AFRICAN DEVELOPMENT BANK

REPUBLIC OF SOUTH AFRICA

RESULTS-BASED COUNTRY STRATEGY PAPER, 2008 - 2012

REGIONAL DEPARTMENT, SOUTH A (ORSA)

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RESULTS-BASED COUNTRY STRATEGY PAPER

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CURRENCY EQUIVALENT

1 UA	=	US$ 1.59527 (February 2008)
1 UA	=	ZAR 11.8528(February 2008)

FISCAL YEAR

1 April to 31 March

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ACRONYMS AND ABBREVIATIONS

ADB	African Development Bank
ADF	African Development Fund
AIDS	Acquired Immune Deficiency Syndrome
ANC	African National Congress
ASGISA	Accelerated and Shared Growth Initiative for South Africa
BEE	Black Economic Empowerment
BBEE	Broad-Base Black Economic Empowerment
CIDA	Canadian International Development Agency
COSATU	Congress of South African Trade Unions
CPIA	Country Policy and Institutional Assessment
CPIX	Consumer Price Index (Excluding Interest Rates on Mortgage Bonds)
DBSA	Development Bank of South Africa
DENEL	South African Defence Company
DFI	Direct Foreign Investment
DFID	UK Department for International Development
DFIs	Development Finance Institutions
EFA	Education for All Programme
EIB	European Investment Bank
ESKOM	Electricity Corporation
ESW	Economic and Sector Work
EU	European Union
FAD	IMF – Fiscal Affairs Department
GDP	Gross Domestic Product
GEAR	Growth, Employment and Redistribution Programme
GTZ	Deutsche Gesellschaft für Technische Zusammenarbeit (German Technical Cooperation)
HIV	Human Immunodeficiency Virus
HSRC	Human Sciences Research Council
ICA	Investment Climate Assessment
IDC	Industrial Development Corporation
IFC	International Finance Corporation
ILO	International Labour Organization
IMF	International Monetary Fund
JSE	Johannesburg Stock Exchange
LDC	Less Developed Countries
LIC	Low Income Countries
LoC	Line of Credit
MDGs	Millennium Development Goals
MIC	Middle Income Countries
MTEF	Medium-Term Expenditure Framework
NEDLAC	National Economic Development and Labour Council
NEPAD	The New Partnership for Africa's Development
NGO	Non-Governmental Organization
NHFC	National Housing Finance Corporation
ODA	Official Development Assistance
OPSM	Private Sector Department
PDIs	Previously Disadvantaged Individuals
PPP	Public Private Partnership
RDP	Reconstruction and Development Programme
SACU	Southern African Customs Union

SADC	Southern African Development Community
Safex	South African Futures Exchange
SACP	South African Communist Party
SARB	South African Reserve Bank
SMEs	Small and medium enterprises
SMMEs	Small Medium and Micro Enterprises
SOEs	State Owned Enterprises
STA	IMF – Statistics Department
TELKOM	Telecommunications Company
TNC	Trans-National Companies
TransNet	Transport Corporation
UN	United Nations
UNDP	United Nations Development Programme
UNISA	University of South Africa
USAID	United States Agency for International Development
WHO	World Health Organization
ZAR	South African Rand

Executive Summary

I. Introduction

The 2008-2012 Country Strategy Paper (CSP) for South Africa has been developed in collaboration with the National Treasury – the Bank's principal counterpart in South Africa – and through consultations with other country stakeholders. It outlines the recent economic and social developments in the country, identifies the challenges the country is facing, and proposes a medium-term Bank Group intervention strategy that is in line with the country's development agenda and regional integration aspirations as well as the Bank Group Vision Statement. The CSP provides the framework for the Bank's collaboration with South Africa in the next five years while providing the necessary flexibility to respond to new demands.

II. The Economy

South Africa has one of the most progressive constitutions in the world, which guarantees both civil and socio-economic rights and the political environment is conducive to political debate, dialogue and contestation. The South African economy is well diversified and it is the largest and most sophisticated in Africa. The robust growth which the economy has seen over the past seven years is anchored on the sound, transparent and predictable policies which the government has adopted since 1994 on the one hand and on favourable international environment on the other. The country is endowed with rich natural resources, has a "first-world" infrastructure, a large domestic market and is being well-positioned technologically to be able to compete in the global market. However, to fully exploit the huge potentials that exist in the economy, efforts must be intensified to address the emerging problem of electricity shortage, low gross domestic savings and investment, weak capacity and skill shortages in critical areas, as well as the threats posed by the "second economy" which needs to be integrated into the mainstream, without endangering macroeconomic stability; the relatively high levels of poverty; high levels of unemployment and inequalities; the HIV/AIDS pandemic; and land redistribution.

III. The Development Agenda of the Government

Since democratisation in 1994, the South Africa Government's development agenda and poverty reduction strategies have evolved over time. These include the Reconstruction and Development Programme (RDP) in 1994, the Growth, Employment and Redistribution (GEAR) programme in 1996 and the Accelerated and Shared Growth Initiative for South Africa (ASGISA) in 2006. The twin objectives of the ASGISA are to halve the level of poverty and unemployment by 2014 and enable South Africa to achieve and sustain high average economic growth rates of 4.5% for the period 2004-2009 and 6% between 2010 and 2014.

IV. Constrains to the Bank's Operations in South Africa

South Africa has made limited use of development assistance and donor resources because it has ample internal resources in addition to its ability to easily access international capital markets at relatively competitive prices. The government has therefore, directed the Bank to focus its lending operations on the SOEs and the private sector. Other factors that have constrained the Bank's operations in South Africa include: (i) competition from other donors especially those offering concessional resources, (ii) the Bank's rules of procedures which are perceived to be cumbersome, and (iii) lack of local presence in South Africa.

V. The Bank Group Assistance Strategy

The Bank's strategy for South Africa for the period 2008-2012 is underpinned by the ASGISA which had as its overarching objective poverty reduction. The proposed strategy recognises that in South Africa, resource availability is not a binding constraint to implementing economic and social development programmes. The strategy also recognizes the authority's desire to ensure that all government projects and programmes pass through the budget process. The strategy proposes three strategic pillars, namely, *Enhancing Private Sector Competitiveness, Partnership for Regional Integration and development, as well as Knowledge Management and Capacity Building.* The strategic objectives consist of a number of intermediate outcomes. These include (i) improvement of infrastructure services; (ii) improved financial intermediation, especially for SMEs; (iii) support for regional infrastructure; (iv) facilitation of cross-border investment; (v) use of South Africa's expertise for institutional development of less developed African countries; (vi) improved knowledge in support of the lending programme and policy dialogue; and (vii) improved capacity in government, municipalities, private sector and civil society.

VI. The Bank Group Assistance Programme

The assistance programme will emphasise the knowledge management and sharing aspect of the strategy, while also providing resources targeted at the infrastructure sector (including cross-border investment in infrastructure), the private sector and SOEs. The ESW programme will provide the analytical underpinning of the lending programme, facilitate policy dialogue and broaden the scope of private sector development. In agreement with the authorities, ESW and capacity building will be programmed on the basis of their contribution to achieving the CSP outcomes. Partnership with South African institutions and other development partners will be sought in the preparation of these reports in order to maximize the use of available technical and financial resources, as well as build common ground around critical policy issues. The dissemination of key analytical work will be ensured during the CSP period to build wide and strong partnerships with the country.

VII. Areas Requiring Dialogue

The Bank will undertake dialogue with the authorities and other stakeholders on the role that it can play in promoting the development of the local capital markets through its lending and technical cooperation activities as well as to support capacity building of the municipalities. Also, the Bank will continue to engage the authorities in dialogue on how to expand its portfolio in the country, how to effectively partner with South Africa in fostering regional integration and what changes the Bank needs to undertake in the way it does business to be more relevant operationally and institutionally as a development partner with the country

VIII. Conclusion and Recommendation

South Africa has a strong economic performance track record and represents investment opportunities for the Bank. The medium-term outlook is also encouraging but there are a number of challenges facing the country including high unemployment and inequality, as well as uplifting the 'second' economy without damaging the growth prospect of the 'first' economy. Government is however, making progress in addressing these challenges from its own resources.

The Board is requested to consider and approve the proposed 2008-2012 Bank Group assistance strategy for South Africa and to note the indicative lending limit set between UA 476 and UA 984 million per year over the period 2008-2012, for Bank Group operations in South Africa.

1. INTRODUCTION

1.1 The last 2003-2005 Country Strategy Paper (CSP) for South Africa (ADB/BD/WP/2003/21) was approved by the Boards of Directors on 11 June 2003. An update of the 2003 – 2005 CSP (ADB/BD/IF/2007/128) was also distributed to the Board in June 2007, to provide the strategic basis of continued operations in South Africa pending the finalization of the new CSP. The 2003-2005 Country Strategy was underpinned by the Government's *Medium Term Expenditure Framework 2003-2005* (MTEF) aimed at adapting the economy to globalisation with accelerated growth and promoting the democratisation of the ownership of the means of production. The Boards noted that the Government had made substantial progress in delivering social services to the disadvantaged segments of the society and commended the Government for its prudent fiscal and monetary policies. The Board also commended the Government for its active role in the area of regional integration and in NEPAD.

1.2 South Africa continues to face a number of development challenges. The challenges include high income inequality, uneven human resources development, a relatively high HIV/AIDS infection rate, high crime rate, and high unemployment. Most of these challenges emanate largely from the dual nature of the inherited economy organized along racial lines. The most serious challenge facing the country is that of integrating the so-called "first and second economies". South Africa also presents business opportunities for the Bank, especially in the area of private sector and infrastructure (including cross-border infrastructure) development. (Box 1 presents country snapshot).

Box 1: South Africa – Country Snapshot

South Africa has a land area of 1.2 million square kilometres, and a long coastline that stretches for more than 2500kms from Namibia to Mozambique. The country has a varied climate and topography that includes large plateau, the savannah, steep escarpment, and a narrow coastal plain. The country also has rich biodiversity, accounting for close to 10% of the world's total known bird, fish and plant species, and over 6% of the world's mammal and reptile species.

South Africa is a multiparty parliamentary democracy in which an executive president shares power with the Parliament. The National Parliament has two chambers, a lower and an upper chamber. The lower chamber is the National Assembly, and it has 400 members, elected for a five-year term through the system of proportional representation. Of these, 200 members are elected from national party lists, while the other 200 are elected from party lists in each of the nine provinces. The upper house is the National Council of Provinces, which has 90 members, elected for a five year term by the provincial parliaments, where each of the nine provinces has a delegation consisting of ten members.

The population of South Africa was estimated at 48.6 million in 2007, with about 57.8% of the people residing in urban areas. As more Africans are absorbed into the formal economy, average household size has been decreasing across all provinces. In the country as a whole, 16.4% of households were single person households in 1996, increasing to 18.5% in 2001. At the other extreme, 16.2% of households in 1996 contained seven or more people, decreasing to 13.8% of households in 2001. Gauteng had the smallest proportion of households containing seven or more people (8.7% in 1996 and 7.1% in 2001). There were 3.4 million female-headed households in 1996 (37.9%), increasing to 4.8 million in 2001 (42.6% in 2001). Altogether 8.0% of all households were living in overcrowded conditions in October 2001. There has been much concern about the effect of HIV/AIDS on the future size of the South African population. The overall estimated HIV-prevalence rate is approximately 10-13% and is translated in the diminishing life expectancy at birth from 54.7 years in 2001 to 49.3 years in 2007, while both Infant Mortality and Under-five mortality remains stagnant. Addressing socio-economic impact of HIV/AIDS at all levels and in all sectors remains a priority in the South African development agenda. The population living below the poverty line as a percentage of the total population (incidence of poverty) estimated at 57.0% in 2001 and those living below $1 a day (extreme poverty) estimated at 8.6% in 2004 are relatively high and the unemployment rate at 25.6% in March 2007 is also high. This is further compounded by the relatively high unequal distribution of income and wealth, with a gini coefficient of 0.59.

South Africa is a small open economy with its share in world exports and imports estimated at 0.89% and 0.87% respectively in 2005. Commodity based products dominate the country's exports, with platinum, diamonds (excluding industrial), gold and coal as the four principal exports. The country's major trading partners are the United States, the United Kingdom and Japan.

1.3 The major challenge facing the Bank in doing business with South Africa is how to build an effective partnership with the country and its institutions for the promotion of national and regional development using the country as a growth pole for its less developed neighbours. This is a major issue the 2008-2012 CSP attempts to address. Developed in consultation with the National Treasury and other stakeholders including sector ministries, the private sector and the civil society, this CSP adopts an approach which defines broad strategic priorities for the CSP period while specific activities to be undertaken are to be identified and agreed upon with the relevant beneficiaries periodically in a manner consistent with their planning and budgeting cycles. It proposes a medium-term Bank's intervention strategy that is in line with the country's development priorities and regional integration aspirations as well as the Bank Group Vision Statement.

2. THE SOUTH AFRICAN ECONOMY

2.1 *Strengths*

Table 1: Corruption Perception Index (CPI)

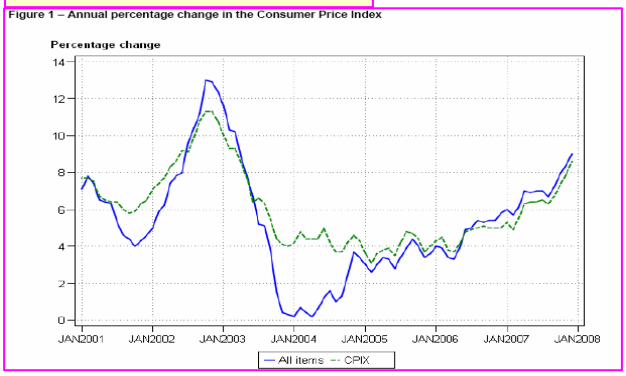
	2002	2003	2004	2005	2006	2007
Botswana	6.4	5.7	6	5.9	5.6	5.4
Malawi	2.9	2.8	2.8	2.8	2.7	2.7
Namibia	5.7	4.7	4.1	4.3	4.1	4.5
Nigeria	1.6	1.4	1.6	1.9	2.2	22
South Africa	4.8	4.4	4.6	4.5	4.6	5.1
Tanzania	2.7	2.5	2.8	2.9	2.9	3.2
Zambia	2.6	2.5	2.6	2.6	2.6	2.6
Zimbabwe	2.7	2.3	2.3	2.6	2.4	2.1

Source: Transparency International (2007)

2.1.1 **Stable polity, good governance and sound public financial management systems**. South Africa has one of the most progressive constitutions in the world, which guarantees both civil and socio-economic right, and the political environment is conducive to political debate, dialogue and contestation. The Corruption Perception Index shows a moderate level of corruption for South Africa vis-a-vis other countries in Africa (see Table 1). Commitment to good governance has been one of the priorities of South Africa since the end of apartheid in 1994. South Africa has a relatively sophisticated and comprehensive framework, which deals with transparency in procurement and financial management and there is a well-developed legislation which regulates the financial management of both the public and private sectors in line with international best practice. Compliance with these pieces of legislation is normally good.

2.1.2 **Robust economic growth.** South Africa has the largest and most sophisticated economy in Africa. Its economic growth has been robust and in an upswing since September 1999 with a sustained positive real GDP growth. Annual real GDP growth has averaged about 4.0% per annum over the past seven years. It is estimated that real GDP grew by 5.6% in 2007 driven on the demand side by the lagged impact of earlier interest rate cuts and strong domestic spending, and, more significantly, on the supply side by a pickup in investment, strong commodity prices and a weaker rand.

Figure 1 - South Africa: Inflation Rate (%)



2.1.3 **Sound, transparent and predictable economic policies** has helped to deliver low fiscal deficit and public debt ratios. Until recently, the CPIX inflation rate has remained within the target range of 3% - 6% which it attained in September 2003[1] and fiscal balance has improved from an average deficit of 3.5% of GDP during 1996-2000 to a surplus of 0.4% in 2006. Government's domestic debt has been scaled back from 45.3% of GDP in 2001 to 34.8% in the second quarter of 2006 while foreign debt at the end of 2006 was 22.4% of GDP compared to 29.2% in 1999. The improved macroeconomic conditions have helped to reinforce South Africa's credit standing in the international markets. This coupled with the strength of the rand in recent years has encouraged the sale of rand-denominated bond in the international debt markets, making it possible for the government to borrow off-shore in rand and at a relatively low sovereign spread. Consequently, an ever increasing share of the country's foreign debt (about 43.8% in the first quarter of 2006) is rand-denominated. In spite of the volatility of the rand and South Africa's vulnerability to capital outflows, the authorities remain committed to liberalizing capital controls to further enable South African companies to engage in strategic international partnership.

[1] The CPIX inflation rate breached the 6 per cent upper limit of the SARB's inflation target band from April 2007.

2.1.4 **Solid resource base.** Mining has traditionally been a very important sector in the South African economy in terms of output, employment and exports and the country's rich resource serves as one of the base for its economic strength. In addition to having a well-organized commercial agricultural system which exports a variety of products, South Africa is endowed with one of the richest and most diverse concentration of mineral resources in the world. In terms of size and value, the country has one of the top ten mining and mineral processing industries in the world. It is a major player in diamond and coal mining and exports, and occupies a dominant position in terms of reserves and production of a variety of metal and mineral resources in the world. It is believed that the country's natural resources are yet to be fully explored and that there is still potential for the discovery of other minerals.

2.1.5 **Relatively well diversified economy.** Over the past four and half decades, the South African economy has developed from being a primary sector-driven economy into a relatively well diversified tertiary sector-driven economy. Consequently there has been a decline in the country's traditional exposure to the fluctuations of commodity prices and an increase in the resilience of the economy. The primary sector, which contributed almost a quarter of gross value added during the 1960s, now accounts for barely 10.5% while the tertiary sector's contribution has risen from about 50% to 66%. The growth in the tertiary sector over this period has been driven mainly by two major sectors – government services, and financial and business services. The impressive growth and sophistication of the financial services sector in South Africa, a sector which was originally developed to support the development of mining activity is a considerable asset to the country in a modern world in which the role of global finance has become increasingly important.

Table 2: Percentage Contribution to Total Nominal Value Added at Basic Prices by Sectors

Sectors	1960	1975	1985	1995	2006
Agriculture, forestry and fishing	11.2	7.7	5.2	3.9	2.8
Mining	12.4	11.1	14.2	7.0	7.7
Total Primary Sector	**23.6**	**18.7**	**19.4**	**10.8**	**10.5**
Manufacturing	20.1	22.7	21.8	21.2	18.4
Electricity, gas and water	2.4	2.3	4.0	3.5	2.4
Construction	3.0	5.1	3.5	3.2	2.6
Total Secondary Sector	**25.5**	**30.1**	**29.4**	**27.9**	**23.5**
Wholesale and retail trade, catering and accommodation	13.9	13.5	11.0	14.3	14.2
Transport, storage and communication	9.9	9.1	8.4	8.9	9.4
Finance, insurance, real estate and business services	10.6	12.5	13.5	16.4	21.7
Community, social and personal services	16.5	16.1	18.2	21.7	20.7
Total Tertiary Sector	**50.9**	**51.2**	**51.2**	**61.3**	**66.0**
Gross Value Added at Basic Prices	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source: South African Reserve Bank

2.1.6 **Relatively large domestic market and access to international markets.** South Africa's population was estimated at 48.6 million in 2007 with 57.8% residing in urban areas. South Africa is a consumer market and growth in consumer spending, especially among black consumers, which accounted for a significant portion of total household expenditure has been the key driver of economic expansion in recent times. The size of the market has been boosted by the growing black middle class who spend a larger proportion of their income on consumption given that their average propensity to consume is higher than the national average. With the largest market in Sub-Saharan Africa, in terms of purchasing power, and given its strong influence over the region, South Africa is an attractive location for investment, consumer goods, producer goods, ICT, as well as a large market for construction and construction material. South Africa also benefits form its proximity and access to several expanding Africa markets in SADC and West Africa. These markets provide South African enterprises with new outlets and business opportunities.

2.1.7 **South Africa's financial sector is well-developed and relatively sophisticated.** The emerging market status of South Africa notwithstanding, the country has a sophisticated financial sector. Its financial and capital markets are well developed and the regulatory framework is in line with international standards. The financial sector, jointly with the insurance, real estate and business services accounted for about 22% of the country's real value added in 2006 and together with other service sectors has proved to be a pillar for the country's economic growth over the years. The South African financial market is relatively deep and can provide virtually any financial product that is available in any of the world's sophisticated financial markets allowing the country to meet its capital needs. Despite the dominance of the government in the bond market, corporate listings which started in 1992 are now becoming more common as companies diversify their capital raising methods. The Johannesburg Securities Exchange (JSE) is one of the top stock exchanges in the world and Africa's biggest in terms of market value. It has market turnover of US$312 billion, liquidity of 41.6% and a ranking of 19th in the world at the end of March 2006. On June 5, 2006, the JSE became a listed company on its own market, thus turning it from a club of stockbrokers to a more transparent limited company.

2.1.8 **Good infrastructural facilities.** There is a close link between the availability of good infrastructure and economic growth. Infrastructure impacts the geographic speed of economic activities, provides competitive inputs prices, skills, technology, and support to exports. It is critical for the development of tourism, the attraction of foreign investors as well as to making the private sector adaptive, innovative and globally competitive. Thus one should expect that an increase in the efficiency of infrastructure should lead to a concomitant improvement in growth performance, service provision and development outcomes. Though currently requiring substantial investments to upgrade standards, South Africa's infrastructure is highly developed by African standards. With infrastructure at par with that of Europe, Japan and the United States of America, South Africa has an unrivalled opportunity in a region poised for integration into the global economy.

Table 3: Business Environment in South Africa (World Bank Report, Doing Business in 2008)

	Mauritius	South Africa	Namibia	Thailand	Malaysia
Starting a business					
No. of Procedures	6	8	10	8	9
Time (days)	7	31	99	33	24
Dealing with licences					
No. of Procedures	18	17	12	11	25
Time (days)	107	174	139	156	285
Registering property					
Time (days)	210	24	23	2	144
Protecting investors					
Investor protection index (0-10)	7.7	8	5.3	6	8.7
Paying taxes					
Taxation of gross profits (%)	21.7	37.1	26.5	37.7	36
Trading across borders					
Time for exports (days)	17	30	29	17	18
Time for imports (days)	16	35	24	14	14
Overall rank Worldwide (out of 175)	**27**	**35**	**43**	**15**	**24**

2.1.9 **An environment that is conducive to private sector investment.** The private sector is the dominant sector in South Africa, accounting for over 70% of GDP in recent years and is the main employer and primary generator of exports. The private sector business climate and incentives in South Africa are regarded as one of the most conducive and competitive within the sub-region (see Table 3). The business environment is highly conducive to entrepreneurship, investment, innovation, and marketing. The legal system (property rights, contract settlement, speed of resolution of litigation, etc.) is well developed and functional. The judicial system and laws relating to commercial transactions, trade and investment, maritime activities, and competitive practices are recognised as comparable to those in OECD countries. However, to further enhance the contribution of the private sector to economic growth, there is the need to accelerate entrepreneurship development among black South Africans and to ensure that the competitiveness of the economy is not compromised by local sector-based (informal) pricing agreements and foreign entry barriers.

2.2 *Weaknesses*

2.2.1 **Emerging infrastructure shortage, particularly in electricity and transport.** Though South Africa's infrastructure is considered to be highly developed by African standards, the country continues to lag behind in its infrastructure investment when compared with countries of similar development level. Inadequate investment, particularly in the area of electricity generation and transport is potentially serious given that these sectors have long been an integral part of the engine of growth and a central component of sustainable development in South

Africa having been found to exert the largest and most robust impact on aggregate growth.[2] The reliability of power supply in South Africa is now being called into question given the performance of the electricity sector which has been below optimal in recent times. Also, the consequences of inadequate investment in the transport sector in the last 20 years are manifest in bottleneck in ports and railway networks. Unless there is urgent intervention, the problems of power shortage and transport bottleneck are expected to become acute in the coming years and could pose a serious threat to sustained economic growth and international competitiveness for the country.

2.2.2 **Chronic shortage of savings and investment**. Investment in physical and human capital is one of the major sources of economic growth. While foreign savings can be an important source of domestic investment, particularly in the form of foreign direct investment, an economy typically cannot rely entirely on foreign investment and additional domestic saving needs to be mobilized to finance growth. With investment rates below 20% of GDP, South Africa has uncharacteristically low levels of investment by emerging markets standards. The below average performance on this count has been due to low gross domestic savings which amounts to only about 14% of GDP, whereas investment in the expansion of productive capacity requires more than 20% of GDP. The low savings rate partly reflects the relatively high predisposition to consume and the growing indebtedness of South Africans due to high prevalence of credit facilities. To sustain current rates of economic growth, urgent action needs to be taken to increase domestic savings and investment.

2.2.3 **Weak capacity and skill shortages in critical areas in the context of a growing economy.** At the municipal level, there is a serious problem of lack of capacity and at all levels in South Africa there is an oversupply of unskilled workers (unemployment) and a shortage of skilled workers. The structural shift that has taken place in the economy, in favour of the services sector at the expense of the primary sectors, has tended to shift labour demand away from unskilled to semi-skilled and skilled occupations. Consequently, high unemployment now coexists with shortage of skilled workers, especially engineers, scientists and artisans. The situation is further aggravated by the accelerating rate of skills emigration (brain drain), especially at executive level. The pronounced shortage of skilled workers, especially financial experts is affecting the government's capacity to manage programme spending and social service delivery and if not addressed urgently is likely to become one of the most important factors inhibiting higher long-term economic growth. Immediate and definitive action needs to be taken to increase capacity and skills development especially in the area of public financial management, particularly at the provincial and municipal levels.

2.3 *Opportunities*

2.3.1 **Huge planned investment in infrastructure presents an opportunity to the private sector and the Bank.** With current emphasis on increased investment, especially on infrastructure, it is expected that the government fixed capital formation would expand by about 7% a year over the next three years. This will be supplemented by massive investment plans of SOEs like Eskom and Transnet, as well as, by private investment which is also projected to increase in the medium-term, driven by growth in consumer demand, low interest rates and a strong domestic currency. The substantial new investment that will be required in South Africa's infrastructure sector presents an opportunity to the private sector which may be required to play an increasing role in this sector to the Bank in view of its emphasis on infrastructure. In addition to the expected large infrastructure and social project spending by the government and SOEs,

[2] Bogetic Z and Fedderke JW. Infrastructure and Growth in South Africa: Business Map. Benchmarking, Productivity and Investment Needs. Paper presented at Bi-Annual Conference of Economic Society of South Africa, 7 – 9 September 2005. Durban South Africa.

expected increase in investment spending for the 2010 FIFA World cup have greatly increased the financial needs of both the government and the SOEs necessitating them to explore new funding sources.

2.3.2 **Cross-border investment and opportunities for regional integration.** South Africa's private institutions and SOEs are actively involved in a range of projects across the continent. By the end of the 1990s, South Africa had over 900 Trans-National Companies (TNCs) seven of which were among the top 50 non-financial TNCs operating in developing countries in 2002. A further 2,044 foreign affiliates, most of which had an African focus, were based in South Africa by the end of 2002, indicating South Africa's position as a launching pad for foreign investment into the rest of Africa. South Africa's TNCs are rapidly expanding in Africa, presenting opportunities in terms of larger markets and diversification for these TNCs as well as increased competition and efficiency in the countries in which they operate. Also, South Africa possesses expertise which could be tapped for the development of its neighboring less developed countries (LDCs) and Africa in general.

2.4 *Threats and Challenges*

2.4.1 The key threats and challenges that confront the South African economy include relatively high poverty level; high unemployment and uneven human resource development to meet the demands of a relatively sophisticated economy; the HIV/AIDS pandemic; and, the integration of the "second economy" into the mainstream, without endangering macroeconomic stability.

2.4.2 **Reducing the relatively high poverty level remains a key challenge.** In view of South Africa's middle income country status, the population living below the poverty line as a percentage of the total population (incidence of poverty) estimated at 57.0% in 2001[3] and those living below $1 a day (extreme poverty) estimated at 8.6% in 2004 remains relatively high. The incidence of poverty also varies across provinces, from being very low in Western Cape and highest in Eastern Cape. On the basis of per capita GDP in purchasing power parity terms, South Africa is one of the fifty wealthiest nations in the world but the Human Development Report of 2007/08 ranked South Africa 121 on the Human Development Index scale. Despite its relative wealth, the distribution of income and wealth in South Africa is among the most unequal globally, with a gini coefficient of 0.59. Also with a life expectancy at birth of 49.3 years it ranks among the worst 30 countries. This situation poses a serious threat not only to the country's socio-political stability but also to the ability of the country to sustain the robust economic growth which it has enjoyed in recent years since it is a well known fact that countries with less equal distribution of income tend not to grow as fast as those with more equitable distributions.

Table 4: Key Labour Indicators, Sept 2001 compared to March 2007

Labour Market Category (R '000)	**Sept '01**	**Sept '05**	**Mar. '07**
Employed	11,181	12,301	12,648
Unemployed (official definition)	4,655	4,487	4,336
Total Economically active (employed & unemployed)	**15,836**	**16,788**	**16,984**
Not Economically active	12,281	12,909	13,211
Total aged 15 - 65 years	**28,117**	**29,697**	**30,195**
Unemployment rate	29.4%	26.7%	25.5%
Labour force participation rate	56.3%	56.5%	56.2%
Labour absorption rate	39.8%	41.4%	41.9%

1. Revised on the basis of the new population estimates
Source: Labour Force Survey, September 2001, September 2005 and March 2007

2.4.3 **Unemployment remains a major development challenge** with significant effects on economic welfare, production, erosion of human capital, competitiveness, social exclusion, crime, and social stability. The employment coefficient in South Africa has been declining in recent times while labour participation and absorption rates are quite low. This is indeed a cause for deep worry because it means that even with a relatively high rate of economic growth the

[3] Poverty estimates were calculated using a poverty line that varies according to household size. A household of 4 persons has a poverty income of R1,290 per month (R43 a day or $6.3 a day at end December 2007 exchange rate). See Human Sciences and Research Council, Fact Sheet on South Africa, Fact Sheet No: 1, 26 July 2004

achievement of meaningful growth in job creation by the country is low. This perhaps explains why in spite of the impressive and sustained economic growth performance of the country in recent years, the unemployment rate remains rather high at 25.5% in March 2007 (see table 4). To ensure that the country's progress towards the achievement of its socio-economic goals are not undermined, efforts must be intensified at addressing, in a sustainable manner, the potentially adverse consequences not only of the high level of unemployment but also of poverty and inequality on growth and political stability.

2.4.4 **The second economy poses serious development challenges.** South Africa continues to be characterised by sharp economic dualism with a sophisticated industrial economy alongside an informal economy (the "second economy"). Large segments of the population that constitute the second economy continue to live in abject poverty and this is a potential source of social strain. According to the official definition, the second economy comprises largely the informal, marginalised, unskilled sub-sector of the national economy, populated by the unemployed and those unemployable in the formal sector. It is estimated that about 6.2 million people or about 20% of the working age population between 15 and 64, survive in the second economy. Government has embarked on a number of initiatives to address the challenges of the second economy, including an expanded public works programme, provision of social housing, promoting the development of SMEs and land reform, which have the potential to achieve greater social cohesion, and contribute to reduction of poverty and inequality.

2.4.5 **The HIV/AIDS pandemic also presents a significant development challenge**, to which the government, NGOs and private sector employers, are giving particular attention. The infection rates in South Africa are quite high and with 5.5 million people living with HIV in 2005, the country's AIDS epidemic is one of the worst in the world.[4] However, the 2007 AIDS Epidemic Update – Global Summary reported a prevalence rate of 18.8% among adults (age 15 – 49 years) compared to 20.1% and 20.9% in 2001 and 2003 respectively, suggesting that HIV infection levels might be levelling off.[5] The prevalence rate is highest in the key sectors of mining, transport, construction, and government services and increases with increasing level of schooling.[6] This is indeed a grim picture given that HIV/AIDS poses a serious constraint on economic development in South Africa through its numerous impacts on households and individuals, the productive capacity of the economy, and government finances and it is a major challenge to maintaining and possibly improving living standards.

2.4.6 **Access to land possession and usage remains a potential threat.** Land is considered to be the single most important factor in social, political and economic empowerment and it has a central role to play in wealth distribution. The exclusion of a large segment of society from land ownership and resources could result in poverty, poor health, environmental degradation and unemployment with the potential of unrest for a large segment of the population. Land in South Africa is an emotive and volatile issue and its redistribution is usually perceived as having the potential of raising tension. However, if handled correctly, land reforms may work to undermine racial division instead of exacerbating it. Since 1994, the government has pursued land reform in a considered, reasonable and largely market-oriented manner. The government is aware that its supporters expect a pacing up of the land reform process which has been relatively slow but also knows that if not properly handled it could destabilize the economy. The government's land reform programme which was launched in 1994 set a target of 30% of agricultural land under black ownership by 2015 but only 4% rate has been achieved at present partly due to difficulties in reaching agreement with current land owners under the "willing-buyer/willing seller"

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[4] 2006 Report on Global AIDS epidemic, Joint United Nations Programme on HIV/AIDS (UNAIDS) 2006, Annex 2: HIV and AIDS estimates and data, 2005 and 2003.

[5] AIDS Epidemic Update, Joint United Nations Programme on HIV/AIDS (UNAIDS) and World Health Organization (WHO) 2007, pp 11

[6] Nelson Mandela/HSRC Nationwide Study of HIV/AIDS

approach. The government has resolved to adopt a new approach that involves greater reliance on expropriation but grounded on well-defined legal principles with appropriate compensation. This does not however, portend an immediate and widespread takeover of white farmland.

3. UNDER-PINNING NATIONAL DEVELOPMENT AGENDA

3.1 Key Elements of the Government Development Agenda

3.1.1 **South Africa Government's development agenda has evolved over time.** First the government implemented the Reconstruction and Development Programme (RDP) which was put in place in 1994. The macroeconomic component of the RDP was further elaborated in 1996 with the adoption of the Growth, Employment and Redistribution (GEAR) programme. In 2006, the Government announced the Accelerated and Shared Growth Initiative for South Africa (ASGISA).

3.1.2 **The ASGISA was formulated to address the major binding constraints to accelerated growth and economic performance**. The twin objectives of the ASGISA are to halve the level of poverty and unemployment by 2014 and enable South Africa to achieve and sustain high average economic growth rates of 4.5% for the period 2004-2009 and 6% between 2010 and 2014. ASGISA proposes a set of interventions that will focus on six broad categories namely: macroeconomic reforms, including the continued build-up of official foreign reserves to reduce currency volatility; infrastructure programmes (infrastructure spending of R400bn); sector/industrial investment strategies; skills and education initiatives (human resource development, including internships and Priority Skills Acquisition programme); the integration of the "second economy" into the mainstream; and public administration reforms.

3.2 Assessment of Implementation Progress of ASGISA

3.2.1 **The difficulty one faces in assessing the ASGISA is the lack of clear monitorable indicators and outcomes.** An important feature of ASGISA however, is its focus on creating a socio-economic environment that would enable those engaged in the second economy to graduate into the first economy thus contributing to poverty reduction. In this regard, it contains strategies geared towards the empowerment of blacks in general and women in particular to make them active participants in the economy. Also, specific programs have been designed to deliver social services, develop rural infrastructure, strengthen skills of different members of society including the disabled, and provide employment opportunities through massive public works programs.

3.2.2 **The government faces a number of challenges in the implementation of ASGISA** including striking a balance between demands for macroeconomic stability, growth, and private sector development on the one hand, and employment creation, reduction in poverty and promotion of social equity on the other. There is also the challenge of coordinating activities across different tiers of government: national, provincial and municipal levels. In addition, the government needs to go beyond the allocation of resources and begin developing systems to reduce duplication of efforts and assess the effectiveness of its support for priority areas. Other challenges include bridging the rural-urban divide in access to social services and developing the capacity necessary at the lower tiers of government such as municipalities to improve results on the ground.

3.2.3 **The Government has put forward an ambitious public sector investment programme mostly in building infrastructure**. However, shortage of skills and limited capacity poses the greatest threat to the implementation of the programme. Government has admitted that administrative capacity to implement the development agenda is weak, especially at local government level, yet the bulk of the planned capital spending will be carried out at the provincial and municipal government levels. In spite of recent efforts to improve workers' skill, the country may in the short-term have to rely on expatriate skilled workers such as engineers, scientists and project managers to close the skills gap.

3.3 The Partnership Framework

3.3.1 **Although there is no institutionalized Coordination Mechanism, Donor presence remains strong in South Africa.** The World Bank's work in South Africa is limited to country analytical work and the provision of technical assistance. Most recently, the emphasis in the policy dialogue and knowledge work has been on urban and rural development (urban and municipal development, land reform and agriculture, private sector development and the environment) and regional integration. The IFC has also built a very strong operational presence in South Africa, and its portfolio in the country is the second largest after Nigeria. As at May 2007, the IFC's portfolio in South Africa stood at US$342 million. The IFC strategy in South Africa focuses on supporting South African companies going north and going global; providing advice and financing within South Africa where there are underserved niches in the local market; and offering advisory services and related support for smaller business with focus on the informal sector and education.

3.3.2 The IMF undertook a Fiscal Affairs Department (FAD) mission in 2003 to discuss with the National Treasury their draft royalty bill (published in March 2003) and a monetary and financial statistics mission also took place in 2003 with a follow-up visit during May – June, 2004. In March 2005, an IMF – Statistics Department (STA) mission undertook a review of South Africa's Labour Force Statistics and recommended steps to produce statistics that are more reliable, better quality, and more closely aligned with ILO standards. The last Article IV Consultation report for South Africa was presented to the Executive Board of the IMF on 06 August 2007. The IMF Board noted that South Africa has started to reap the benefits of sustained sound macroeconomic management and structural reforms, recently supported by favourable external conditions.

3.3.3 Among the bilateral donors, the United States is the largest, and focuses on HIV/AIDS and poverty reduction. The European Union (EU) concentrates on health, education, criminal justice reform and community water projects. Other major bilateral donors include the United Kingdom (health, private sector development, democracy and governance, labour and criminal justice); Germany (democracy and governance, education, health and economic policy); and Sweden (democracy, governance, labour, and poverty alleviation). The 13 UN agencies in South Africa focus on HIV/AIDS, rural development, and regional integration.

3.3.4 **South Africa puts a great deal of emphasis on mutual commitment to the implementation of the Paris Declaration.** In this respect, South Africa holds partners responsible for honouring their commitment under the Paris Declaration and also requires partners to inscribe this commitment in their partnership agreements and country assistance strategy documents. Emphasis is put on harmonisation of donor procedures and adoption of country systems. In this regards, the Bank will ensure the implementation of the provisions of the Paris Declaration in its operational dealings with South Africa.

4. <u>BANK GROUP STRATEGY FOR ENHANCED PARTNERSHIP WITH SOUTH AFRICA</u>

4.1 Portfolio Management Issues

4.1.1 **The Bank Group has a limited portfolio in South Africa but can do more in view of the huge potentials of the economy.** The Bank Group operations in South Africa commenced in 1997 and as at the end of 2007, 16 operations have been approved. Except for one in the energy sector, all of the approved operations in South Africa are in the financial sector. Five operations were approved under the public sector window consisting of 4 lines of credit (LoCs) and a guarantee of bond issue to DBSA which was subsequently cancelled (see annex 5 for details). The remaining operations are private sector operations the latest of which are a US$500 million senior loan to Eskom Holdings Ltd., and a ZAR 1 billion subordinated debt to Nedbank approved in 2007. The objectives of the Eskom Investment Program are in accordance with the CSP goals of assisting the Government in achieving the Accelerated Shared Growth Initiative of South Africa (AsgiSA) and supporting the improvement of infrastructure services while the subordinated debt to Nedbank is in line with the CSP objectives of providing affordable housing for previously disadvantaged people, expansion of funding to BEE, and facilitating cross-border Sub-Saharan Africa transactions.

4.1.2 **Though small, portfolio performance has been generally satisfactory.** For the four public sector projects that have now been completed, there were regular supervision and in all cases, the projects were rated satisfactory. Also, the Project Completion Reports indicated satisfactory implementation of the projects.

4.2 Assessment of the Previous Strategy Implementation

4.2.1 **The 2003–2005 CSP did not spell out outcomes and measurable indicators, hence only a partial assessment can be made.** The key objective of the 2003-2005 CSP for South Africa was to support the Government's goal of adapting the economy to successful globalisation with accelerated growth and democratisation of the ownership of the means of production. The operations strategy to achieve these goals included: (i) lending activities mainly to parastatals and DFIs with and without Government guarantee; (ii) non-lending activities involving institution building projects and Economic and Sector Work (ESW) as well as the leveraging of these parastatals’ comparative advantages in infrastructure development to fund multinational projects in the context of the NEPAD and the Bank’s own Vision on regional integration; and (iii) co-financing of private sector projects with the SOEs, together with LoCs to private financial institutions. The results were partially achieved, especially with regard to lending to parastatals and DFIs, while the implementation of the non-lending programme and dialogue between the Bank and the Government were modest. The Bank was, however, active in the South African capital markets, issuing a R900 million local currency bond in May 2005.

4.3 Factors Constraining the Bank’s Partnership with South Africa

4.3.1 **Available internal resources limit Bank’s operations in South Africa.** ODA accounts for only 1 to 2% of South Africa’s national budget as the country has made limited use of development assistance and donor resources because it has ample internal resources in addition to its ability to easily access international capital markets at relatively competitive prices. Also, the government has been wary of borrowing from the multilateral finance institutions because of the perceived risk of aid dependency and conditionality and has expressed a wish not to borrow from international financial institutions, including the IMF and the World Bank. It is the authority’s desire to ensure that all government projects and programmes pass through the budget process. As a result, the authorities have requested that all discussion with line ministries on project/programme financing should be channelled through National Treasury. In addition the government has directed the Bank to focus its lending operations on the SOEs and the private sector. The challenge for the Bank therefore is how to be relevant institutionally and operationally in South Africa in terms of lending and advisory services.

4.3.2 **Competition from other multilateral and bilateral development institutions also limits investment opportunities for the Bank in South Africa.** There are investment opportunities in the SOEs and the private sector but the Bank is perceived as not being competitive as other players. Institutions such as European Investment Bank (EIB) and some bilateral donors such as DFID, USAID, GTZ and CIDA also provide some grants resources. However, the enhancement of the middle income countries (MIC) Trust Fund and the Japanese facility for private sector development, being managed by the Bank and flexibility in charging commitment fees for Non-Sovereign Guaranteed Loans (NSGLs) now provide the Bank with a window of opportunity to enhance its competitiveness in this market vis-à-vis the other players.

4.3.3 **Bank's rules of procedure are perceived to be too cumbersome**. Apart from direct cost of borrowing, clients are sensitive to the indirect cost in the form of transactions costs. These are incurred when loan processing take a long time to finalise and cumbersome procurement and disbursement procedures and legal rigidity constrain timely disbursement of loan proceeds. Clients would avoid such costs if resources could be sourced elsewhere, including the international capital market, even at higher financial cost. The huge investment opportunities in South Africa not withstanding, this factor has limited Bank's participation in the market. In recent times, lending operations to public entities has almost dried up because of the change in policy towards parastatals which now requires them to source their funds directly from the market on the strength of their balance sheets. Although, the introduction of the NSGL product by the Bank is meant to take advantage of this changing policy, some of the MICs cited the stringent financial performance standards specified in the NSGL Guidelines to qualify for Bank's lending under this product as a constraint to their SOEs in taking advantage of the facility. It should however, be noted that this is a standard requirement in the business given the high risk involved in lending to SOEs without government guarantees.

4.3.4 **The Bank has not taken adequate advantage of the opportunities for partnership with South Africa in the area of regional integration and development**. South Africa plays a critical role in NEPAD and SADC and the economies of its neighbouring countries are critically dependent of their relationship with South Africa for trade, investments, exports and imports. However, partnership between the Bank and South Africa in the sphere of regional integration and development has been limited. Going forward therefore, a major challenge for the Bank is how to improve partner with South Africa and its institutions to promote regional development.

4.3.5 **Lack of local presence in South Africa hinders the Bank's effective partnership with the country.** South Africa was among the first group of five countries programmed to have field offices. However, the regional office earmarked for South Africa could not be opened because the Host Country Agreement could not be concluded due to disagreements over one of its provisions. This lack of local presence has constrained effective partnership with South Africa and has resulted in the inability of the Bank to dialogue meaningfully with the authorities and the development partners that are currently resident in the country. The Mozambique Regional Office, expected to cover South Africa and other MICs in the region, has not been sufficiently equipped to play this role effectively.

4.4 Strategy for Enhanced Partnership with South Africa and the Strategic Pillars.

The Approach of the Strategy

4.4.1 The proposed strategy sets the framework within which the Bank will enhance its partnership with South Africa during the period 2008 – 2012 by collaboratively using the immense strength that the country has to maximize the opportunities which are identified in section 2 and to take necessary correction measures to ameliorate the identified weaknesses and potential threats. The proposed strategy for South Africa has been developed using the participatory approach, in which extensive consultations were held with the National Treasury and the various stakeholders. It is anchored on the country's development agenda as articulated in the ASGISA and the Medium Term Budget Policy Statements and attempts to build on the previous CSP.

4.4.2 The approach being proposed for adoption by the Bank to enhance its partnership with South Africa under the current CSP is positioned within the context of previous proposals for enhancing the Bank's supportto Middle-Income Countries[7] and the new comprehensive MIC strategy being developed by the Bank. The reports identified assistance to MICs in accelerating their integration into global markets as the pillar around which the Bank should establish its identity in MICs.

4.4.3 In line with the above, this Country Strategy Paper for South Africa will support the country's national priorities as articulated in its development agenda, the ASGISA, as well as its international development aspirations which has three components namely, consolidation of the African Agenda, South-South Cooperation and Solidarity, and North-South dialogue and partnership. The Bank's partnership with South Africa during the CSP cycle will rest on three strategic pillars: (i) enhancing private sector competitiveness so as to engender growth, employment creation and poverty reduction; (ii) partnership for regional integration and development; and (iii) knowledge management and capacity building (see Table 5). The approach is to define broad strategic priorities for the CSP period while specific activities to be undertaken will be identified and agreed upon with the relevant beneficiaries (private sector, paratatals, and/or public sector) periodically in a manner consistent with their planning and budgeting cycles.

4.4.4 The details of the results framework of the Bank's strategic priorities are presented in Annex 1. Where feasible, the CSP identifies quantitative targets to be attained during the implementation period. It is important to note that this is the first CSP for South Africa that attempts to identify outcomes and measurable results, and as such, there will be a continuous attempt to more clearly define expected outcomes and refine the indicators used to measure results. The three strategic objective (Pillars) are elaborated upon below.

Table 5 Summary of the Strategic Pillars for the 2008 – 2012 CSP

	Pillar 1: ***Enhancing Private Sector Competitiveness***	**Pillar 2:** ***Partnership for Regional Integration and Development***	**Pillar 3:** ***Knowledge Management and Capacity Building***
Broad Areas of Focus	(i) Support the Improvement of Infrastructure Services (ii) Improve Financial Intermediation especially for SMEs	(i) Support for Regional Infrastructure (ii) Facilitation of Cross-border Investment (iii) Using South Africa's expertise for the institutional development of less developed African countries	(i) Improved knowledge in support of the Lending Programme and Policy Dialogue (ii) Improve capacity in Central Government Ministries, Municipalities, and SOEs

Strategic Objective I: Enhancing Private Sector Competitiveness

4.4.5 The first pillar is focused on the theme of Private Sector Competitiveness and is aimed at supporting the government's infrastructure programme which is one of the key constraints to private sector development targeted by the ASGISA as well as support for financial intermediation also critical for private sector development. Consequently, this pillar has two outcomes namely, (i) Infrastructure improvement and (ii) improving financial intermediation for SMEs.

[7] ADB/BD/WP/2002/47, 22 May 2002 and ADB/BD/WP/2005/12, 8 February 2005

4.4.6 *Support the improvement of Infrastructure services (CSP Pillar 1 - Outcome 1).* South Africa's infrastructure has suffered from a long-term decline in investment, especially from government and as a result infrastructure development reflects an urgent and medium-term structural constraint to development in South Africa. Access remains a major challenge, partly as a legacy of apartheid, which left large sections of the (mainly black) population un- or under-serviced. The other main challenge facing infrastructure development in South Africa is the dichotomy in the state, quality and the distribution of facilities at the national, provincial and local levels that can be traced also to past apartheid policies. While at the urban level, South Africa is relatively well endowed with the supply of good infrastructure, in the rural areas, urban neighbourhoods, and peril-urban townships populated mainly by blacks, the supply, quality and maintenance of services is limited. These areas are in need of massive investments in infrastructure in order to bring them at par with the rest of South Africa.

4.4.7 In order to support private sector competitiveness in South Africa during the CSP period, the Bank will seek to support projects particularly in infrastructure that will foster the business enabling environment. There is a strong support by the South African authorities for the use of public-private partnership (PPP) mechanism for infrastructure provision and for the Bank to play a major role in this process. The Bank will seek to support public-private partnerships in infrastructure with the long-term objective of improving the efficiency and quality of public services and improving the environment for the domestic private sector. In addition to project financing the Bank would consider the use of guarantees for PPP in infrastructure. The Bank will also seek to support sub-national entities in the provision of infrastructure in local communities. In this regards, the Bank could channel it resources through SOEs that have major responsibilities for infrastructural provision and DFIs that support infrastructural development both at sub-national, national and regional levels.

4.4.8 *Improve financial intermediation, especially for SMEs (CSP Pillar 1 - Outcome 2):* South Africa is likely to remain a highly intermediated market for the wealthier population, with banks expected to maintain their dominant role in the financing of the economy. In spite of its dominant role, the financial sector has not effectively provided credit to small entrepreneurs, particularly emerging SMEs and black businesses, and there has also been insufficient investment of the savings pool into targeted investments of national priority. This is despite the fact that SMEs play a particularly prominent role within the private sector, with their share of total economic output estimated at more than 70% of total private sector output, and employing over 60% of the total labour force.

4.4.9 During the 2008-2012 CSP period, the Bank's support will continue to be geared towards promoting local entrepreneurship, especially for micro-enterprises and SMEs, who play a leading role in creating jobs and contributing to poverty reduction. The Bank will partner with financial institutions to: (i) expand their services to previously under-served markets, notably the affordable housing, SMEs and consumer finance segments; (ii) facilitate broader participation in economic growth; and (iii) expand their financial services in the rest of Africa especially the SADC region. Such partnerships include direct investments and risk sharing arrangements and co-financing. The aim is to work with financial institutions to give micro-enterprises and SMEs broader and deeper access to the financial market, by promoting financial products that can lower intermediation costs. In this regard, the feasibility of extending agency line of credit, which the Bank pioneered with the Nedbank, to other viable banks will also be explored.

4.4.10 This pillar (Enhancing Private Sector Competitiveness) and the associated two outcomes are strategic for private sector development in South Africa. The Bank will reinforce them by providing credit enhancement facilities such as guarantees, local currency lending, and other appropriate instruments as well as by strengthening its partnership with the IFC for co-financing of viable private sector operations. The Bank will also collaborate with the World Bank and the

World Economic Forum in the preparation of Investment Climate Assessments (ICA) and the African Competitiveness Reports. Thus, the Bank, through the Chief Economist's Office and the Regional Department-South A, will collaborate with the World Bank, in the follow-up analysis of the 2005 ICA and in the preparation of future ICAs for South Africa.

Strategic Objective II: Partnership for Regional Integration and Development

4.4.11 South Africa is SADC's most developed economy, and has a GDP which is over 75% of the combined GDP of the other Southern African countries. Also, South Africa's influence in the rest of the continent is considerable – an additional percentage point of South Africa's growth is estimated to be associated with 0.5% to 0.75% GDP growth increases in the rest of Africa. South Africa is a major driving force behind the NEPAD initiative and the African Peer Review Mechanism. A South Africa with a vibrant and flourishing economy can therefore be an engine of growth to its neighbours and provide an essential ingredient to the Bank's effort to promote regional development and poverty reduction in the SADC region.

4.4.12 The South African authorities endorses regional integration and regional operations as the greatest potential area of collaboration with the Bank during the CSP period and have expressed strong interest in strengthening partnership with the Bank in support of the development of regional infrastructure for improved connectivity and regional integration. The goal of South Africa is to increase the level of its trade with the rest of the continent, including increasing its imports from the continent. Consequently, under this pillar the Bank's strategy would be to partner with South Africa to foster regional integration and development in the SADC economic space as well as in the rest of Africa. This pillar will focus on three broad areas as follows: (i) Support for Regional Infrastructure; (ii) Facilitating Cross-border Investment; and (iii) Using South Africa's expertise for the institutional development of other African less developed countries.

4.4.13 *Support for Regional Infrastructure* (CSP Pillar 2 - Outcome 1). To strengthen connectivity and facilitate cross-border activities, the Bank will continue to provide support for regional physical infrastructure in transportation, telecommunications, and energy especially in infrastructure projects along economic and development corridors[8] (spatial development initiatives) within the SADC region. This will be done through financing of multinational projects under the NEPAD initiative for which South Africa has given a strong support and the Regional Assistance Strategy (RAS) for Southern Africa approved by the Boards in November 2004, with a view to enhancing the region's competitiveness and promoting greater sense of community. The South African authorities indicated that the country may be willing to access financial resources from the Bank in support of regional operations. SADC and its subsidiary organizations would be important partners for these regional projects, the capacity constraints in the SADC Secretariat notwithstanding. In this respect the Bank will seek to develop a trilateral partnership with SADC and South Africa in identifying and packaging regional projects. The role of private sector as financial participants through PPP in regional infrastructure development would also be encouraged and supported by the Bank not only because of their financial contribution but also because of the other efficiencies that private sector involvement brings. In addition, the Bank will build on its past efforts of partnering with South African DFIs including DBSA and IDC, the power sector parastatal Eskom, and private sector organisations such as NEPAD Business Foundation in providing financial and knowledge resources for accelerated development of regional infrastructure. The Bank may develop individual Memorandum of Understanding (MOU) with these key institutions to inform these partnerships.

[8] An economic or development corridor or spatial development initiative is a geographical area in which infrastructure investments are linked directly with trade, investment, production and tourism potentials.

4.4.14 *Facilitation of Cross-border Investment* (CSP Pillar 2 – Outcome 2) South Africa is increasingly becoming a springboard for trans-national companies' cross-border investment into other African countries. A number of the trans-national organisations have their headquarters in South Africa and are looking into expanding into other African countries. The Bank will play a facilitating role for South African cross-border investment by partnering with South Africa and its institutions through the provision of financial resources in support of the country's initiatives to reach out to its neighbours and cross-border investment activities of South African businesses and SOEs both within SADC and in the rest of Africa. The Bank is also exploring the possibility of partnering with institutions that support cross-border SME development in South Africa. These include Enablis and Grofin, two South African based SME funds with regional focus that combine finance and technical assistance to support growth-oriented SMEs. Thus, SME development also provides further opportunities for the Bank to deepen its interventions in South Africa.

4.4.15 *Using South Africa's expertise for the institutional development of Other African Countries* (CSP Pillar 2 - Outcome 3). Compared with its neighbours and most other African countries, South Africa has a much more developed system and expertise in various fields, which could be utilised for the benefit of other less developed African countries. Under this pillar, the Bank will strive to foster the expansion of cooperation between South Africa and other regional member countries, especially those in the SADC region, through greater use of South African know-how to the benefit of the rest of the continent. South Africa presents an opportunity to share its home-grown experiences in the areas of financial management, customs administration, tax reforms and training through the South African Tax Institute, amongst others. This knowledge sharing and skills transfer scheme could be operationalised through a tripartite arrangement involving the Bank, South Africa and the third party country, with the Bank acting as a catalyst. For example, South Africa has a well developed PPP framework and has also helped to establish National Revenue Authorities in a number of African countries.

Strategic Objective III: Knowledge Management and Capacity Building

4.4.16 The third pillar is focused on the theme of Knowledge Management and Capacity Building and is aimed at supporting the lending programme and policy dialogue through improved knowledge as well as support for the development of critical capacity in government, municipalities, private sector, and the civil society.

4.4.17. *Improve Knowledge in Support of the Lending Programme and Policy Dialogue* (CSP Pillar 3 - Outcome 1). The Bank will develop knowledge partnership with South Africa and South African Institutions and other development partners in South Africa. Knowledge management and capacity building are also particularly important for achieving maximum development impact as envisaged under the ASGISA. This will require significant investment in high-quality, demand-driven economic and sector work (ESW) using grant resources, for example the MIC Fund and bilateral resources. Thus, ESW programme will provide the analytical underpinning of the lending programme, facilitate policy advice and broaden the scope for private sector development. Consistent with the Bank's focus on management for results and outcomes, ESW and capacity building will be programmed on the basis of their contribution to achieving the CSP outcomes.

4.4.18 *Improve Capacity in Central Government Ministries, Municipalities, and SOEs* (CSP Pillar 3 - Outcome 2). The objective would be to use grant resources through the MIC Trust Fund and bilateral resources to contribute to the improvement of the competence of staff in key technical positions so as to improve institutional performance, roles and responsibilities in government ministries, municipalities and parastatals. In this regards, the Bank will undertake capacity building and staff exchange programmes in key sectors and ministries in South Africa during the period covered by the proposed CSP.

4.4.19 In pursuance of this strategic objective, the Bank will explore ways of working with existing national programmes for municipalities such as the "Project Consolidate" which aims to improve provincial and local administration, including through the deployment of skilled professionals where they are most needed, as well as the DBSA's "Siyemza-Manje" initiative (Doing the right thing now) a project for municipal capacity building expected to help the municipalities in identifying the engineering expertise to execute municipal projects successfully. To ensure the programmes build sustainable capacity, the Bank will partner with these initiatives by facilitating exchange programmes in areas where needs are identified in the municipalities and in the SADC region. It is also expected that the Bank's support for PPP operations would have some direct impact on improving the competence of staff in key technical positions and performance in the public sector through their exposure to the skills of the private sector and the opportunity to capture the efficiency of the private sector. The Bank will also work with relevant departments of key academic and professional institutions in South Africa on ESW. Partnership with other development partners such as the World Bank, European Union and UNDP will also be sought in order to maximize the use of available technical and financial resources, as well as build common ground around critical policy issues. Knowledge sharing of the Bank's ESW will be an integral activity of the CSP implementation. As such, dissemination of key analytical work will be ensured during the CSP period to build wide knowledge sharing.

4.4.20 The Bank, having been designated as a strategic partner in the African Peer Review Mechanism (APRM) by the African Heads of State and Government, will continue to support the implementation of the recommendations of the APRM Country Review Report for South Africa through exchange and dialogue with the South African authorities. In addition to the country specific analytical work, South Africa could also benefit from on-going and planned regional studies being undertaken in the context of the RASP for Southern Africa. The Bank and SADC have agreed to undertake a study on Financial Integration and Capital markets Development in Southern Africa. The study will evaluate SADC financial integration and SADC financial system structures, explain the factors driving the process of financial integration, and discuss obstacles to integration as well as suggest policy responses to speed up the process of financial integration and capital markets development within the region.

4.5 Operationalizing the Partnership Strategy

Lending Operations

4.5.1 The results framework of the proposed CSP would be flexible in application. This is consistent with the stated approach of defining broad strategic priorities for the CSP period while making room for specific activities to be identified and agreed upon with the relevant beneficiaries (private, SOEs and public sector) periodically in a manner which is consistent with their planning and budgeting cycle. As such, the proposed work programme is intended to be tentative, and is subject to further detailed discussions and agreements with the relevant authorities. In this regards, the Bank, especially its Private Sector Department, will continue to undertake sensitisation and identification missions to South Africa, with a view to building the pipeline of projects and programmes. This approach will ensure that the Bank's programmes are demand driven and responsive to the emerging needs of the country. It would also afford the Bank the latitude to seize emerging opportunities to build new partnerships.

4.5.2 For the period 2008-2010, two infrastructure operations and one operation with a local development finance institution are envisaged. All these operations are likely to be provided under the Bank's non-sovereign guarantee scheme. The proposed operation with the local development finance institution will have a regional focus. It will seek to promote stronger economic integration within Southern Africa by supporting regional infrastructure projects as well as facilitate export oriented investments by private enterprises. The intermediate outcomes of the project include increasing the availability of financial resources for regional infrastructure projects, and improving financial intermediation for infrastructure financing.

4.5.3 In addition, there is on-going discussions with UNISA in the areas of assistance to fragile states of Africa, teacher development, accreditation, quality assurance, and establishment of regulatory frameworks for distance education, and partnering with UNISA as key service provider in distance learning education in the context of Bank-Funded projects in other countries.

Non-Lending Activities

4.5.4 During the programming cycle, the Bank will undertake ESW to deepen the Bank's partnership with South Africa on knowledge management. The work programme will encompass a number of areas which will be agreed with the authorities and other stakeholders, including among others, issues of human development and social inclusion, gender, inflation and exchange rate volatility, and the development of the second economy. In this regards, the Bank will collaborate with relevant departments of key academic and professional institutions in South Africa to undertake in-depth studies with a view to improving the knowledge base and its pipeline of projects in the country.

4.5.5 In pursuance of the objective of knowledge management and capacity building at the regional level, the Bank would use resources from the Infrastructure Project Preparation Facility (IPPF) which is housed in the Bank, the MIC Trust Fund and other bilateral resources to support capacity building for SADC and capacity for the preparation of regional projects. The Bank would collaborate with existing regional learning networks, for instance, the network of senior budget officials (the Collaborative Africa Budget Reform Initiative, or CABRI), which was started by South Africa, Uganda and Mozambique and has spread to about 20 countries, the network on statistics, the energy network, association of public utilities, etc. In this regards, the Bank would partner with South Africa to build the statistic capacity of countries in SADC during the CSP period.

4.5.6 The South African authorities have requested the Bank to consider collaborating with South Africa's Department of Trade and Industry on a project which will bring together in a single document all relevant information on the process of establishing a business in South Africa which should include the provision of information to public and private sector on the regulatory environment, how to open businesses, government policies to facilitate private sector activities, company registration processes, etc. The Bank will also seek to collaborate with South African Institutions including the South African Institute of International Affairs to undertake a study on the impact of South Africa on its Neighbours, the extent to which South Africa is a growth pole for the region and the role the Bank Group could play in enhancing the spill over effects of growth in South Africa. The projects could be supported by the Bank with grant resources from the MIC Trust Fund and other bilateral funds.

4.5.7 One ESW already agreed with the authorities is preparation of a Gender Profile and the team to undertake the study is being put together. The objective of the study will be to enhance Bank's dialogue with the Government on gender related issues, and to help identify future areas of intervention that will support gender mainstreaming. It is expected to be a joint activity with the Government, and the final report is expected to help Government prioritise its own activities regarding women and vulnerable groups, and be a resource document for people both within and outside of South Africa.

4.5.8 As a part of the CSP preparation process, the Bank prepared a Private Sector Country Profile (PSCP) for South Africa which was also discussed with the country stakeholders during the CSP dialogue mission and provided input into the CSP. The PSCP aims at enhancing the Bank's knowledge of the private sector structure, composition and strategies. The PSCP will assist the Bank in broadening the understanding of the investment climate, identifying major constraints and risks that have to be taken into account in formulating strategies for private sector development and designing and implementing investment projects.

4.5.9 Another critical ESW that will also be undertaken early in the programming cycle will be on the effectiveness of the Bank's partnership with South Africa. The study will attempt to answer the question why the Bank's investment operations in South Africa have been limited. The study will suggest necessary changes in the way the Bank does business so as to better take advantage of available investment opportunities in the country as well as deepen its partnership with South Africa for national and regional development.

4.5.10 **Local presence is critical to the operationalisation of the enhanced partnership strategy.** The Bank's partnership with South Africa cannot be effective if there is no local presence in the country. In this context the Bank and the Government are revisiting the initial plan to establish a regional office in South Africa and progress is now being made in resolving outstanding issues. The Office will facilitate effective dialogue with the authorities and country stakeholders on the various aspects of the strategy articulated above and facilitate collaboration with other development partners resident in the country.

Country Risk Profile and Financial Flexibility

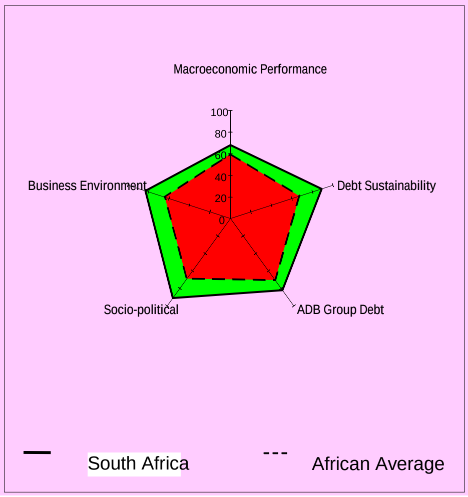
Figure 3 Business / Governance Environment

South Africa Ranking within Africa

First Quintile	First Quintile	First Quintile	First Quintile	First Quintile	First Quintile
Second Quintile	Second Quintile	Second Quintile	Second Quintile	Second Quintile	Second Quintile
Third Quintile	Third Quintile	Third Quintile	Third Quintile	Third Quintile	Third Quintile
Fourth Quintile	Fourth Quintile	Fourth Quintile	Fourth Quintile	Fourth Quintile	Fourth Quintile
Fifth Quintile	Fifth Quintile	Fifth Quintile	Fifth Quintile	Fifth Quintile	Fifth Quintile
Yr 2008	Yr 2006	Yr 2007	Yr 2007	Yr 2006	Yr 2006
Ease Doing Business (WB)	FDI (OECD)	Corruption Perception (TI)	Political Stability (KKIndex)	Governance. Factor (ADB)	CPIA (ADB)

4.5.11 As a middle income country, lending to South Africa will be guided by the Bank's credit worthiness analysis and exposure indices as well as performance under the CPIA. An analysis of the Bank's CPIA results over the period, 2005 and 2006 indicates that South Africa has shown consistently strong CPIA rating having been rated overall above 3.75 in both years. The 2006 evaluation under CPIA was satisfactory and placed South Africa in the First Quintile and number one overall among 53 countries and in all the four broad policy clusters.

Figure 4: South Africa: Country Risk at a Glance (2008)



4.5.12 Based on the Bank's internal rating process, South Africa is the best rated country in 2006 with an overall rating of 1 (very low risk) and performed significantly above the African average on all five risk indices (see figure 4). South Africa's debt profile, internal and external, is sustainable. The country's portfolio, though relatively small, is amongst the leading portfolios within the Bank. Indeed the Bank's outlook for South Africa is in line with ratings of Baa1 from Moody's and BBB+ from S&P. Thus, country risk is also not a constraint to extending investment resources to South Africa if demand exists.

4.5.13 The CPIA assessment and the Bank's credit worthiness analysis revealed that South Africa is a very low risk country and a strong performer. Based on the above analyses the proposed lending scenario for South Africa during the programming period is the base-case scenario under which South Africa's indicative annual sustainable lending programme is UA 676 million. However, the Bank's annual lending programme in South Africa during the CSP period will also depend on the demand for resources (public and private) and the type of instruments used to assist the country. The annual lending envelope will thus vary between UA 476 million (if emphasis is put on private sector operations and fast disbursing instruments) to UA 984 million (if emphasis is put on public sector operations and slow disbursing instruments).

5. RESULTS-BASED MONITORING AND EVALUATION

5.1 Monitoring of CSP Outcomes and Performance

5.1.1 The Results Framework establishes the result chains for the Bank strategy and defines the performance indicators for monitoring progress *vis-à-vis* longer term strategic goals for the country. In most cases, intermediate indicators and milestones are quantified with expected target ranges; in others, more qualitative information is required. In line with the self-monitoring principle incorporated in the results based assistance strategy, a mid-term review will be undertaken midway into the implementation of the CSP to assess implementation progress of the strategy at mid-course. The objective is to take stock of progress made, constraints and challenges encountered during the first half of the implementation of the CSP with a view to drawing useful lessons for the remaining CSP period. The mid-term review of the CSP will also provide an opportunity to improve on the results framework proposed in the current CSP and will involve an assessment of the Bank Group's and the country stakeholders' performance in terms of adequate monitoring of the implementation of the strategy, effectiveness and efficiency in managing the portfolio and the adequacy or otherwise of the level of support from the National Treasury and the Bank Group during the first half of the implementation of the CSP.

5.2 Managing Risks

5.2.1 There are three main risks that could seriously affect the implementation of the proposed strategy. First, as the strategy is focussed on the private sector, maintaining a conducive business environment will be critical to its successful implementation. However, inflation pressures as well as exchange rate volatility is considered to be a major threat to business confidence. This risk is known to the authorities and is expected to be mitigated by continued fiscal discipline, the moderate trend in unit labour costs and the benign world inflation. The Bank will also closely follow through policy analysis and policy dialogue.

5.2.2 Another major risk is the high level of social demands, especially at local level, which puts considerable pressure on the local government elected in 2005 to produce immediate results. Also at the national level, frustrations may increase due to the slow pace and uneven progress of black economic empowerment, which is sometimes considered not broad enough. The Government is taking steps to minimise this risk by specifically addressing the challenges of the so-called second economy through planned investments in local infrastructure and service delivery at national, provincial and local government levels. The Bank's involvement with sub-national authorities in the area of capacity building will also contribute to mitigating this risk.

5.2.3 A third risk has to do with the cost of the Bank's loan products. The authorities have indicated that they find borrowing from the ADB window too expensive, especially with regard to pricing. There is, therefore, a risk that envisaged operations to SOEs and the private sector may not materialise if cheaper alternative sources of financing is available to them. To mitigate this risk the Bank is currently articulating its strategy for Middle Income Countries (MICs) to ensure competitiveness of its loan products and is also increasing the funds allocated to technical assistance. The proposed ESW on effective partnership with South Africa is also expected to throw up recommendations which would mitigate this risk.

5.3 Country Dialogue Issues

5.3.1 ***Support to Sub-national entities.*** The Bank will undertake detailed dialogue with the authorities and other stakeholders on the role that it can play to support sub-national entities. The Bank's support to sub-national entities will also put emphasis on knowledge sharing and capacity building at the levels of provincial government and local government to improve service delivery. In this context, two ESW on municipal financing and provision of affordable housing have been prepared by the Bank.

5.3.2 **South Africa serving as a growth pole for the Southern Africa sub-region and for regional integration and development.** For South Africa to evolve as a meaningful growth pole in Southern Africa there is the need for continued dialogue with a view to finding answers to the following and similar questions: How can South Africa's neighbours derive maximum benefit from the partnership arrangement between the Bank and South Africa? What should South Africa and the Bank be doing to assuage the perception by South Africa's neighbours of dominance related to its strong economic position in the region? What should be done to ensure that South Africa's neighbours do not see the regional integration partnership between the Bank and South Africa as a means to merely use them as retail outlets rather than production/development partners?

6. CONCLUSIONS AND RECOMMENDATIONS

6.1 Conclusions

6.1.1 South Africa has a strong economic performance track record and represents investment opportunities for the Bank. The medium-term outlook is also encouraging but there are a number of challenges facing the country including high unemployment and inequality, as well as uplifting the 'second' economy without damaging the growth prospect of the 'first' economy. Government is however, making progress in addressing these challenges from its own resources.

6.1.2 The Bank would combine lending operations, especially to parastatals and the private sector, with knowledge deepening and sharing to enhance its advisory role and policy dialogue. To take advantage of the investment opportunities, especially in the area of infrastructural development (including regional infrastructure) the Bank will continue to explore ways to minimise transactions costs and encourage the use of country systems in the spirit of the Paris Declaration. Local presence in the country through the establishment of the South Africa Regional Office will also be critical for the enhancement of the Bank-South Africa partnership.

6.2 Recommendations

6.2.1 The Board is requested to consider and approve the proposed 2008-2012 Bank Group partnership strategy for South Africa aimed at enhancing private sector competitiveness, regional integration and knowledge management; and a lending programme oriented towards providing support for infrastructure development (including cross-border investment in infrastructure), SMME development, as well as non-lending operations focusing on Economic and Sector Work and capacity-building activities. The Board is also invited to note the indicative lending limit set between UA 476 and UA 984 million per year over the period 2008-2012, for Bank Group operations in South Africa.

ANNEX 1 SOUTH AFRICA – RBCSP: Results Framework Monitoring Matrix			
Broad Government Objectives	***Broad Areas of AfDB Focus***	***Expected Outcomes During the CSP Period***	***Output/Progress Indicators***
Strategic Objective/Pillar I : Enhancing Private Sector Competitiveness			
Targeted investments in the rural areas and urban neighbourhoods and peri-urban townships to improve the quality and the distribution of infrastructure facilities in order to bring them at par with the rest of South Africa	***1. Support the Improvement of Infrastructure Services***	• Increase capital spending at all levels of government for infrastructure spending • Reduce the backlog of maintenance and increase the amount of resources for maintenance services for infrastructure • Increase the provision of local roads, bulk water infrastructure and water supply network • Improved reliability of energy supply and its access to the poor	Provide support to at least two (2) infrastructure or other projects that contributes to the improvement of the enabling business environment. Support to at least one (1) PPP project in infrastructure and provision of guarantees to PPP in infrastructure. Increased capital expenditure budget of local authorities by providing support to municipalities in the provision of infrastructure in local communities. Electricity supply reliability measured by average number of hours of energy outage per consumer per year.
i. Increase Levels of Investment in the First Economy ii. Lower Cost of Doing Business and Enhance Levels of Competition iii. Promote expansion of job creating manufacturing and services sectors iv. Promote enterprise growth, especially Black-end women-owned and managed v. Pay particular attention to further growth of the small and medium business Sector • Improve access to finance for micro-enterprises, including access to finance for SME's. • Increase the rate of investments by exploiting private investment, development of SMME's etc • Ensure incorporation of SMME needs in sector strategies, and promote specific sectors such as arts and crafts to benefit Second Economy communities	***2. Improve Financial Intermediation, especially for SMEs***	• Increased access to capital by private sector, especially SMEs and black enterprises • Improved business and investment environment • Improved black and women participation in meaningful ownership, control, management and high-level skill positions in the sector	Increase in the number of Previously Disadvantaged Individuals (PDIs) that are able to overcome their financial and technical constraints and buy into SME franchise. Expansion of services of technical assistance and financial institutions to previously underserved markets`. Needs of SMMEs are incorporated into sector strategies via the Customised Sector Programmes methodology Each financial institution in South Africa to attain, by 2010, a minimum of 25% black ownership, measured at the holding company level
Strategic Objective/Pillar II: Partnership for Regional Integration and Development			
(i) Increase regional trade and investment.	***1. Support for Regional Infrastructure***	• Provide funding in support of multination projects in physical infrastructure and energy project with regional dimension and impacts. • Provide funding in support of infrastructure projects along economic and development corridors (spatial development initiatives).	• Increase participation by South African companies in regional infrastructure and energy projects. • Increase in number and investment volume of projects finance by the Bank in SADC region and in South Africa with regional impacts. • Number of SDI projects that are financed by the Bank

	2. Facilitation of Cross-border Investment	• Facilitate cross-border investment, particularly in infrastructure and energy. • Partner with institutions that support cross-border SMME development in South Africa.	• Progress in the process of establishing a SADC regional free trade area. • Increase in the number and volume of bond issuance by the Bank in the domestic capital market in the SADC region.
	3. Using South Africa's expertise for the institutional development of African LICs	• Partner with South Africa to develop national systems in other SADC and African countries in areas where South Africa has well developed framework and systems. • Partner with South African institutions, including the JSE to strengthen and deepen regional institutions including financial markets.	• Increase in the number of national institution that received technical assistance for development of national systems through partnership with SA in SADC countries in particular and other African countries in general. • Increase in the number of transactions undertaken in the stock exchanges within the region.
Strategic Objective III: Knowledge Management and Capacity Building			
(i) Strengthening the capacity of the state to implement programs and provide services. (ii) Support to municipalities to improve planning and implementation of programs.	***1. Improve Knowledge in Support of the Lending Programme and Policy Dialogue***	• Develop knowledge partnership between the Bank and South Africa and South African Institutions • Develop knowledge partnership with other development partners in South Africa.	• Develop knowledge building and sharing relationship with at least 2 key institutions in South Africa. • Undertake at least 1 knowledge building and sharing activity and 1 ESW with key South African Institutions • Undertake at least 1 knowledge and sharing activity and 1 ESW jointly with development partners • Increase media coverage of ADB knowledge products and activities in South Africa
	2. Improve Capacity in Central Government Ministries ,Municipalities, and SOEs	• Improve competence of staff in key technical positions and improve institutional performance, roles and responsibilities	• At least 2 capacity building and staff exchange programmes in place in key sectors and ministries.

ANNEX 2

ACHIEVING MILLENNIUM DEVELOPMENT GOALS

4.1 **South Africa is on course in meeting the Millennium Development Goals**. The 2005 UNDP Millennium Development Goals Country Report for South Africa shows that, except for HIV/AIDS, the country is well on track to meet all MGD goals and targets. It has in fact, already met some of them (see table A2 - 1). This may be related to the fact that the democratic government set for itself many goals similar to the Millennium Declaration when it came to power in 1994. With the exception of health indicators, South Africa outperforms Sub-Saharan Africa in every other indicator, and also outperforms the Middle East and North Africa region in the majority of indicators. However, compared with middle-income countries outside Africa, its performance is lower, suggesting that more effort is required for the country to catch up with this group of countries.

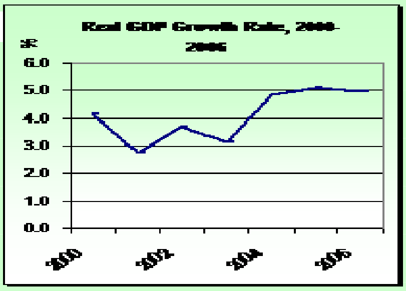
Table A2 - 1: South Africa: Millennium Development Goals

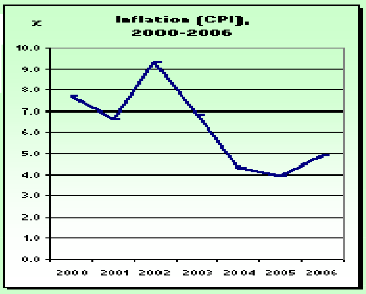
MDG Goal	Indicator	1990/01	2000	2004/05	2006/07
Goal 1: Eradicate Extreme Poverty	Poverty (US$1 a day head count ratio, %)	…	7.6	8.6	…
	Share of Consumption to poorest quintile (%)	3.6(1995)	3.5	3.5	…
Goal 2: Achieve Universal Primary Education	Primary education completion (gross intake to final primary grade, %)	…	91.289	100.0	…
	Secondary Enrolment (gross, %)	78.3	81.4	91.5	91.0
Goal 3: Promote Gender Equality	Ratio of girls to boys in primary and secondary school (%)	102.0	101.0	100.0	100.0
	Women in non-agricultural sector (% of total non-agricultural employment)	…	…	16	…
Goal 4: Reduce Child Mortality	Child mortality (under 5 mortality rate per 1000)	72.7	73.1	70.0	66.0
	Measles immunisation (% of children ages 12-23 months)	79.0	77.0	84.0	85.0
Goal 5: Improve Maternal Health	Maternal mortality ratio (modelled estimate per 100,000 live births)	230..	104(2002)	110(2003)	…
	Births attended by skilled health staff (% of total)	82.0(1995)	84.4(1998)	92(2003)	…
Goal 6: Combat HIV/AIDS and other diseases	HIV prevalence (% of the pop. ages 15-49)	…	19.9	16.2	18.6
	Incidence of TB (per 100,000 people)	224.0	563.4	645.0	722.4
Goal 7: Ensure environmental sustainability	**Access to improved water source (% of the population)**	**83.0**	70.0	88.0	84.7
	Access to improved sanitation facilities (% of the population [2004]	63	86	65	71
Goal 8: Develop a global partnership for development (new technologies)	Fixed-line and mobile phone subscribers (per 1000 people) **[2005]**	…	353	825	…
	Internet users (per 1000 people)	…	64.9	109	…

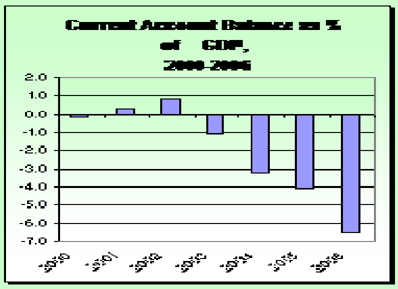
Source data: ADB Statistics Department and Country Reports.
…: Data not available
**: Fixed line only*

Annex 3: South Africa
Selected Macroeconomic Indicators

Indicators	Unit	2000	2002	2003	2004	2005	2006	2007
National Accounts								
GNI at Current Prices	Million US $	0	122,973	135,145	172,574	231,064	260,242	...
GNI per Capita	US$	3,050	2,640	2,870	3,630	4,820	5,390	...
GDP at Current Prices	Million US $	132,877.9	110,874.9	166,653.5	216,443.7	242,001.6	255,108.2	274 809.6
GDP at 2000 Constant prices	Million US $	132,877.9	141,519.6	145,935.0	152,996.7	160,784.6	168,788.9	177 397.1
Real GDP Growth Rate	%	4.2	3.7	3.1	4.8	5.1	5.0	5.1
Real per Capita GDP Growth Rate	%	2.7	2.5	2.0	3.9	4.3	4.3	4.5
Gross Domestic Investment	% GDP	15.9	16.1	16.9	17.6	18.4	20.5	20.4
Public Investment	% GDP	2.7	2.6	3.4	1.6	2.2	2.0	2.2
Private Investment	% GDP	13.2	13.4	13.5	16.0	16.1	18.5	18.3
Gross National Savings	% GDP	15.8	16.9	15.8	14.4	14.1	13.9	14.7
Prices and Money								
Inflation (CPI)	%	7.7	9.3	6.8	4.3	3.9	4.9	5.0
Exchange Rate (Annual Average)	local currency/US$	9.9	11.7	9.9	8.7	9.0	10.5	...
Exchange Rate (End of Period)	local currency/US$	7.6	8.6	6.6	5.6	6.3	7.0	...
Monetary Growth (M2)	%	7.2	7.6	14.8	8.8	19.9	10.7	...
Money and Quasi Money as % of GDP	%	54.1	53.5	57.0	55.9	60.9	60.1	...
Government Finance								
Total Revenue and Grants	% GDP	22.9	23.3	23.2	24.0	25.6	26.7	27.6
Total Expenditure and Net Lending	% GDP	24.8	24.5	25.2	25.7	26.2	26.3	26.9
Overall Deficit (-) / Surplus (+)	% GDP	-1.9	-1.2	-2.0	-1.7	-0.6	0.4	0.7
External Sector								
Exports Volume Growth (Goods)	%	16.8	1.0	0.1	2.9	8.0	5.6	10.3
Imports Volume Growth (Goods)	%	5.4	5.4	8.0	14.5	10.7	18.4	11.0
Terms of Trade Growth	%	-9.1	2.3	0.9	0.7	0.7	4.4	-0.4
Current Account Balance	Million US $	-171.9	920.4	-1,805.8	-6,919.6	-9,793.3	-16,608.1	-18,495.2
Current Account Balance	% GDP	-0.1	0.8	-1.1	-3.2	-4.0	-6.5	-6.7
External Reserves	months of imports	2.7	2.8	2.2	3.0	3.6	3.6	...
Debt and Financial Flows								
Debt Service	% exports	13.8	12.8	12.7	10.6	8.3	8.4	9.0
External Debt	% GDP	27.8	29.7	22.9	20.1	19.1	22.4	21.5
Net Total Financial Flows	Million US $	-493.3	3,000.1	5,427.0	10,235.7	3,638.5	...	...
Net Official Development Assistance	Million US $	487.3	504.6	641.3	628.2	700.0	...	...
Net Foreign Direct Investment	Million US $	887.9	756.7	733.7	799.2	6,250.8	-323.5	...







Source : ADB Statistics Department; IMF: World Economic Outlook, September 2007 and International Financial Statistics, October 2007;
World Bank: Development Data Platform Database, September 2007. United Nations: OECD, Reporting System Division, January 2007.

Notes: … Data Not Available

Last Update: February 2008

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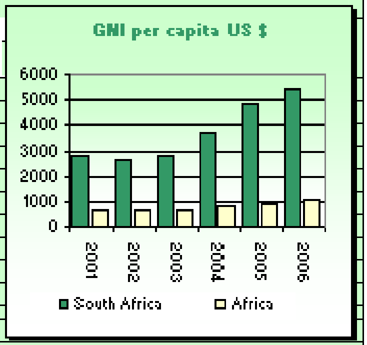
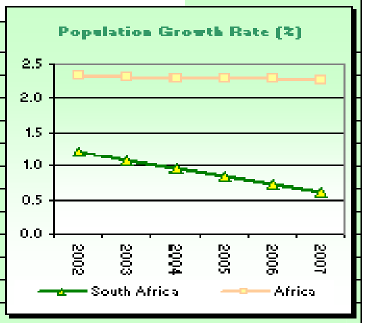
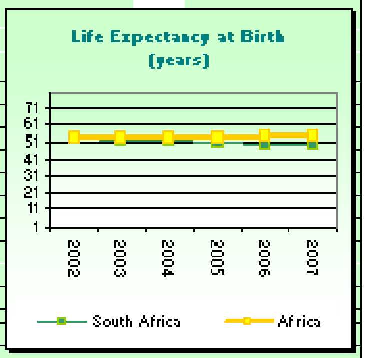
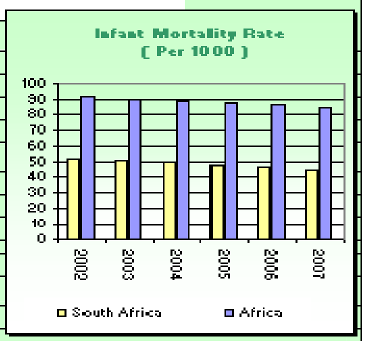
Annex 4: South Africa
COMPARATIVE SOCIO-ECONOMIC INDICATORS

	Year	South Africa	Africa	Developing Countries	Developed Countries
Basic Indicators					
Area ('000 Km²)		1 221	30 307	80 976	54 658
Total Population (millions)	2007	48.6	963.7	5 448.2	1 223.0
Urban Population (% of Total)	2007	57.8	39.8	43.5	74.2
Population Density (per Km²)	2007	39.8	31.8	65.7	23.0
GNI per Capita (US $)	2006	5 390	1 071	2 000	36 487
Labor Force Participation - Total (%)	2005	40.1	42.3	45.6	54.6
Labor Force Participation - Female (%)	2005	39.1	41.1	39.7	44.9
Gender -Related Development Index Value	2005	0.667	0.475	0.694	0.911
Human Develop. Index (Rank among 177 countries)	2005	121	n.a.	n.a.	n.a.
Popul. Living Below $ 1 a Day (% of Population)	2004	8.6	34.3	...	...
Demographic Indicators					
Population Growth Rate - Total (%)	2007	0.6	2.3	1.4	0.3
Population Growth Rate - Urban (%)	2007	1.0	3.5	2.6	0.5
Population < 15 years (%)	2007	31.8	41.0	30.2	16.7
Population >= 65 years (%)	2007	5.1	3.5	5.6	16.4
Dependency Ratio (%)	2007	56.9	80.1	56.0	47.7
Sex Ratio (per 100 female)	2007	96.7	99.3	103.2	94.3
Female Population 15-49 years (% of total population)	2007	26.8	24.2	24.5	31.4
Life Expectancy at Birth - Total (years)	2007	49.3	54.2	65.4	76.5
Life Expectancy at Birth - Female (years)	2007	49.7	55.3	67.2	80.2
Crude Birth Rate (per 1,000)	2007	22.3	36.1	22.4	11.1
Crude Death Rate (per 1,000)	2007	17.0	13.2	8.3	10.4
Infant Mortality Rate (per 1,000)	2007	44.8	85.3	57.3	7.4
Child Mortality Rate (per 1,000)	2007	66.0	130.2	80.8	8.9
Total Fertility Rate (per woman)	2007	2.6	4.7	2.8	1.6
Maternal Mortality Rate (per 100,000)	2003	110.0	622.9	450	9
Women Using Contraception (%)	2003	50.6	26.6	59.0	74.0
Health & Nutrition Indicators					
Physicians (per 100,000 people)	2007	75.3	38.2	78.0	287.0
Nurses (per 100,000 people)	2007	329.3	110.7	98.0	782.0
Births attended by Trained Health Personnel (%)	2003	92.0	43.7	56.0	99.0
Access to Safe Water (% of Population)	2006	84.7	62.3	78.0	100.0
Access to Health Services (% of Population)	2004	...	61.7	80.0	100.0
Access to Sanitation (% of Population)	2006	71.0	44.2	52.0	100.0
Percent. of Adults (aged 15-49) Living with HIV/AIDS	2007	18.6	4.5	1.3	0.3
Incidence of Tuberculosis (per 100,000)	2006	722.4	298.3	144.0	11.0
Child Immunization Against Tuberculosis (%)	2006	97.0	78.1	82.0	93.0
Child Immunization Against Measles (%)	2006	85.0	68.0	73.0	90.0
Underweight Children (% of children under 5 years)	2003	9.0	39.0	31.0	...
Daily Calorie Supply per Capita	2004	3 004	2 434	2 675	3 285
Public Expenditure on Health (as % of GDP)	2007	3.1	5.6	1.8	6.3
Education Indicators					
Gross Enrolment Ratio (%)					
Primary School - Total	2005/06	103.0	96.7	91.0	102.3
Primary School - Female	2005/06	101.0	90.4	105.0	102.0
Secondary School - Total	2005/06	91.0	43.1	88.0	99.5
Secondary School - Female	2005/06	92.0	36.5	45.8	100.8
Primary School Female Teaching Staff (% of Total)	2005/06	74.4	47.5	51.0	82.0
Adult Illiteracy Rate - Total (%)	2007	12.2	33.3	26.6	1.2
Adult Illiteracy Rate - Male (%)	2007	11.6	25.6	19.0	0.8
Adult Illiteracy Rate - Female (%)	2007	12.7	40.8	34.2	1.6
Percentage of GDP Spent on Education	2007	4.6	4.7	3.9	5.9
Environmental Indicators					
Land Use (Arable Land as % of Total Land Area)	2005-07	12.1	6.0	9.9	11.6
Annual Rate of Deforestation (%)	2000-07	0.1	0.7	0.4	-0.2
Annual Rate of Reforestation (%)	2000-07	2.0	10.9	...	...
Per Capita CO2 Emissions (metric tons)	2005-07	7.4	1.0	1.9	12.3









Sources : ADB Statistics Department Databases; World Bank: World Development Indicators; UNAIDS; UNSD; WHO, UNICEF, WRI, UNDP; Country Reports from MOH, MOE, National Treasury Department

last update : February 2008

Note : n.a. : Not Applicable ; … : Data Not Available;

Annex 5

SOUTH AFRICA: BANK GROUP APPROVED OPERATIONS

TABLE A4 – 1: PUBLIC SECTOR GUARANTEED LOANS (As at 31 December 2007)

Operation	Date of Approval	Date of Signature	Date of Entry into Force	Approved Amounts		Amount Disbursed	% Disbursed	Status
				Rand Million	US $ Million			
A. Public Sector Operations								
1. First Line of Credit to DBSA	15/12/1997	27/10/1998	29/12/1998	340.0	70.0	340.0	100%	Completed
2. Second Line of Credit to DBSA	10/11/1999	29/11/1999	07/08/2000	500.0	-	500.0	100%	Completed
3. Line of Credit to IDC	28/06/2000	03/01/2003	15/04/2003	-	100.0	100.0	100%	Completed
4. Guarantee of Bond Issue to DBSA	03/05/2000	Cancelled before signing		-	330.0	-	-	Cancelled
5. Third Line of Credit to DBSA	16/07/2003	05/08/2004	07/12/2004	-	100.0	100.0	100%	Completed

TABLE A4 – 2: NON-SOVEREIGN GUARANTEED APPROVED OPERATIONS (As at 31 December 2007)

Operation	Date of Approval	Date of Signature	Type of Investment	Currency	Approved Amounts Million	Amount Disbursed	% Disbursed	Status
1. South African Infrastructure Fund	11/06/1997	23/07/97	Equity	Rand	113. 075	113.075	100%	Equity Participation On-going
2. Msele Ned Ventures Ltd.	11/12/1997	11/11/98	Equity	Rand	12.0	12.0	100%	Equity Participation Bank divested its equity in 2004
3. Infrastructure Finance Corporation (INCA I)	08/12/1999		Loan	Rand	200.00	0	0%	Cancelled
4. Infrastructure Finance Corporation (INCA II)	18/09/2002	cancelled	LoC	US$	20.0	-	-	Cancelled
5. FirstRand Bank Ltd	09/07/2003	cancelled	Loan	US$	75.0	0	0%	Cancelled
6.Non Sovereign Guarantee Line of Credit to IDC	05/11/2003	26/11/2004	LoC	US$	50.0	25.0	50%	Undisbursed balance cancelled
7. Development of SMEs through Franchising	19/05/2004	30/04/2005	LoC	Rand	45.0	0	0%	To be cancelled
8. Credit Risk Sharing Agency to NEDCOR	01/12/2004	20/07/2005	LoC	Rand	1000.0	0	0%	On-going
9. Fourth Line of Credit to DBSA	21/07/2006	21/06/2007	Loc	USD	100.0	0	0%	On-going
10 Eskom	28/06/2007		Loan	USD	500.0	0	0%	On-going
11 Nedbank Subordinated Bond	28/06/2007	02/07/2007	Bond/Equity	Rand	1,000.0	1,000.0	100%	On-going

ANNEX 6
SOUTH AFRICA: ADMINISTRATIVE MAP
COUNTRY STRATEGY PAPER (2008 – 2012)

This map was provided by the African Development Bank exclusively for the use of the readers of the report to which it is attached. The names used and the borders shown do not imply on the part of the Bank and its members any judgment concerning the legal status of a territory nor any approval or acceptance of these borders.