NATIONAL ASSEMBLY

QUESTIONS FOR WRITTEN REPLY

QUESTION NUMBER: 660 [NW870E]

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660. Ms K N F Hlonyana (EFF) to ask the Minister of Finance:

(a) How does the National Treasury plan to address the potential impact of rising US interest rates on the debt servicing costs and (b) what strategies are implemented to reduce the exposure of the Republic to currency fluctuations in the long term? NW870E

REPLY:

A) The impact of rising U.S. interest rates on debt service costs is twofold. Firstly, rising U.S. rates directly affect the sovereign's dollar-denominated debt, which constitutes about 10 percent of the total debt portfolio. Secondly, U.S. rates serve as a base rate for domestic borrowing costs, meaning that, all else being equal, higher U.S. rates translate to higher domestic debt service costs.

Debt service costs are determined by debt levels, new borrowing, and macroeconomic variables such as interest rates, inflation, and exchange rates. Sensitivity analysis of debt and debt service costs to changes in macroeconomic variables—such as interest rates, inflation, and exchange rates—shows that a 1 percentage point increase in inflation and interest rates, along with a R1 depreciation of the rand against the dollar, results in a R50.7 billion increase in gross loan debt and a R7.9 billion increase in debt service costs.

To mitigate these risks, the National Treasury has set a strategic benchmark for external debt at a range of between10 to 15 percent of the total debt portfolio, as external debt is most sensitive to U.S. rates. The current level of foreign currency denominated debt is below 10 percent. The share of short-term debt, such as treasury bills and floating rate notes, was increased marginally in response to the higher U.S. interest rate environment. It should be noted that the Federal Reserve is expected to begin cutting interest rates later this month, bringing an end to the rising interest rate cycle seen previously.

B) Government continues to finance its gross borrowing requirement in a prudent and sustainable manner within its strategic risk benchmarks. The financing strategy enables government to employ a range of instruments to meet its borrowing needs, while reducing risks associated with refinancing and currency fluctuations, and containing aggregate borrowing costs.