AFRICAN DEVELOPMENT BANK

REPUBLIC OF SOUTH AFRICA

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SOUTHERN AFRICA RESOURCE CENTER (SARC)

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1 UA = US$ 1.50833
1 UA = Euro 1.1565
1 UA = ZAR 12.2788

FISCAL YEAR

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ACRONYMS AND ABBREVIATIONS

ADB	African Development Bank
ADF	African Development Fund
ANC	African National Congress
ASGISA	Accelerated and Shared Growth Initiative of South Africa
BRICS	Brazil, Russia, India, China and South Africa
CPPR	Country Portfolio Performance Report
CSP	Country Strategy Paper
COMESA	Common Market of Eastern and Southern Africa
COPE	Congress of the People
DFID	UK Department for International Development
EAC	East African Community
EMBI	JP Morgan’s Emerging Markets Bond Index
GDP	Gross Domestic Product
GoRSA	Government of Republic of South Africa
HEST	Higher Education, Science and Technology
HIV/AIDS	Acquired Immunodeficiency Virus/Acquired Immunodeficiency Syndrome
IMF	International Monetary Fund
IFC	International Finance Cooperation
JICA	Japanese International Cooperation Agency
MDGs	Millennium Development Goals
NDP	National Development Plan- Vision for 2030
NGP	New Growth Path 2011-2020
NPC	National Planning Commission
OECD	Organization for Economic Cooperation and Development
OSBP	One-stop Boarder Post
PEFA	Public Expenditure and Financial Accountability
PPPs	Public-Private Partnerships
SADC	Southern African Development Community
SACU	Southern African Customs Union
SIPs	Strategic Integrated Projects
SMME	Small, Medium and Micro Enterprises
UA	Unit of Account
UNDP	United Nations Development Program
WHO	World Health Organization

GENERAL MAP OF SOUTH AFRICA

EXECUTIVE SUMMARY

South Africa's potential growth has slowed over the last few years. Considerable efforts will be needed to meet the Government's goal of raising per capita income to at least US$ 13,750 and to create 11 million new jobs by 2030. Moreover, inequality continues to be very high, suggesting that making growth more inclusive remains an important policy challenge.

The authorities have diagnosed the key constraints to raising potential growth and recognize the need for deep-rooted structural reforms. The broad aim of the reforms is to raise the share of private investment, including 'green growth' technologies, and improve the level of education and skills in order to raise productivity levels closer to those of other emerging market countries. Towards this end, reforms envisage improvements in governance and inclusiveness, promoting catalytic investment projects, focusing on high value-added manufacturing and services sectors, as well as broader economic reforms to raise incomes of the poorest households and reform public finances to ensure their sustainability and remove distortions.

The New Growth Path and the National Development Plan support the government's long-term goal of building a harmonious and prosperous society through livelihood improvement, and regionally balanced and environmentally sustainable growth. Reforms will be carried out to stem rising income inequality, address structural imbalances, and further open up the economy. Public expenditure will be geared towards livelihood improvement, and strong support will be provided to education, healthcare, social security and public housing. Infrastructure remains a high priority with an emphasis on promoting rural development and emerging strategic industries, in particular modern clean energy and environment-friendly technologies, while piloting development of green and low-carbon cities. Resource conservation to combat climate change and improve natural resource management is a priority

This new CSP therefore seeks to position the Bank to continue playing a catalytic role in South Africa's development process through an enhanced operational focus on innovation and value addition to support manufacturing and job creation. It promotes intensified focus on generating knowledge, sharing best practices, building capacity, and fostering regional cooperation. Lending activities will include smaller demonstration and pilot-type projects for scaling-up through domestic financing. This, in turn, would facilitate knowledge sharing among executing agencies and with other developing member countries through South-South cooperation, and foster a stronger strategic focus on inclusive and environmentally sustainable growth as well as regional cooperation and integration. The opening of the Southern Africa Resource Centre (SARC) has ensured better partner coordination. SARC is working closely with South Africa and the Regional Economic Communities to deepen regional integration and economic cooperation to enhance the region's competitiveness and diversification of economic activity to spur inclusive and sustainable growth. The opening of SARC has also enhanced portfolio performance through (i) improved consultation with local authorities, as well as development partners for joint initiation, design, financing and monitoring of projects, and (ii) timely support to capacity development of implementing agencies in various aspects of project management. In addition, collaboration between ECON and SARC has significantly enhanced Bank capacity to respond with knowledge solutions on emerging issues as well as preparation of influential policy notes on key issues.

I. INTRODUCTION

1.1 **The Bank's current Republic of South Africa Country Strategy Paper (CSP) 2008-2012 (ADB/BD/WP/2008/12/Revised) was approved by the Bank's Board of Directors in April 2008**. This new CSP for the period 2013-2017 is anchored on the country's new development strategies, the New Growth Path (NGP) and the National Development Plan- vision for 2030, and on the Bank's new long-term strategy (LTS) 2013-2022. The CSP provides an assessment of the country's development prospects and challenges, national strategic options, and the role that the Bank could play, in collaboration with the Government and other development partners, in helping the country realize its development goals.

1.2. **A number of factors make a new country strategy for South Africa timely**. These include, among others: chronic high level of unemployment, poverty and inequality despite steady economic growth during the past decade; the recent announcement by the Government of large scale medium and long term infrastructure investment plans; the country's accession to the BRICS group of fast growing emerging market economies; and the adoption of new development strategies by the Government and the Bank Group. These together provide an opportunity for both South Africa and the Bank to build a renewed partnership to foster the country's economic development and regional integration in Southern Africa.

II. COUNTRY CONTEXT AND PROSPECTS

2.1. Political Context

2.1.1. **South Africa is a constitutional multiparty democracy characterized by free and fair elections.** It is also characterized by a dominant political party with the African National Congress (ANC) winning landslide victories in all four democratic elections since the end of the Apartheid regime in 1994. The ANC's liberation credentials and economic resources make it difficult for opposition parties to break into electoral politics. The ANC's long-term power is guaranteed through its participation in the Tripartite Alliance with the South African Communist party and the Congress of South African Trade Unions. The balance of power within the Tripartite Alliance remains strongly in favor of the ANC.

2.1.2. **The debate on land reform and nationalisation of mines still occupy policy debates within the ruling party and is likely to intensify leading up to the party's national elective conference in December 2012 and the next general elections in 2014.** The ability of the Government (at the national, provincial, and municipal levels) to deliver essential social services in the townships, informal settlements, and rural communities remains a serious challenge.

2.2. Economic Context

2.2.1. **Following a strong recovery from the downturn of 2008‒09, economic momentum in South Africa is losing steam against the backdrop of a weaker external environment**. As the recovery took hold, macroeconomic policies moved towards a less accommodative stance from early 2010. As a result, inflation remains contained but outside the target band of 3-6 percent and the rapid post-crisis buildup in public debt to finance the 2010 FIFA World Cup and household debt is leveling off. More recently, the growth of manufacturing exports has begun to ease, while commodity exports have thus far remained resilient. With regard to sectoral trends, the contribution of the primary sector (mining and agriculture) to GDP has declined substantially, while that of the secondary sector (manufacturing, electricty; gas and water; and construction) declined marginally. The contribution of the tertiary sector grew from 49 percent in 1994 to 57 percent in 2011.

2.2.2. **Increasing potential growth and reducing income inequalities are the key challenges over the medium term.** High and stable growth requires sustained structural reforms anchored around medium-term fiscal consolidation. This would help raise productivity and target public assistance to the most needy. To further deepen the inclusiveness of growth, consideration could be given to use the institutional frameworks to introduce innovative social partnerships in critical areas such as skills development and job creation for youths. Strong partnerships with the manufacturing and energy sectors would also boost growth and create employment opportunities in green growth technologies.

2.3. Recent Economic Developments and Outlook

2.3.1. **Economic activity is easing.** Following the rebound in 2010, private consumption growth remained strong through the third quarter of 2011 giving robust employment and wage growth. Manufacturing export growth has weakened, although commodity exports have nevertheless continued to grow at a healthy pace. Forward-looking sentiment indicators suggest less optimistic near-term prospects (Figure 1).

2.3.2. T**he output gap has widened slightly but inflation remained contained**. This reflects the timely monetary policy tightening that began in 2010 and the easing of temporary supply side factors which had increased headline inflation in the middle of 2011. Core inflation rose modestly, reaching 4.6 percent in May 2012, reflecting the recovery in domestic demand.

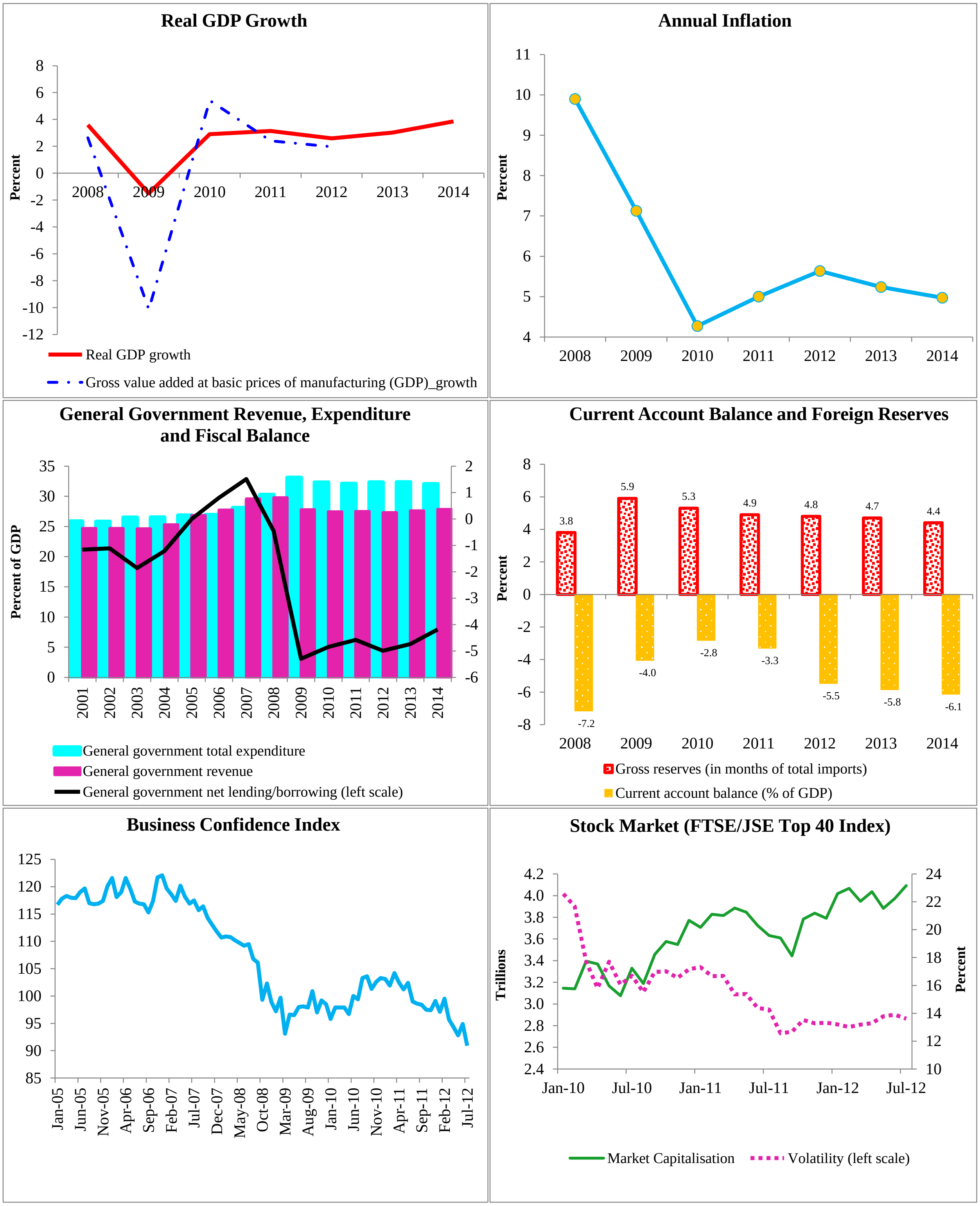
2.3.3. **The monetary policy stance has correctly balanced the risks to growth and inflation.** Headline inflation is projected to ease in 2012 as domestic demand moderates. As a result, policy rates should be maintained around current levels, but should be eased if growth prospects worsen significantly. The authorities should continue to allow two-way flexibility of the exchange rate to allow the currency to move in line with fundamentals, while limiting intervention to smooth out excess volatility.

2.3.4. **Notwithstanding the weakening environment, South Africa's external position remains strong.** The real effective exchange rate remained broadly stable in the year through July 2012 before the recent episode of market volatility, and the current account surplus is expected to have remained roughly constant in 2012. This reflects stronger commodity exports being offset by robust consumption and capital goods imports.

2.3.5. **Continued strong growth in credit to households has increased household indebtedness in recent years**. Bank credit to the private sector has risen by 13.7 percentage points to 87 percent of GDP during 2002−2008 and has averaged about 77 percent of GDP since then. Despite the recent growth of credit, the banking system remains sound. Overall credit growth continues to decelerate since 2008, but there are no evident signs of overheating or asset price pressures. Against an average capital adequacy ratio of 14.3 percent over 2009-2011 period nonperforming loans have declined by 1.2 percentage points to around 4.6 percent in March 2012. Housing prices rose by 3.3 percent nationwide during 2008−2011 period, but have eased more recently and remain in line with fundamentals, although certain areas have seen sharp rises.

2.3.6. **Fiscal policy continues to be countercyclical in support of growth and employment given the continued weakness in global markets**. Barring significant spending shortfalls at the

Figure 1. South Africa Selected Economic Indicators



Sources: SA National Treasury, SA Reserve Bank, SA Statistics, SA Chamber of Commerce and Industry, SA JSE Limited, AfDB, IMF

subnational level due to capacity constraints, the authorities will likely miss their fiscal deficit target of 4.6 percent of GDP for 2012. Government spending on wages is projected to be higher by 7.0 percent compared to the budget reflecting recent agreements with the unions. This is not offset by revenues which are estimated to grow in line with the budget at 27.4 percent of GDP.

To achieve the authorities' projected deficit path and generate sufficient fiscal space, consolidation needs to be faster than under the current medium-term scenarios.

2.3.7. **Financial market volatility has risen alongside higher global risk aversion.** Capital flows were robust through the first half of 2012 led by portfolio bond inflows. However, foreign investors subsequently scaled back their exposures, mainly in equity markets and Government securities, prompting a rand depreciation of around 8 percent against the U.S. dollar since the beginning of 2012. Business Confidence Index which measures relative business confidence over time is showing a downward trend. The EMBI sovereign spreads for South Africa highlighting investor risk aversion with respect to South African securities has been volatile but trended downward since the beginning of 2012.

2.3.8. **The risks to growth over the medium term are tilted to the downside**. While a softening in activity is envisaged in 2012, the risks of a sharper slowdown are substantial if the Eurozone crisis continues to deepen. There is enough scope for monetary policy to be eased if the growth outlook weakens substantially, but fiscal space is more limited. Domestic downside risks include the potential that households will be unable to sustain their consumption growth due to high levels of indebtedness, and that credit quality may decline with income. This could be exacerbated by a tightening of financing conditions. If downside risks materialize, temporary expenditure measures could be put in place but would need to be solidly framed within a credible medium-term consolidation plan. On the upside, a swift and decisive resolution of the crisis in Europe as well as faster growth in other major advanced economies would increase South African exports.

2.4. Business Environment and Competitiveness

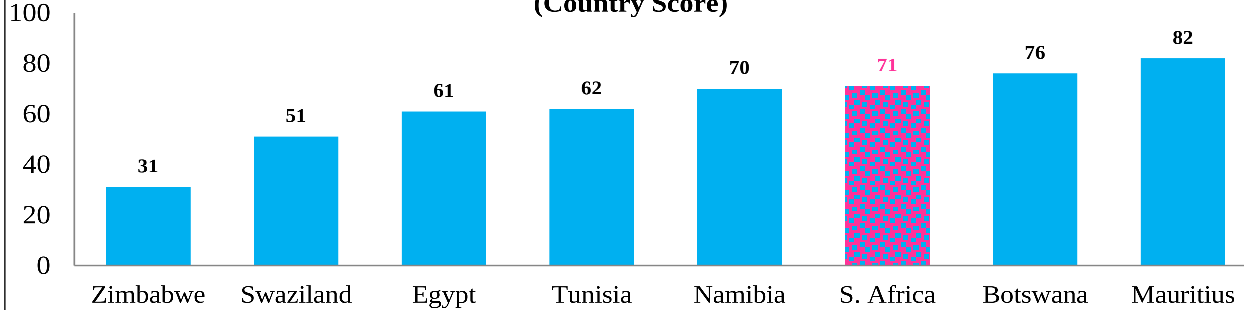
2.4.1. **The assessments of private business regulatory climate indicate that the country remains one of the most conducive in Africa.** The World Bank's **Doing Business 2012 Report** ranks South Africa 35th globally and 2nd in Africa after Mauritius. In 2010/11 South Africa implemented a new company law, which eliminated the requirement to reserve a company name and simplified the incorporation document. It also reduced the number of days required to register property and simplified business exit regulatory requirements. The Government has also introduced a number of measures to ensure equity and efficiency of the tax system, including reducing the number of tax paid from 12 in 2006 to 9 in 2010 and total tax rate as percent of commercial profit from 37.6 percent in 2006 to 30.5 percent in 2010. Import tariff has been reduced significantly; tax on international trade and transactions accounted for 4.5 percent of tax revenue in fiscal 2011/12 compared to 4.8 percent in fiscal 2006/07.

2.4.2. **In spite of these measures challenges remain.** Trading across borders remains difficult, with the country ranking 144th out of 183 countries. For instance, it takes 30 days to export and 31 days to import compared to 5 and 4 days, respectively, in Singapore. The product market regulation is also regarded as relatively onerous partly due to the presence of significant number of parastatals which enjoy near monopoly positions. The South African economy is highly concentrated and anticompetitive trade practices are widespread. Labor laws are characterized by a considerable degree of rigidity in hiring and firing workers, while minimum wage demanded by new entrants is considered to be three times the average for the other BRICS countries. Apart from these, historical and new barriers to growth and formalization of microenterprises remain high, exacerbating the unemployment problem.

2.5. Governance

2.5.1. **South Africa has performed well in terms of governance.** It has well-functioning democratic institutions, independent and vibrant media and respect for the rule of law, which have ensured peace and stability. The judiciary is independent and accountability and transparency norms are generally adhered to. The country has consistently scored well in all the categories of Bank Group's County Policy and Institutional Assessment, with the exception of equity of public resource use and human resource development. South Africa is ranked 5th out of 53 African countries with an overall score of 71 (out of the highest possible score of 100), in the 2011 Mo Ibrahim Index of African Governance (See Figure 2).

Figure 2. 2011 Ibrahim Index of African Governance (Country Score)



Source: Mo Ibrahim Foundation
Note: Score are out of 100 and higher is better

2.5.2. **Government initiatives against corruption are coordinated by the Department of Public Service and Administration.** In the last ten years South Africa has fallen 33 places in the Transparency International Corruption Perceptions Index. In the 2012 index South Africa has been ranked 69 out of 176 countries with a score of 4.3 out of 10. Greater efforts are required to reduce corruption, especially in the procurement of goods and services. The auditor general in his audit report has sighted procurement of goods and services for government and the widespread habit of officials and/or their families doing business with their own departments as the most fertile areas of corruption.

2.5.3**. South Africa has well performing public financial management systems at the national level as indicated in the last PEFA conducted in 2008**. Continued improvements in the overall public financial management environment over the years demonstrate the government's commitment to the reform process. As a result, the transparency, comprehensiveness and credibility of the budget, debt management and external scrutiny and oversight are significantly enhanced. Nonetheless, improvements are required at the municipal and provincial governments, which have seen some unfavorable audit reports from the Office of the Auditor General over the years. The weaknesses in the municipal and provincial governments have been mainly attributed to poor governance structures, supply chain management issues and capacity constraints (both in terms of human skill and systems), and staff turnover amongst the skilled accounting and finance personnel. The Government is working on addressing them through improvement of the ICT environment and a public financial management capacity development strategy, which targets both the national and provincial Governments.

2.5.4. **The national procurement policies for national competitive bidding in South Africa are generally consistent with the Bank's Rules and procedures.** In 2003, National Treasury issued a Policy Strategy to Guide Uniformity in Procurement Reform Processes in Government.

Preferential Procurement Policy Framework Act was amended to integrate preferences with legislation on Black Economic Empowerment. In 2007, the government issued the Municipal Regulations on Minimum Competency Levels. This provides minimum levels of educational qualifications and experience for Supply Chain Management personnel. There is also increasing movement towards e-procurement in the public sector, including training for small and medium firms. The Bank undertook an assessment of the South African national procurement procedures in 2011 to determine the conditions under which they will be used for awarding contracts under national competitive bidding in Bank financed projects**.** The main deviations of the procurement procedures are with respect to compliance with the Bank's fiduciary obligations, and compliance with internationally accepted best practice.

2.6. Trade and Regional Integration

2.6.1. **South Africa has succeeded to reinsert its economy back into world trade following a long period of internal political difficulties and international reactions to the apartheid regime.** The ratio of trade in goods and services to GDP rose from 41 percent in 1994 to 53 percent in 2011 indicating that the international exchange of goods and services has been an ever more important element of economic activity in South Africa in the post-apartheid era. However, since the mid-1990s, the trade sector has not been able to keep up with developments in world markets – especially in intermediate goods. South Africa‘s position in the global trade architecture has remained constant or even deteriorated slightly since 1995. This flat trend contrasts with the performance of its BRICS partners (Brazil, Russia, India and China) who continued to deepen their integration into world trade supply chains after 1995.

2.6.2. **South Africa has significant interests in the SADC region and in regional integration.** It dominates the region economically, accounting for 41 percent of SADC's total trade and about 63 percent of SADC's GDP. It has the requisite economic capability and levels of diversification that are required to drive economic integration in a manner that is mutually beneficial to the region – technology transfer, reduce poverty, foster social development and promote collective protection of the environment, particularly in the case of shared (transboundary) natural resources. South Africa's economic weight and growth spillovers to the rest of the region have traditionally underpinned its key role in trade and economic integration initiatives in the region. Besides its important role in SACU, South Africa is also engaged in ongoing liberalization efforts within SADC. The official launch of the SADC Free Trade Area in August 2008 paved the way for a broader customs union, monetary union, and a common market in the future. The current global economic crisis has prompted ambitious discussions to create a unique trading block involving COMESA, EAC and SADC that would serve as a stepping-stone towards the creation of an African Economic Community.

2.6.3. **Since 1994, South Africa has gained prominence on the international stage.** It is an active member of key multilateral institutions and a key player at the G-20, and the G-24. South Africa joined the BRICS in April 2011 and is an avid promoter of South-South cooperation (see Box 1).

2.7. Poverty, Social Inclusion and Equity

2.7.1. **South Africa is the world's most unequal society.** Despite South Africa's position as Africa's economic powerhouse, its wealth is spread more unevenly than in any other country in

Box 1. South-South Cooperation-Opportunities and Challenges

South Africa is a becoming a key player in global institutions. In addition to regional and continental memberships, South Africa is a member of the International Monetary Fund, the World Bank, the World Trade Organization and the United Nations system in general. With other emerging markets, it is playing a pivotal role in reshaping global governance and financial and trade architecture. Its membership of the G20 group of advanced and emerging economies is in line with the shifting balance of global economic power. In April 2011, South Africa became the fifth partner of the BRICS. The strategic role of these emerging economies cannot be overstated. The early twenty-first century has seen the beginning of a considerable shift in the global balance of power. Major international governance challenges can no longer be addressed without the ongoing co-operation of the large countries of the global South.

Opportunities for South-South Cooperation: Since emerging market countries, especially the BRICS, began their steady climb, international cooperation has been faced not only with new opportunities, but also with a number of specific challenges. In the past decade South-South trade has expanded more quickly than North-South trade. South-South investment too has shown unprecedented dynamism driven by complementary structures in the two regions—African raw materials for industrial, manufacturing and service industries. Investors from the South often have important regional know-how, use appropriate technologies and prove more willing to take business risks in a difficult political environment. A further indicator of the increased importance of South-South cooperation is the fact that countries in the South have become an additional source of official development assistance but along the lines of the **Baudung Principles**, especially that of non-interference in the recipient country's internal affairs.

Challenges of South-South Cooperation: While the positive sides of the current South-South dynamism are to be seen primarily in the increased inflows of resources, especially to the benefit of poor developing countries, many African states face major challenges because of increased dependence on raw materials and the greater pressure of competition from Asian countries in the case of light manufactures. The high-level dialogues between the G8 and the five leading anchor countries (Brazil, China, India, Mexico and South Africa) announced as part of the **Heiligendamm process** may help considerably to ensure that benefits are derived from closer South-South cooperation and that conceivable risks are discussed. Partners are determined to work to strengthen complementarity between them, building on their common objectives and learning from each other. During the political debate new relations have also been identified from time to time.

BRICS Bank: An important initiative resulting from the BRICS grouping is the proposal for the creation of a BRICS Bank – a developmental-focused finance institution to support and drive commerce between the BRICS economies and South-South cooperation. While it may be necessary to develop a financial institution to support trade and development within the BRICS, the strategic question for Africa and the Bank is how the BRICS bank will benefit African business and the African development and integration agendas. The headline is that the bank will direct sovereign wealth to serve the development needs of the developing economies: a "South-South" bank. The multilateral bank may emulate BRICS financial institutions such as Development Bank of South Africa, China Development Bank and the Brazil Development Bank, which have direct capital to designated "strategic" projects in domestic economies as well as projecting commercial interests abroad.

Knowledge work: Broader support for South-South cooperation for knowledge sharing and technology transfer will be a key feature of the new CPS, including expanded cooperation with the centers of excellence in South Africa. The Bank will actively promote knowledge sharing between centers of excellence in South African and the rest of the BRICS for showcasing innovative projects, developing capacity, and encouraging institutional reform. Through the South-South knowledge sharing platform, South Africa will be an entry point to knowledge sharing between the BRICS and the rest of the continent. To this end, South-South regional and continent wide knowledge sharing initiatives will be actively promoted.

the world; the gap between rich and poor is wide. The top deciles accounts for 58 percent of the country's income while the bottom deciles accounts for 0.5 percent. Income Gini coefficient remains around 0.70 while consumption Gini was 0.63 in 2011 (see Annex 2). Its dual economy is characterized by a well-developed economy on one hand and an underdeveloped and marginalized one on the other. High structural unemployment and considerable social challenges include violent crime and an HIV/AIDS pandemic. Real poverty has declined due to redistribution – an increase in government grants – rather than growth in the country's productive capacity. The percentage of individuals that benefited from social grants has increased significantly from 12.9 percent of the total adult population in 2002 to 29.6 percent in 2011, while the percentage of individuals that were at risk of food insecurity decreased from 27.1 percent of total population to 23.3 percent between 2002 and 2011. Yet this redistribution remains limited.

2.7.2. **South Africa is characterized by chronic high levels of unemployment.** The total number of unemployed labour force reached 4.47 million during the second quarter of 2012. Of these, 49.8 percent are women; 59.3 percent of the unemployed did not complete grade 12, while 6.3 percent had tertiary qualification. About 52.7 percent of African and Coloured population is unemployed, while 9.5 percent of Indians and 5.7 of Whites are unemployed. Over 50 percent of youth is unemployed. The main cause of the high unemployment remains the mismatch between the skills the population can offer and the formal sector requirements. The situation has been worsened by the global financial and economic crisis. South Africa lost 870,000 jobs between the fourth quarter of 2008 and the fourth of quarter of 2009 due to the global economic downturn. The UNDP Human Development Report 2011 ranks South Africa 123rd out of 187 countries, placing it in the category of countries that have achieved modest levels of human development.

Box 2. Unemployment and Need for Greater Economic Transformation

Deeply entrenched legacy issues and post-apartheid economic policy that focused on exports of primary products has failed to address the structural unemployment rate of about 25 percent, which has the potential to be establishing over the medium term. Prior to 1994, South Africa's development was based on exports of primary products, particularly gold and other minerals. Manufacturing developed gradually, stimulated by state-led and private investment. The post-apartheid Government starting in 1994 pledged to drive a structural transformation of the economy to redress the apartheid legacy of poverty and inequality. Almost two decades later, the challenge remains and inequality continues to grow. The economy is now dominated by finance capital and owners of mineral-energy resources. Platinum has replaced gold as the key mineral export. South Africa's manufacturing sector which was strong prior to 1994 has declined. Globalization has meant a collapse of the tariff barriers that protected manufacturing, and the influx of cheap manufactured goods has led to the decline of local industries. The local shoe and clothing manufacturing industry, for instance, has been dramatically reduced as a result of imports from Asia. The decline of manufacturing has increased structural unemployment (See Annex VIII).

2.7.3. **Poverty levels remain unacceptably high.** Incidence of poverty in rural areas is more than twice as high as in the urban areas. The proportion of the population living below US$1.25 (PPP) per day was 13.8 percent in 2011 (See Annex 2). About 69 percent of those who live in poverty live in rural areas and 31 percent live in urban areas. Although access to basic social services is relatively high, (nearly 90 percent of South Africa's households have access to piped water and 83 percent are connected to electricity supply), however, access to decent housing remains a major challenge with nearly 19 percent of households living in informal settlements. Through active Government interventions in fighting poverty, South Africa has more than halved the population living in extreme poverty and thus met the MDG 1 ahead of the target date.

2.7.4. **The national literacy rate remains very high and universal access and gender parity have been achieved in schooling in 2010 and about 99 percent of children complete grade 1 to 9**. Youth functional illiteracy fell to less than 10 percent in 2009. However, the quality of education for poor black South Africans remain inadequate. Only 1 percent of African schools are among top performing on high school certificate results, as compared to 31 percent for formerly privileged schools. The key concern for the Government remains improving the quality and the functionality of the education system particularly within historically black and chronically underperforming sections of the country is schooling system.

2.7.5. **Substantial progress has been made in the prevention of malnutrition, mother to child transmission of HIV, immunization coverage and access to free health care facilities.** In spite of these, the national incidence of severe malnutrition averaged 7.8 percent and studies indicate a rising trend in child mortality in recent years. The under-five mortality rate of 54.3 in 2011 was far higher than the target of 20 deaths per thousand live births by 2015. A key concern for the Government is how to make optimal use of current health resources to achieve better health outcomes for children, while ensuring the quality and effectiveness of implementation. Moreover, despite having the largest antiretroviral treatment program in the world, the country had not achieved the goal of universal access to antiretroviral treatment for all those who need it by 2010. As a result, it is unlikely to achieve the MDG of halting and reversing the spread of HIV and tuberculosis by 2015.

2.8. Gender

Women's access to political power and decision-making has improved since 1994. A number of departments (national and provincial) have made considerable progress in gender representation at senior management levels. Despite improvements in addressing the gender divide, the authorities and development partners acknowledge that the empowerment of women remains a slow process especially at the provincial level. South Africa's success in bringing about gender equality has perhaps been most visible in the area of politics and decision making, particularly in national parliament where 42.3 percent of Members of Parliament and 39 percent of cabinet ministers are women in 2012. More needs to be done, to improve the lives of rural black women. The Government has successfully tackled gender gaps in education. Access to health services has greatly improved but it is still very unequal. HIV/AIDS infection rate remains high, with women primarily affected due to poverty. Social security services have greatly improved and numerous legislations on women's rights have been promulgated.

2.9. Environment and Climate Change

The Government has made significant achievements in developing a robust and conducive policy, strategic, institutional and analytical framework for addressing climate change impacts that the country is currently facing. Through the recently adopted National Climate Change Response Policy which guides the implementation of climate change initiatives, work is underway to mainstream climate change adaptation, mitigation and disaster risk management priorities into key economic sectors which include: (i) water; (ii) agriculture; (iii) health; (iv) biodiversity and ecosystems; and, (v) human settlements. On mitigation, the Government is currently assessing the existing potential for reducing carbon dioxide, while at the same time identifying priority adaptation measures to be incorporated into sectoral plans to ensure climate change issues are addressed. A national Monitoring and Evaluation system is being set up for data collection, monitoring and reporting that will detail up-to date emissions data in the form of a greenhouse gas inventory; develop indicators for measuring the transitional process to low carbon development and climate resilient economy and society; and, analyze the impact of mitigation and adaptation measures and track funding flows. A governance structure, housed within the Department of Environmental Affairs, has also been set up to coordinate and manage climate change initiatives. South Africa also signed a comprehensive Green Economy Accord with various social partners in 2011 to create more than 300,000 jobs over the next decade.

III. HIGHLIGHTS OF PREVIOUS BANK COUNTRY STRATEGY

3.1. **The key strategic directions of the Country Strategy Paper (CSP) 2008-2012 were:** (i) enhancing private sector competitiveness; (ii) partnership for regional integration and development; and, (iii) knowledge management and capacity building. The CSP was reviewed and updated in November 2009 and reaffirmed the relevance of the main pillars of the strategy.

3.2. **Bank Portfolio:** Bank Group portfolio in South Africa has 23 operations with a total commitment of UA3.23 billion. The portfolio comprises of 5 public sector projects (including 2 loans and 3 grants), 8 private sector loans and 10 private sector multinational loans and equity investments. Public sector projects account for 61.5 percent of total operations, while private sector loans account for 33.1 percent and private sector equity investments take up the balance. Bank operations in South Africa are dominated by the energy sector (which takes up 62 percent) and finance (21.4 percent). The remaining investments cover transport and communication, mining beneficiation, support to SME development, and water and sanitation (See Annex IV).

3.3. **Performance of Bank Group Portfolio:** The overall performance of the Bank Group portfolio is satisfactory. As at end of June 2012, the average disbursement rate was 53 percent (See Annex V). Although most projects encountered start up delays, progress towards achieving CSP outputs has generally been satisfactory with noticeable progress in implementation in the priority sectors. It is too early for the outcome targets, especially long-term outcomes, to materialize.

3.4. **Lessons from Past Strategy and Interventions:** The CSP Completion Report and Country Portfolio Performance Review (CPPR) provided important lessons that have informed the design of the new CSP (See Annex VI for the Summary Completion Report). Box 3 below highlights the key lessons that informed the design of the new CSP.

Box 3. Lessons from CSP Completion Report and CPPR

- **Better benchmarking of Results framework**. The need for clear baseline data for the output and outcome indicators to ensure better monitoring of results.
- **Support for energy companies and various modalities of** carbon trading and finance can make a positive contribution to green development. Emphasis on innovation and clean technology requires the Bank to continuously improve staff's knowledge of emerging technologies.
- **Improved connectivity is correlated with increased business cooperation, cross-border trade, and investments.** The country program can reinforce the Bank's regional integration initiatives by focusing on transport connectivity and border town development to promote economic corridors;
- **There is a need to focus on more vigorous application of project readiness filters** to improve quality–at-entry and address systemic obstacles in processing and implementing projects.
- **Need for the Bank to add value to the development process of middle-income** countries like South Africa with an expanded focus on private sector development as well as encouraging more public-private partnerships.
- **More innovative approaches are needed to support the SME sector.** Due to availability of low cost loans to the private sector from the Government, especially to SMEs, and in addition to direct funding, the Bank will explore new mechanisms for supporting private sector development.
- **The Bank should continue to explore cooperation with South African institutions**. To catalyze financing for regional infrastructure greater attention should be paid to capacity development and inter-agency coordination to facilitate increasingly complex financing initiatives.
- **The transaction costs involved in accessing MIC and Bilateral Trust Funds are considerable**. The Bank will seek to simplify and streamline its fiduciary processes and being more flexible without compromising standards.
- **For MICs, the Bank should look beyond the provision of financial assistance** as the main modality for development cooperation and emphasize other value-added partnership modalities including serving as an agent for capacity development, knowledge management, technology facilitation, and South-South cooperation.

IV. THE COUNTRY STRATEGY

4.1. Government National Strategy

4.1.1. **The New Growth Path and the National Development Plan** support the Government's long-term goal of building a harmonious and prosperous society through livelihood improvement, and regionally balanced and environmentally sustainable growth. Reforms will be carried out to stem rising income inequality, address structural imbalances, and further open up the economy. Public expenditure will be geared towards livelihood improvement, and strong support will be provided to education, healthcare, social security and public housing. Infrastructure remains a high priority with an emphasis on promoting rural development and emerging strategic industries, in particular modern clean energy and environment-friendly technologies, while piloting development of green and low-carbon cities. Resource conservation to combat climate change and improve natural resource management is also a priority.

4.1.2. **The National Development Plan (NDP) builds on the Government's New Growth Path (NGP), which targets 5-million new jobs by 2020**. It sets an ambitious target of reducing South Africa's unemployment rate from 25 percent in 2011 to 6 percent by 2030 by creating 11million new jobs. This will require meeting the subsequent target of annual average GDP growth of around 5½ percent between now and 2030. Both the NGP and the NDP focus strongly on economic interventions to achieve job-creating growth. To increase both employment creation and economic growth, the plan proposes 8 interventions:

- Raising exports, focusing on areas in which South Africa already has endowments and comparative advantages, such as mining, construction, mid-skill manufacturing, agriculture and agro-processing, tourism and business services;

- Increasing the size and effectiveness of the country's innovation system, and ensuring closer alignment with companies that operate in sectors that fit in with the growth strategy;

- Improving the functioning of the labor market to help the economy absorb more labor, through reforms and specific proposals concerning dispute resolution and discipline;

- Supporting small business through better coordination of the activities of small business agencies, development finance institutions, and private and public incubators;

- Improving the country's skills base through better education and vocational training;

- Increasing investment in social and economic infrastructure in order to lower costs, raise productivity and bring more people into the mainstream of the economy;

- Reduce the regulatory burden in sectors where the private sector is the main investor, such as broadband internet connectivity, to achieve greater capacity and lower prices; and,

- Improve the capacity of the state to implement effective economic policy.

Industrial Policy Action Plan remains the key pillar of the NGP and has put in place necessary platforms to unlock growth and employment generation in a range of sectors including the amendment of procurement regulations; the launching of the manufacturing competitiveness enhancement programme; greater strategic alignment of trade and competition policy with industrial policy; and interventions designed to stimulate sub regional growth through Special Economic Zones, among others.

4.1.3. **Intersection with the Bank's Long-Term Strategy (LTS):** The Bank's new LTS objectives of supporting inclusive and the transition to green growth are consistent with the main priorities of the NGP and the NDP. In particular, the Bank's focus on infrastructure, skills development and regional integration is consistent with South Africa's approach to development, while the emphasis on environmental protection and addressing the impacts of climate change is consistent with the Government's approach to environmentally sustainable development. Both the Bank and the Government share the goal of strengthening private sector development and South-South cooperation for knowledge sharing. An improved investment climate will enhance private sector development. South Africa's priority areas of infrastructure, manufacturing, skills development, and environment are shared with the LTS.[1] In other words, South Africa's priority of creating a harmonious and prosperous society, by reducing inequalities, is in line with the inclusive growth objective of the LTS, while the focus on climate change and environmental issues is in line with the transition to green growth agenda. Development of lagging regions and cooperation on environment and climate change are expected to contribute to enhanced regional cooperation and integration. Good governance, gender equity, and knowledge solutions are also key components of the LTS.

Box 4. The Link between Bank LTS, Southern African RISP, and South African CSP 2013-2017

The Bank Group Long Term Strategy strives to support the twin cross-cutting objectives of inclusive growth and transition to green growth in the Regional Member Countries. It focuses on five core operational priorities that will inform all of its activities, namely infrastructure development, regional integration, private sector development, governance and accountability, and skills and technology. The Southern Africa RISP conforms to the themes of the LTS and is underpinned by the Bank's Regional Integration Strategy, which focuses on regional infrastructure and capacity building in support of infrastructure interventions. Regional integration remains key to the Bank's mandate and is an important continental initiative. The Bank is well positioned to play a lead role in fostering the integration of Africa's economies to create larger more attractive markets, linking landlocked countries to international markets, and support intra-African trade. Regional member countries see the private sector as key partner in ensuring quality and sustainable growth. The Bank will therefore assist RMCs create an enabling environment for expanding domestic and foreign investment and promote the development of African businesses and entrepreneurs to attain inclusion and seize green growth opportunities to create jobs and enhance wealth. The South Africa CSP 2013-2017 is fully aligned with the strategic thrust of the Bank's LTS and the Southern Africa RISP. The two proposed areas of focus, infrastructure, and regional integration, driven by private sector development, human capital development, knowledge services, and governance will significantly contribute to reduction in poverty and inequality, while addressing challenges of environmental sustainability.

4.1.4. **Relevance of the CSP Completion Report**: The findings and recommendations of the last CSP as described in paragraph 32 above remain highly relevant to the preparation of the new CSP given the high degree of continuity between the Government's NGP and NDP. In particular, the new CSP's focus on skills development for job creation will reinforce the Government's ongoing emphasis on inclusive growth and fostering social cohesion while ensuring green

[1] A report on "Manufacturing, Productivity, Innovation and Jobs: A comparison with the BRICS" is summarized in Annex VIII. The New Growth Path, as well as the Industrial Policy Action Plan, regard manufacturing as the main driver of growth and employment. The Government has introduced the Manufacturing Competitiveness Enhancement Scheme to revitalize the sector to reverse the current trend of deindustrialization and promote employment creation. The manufacturing sector study contributes towards this effort.

economic development. Further, a longer time is required to implement fully the strategic repositioning initiated under the previous CSP.

4.1.5. **Coordination of the Bank's assistance:** Development assistance constitutes less than 1 percent of the South African budget and there is no institutionalized donor coordination mechanism in South Africa. The Ministry of Finance and National Treasury coordinate the Bank's development assistance to South Africa. The Bank consults regularly with relevant line ministries and local government agencies. In addition, the Bank maintains regular contact with development partners and civil society groups to exchange information and foster cooperation in areas of common interest. The initiative to cooperate with DFID on regional integration is one of such engagements. The Bank also works with private sponsors, state-owned enterprises and domestic financial institutions on issues related to private sector development. Infrastructure investment including support to transition to green growth remains the main area of comparative advantage for the Bank. South Africa has launched a massive infrastructure investment plan worth R3.2 trillion over the next decade and the Bank is well positioned to tap into further financing opportunities during the current CSP period.

4.1.6. **Apart from the Bank, South Africa's major development partners with field presence in the country include the World Bank, the European Union, DFID and the United Nations Agencies (Annex VII).** The World Bank is one of the main co-financiers of the largest Bank project in South Africa (the Eskom Medupi Power project). The Bank has emphasized the use and strengthening of the country systems to build effective institutions in line with the Paris Declaration and Accra Agenda, as well as the Busan Partnership for Effective Development Cooperation. The use of country systems for financial management of Bank funded projects is the main area that requires greater improvement in donor harmonization.

4.2. The Bank's Country Strategy

4.2.1. **Goals, Objectives, and Assistance Approach:** The new CSP seeks to adapt to South Africa's rapidly changing circumstances and set a new foundation for the continuously evolving partnership with the Bank. Almost two decades of successful reforms have helped South Africa maintain its position as Africa's largest economy and facilitated a swift transition to the rank of major world economies. In line with its growing economic strength and international status, South Africa has come to play an increasing role in promoting regional and pan-African integration, continental and global public goods, sharing knowledge, and providing development assistance both bilaterally, as well as through multilateral finance institutions (See Box 1).

4.2.2. **Despite these, South Africa continues to face complex development challenges, including significant poverty, sharp income inequality, and widening regional disparities**. In addition, South Africa's economy is highly carbon-intensive, and its greenhouse gas emissions per capita are similar to that of industrialized countries, partly because of its strong reliance on coal, which places it at the center of the global climate change challenge. Failure to address more decisively the rising fiscal pressures and social agenda would jeopardize South Africa's long-term growth prospects. Thus, there remains important and challenging development work for the Bank to undertake in South Africa, which continues to rely on external financing and technical assistance (TA) to complement its own financing and expertise to catalyze policy reform, introduce innovation, access new technology, and adopt international best practices.

4.2.3. **The new CSP therefore seeks to position the Bank to continue playing a catalytic role in South Africa's development process through an enhanced operational focus on**

innovation and value addition to support manufacturing and job creation. It promotes intensified focus on generating knowledge, sharing best practices, building capacity, and fostering regional cooperation. The Bank's comparative advantage is that South Africa's higher education system is characterized by weak knowledge production that often does not translate into innovation to support manufacturing and create jobs. Lending activities will include smaller demonstration and pilot-type projects for scaling-up through domestic financing. This, in turn, would facilitate knowledge sharing among executing agencies and with other developing member countries through South-South cooperation, and foster a stronger strategic focus on inclusive and environmentally sustainable growth as well as regional cooperation and integration.

4.2.4. The opening of the Southern Africa Resource Centre (SARC) has ensured better partner coordination. SARC is working closely with South Africa and the Regional Economic Communities to deepen regional integration and economic cooperation to enhance the region's competitiveness and diversification of economic activity to spur inclusive and sustainable growth. The opening of SARC has also enhanced portfolio performance through (i) improved consultation with local authorities, as well as development partners for joint initiation, design, financing and monitoring of projects, and (ii) timely support to capacity development of implementing agencies in various aspects of project management. Further, collaboration between ECON and SARC would significantly enhance the Bank's capacity to respond with knowledge solutions on emerging issues, as well as preparation of influential policy notes on key issues.

4.2.5**. Country Strategy Pillars: The CSP for 2013-2017 is closely attuned to the needs of South Africa as a large middle-income country**. Guided by the Government's commitment to "pro-poor, pro-job, pro-growth, and pro-environment" development, the two strategic pillars are infrastructure; and regional integration. The pillars are consistent with the Government's longer-term master plans of job creation and inclusive growth and climate change action plans. Synergies between the lending, TA, and Analytical Advisory Assistance (AAA) programs will be strengthened as will the complementarity between public sector and non-sovereign operations by mainstreaming private sector development across the full range of operations. Further, other cross cutting themes such as knowledge solutions, good governance and capacity development, and gender equity will be actively pursued to maximize development impacts.

Pillar 1: Infrastructure. The Bank will support government efforts to achieve growth that is more inclusive through infrastructure development. The Bank's public sector operations will seek to strengthen the enabling environment for private sector development by financing infrastructure development while the non-sovereign operations will continue to finance catalytic projects, including improved financial and logistical services, and public-private partnerships (PPPs) for infrastructure investment, particularly in clean energy, urban environmental protection, and social infrastructure. **The Bank will support the government's efforts to foster a cleaner and more sustainable growth process by strengthening capacity of environmental management and pilot testing cutting-edge clean energy and energy efficiency technologies**. Support for the development of low-carbon transport systems, particularly in public transport; strengthening protection and sustainable use of land, water and forest resources; helping to develop model livable and low-carbon cities; and promoting the development and institutionalization of green financing instruments will be key drivers for Bank engagement. The South African government has launched R840 billion medium and R3.2 trillion long-term National Infrastructure Plan in 2012 to transform the economy, create jobs, ensure inclusive growth and promote regional integration. The plan also identifies lack of skills and capacity in particular lack of engineers, technologists, and technicians as well as project managers as the main constraint to implement the program. On skills development, the Bank will support the Government's efforts to achieve inclusive growth through interventions in Higher Education, Science and Technology (HEST) for innovation and technical skills for the implementation and maintenance of the critical infrastructure. Inclusive growth and equity would benefit from greater private sector participation in the economy to generate better employment prospects, as private companies generate the largest share of GDP growth and employment.

Pillar 2: Support for Regional Integration. This pillar will provide the link that is needed between the country strategy and the RISP. In this regard, the regional orientation of the country program will be further strengthened to complement the Bank's support for regional cooperation programs, particularly the Southern Africa Regional Integration Strategy and SADC programs. The Bank will continue to work closely with the Government to support regional integration through country projects and TA, with a focus on transport connectivity, clean energy, development of corridor cities, and trade facilitation to promote economic corridors for regionally inclusive development. In addition to these, the Bank will seek to strengthen the enabling environment for private sector development by supporting policy and regulatory reforms, and improving access to finance. The Bank's non-sovereign operations will continue to finance catalytic projects, focusing on innovative financing solutions (i.e. microfinance, SMEs, green finance, lines of credit to financial institutions for cross border investments, and trade finance). The Bank will also strengthen capacity and strategy development support for government agencies involved in regional programs. Support for regional integration will continue to reinforce the country program's efforts to reduce regional imbalances. Further, the Bank will strengthen efforts to promote knowledge sharing between South Africa and other regional and non-regional member countries for expanded South-South cooperation mainly through ESWs.

4.3. Cross-Cutting Issues

4.3.1. **Knowledge solutions: Knowledge sharing will be more actively promoted in all the priority sectors to promote best practices and scaling up of successful demonstration projects.** Capacity development and policy advisory technical assistance will be complemented by Analytical Advisory Assistance to enhance the Bank's responsiveness to government requests for policy advice on a wider range of issues. The Bank will also actively promote knowledge sharing among executing and implementing agencies for showcasing innovative projects, developing capacity, and encouraging institutional reform. Further, broader support for South-South cooperation for knowledge sharing will be a key feature of the new CSP, including expanded cooperation with the South Africa's centers of excellence and the BRICS.

4.3.2. **Gender equity: Gender equity will remain the key component of the strategy and will be proactively incorporated in loans and technical assistance.** Project preparatory technical assistance will identify ways in which gender can be mainstreamed and gender action plans will be prepared during project formulation and included in the project appraisal. Gender performance targets, indicators and benchmarks will also be included in the design and monitoring frameworks of relevant projects as appropriate. Where feasible, gender-disaggregated data will be identified and collected as part of project monitoring and evaluation, and included in gender action plans.

4.3.3. **Good Governance: The Bank will support government efforts to strengthen the policy, legal, fiduciary and regulatory frameworks and practices to** (i) improve delivery and management of infrastructure and public services, and (ii) promote the enabling environment for private sector development. The Bank will also provide support for PPPs, reform of tariffs and cost-recovery policies for sustainable development of clean energy and municipal services, and adoption of regulations and market-based solutions to encourage natural resource conservation. Further, the Bank will expand its support for capacity development and sharing of good practices, including from its non-sovereign operations.

V. STRATEGY IMPLEMENTATION

5.1. Indicative Resource Parameters

5.1.1. **South Africa is an ADB only country in the Bank's country classification system and is eligible for ADB financing**. According to the three-year rolling plan and budget 2013-2015, the indicative sovereign lending level is about UA700 million per annum during 2013-2015, broadly in line with the average annual lending in the previous CSP period, 2008-2012. The annual sovereign lending level beyond that point would continue to be formulated in the context of the annual work program and budget framework exercise (See Table 1).

5.1.2. **In terms of financing, actual ceilings for the Bank financing will be determined by project-specific considerations, Bank's risk exposure and available co-financing**. The Bank will draw on a mix of financing instruments to provide longer-term financing predictability and integrate support for reform programs and capacity development with investment operations. The use of multi-tranche financing facilities, sector development programs, sector loans, retroactive financing, and global funds will be explored, in addition to policy-based loans, investment projects, and technical assistance projects. Non-sovereign operations will follow the Bank's prudential exposure limits and continue to mobilize commercial financing and private participation in Bank financed projects. SARC and the Private Sector Operations Department will work closely to create further synergies between public and non-sovereign sector operations.

5.1.3 **Trust Funds and Grants:** Looking further ahead, the Bank's partnership with South Africa is anticipated to continue to evolve toward an engagement and relationship based primarily on the development and sharing of innovation, knowledge, management experience, and international best practices and technology. The Bank will continue to mobilize grant resources from its administered and global trust funds, for activities related to human development, promotion of regional integration initiatives, clean energy and clean coal technologies, and other climate-change related issues.

Table 1. Indicative lending and non-lending operations

Operations	2013 UA million	2014 UA million	2015 UA million	Department
Lending program				
Climate Resilient Green Economy (Sector Budget Support)	100	…	…	ONEC
Transmission Grid Strengthening	…	200	…	ONEC
Eskom renewable energy	…	…	100	ONEC
Water Supply, Health and Sanitation Program	100	…	80	OWAS & OSHD
Lesotho Highland Water Supply Project Phase II	…	150	…	OWAS
Private sector development operations (infrastructure, manufacturing, regional integration, and enhancing productive capacity of SMEs, PPPs)	400	350	450	OPSM & OSHD
Higher Education Science and Technology	…	100	…	OSHD
Subtotal	600	800	630	
Non-lending program				
Manufacturing, Productivity, Innovation, and Jobs : A Comparison with the BRIC	0.03	…	…	SARC
The Role of South Africa in Regional Integration in Southern Africa		0.3	…	SARC
Update of the Feasibility Study of Moloto Development Corridor	0.5	…	…	OITC
The Model shift from Road to Rail freight traffic	0.10	…	…	OITC
Independent System Market Operator	0.6	…	…	ONEC
Reduction of greenhouse gas emissions in agriculture and forestry through soil sequestration	1.3	…	…	OSAN
Modeling Costing and Financing Options for Expansion of Higher Education Infrastructure	…	0.08	…	OSHD
Impacts Evaluation of NHI Pilot Program		0.02		OSHD
Sub total	**2.5**	**0.4**		
Total	**602.5**	**800.4**	**630.0**	

Note: ONEC = Energy, Environment and Climate Change; OSHD = Human Development; OPSM = Private Sector; OWAS= Water and Sanitation; OSAN= Agriculture and Agro-Industry; and OITC= Transport and ICT.

5.1.4. **The indicative lending operations in Table 1** include both the validated and proposed pipeline for the initial three-year period and are fully aligned with the two strategic areas of focus. Dialogue is continuing with the National Treasury to explore lending opportunities with two State Owned Enterprises: the South African Airways and the African Exploration Mining and Finance Corporation. The Airways has already issued expression of interest for funding by the commercial banks to purchase airplanes worth USD900 million over the next five years.

5.2. Program Overview and Sector Focus

5.2.1. **Bank support will be demand-driven and results-based, and will focus on government priorities that reflect the Bank's comparative advantage in specific areas that have potential to contribute to job creation and inclusive and environmentally sustainable development**. Compared to the previous CSP, operations within each priority sector will be more selective in line with the joint emphasis on innovation and value addition to facilitate further sector repositioning. All the Bank lending and TA will accordingly be carefully screened to ensure value addition, transition to green growth or social development orientation, and enhanced synergies with regional cooperation and integration programs in line with the proposed strategic pillars. Support for innovative financing solutions and access to finance in the priority sectors remains an important operational objective. The Bank will continue to support microfinance, SME finance, affordable housing, agro-processing and agriculture, green finance, and municipal finance. The Bank will explore direct financing opportunities through on-lending to the recently constituted new Small Enterprise Finance Agency (SEFA) under the Industrial Development Corporation (IDC).

5.2.2. **Energy**: **Ambitious targets have been set by the Integrated Resource Plan to improve energy efficiency, reduce carbon emissions and encourage development of clean energy resources.** The Bank's support to the energy sector will seek to play a leadership role in introducing cutting-edge technologies for high-impact climate change mitigation, particularly to reduce coal dependence. The Bank will provide support in five areas: (i) energy efficiency and conservation, development of energy service companies, and application of smart grid technologies; (ii) renewable energy, including wind, concentrated solar, biomass, geothermal and small hydropower; (iii) cleaner and lower carbon fossil fuel technologies and carbon capture and storage; (iv) access and transmission grid strengthening; and (v) development of regional power projects and trading arrangements. While South Africa aspires to reduce the share of coal in energy mix to 48 percent in 2030, it at the same time envisions expanding dry-cooled coal generations over the plan period. The Bank will continue to support environmentally efficient coal projects with particular focus on grid strengthening. Knowledge solutions, TA, and grant resources will support innovative demonstration projects and the development of carbon trading systems. The scaling up of low carbon technologies, particularly in clean energy, hinges on securing financing on attractive terms. Mobilizing low-cost financing, including supporting the government to gain access to concessionary resources being made available for greenhouse gas mitigation in the energy, transport, and land use sectors at the global level will therefore be an integral part of the strategy (See Annex VII for more details).

5.2.3. **Transport: The Bank's support will increase the role of lower carbon and safer transport modes**. It will improve the management and maintenance of transport assets, encourage efficient delivery of public transport services, and contribute to regional connectivity and trade facilitation, particularly through efforts to integrate safety considerations, foster multimodal services, improve asset management and maintenance, and incorporate intelligent system design technologies. Key areas of support include: (i) road network rehabilitation, rural roads, more effective road maintenance systems, and road safety; (ii) efficient and safe railways and ports with strong regional dimensions and facilitation of containerization; (iii) urban public transport, multimodal passenger hubs, and traffic demand management; (iv) inland waterways and inland ports; and (v) multimodal logistics centers, logistics services, and intelligent transport systems.

5.2.4. **Natural resources, water, and agriculture**: **Increasing water scarcity and weather volatility threaten the South Africa's efforts to meet its food security, rural livelihood and natural resource management objectives.** The Bank will support demonstration projects that contribute to sound land, water and natural resources management and climate change initiatives that also support rural livelihood improvement through contract farming schemes and other market-driven opportunities. The Bank will also support water and sanitation operations geared towards achieving the sector goal of attaining universal access to affordable and sufficient water supply and sanitation services.

5.2.5. **Education**: **Skill shortages and skill mismatches affect all sectors of the economy**. The Bank will assist the government to enhance skills development through interventions in HEST for innovation and technical skills for the implementation and maintenance of the critical infrastructure. In this regard, the Bank will support the government's efforts to close skills gaps for the Strategic Integrated Projects (SIPs) covering social and economic infrastructure across the nine provinces as stipulated in the 2012 National Infrastructure Plan. The Bank will also support the government's derive to develop an integrated skills plan for the next 20 years across all the SIPs. According to the Engineering Council of South Africa, South Africa has one engineer per 3166 of the population, well behind Brazil (227), the UK (311) and Chile (681). In 2011, there were only about 15000 professional engineers in South Africa.

VI. RESULTS MANAGEMENT

6.1. Monitoring

A CSP results framework designed to focus the Bank assistance on the delivery of results is shown in Annex I. The results framework will serve as a management tool for the Bank and the Government in several respects: (i) progress made in achieving outcomes will be carefully monitored each year through the Bank project and TA review missions and annual portfolio reviews; (ii) individual project and program interventions will be designed to contribute to CSP outcomes; and (iii) tracking and evaluating the success of the CSP (See Box 5 on the role of SARC).

6.2. Risks

Three major risks could hamper the implementation of the proposed strategy.

- **Global economic environment:** South Africa remains vulnerable to unexpected movements in capital flows and commodity prices. Volatility in capital flows complicates monetary policy. High international oil prices could push up the government's domestic subsidy bill and crowd out resources required for essential infrastructure investments, social services, and other pro-poor programs. Surges in oil and food prices could fuel inflation and reduce living standards of poor and near-poor households. The Bank will continue to support government-led medium-term reform programs, and will consider the government's request for support to respond to changing global conditions. Committing to a medium-term anchor accompanied by well-articulated revenue and expenditure measures, while allowing room for automatic stabilizers to operate and some discretionary spending to counter cyclical downturns, would help cement credibility.

- **Public–private partnership:** Delivering investments in infrastructure and services in ways that leverage private participation is central to the CSP. Key risks include inability of the government to address issues in land acquisition, tariff setting, and state-owned enterprise reform that are needed to encourage PPPs in infrastructure investments. The Bank will work with the government to develop a pipeline of feasible PPP projects, and will focus its policy dialogue and capacity development support in areas with sound prospects for advancing private participation in infrastructure provision.

- **Skills mismatch and social tensions:** Finally, failure to achieve minimum growth rates of at least 5 percent as envisaged in NGP, the skills mismatch and the resulting chronic high level of unemployment, poverty and inequality could cause social tension and derail the democratic gains made during the past 18 years. Lack of skills and capacity at national, provincial and local government levels but also skills gaps in the private sector continue to hamper project implementation. To help mitigate this risks, Bank programs would include a skills building component aimed at increasing ownership and employment opportunities and a stronger team-based approach will be encouraged to provide both policy and project based support.

Box 5. The Role of Southern Africa Resource Center (SARC) in Implementing the CSP

Quality assurance is essential to maximizing the CSP's development effectiveness. The government has asked the Bank to gradually shift to more project investments (within programmatic frameworks) to address binding constraints to inclusive and environmentally sustainable growth, especially infrastructure and related services. The transition to increased project support will be gradual and may be adjusted during the CSP period to respond to changing government needs for policy-based support and for the Bank resources and expertise. To support the CSP implementation, SARC is working to strengthen the staff mix, focus and deployment responses.

With the opening of SARC, the new Delegation of Authority Matrix, and adequate and timely deployment of key staff, the Bank will strive to sustain high quality standards by: (i) strengthening upstream consultation for joint initiation of projects and TA; (ii) improving project conceptualization and design; (iii) delegating greater project administration responsibilities to SARC Tasks Managers; and (vi) expanding capacity development of executing and implementing agencies in various aspects of project management, including fiduciary safeguards, and the design and use of results frameworks. Consultation workshops will be used to share best practices in project management, discuss initial project and TA concepts, and encourage scaling up of innovative projects for wider replication.

The establishment of SARC earlier this year is also contributing to improve partner coordination. This will continue to be emphasized during the CSP period. SARC will continue to work closely with South Africa and the Regional Economic Communities to deepen regional integration and economic cooperation to enhance the region's competitiveness and for diversifying economic activity to spur more inclusive and sustainable growth.

South Africa continues to face complex development challenges. This Bank Group strategy is designed to support the Government's efforts. The CSP for 2013-2017 is closely attuned to the needs of South Africa as a large middle-income country. Guided by the government's commitment to "pro-poor, pro-job, pro-growth, and pro-environment" development, the two strategic pillars are infrastructure, and regional integration. The pillars are consistent with the government's longer-term master plans and climate change action plans.

7.2. Recommendation

The Board of Directors is invited to consider and approve the proposed Country Strategy Paper for the Republic of South Africa for 2013-2017, based on a sustainable annual lending envelope ranging from UA600 to 700 million.

ANNEX I. COUNTRY STRATEGY RESULTS FRAMEWORK

Country Development Goals

1. Increase GDP growth to at least 5 ½ percent by 2015.
2. Reduce the unemployment rate to 15 percent by 2020 and 6 percent by 2030 from 25 percent in 2012.
3. Reduce population living below poverty line of US$2 per day to 0 percent in 2030 from 33 percent in 2009 (13.8 percent below US$1.25 in 2011).
4. Promote environmentally sustainable economic development; green growth with rich biodiversity.

Government Sector Objectives	Constraints hindering achievement of desired outcomes	Final Outcomes (by 2017)	Final Outputs (by 2017)	Mid-Term Outcomes (by 2015)	Mid Term Outputs (by 2015)	Bank Group Interventions during CSP period (ongoing & proposed)
PILLAR 1: INFRASTRUCTURE						
1. INFRASTRUCTURE DEVELOPMENT						
ENERGY						
Development of energy infrastructure to enhance economic growth, employment, poverty reduction; and environmental sustainability	Lack of resources for expanded energy infrastructure investment High cost and uncertainty of green energy technology	Increase in household access to electricity to 85% (baseline: 82.7% in 2011) Green energy 9% of energy mix (baseline: 2.2% in 2011) Emission falls to lower limit 398 million metric tonnes CO2 equivalent (583 upper limit) in 2020 (baseline: 500 million metric tonnes CO2 eq. in 2010)	100MW	Increase in household access to electricity to 83.7% Green energy 4% of energy mix Emission falls to lower limit 450 million metric tonnes CO2 equivalent	-	Proposed: Eskom renewable Energy project Climate resilient green economy operations Transmission Grid Strengthening
			100MW		100MW	
			400 Kms transmission lines		-	
			4,764 MW		3,176 MW	Ongoing Medupi Power Project Eskom Renewable energy investment project: Sere and Upp.
			100 MW (Sere)		100 MW (Sere)	
WATER SECTOR						
All South Africans will have access to affordable, sufficient and safe water and hygienic sanitation	Limited water resources; Unevenly distributed water resources; Deteriorating quality of water and sanitation services and pollution;	Household access to water supply to increase to 95% (baseline: 89.5% in 2011) Access to sanitation to increase to 84% (baseline: 79% in 2010)	Lesotho Highland Water Project Phase II completed by 2020	Household access to water to increase to 92%	30% achieved	Proposed: Lesotho Highland Water Project II; Water supply and sanitation project
			1 water supply and sanitation project completed	Access to sanitation to increase to 81.5%	1 water supply and sanitation project completed	
2. Higher Education, Science and Technology for Infrastructure Development						
Enhance research, development and innovation in human capital for a growing knowledge economy	Poor performance of education system in producing learners with ability to pursue mathematics and science studies at higher education institutions	Increased supply of high-level skills in science and technology	Number of civil engineers to increase to 20,000 by 2017 (baseline: 15000 in 2011)	25% achieved	25% achieved	Proposed: Higher Education and Science and Technology

PILLAR 2: REGIONAL INTEGRATION						
REGIONAL INFRASTRUCTURE						
Deepen regional integration and trade, free movement of persons, business, labour and services across the region, and enhance cooperation	Inadequate infrastructure (Transport, Energy and ICT); High transaction costs and costs of tradable goods,	Improved road transport, energy supply and trade facilitation infrastructure	2 transport and 4 power supply projects completed	Improved trade flows and movement of people;	1 transport, 2 power projects completed	Proposed: Regional infrastructure development
		50,620 permanent employment; increase in GDP by US$420 million; increase in fixed investment by US$920 million all at regional level	At least one energy, ICT, roads, water projects in SADC region are completed	50% achieved	50% achieved	Ongoing DBSA 5th Line of Credit
	FACILITATION OF CROSS BORDER INVESTMENT AND TRADE					
	Tight foreign exchange controls; High cost of funds for South African Banks; Lack of knowledge of regional market;	South Africa trade with BRIC to increase to 40% (baseline: 18.6% in 2011) Trade with sub-Saharan Africa 25% (baseline: 18% in 2010) Intra-regional trade in SADC 12% (baseline: 7% in 2010). Improved border clearance efficiency at South African border by 20% from status in 2012	Share of portfolio of South African Banks and major institutional investors in Africa region to increase	50% achieved	50% achieved	Proposed: Regional trade and investment
			7 projects in low income and fragile states completed	50% achieved	50% achieved	Ongoing: Lines of credit IDC
			Two one stop border posts completed;	Reduction in truck waiting time at Beitbridge from 36 hours to under 24 hours 6 months after completion of construction	1 one stop border post built	OSBP project
SUPPORT TO SMEs						
Address the structural imbalance and high level of concentration in the economy, and close the skills gap to enhance the labour absorptive capacity of the economy	Declining share of manufacturing in GDP and the general trend of deindustrialization;	Unemployment falls to 15% in 2020 (Baseline: 25% in 2012)	Share of manufactured output in total output rise to 18% (baseline:13.4% in 2011)	50% achieved	50% achieved	Proposed: Industry, mining and quarrying; and Agriculture value chains
			1 processing (sinter) plant and 1 smelter plant completed	9,500 indirect jobs and 5,000 direct jobs	50% achieved	Ongoing: Kalagadi industrial beneficiation project
			34 farmers and agri-businesses receive loans from Land Bank	50% achieved	17 farmers and agri-businesses receive loans from Land Bank	Land Bank Project
Enhance entrepreneurial skills and investments in SMEs to ensure job creation and poverty reduction	Limited access to finance, high level of crime, Problems of access to land and transport.	Total Entrepreneurial Activity Index (TEAI) reaches 15% (baseline: 8.9% in 2010).	Number of small businesses increase to 2.5 million (baseline: 2.4 million in 2011).	TEAI reaches 13%	Number of small businesses reach 2.45 million	Proposed: Loans SEFA; Financial intermediation with SA commercial banks and DFIs

ANNEX II. SELECTED ECONOMIC AND SOCIAL INDICATORS

Indicators	Unit	Actual				Projection		
		2008	2009	2010	2011	2012	2013	2014
Economic Indicators								
Real GDP Growth Rate	percent	3.6	-1.5	2.9	3.1	2.7	3.4	4.0
Real per Capita GDP Growth Rate	percent	2.5	-2.6	1.8	1.9	1.4	2.2	2.7
Inflation (CPI)	percent	9.9	7.1	4.3	5.0	6.2	5.3	5.1
Exchange Rate (Annual Average)	LC/US$	8.3	8.5	7.3	7.3	…	…	…
Total Revenue and Grants	percent GDP	29.8	27.8	27.5	27.4	27.5	27.7	28.0
Total Expenditure and Net Lending	percent GDP	30.3	33.1	32.3	32.0	31.7	31.4	31.1
Overall Deficit (-) / Surplus (+)	percent GDP	-0.5	-5.3	-4.9	-4.6	-4.3	-3.7	-3.1
Current Account Balance	percent GDP	-7.2	-4.0	-2.8	-3.3	-4.8	-5.5	-5.6
Gross reserves	months of imports	3.8	5.9	5.3	5.6	5.5	5.3	5.1
National Government Debt	percent GDP	27.3	31.5	35.1	36.6	37.5	38.1	37.7

Social Indicators

Indicators	Unit	1990[1]	2000[2]	2011[3]
Population	million	35.2	44.0	50.6
Unemployment	percent	18.8	25.6	24.5
GINI index	index	59.3	57.8	63.1
Poverty headcount ratio at $1,25 a day (PPP)	percent of population)	21.4	26.2	13.8
Maternal mortality ratio (national estimate, per 100,000 live births)		…	165.0	400.0
Total enrollment, primary	percent net	95.0	89.3	85.1
Proportion of seats held by women in parliaments	percent	3.0	30.0	44.5
Prevalence of HIV, total	percent pop (15-49)	6.1	18.1	17.8

Environment and Climate Change Indicators

Indicators	Unit	1990[1]	2000[2]	2011[3]
CO2 emissions from fuel combustion	million tons	298.4	340.3	427.3
Share of renewables in electricity production (incl hydro)	percent	1.7	2.0	2.2
Forest area	percent of land area	6.8	5.7	4.7
Terrestrial protected areas	percent of tot land area	6.5	6.9	6.9
Marine protected areas	percent of territorial waters	0.7	3.3	6.5

Source : South Africa National Treasury, AfDB Statistics Department, IMF: WEO, April 2012 and International Financial Statistics, April 2012; United Nations, OECD, Reporting System Division.

Notes: … Data Not Available;

[1] Latest year available in the period 1990-95; [2] Latest year available in the period 2000-04; [3] Latest year available in the period 2005-11

ANNEX III. COUNTRY PORTFOLIO IMPROVEMENT PLAN

Issues	Actions required	Measurable indicator Timeframe	Responsible	Timeframe
Implementation Preparedness and Effectiveness				
Quality-at-entry and effectiveness delays.	Better project design. Ex ante negotiation of many of the issues leading to delays before Board approval.	Time from approval to first disbursement not to exceed 3 months.	AfDB, South African Govt., and private sector.	Ongoing
Delays in Government Approvals	Ex ante negotiation of many of the issues leading to delays before Board approval . More inclusive consultations with Government to ensure ownership. Better understanding of the project cycle.	All approvals to fall within the proposed 3 months above.	AfDB, South African Govt., and private sector	Ongoing
Quality during implementation	Supervision missions must be regular and staffed with the appropriate skills. Follow-up of supervision reports and timely input of information in SAP, and training of implementing entities on Bank's fiduciary requirements are needed.	At least 2 supervision missions per and at least 1 capacity building workshop and one fiduciary clinic per year.	AfDB, South African Govt., and private sector.	Ongoing
Inadequate sector staff at SARC.	Sector departments need to move more decisively to send staff with appropriate level of delegated authority to the SARC.	Deployment of all approved staff position for SARC..	Sector departments, CHRM and SARC	December 2012
Information disclosure deficiencies	Continuous engagement with clients on what Bank requirements are, particularly with regard to developmental outcomes, environment and social safeguards as well as gender.	Timely submission of details information upon request.	All stakeholders including the Bank.	On going
Fiduciary Management (disbursement and procurement)				
Inadequate financial reporting.	Clarify Bank reporting and auditing requirements to implementing agencies to ensure adequate disclosure of project financial information in periodic and audit reports.	Better monitoring of financial information. Conduct at least 1 fiduciary clinic per year.	Implementing Agency and AfDB	Ongoing
Delays in Procurement and use of country systems.	Implement new DAM. Step up training, and finalize assessment of country procurement procedures. Continue to promote use of country systems	At least one public project will use government procurement rules.	AFDB	End of Dec. 2012
Limited use of National Systems	(i) Continued use of Country Systems in financial management (ii) Finalization of assessment of country procurement rules	At least one public project will fully use national systems	AfDB	Decembe r 2012.
Environmental and Social safeguards				
Limited Follow up of social and environmental safeguards.	Ensure that supervision missions include environmental and social safeguard specialists.	Participation of environmental and social safeguards specialists in participate in supervision missions.	AfDB	Ongoing

ANNEX IV. BANK GROUP PORTFOLIO 2008-2012

Sector Name	Long Name	Approval Date	Effect. Date	Closing Date	Approved Amount (UA) millions	Disb.Rate percent	Age (years since approval)	Implementation Progress (IP)	Development Outcome Indicator (DO)
POWER	Medupi Power Project	14-Oct-09	11-Aug-10	31-Dec-16	1,756.0	43.0%	2.6		
	Eskom Renewable Energy Invest. Project	30-May-11	18-Jul-12	31-Dec-18	233.7	0.0%	1.1		
TRANSPORT	Transnet Ltd	7-Nov-08	5-Oct-11	5-Oct-13	260.0	37.0%	2.1		
FINANCE	Line of Credit to Standard Bank	11-Sep-08	27-May-09	31-Dec-11	140.1	100.0%	3.7		
	Line of Credit to Ned Bank	11-Sep-08	6-Jan-09	28-Feb-10	63.7	100.0%	3.7		
	Global Trade Liquidity Program, Standard Bank of South Africa	7-Sep-09	20-Nov-09	30-Jun-10	67.0	100.0%	2.9		
	Line of Credit to Industrial Development Corporation	19-May-10	26-Sep-11	26-May-13	129.7	53.0%	2.2		
	Summit Development group	20-Sep-10	15-Jun-12	31-Dec-16	15.7	0.0%	1.8		
	Evolution One Equity Fund	27-May-10	3-May-10	31-Dec-16	7.9	26.5%	3.1		
	5th Line of Credit to Development Bank of Southern Africa	3-Feb-11	19-Mar-12	17-Oct-12	192.0	50.0%	1.4		
	Land Bank	20-Jun-12	Pending	Pending	80.2	0.0%	0.2		
MINING & QUARRYING	Kalagadi Beneficiation Loan	18-May-11	Pending	Pending	139.0	0.0%	1.2		
	New Africa Mining Fund	19-Jul-10	16-Jun-11	31-Dec-17	15.7	1.4%			
	Agri Business Investment Fund	28-Jan-09	30-Jun-09	31-Dec-14	9.5	55.0%	3.5		
MULTISECTOR	8 MILES FUND	23-Jun-10	18-Apr-12	31-Dec-17	31.5	0.0%	2.1		
	Development of South Africa One Stop Border Post	22-Dec-11	Pending	Pending	0.2	0.0%	0.6		
INFRASTRUCTURE	Emerging Africa Infrastructure Fund	3-Nov-09	25-May-10	31-Dec-17	27.6	24.0%	2.7		
TELECOMMUNICATIONS	Other Billion (O3b) Equity Fund	10-Jun-10	6-Dec-10	31-Dec-16	31.4	49.6%	2.1		
	New Dawn satellite Project	11-Mar-09	29-Oct-09	31-Dec-12	18.9	67.0%	2.7		
WATER	Integrated Water harvesting	14-Apr-09	15-Dec-09	31-Dec-12	0.3	100.0%	3.3		

Color/Designation	
Red	Unsatisfactory
Orange	Satisfactory
Green	Highly Satisfactory
Grey	Not Available (Not Rated)

ANNEX V. PORTFOLIO MONITORING AND PERFORMANCE INDICATORS OF RATED PROJECTS

Project	Project implementation	Procurement Performance	Financial Performance	Activities and works	Impact on Development	IP	DO	PP/Non PP.
Medupi Power Project								Non PP/Non PPP
Transnet								Non PP/Non PPP
Integrated Water Harvesting								Non PP/Non PPP
LoC Ned Bank								Non PP/Non PPP
LoC Standard Bank Limited								Non PP/Non PPP
LoC GTLP Standard Bank								Non PP/Non PPP
IDC II								Non PP/Non PPP
Other 3 Billion Fund								Non PP/Non PPP
New Dawn								Non PP/Non PPP
Emerging Africa Infrast. Fund								Non PP/Non PPP

Note: PP: Problematic Project; PPP = Potentially Problematic Project; IP = Implementation Performance; DO = Development Outcome

Color/Designation

Red	Unsatisfactory
Orange	Satisfactory
Green	Highly Satisfactory
Grey	Not Available (Not Rated)

Key performance indicators of ongoing projects as at 31 July 2012		
	South Africa	**Bank wide**
Average Project size (UA million)	70.6	33.2
No. active operations	20	749
Average disbursement rate (percent)	53	39.4
No. of ageing projects	Nil	35
Average age	2.4	7.4
Average supervision rate	1.5	1.2
Cancellable projects	2	214
Slow disbursing projects	1	70
Projects not supervised for more than 6 months	Nil	55
Projects at risk	Nil	98
Projects experiencing signature effectiveness and first disbursement delays	3	30

Source: SAP, AfDB

ANNEX VI. SUMMARY OF THE 2008-2012 CSP COMPLETION REPORT

<table>
<tr><th>CSP Priorities</th><th>Validity of Strategic Focus</th><th>Resource Allocation</th><th>Lessons from Strategy and Interventions</th></tr>
<tr><td colspan="4">Core areas of specialization: Enhancing private sector competitiveness; partnership for regional integration; knowledge management and capacity building</td></tr>
<tr><td>Pillar 1: Enhancing Private Sector Competitiveness.
• Support for infrastructure services;
• Support for financial intermediation and SME Development
• Private sector development</td><td>Support was aligned with the government's MTSF. Support to infrastructure was a major focus of government and the Bank provided support to major infrastructural investment programs focusing on energy, water supply and sanitation, and transport infrastructure. Bank strategy was also consistent with

Government's desire to promote local entrepreneurship in various sectors in SMEs, in view of their critical role in job creation and poverty reduction. However, efforts by the Bank to reach SMEs through LoCs to DFIs and commercial banks have not yielded the desired results</td><td>Energy: 2 energy projects for a total of about US$3 billion were approved during 2008-12 to provide support to the energy sector.

Transport: 1 loan totaling US$400 million was approved and another US$400 million B loan was provided by other commercial banks to provide support to Transnet's railway projects</td><td rowspan="3">Better benchmarking of Results framework. There is need for clear baseline data for the output and outcome indicators.

Support for energy companies and various modalities of carbon trading and finance can make a positive contribution to green development. Emphasis on innovation and clean technology requires AfDB to continuously improve staff's knowledge of emerging technologies.

More vigorous application of project readiness filters to improve quality–at-entry and address systemic obstacles in processing and implementing projects.

Need for private sector development staff at SARC. The South Africa portfolio is highly skewed to private sector operations due to the dynamic nature of the sector. The Bank needs to consider deployment of more private sector staff to SARC.

Need for AFDB to add value to the development process of middle-income countries like South Africa with an expanded focus on private sector development as well as encouraging more public-private partnerships.

More innovative approaches are needed to support the SME sector. Due to availability of low cost loans to the private sector from government especially to SMEs and in addition to direct funding, the Bank will explore new mechanisms for supporting private sector development.
Improved connectivity is correlated with increased business cooperation, cross-border trade, and investments. The country program can reinforce AfDB' s regional integration initiatives by focusing on transport connectivity and border town development to promote economic corridors;

The Bank should continue to explore cooperation with South Africa's institutions for regional infrastructure financing; and greater attention should be paid to capacity development and inter-agency coordination to facilitate increasingly complex financing initiatives;

The transaction costs involved in accessing MIC and Bilateral Trust Funds are considerable. The Bank will seek to simplify and streamline its fiduciary processes and being more flexible without compromising standards.

For MICs, ADB needs to look beyond the provision of financial assistance as the main modality for development cooperation and emphasize other value-added partnership modalities including serving as an agent for capacity development, knowledge management, and technology facilitation</td></tr>
<tr><td>Pillar II: Partnership for Regional Integration and Development: This strategic pillar of AfDB assistance, covered the strengthening of cross-border trade and investment; developing regional public goods; and expanding regional cooperation through SADC and new initiatives.</td><td>Bank support was aligned with the Government's objective of increasing regional trade and investments, improved regional infrastructure development, especially along the economic development corridors to facilitate trade flows in the SADC region, and increased capital investment by South African institutions in Africa region

Ongoing investments supported rehabilitation and improvement of regional roads for better connectivity, while TAs provided institutional support.</td><td>Lines of credit to 5 commercial banks and DFIs amounting to nearly US$1 billion have been provided to facilitate cross boarder investment.

Five loans amounting to over US$117 million have been provided to private equity funds for cross-border investment.

Five Equity investments amounting US$121 million helped finance cross border investments in various sectors including mining, agriculture, power; SME development, and other sectors.

Support to One Stop Border Post of US$ 0.3 million (MIC Grant).</td></tr>
<tr><td>Knowledge Management and Capacity Building through:
(i) Improving Knowledge Generation and Sharing
(ii) Improving Capacity for Enhancement of Services Delivery</td><td>Bank support was aligned with the Government's objective of strengthening the capacity of the state to implement programs and provide services, especially at municipal level, support to Government to improve planning and implementation of programs, overall to improve capacity of Government deliver delivering basic services.</td><td>The Bank conducted the following ESWs (i) A study on National Gender Machinery; (ii) A Manufacturing Sector Flagship Study is being finalised; (iii) A Study on capacity building for enhanced service delivery by municipalities is at a preparatory stage.</td></tr>
</table>

ANNEX VII. MATRIX OF MAJOR DONOR ACTIVITIES IN SOUTH AFRICA

	Capacity building and Institution Support	Environment and climate	Investment Climate	Education	Health (HIV/AIDS)	Private sector	Agriculture	Other Humana Development	Water Sector	Energy Sector	Transport	Public Private Partnership (PPP)	Trade	Governance
African Development Bank						+	+		+	+	+		+	
World Bank	+		+							+				
IFC						+								
IMF	+													
European Commission/EIB	+			+	+	+								
UN and its Organs	+	+			+									+
JICA	+	+												
Others, specify														

Source: AfDB and Development Partners

ANNEX VIII. GREEN ENERGY

South Africa is the largest contributor to greenhouse gas (GHG) emissions in Africa. In 2009, the International Energy Agency listed South Africa as the thirteenth highest emitter of carbon dioxide in the world. According to the country's National Climate Change Response Green Paper, the energy sector is the largest source of GHG emissions, accounting for more than 80 percent of the country's emissions. The high emissions are mainly due to the structure of the economy, which has been historically characterised by energy-intensive sectors such as mining, mineral processing and beneficiation.

During the climate change negotiations, within the framework of the Conference of Parties (COP) to the Kyoto Protocol, South Africa committed to contributing to the global greenhouse gas mitigation effort. The emissions trajectory would peak between 2020 and 2025, remaining stable for a decade thereafter, and declining in absolute terms from around 2035. This was on condition that the country received the necessary finance, technology and support from the international community.

South Africa has therefore integrated a climate constraint that takes account of its mitigation commitments, into its energy planning tools including the Integrated Energy Plan (IEP) and the Integrated Resource Plan (IRP) for electricity generation. Furthermore, within the context of the New Growth Path and the country's Industrial Policy Action Plan, South Africa is committed to creating a business environment that facilitates the development of a local renewable energy technology manufacturing, implementation and export industry and that maximises its job creation potential.

According to the IRP, the contribution of coal based electricity plants to total production capacity should drop to 48 percent by 2030. This will be offset by the increased contribution of combined cycle gas turbines (5 percent), open cycle gas turbines (9 percent), renewable energy (33 percent) and nuclear energy (25 percent). The construction of transmission lines will be an important element of the electricity supply expansion investment programme given the need to feed the power generated from the renewable energy initiatives into the grid. In order to cushion the final consumers from the high costs of implementing renewable energy projects, the Government is currently working on the establishment of a Renewable Energy Fund to pool concessionary resources.

A key policy development in the sector is the proposed policy change towards the creation of the Independent System Market Operator (ISMO) which will be responsible for generation planning, system operation and expansion planning and buying of all electricity. The Government is also currently working on the South Africa electrification initiative which seeks to develop a strategy and implementation models to achieve 100 percent electrification in the country by about 2020.

ANNEX IX. SUMMARY OF STUDY: MANUFACTURING, PRODUCTIVITY, INNOVATION AND JOBS—A COMPARISON WITH THE BRICS

The manufacturing sector is at the center of the Government of South Africa's development policy. Growth in manufacturing is seen as critical to enhancing economy wide growth and creating employment. Over the last two decades, South Africa's manufacturing performance has been weak. Manufacturing employment has also been declining consistently over the same period. This is particularly so when compared to emerging markets and the BRIC countries in particular. By contrast, in India, China and most notably in Brazil, the closest comparator to South Africa, manufacturing employment has been rising significantly. More than half of the reduction in South African manufacturing employment has occurred in the labor-intensive sectors.

South Africa's poor performance in terms of innovation is an indicator not solely of current weakness, but also of the likely future prospects for technology and innovation intensive manufacturing and service activities. Measured in terms of economy wide technology and innovation performance indicators South Africa performs poorly in comparison with the other BRIC countries. In only one area, namely in mining related technologies, is there evidence that South Africa is proximate to the global technological frontier. South Africa's presence in mining and related activities is of long standing.

Firm level interviews supplemented by survey data reveal that the most widespread constraint for technology based firms in South Africa is the shortage of skills. The high quality of many South African graduates are a major factor underpinning the success of many technology based firms, however they are in very short supply. Moreover, there are indications that the quality of graduates was declining. Larger and better established firms are able to partially mitigate the skills constraint by the offer of high salaries and graduate bursaries. These options are not available to smaller and newly established firms. The incidence of a shortage of skills and a consequent tight labor market accordingly fall disproportionately on the smaller, less capitalized firms and on the firms in formation.

The shortage of finance is the second most significant constraint cited by technology based firms. Again, these constraints are clearly most binding to newly established firms or firms that have not yet entered the market. Black economic empowerment (BEE) may also have an important impact. There appears to be a near absence of new entrant black owned technology based firms. Black graduates, particularly those with technical and engineering skills, can readily find high paying posts in well established companies. They are consequently far less likely to engage in risk taking new ventures. Black entrepreneurs too, are likely to find far more lucrative opportunities with existent firms.

Manufacturing's linkages to the rest of the economy are declining – both forward and particularly backward linkages. Declining linkages combined with a reduced overall share for manufacturing in the economy and the changing composition within manufacturing away from the more labor intensive sectors – all suggest that the capacity for manufacturing to drive the economy wide output increase and enhance employment is limited and declining.

There are three major conclusions for the broad strategic direction of government's industrial policy.

- First, much more attention needs to be paid to enhancing the employment intensity of manufacturing. In particular, industrial policy will need to be complemented by labor market reforms.
- Second, more attention needs to be paid to the constraints faced by new manufacturing firm entrants and to addressing the constraints that such firms face.

- Third, policy supports that aim to enhance economy wide output and employment growth should pay more attention to the significant heterogeneity of linkages and of employment intensity of the different subsectors in manufacturing as well as to the linkage and employment intensity of other non-manufacturing sectors.

Innovation will be vital to spur growth and prosperity, otherwise South Africa will continue to lose its comparative advantage in the emerging markets. It is clear that South Africa has to foster an economy driven by innovation, exports, Green Growth opportunity and clean energy. This will require investment in human capital and infrastructure to adopt new regimes for trade, patents, immigration and technology transfer; to devise methods for government to work more effectively, and to restore fiscal prudence to budget and debt policies.