium-term forecasts of some figures are not available and are kept constant
2. Represents the unpaid portion of government's subscription to these institutions
3. Represents callable capital provided for in terms of the Development Bank of Southern Africa Act
4. Represents a liability to Reserve Bank in respect of old coinage in circulation and other unconfirmed balances by departments
5. The annual Consolidated Financial Information of National Government contains more information on provisions and contingent liabilities

The National Treasury carefully monitors contingent liabilities and their potential impact on the fiscus. As at 31 March 2012, net loan debt, provisions and contingent liabilities are expected to amount to 46.8 per cent of GDP, and are projected to reach 49.8 per cent of GDP by 2014/15. This remains below the Southern African Development Community's macroeconomic convergence target of 60 per cent of GDP, and compares favourably with many developed countries.

No new guarantees were issued to public entities during 2011/12

The major public entities that hold guarantees are shown in Table 5.15 with details of guarantee commitments set out in Table 10 of Annexure B. No new guarantees were issued during 2011/12. Fees of R59.8 million were received in 2011/12 on the various guarantees provided.

Table 5.15 Guarantee exposure against major state-owned entities and development finance institutions, 2010/11 – 2011/12

Institution	2010/11		2011/12	
R billion	Guarantee	Exposure	Guarantee	Exposure
Total	**470.2**	**149.6**	**470.2**	**170.1**
Of which:				
Eskom	*350.0*	*67.1*	*350.0*	*86.1*
South African National Roads Agency Limited	*40.0*	*18.6*	*40.0*	*23.8*
Development Bank of Southern Africa	*28.3*	*25.9*	*28.3*	*25.9*
Trans-Caledon Tunnel Authority	*25.4*	*18.5*	*25.4*	*18.5*
Transnet	*9.5*	*9.9*	*9.5*	*6.9*
Land Bank	*3.8*	*1.8*	*3.8*	*1.1*

Financing borrowing by state-owned entities

State-owned entities need to borrow against their balance sheets

To invest in infrastructure that contributes to long-term economic growth and broader developmental goals, state-owned entities need to borrow against their balance sheets. Government helps these entities to access financing wherever possible, and provides guarantees where necessary.

During 2011/12, government support through the provision of guarantees reduced the state-owned entities' costs of borrowing on the domestic capital markets by an estimated R70 million. Domestic bond issuances by the entities amounted to about R10.3 billion at end-December 2011 (2010/11: R19.8 billion). During this period Eskom and Transnet increased their foreign bond issuances, while demand for SANRAL and Transnet's domestic bond issuances declined.

Government continues to support efforts by state-owned entities to increase their investor base and encourages them to develop cost-effective financing models. In 2011/12, state-owned entities continued to access financing through multilateral development finance institutions such as the African Development Bank (US$1.3 billion), the World Bank's Clean Technology Fund (US$350 million) and the Agence Française de Développement (€100 million). Over the medium term, state-owned entities will increasingly fund capital expenditure through higher internally generated cash flows, which are estimated to increase from R88.1 billion in 2012/13 to R145.2 billion in 2015/16.

Total borrowing by state-owned entities to amount to R76.9 billion in 2012/13

The National Treasury forecasts that total borrowing by state-owned entities will amount to R76.9 billion in 2012/13, R77.5 billion in 2013/14 and R74.1 billion in 2014/15.

Development finance institutions

Government ensures that development finance institutions have stable financial capacity and access to a mix of funding sources to deliver on their mandates. As shown in Table 5.16, the 57 per cent growth in their asset base from 2006/07 to 2010/11 supported a 58 per cent increase in developmental loans.

Table 5.16 Financial position of development finance institutions, 2006/07 – 2010/11

R billion	2006/07	2007/08	2008/09	2009/10	2010/11
Total assets	119.5	151.0	141.9	161.0	187.9
Total debt	42.2	47.8	48.0	50.7	58.0
Equity	99.5	100.8	91.5	110.7	125.4
Developmental loans	42.4	45.5	52.2	58.5	67.1

Over the medium term, development finance institutions will take advantage of cost-effective funding opportunities, including accessing multilateral funding.

Table 5.17 Projected major sources of funding for development finance institutions, 2010/11 – 2015/16

	2010/11	2011/12		2012/13	2013/14	2014/15	2015/16
R billion	Outcome	Budget	Revised	Estimates			
Domestic loans (gross)	**7.6**	**11.8**	**8.6**	**10.5**	**20.4**	**19.2**	**9.5**
Short-term	2.9	2.7	2.9	2.1	3.5	3.5	2.0
Long-term	4.7	9.1	5.7	8.4	16.9	15.7	7.5
Foreign loans (gross)	**1.3**	**4.2**	**6.9**	**3.4**	**9.7**	**9.8**	**7.7**
Long-term	1.3	4.2	6.9	3.4	9.7	9.8	7.7
Of which:							
Multilateral institutions	*1.3*	*4.2*	*2.4*	*1.2*	*0.8*	*1.0*	*2.0*
Total	**8.9**	**16.0**	**15.5**	**13.9**	**30.1**	**29.0**	**17.2**
As percentage of total:							
Domestic loans	*85.4*	*73.8*	*55.5*	*75.5*	*67.8*	*66.2*	*55.2*
Foreign loans	*14.6*	*26.3*	*44.5*	*24.5*	*32.2*	*33.8*	*44.8*

Development Bank of Southern Africa

DBSA key to implementing government's priority infrastructure investments

As an infrastructure bank, the Development Bank of Southern Africa (DBSA) will play an important role in plans to expand public-sector infrastructure. Government will strengthen the DBSA's balance sheet in line with the role it is expected to play. The bank will also play a larger role in funding and co-funding regional infrastructure projects, alongside other multilateral organisations, to expand economic opportunities within the Southern African Development Community region. The DBSA plans to commit development loans of R77.4 billion over the next five years.

Land Bank

The Land Bank will focus its resources on supporting developing farmers. In 2009/10, government approved a R3.5 billion guarantee that proportionately decreases with any capital appropriated for the Bank. To date, government has recapitalised the Land Bank with R2.5 billion. The remaining R1 billion will be allocated to the Land Bank over the medium term. Government is helping the Land Bank to explore other funding options, including accessing cost-effective funding from multilateral institutions such as the African Development Bank.

Housing

Rural Housing Loan Fund and NURCHA are being recapitalised

Government will recapitalise the Rural Housing Loan Fund and National Urban Reconstruction and Housing Agency (NURCHA), the two housing development finance institutions, with R51.9 million and R200 million respectively over the medium term. The Fund will focus on incremental lending for housing development in rural areas, while NURCHA will support lending for developing contractors to build low-cost housing.

Industrial Development Corporation

IDC plans to invest R107 billion in industrial development over the next five years

The Industrial Development Corporation (IDC) plans to invest R107 billion in industrial development over the next five years. Over the medium term, the IDC will fund its investment through funds generated from new borrowings, sale of shares, loan repayments and profits.

Recommendations of development finance institutions review

In October 2011, in line with the review's recommendation on rationalisation, Cabinet endorsed the merger of Khula, the South African Micro Finance Apex Fund and the IDC's small business activities. This step supports the policy objectives of the New Growth Path and efforts to grow small business. In addition, government is considering rationalising the National Housing Finance Corporation, NURCHA and Rural Housing Loan Fund.

Conclusion

Government's debt management strategies will remain focused on financing borrowing at the lowest possible cost. Debt stock will increase in line with budget deficits and then stabilise in the outer years. The fiscal stance will ensure long-term sustainability of the public finances. Government will continue to support state-owned entities and development finance institutions, enabling them to increase their support for infrastructure development, growth and jobs.