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Funding of Multilateral Development Banks and the Common Monetary Area

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GOVERNMENT SPENDING REVIEWS

Executive Summary

South Africa's membership in the MDBs and the CMA continues to be of **strategic importance** and can be seen as supporting the country to achieve its **national development plan's objectives**, to **reform the global political-economy** and **strengthen regional integration**. The MDBs also have the potential of **providing South Africa** with **finance at more competitive rates** than the markets can offer, that can be utilised for projects, programmes, and budget support. The retention of South Africa's shareholding in the MDBs also supports the country's efforts to reform the global political economy, by ensuring that South Africa has direct representation in the governance structures of these institutions, thereby also **increasing the voice** of developing countries and the Global South.

The main discovery of the Spending Review is that it **did not reveal any savings that could be yielded** within the commitments to the Multilateral Development Banks (MDBs); the Common Monetary Area (CMA) and the New Development Bank (NDB).

Whilst the aren't any measures to yield savings within South Africa's commitments to the MDB and CMA, South African can increases the value for money it gets from its commitments by:

1. Increasing the role off MDB's in South Africa's current funding strategy for the fiscus
2. Maintaining or increasing its shareholding (in the MDB) through Cabinet
3. Placing funding to the CMA on direct charge from the NRF

Firstly, during 2020, the National Treasury increased its borrowing from MDB/I as a result of the Covid-19 pandemic. This is the first time South Africa has borrowed as a sovereign and thus a number of lessons were learnt during the experience. Going forward, South Africa's Funding **Strategy** should include MDBs as a source of finance in its funding mix, to ensure that South Africa takes full advantage of the opportunities that its capital contributions and membership offers, as well as to fund Government's deficit in the most economically favourable way possible. Further the **lending terms** from these institutions are **more favourable** compared to market rates e.g., longer grace period and maturities; below-market interest rates and embedded technical assistance. This may be a possible avenue that would result in the reduction of **the level of debt service cost** of government. National State-Owned Entities have been using this option to address liquidity challenges given persisting fiscal challenges in the country.
With the intention of increasing the role off MDB's in South Africa's current funding strategy for the fiscus, engaging with ALM and P.F. regarding the benefits identified in this report is essential. With the advent of the Covid-19 pandemic, borrowing from MDBs has subsequently been integrated into the funding strategy of the Treasury. Currently, negotiations are underway to source Vaccine funding as well as funding for Budget Support from the World Bank, as part of the implementation of the borrowing strategy.

Secondly, South Africa should **maintain or increase its shareholding** (**recapitalisation**) in the MDBs, since the shareholding links directly to the **voting power and voice** of the country in order to bring **African issues** to the forefront in MDBs. To **ensure balanced continental representation** in the MDBs, South Africa should aim to retain its seat as one of the top three African (Nigeria, Egypt and South Africa) shareholders in the World Bank Group (WBG) and the African Development Bank (AfDB). For example, within the AfDB, Nigeria is the largest shareholder regionally, followed by Egypt and then South Africa. There is a Cabinet mandate for South Africa to strive towards increasing its shareholding within the Bank to 6%. Additionally, there is a very real **reputational risk** for South Africa in the Constituency at the World Bank, as Nigeria and Angola are increasing their shareholding, and are up to date with their capital subscriptions for the 2018 recapitalisation of the International Bank for Reconstruction and Development.
To increase or maintain shareholding in the MDBs, IREP will continue to engage with Public Finance, Assets and Liabilities and the CFO, prior to seeking Cluster and Cabinet approval via a submission. Public Finance will be alerted as soon as a recapitalisation process is triggered by an MDB, to ensure alignment with internal planning and budget process.

Lastly, South Africa **should not pursue the amendment of the CMA payment formula.** Rather the CMA payments should be viewed as policy instruments that must be used to ensure that the CMA can be a foundation for long-term development towards a monetary union in Southern Africa. Thus, any potential savings should be weighed against possible impact on trade and investment. Other considerations are the immediate political fallout and likely spill-over to bodies such as the African Union (AU), Southern African Customs Union (SACU) and the Southern African Development Community (SADC). Given that the standards of living in the region have not converged over the past 19 years, South Africa's case to review the CMA payment formula will be difficult to negotiate successfully.
The option that is being pursued to affect this recommendation, is for IREP to coordinate with P.F. to make inputs into the ongoing process to amend the PFMA, in order for the CMA expenditure to be charged as a **direct charge against the National Revenue Fund**. IREP and P.F. have made submissions to the Legislation Unit regarding the proposal made above. At this point, IREP and P.F. are awaiting the conclusion of the PFMA review to find out if the submission made was successful and await the process to amend the PFMA to conclude and see if the proposal has been considered favourably.

Summary

South Africa is facing a difficult fiscal environment, that is underpinned by low levels of economic growth, a high debt to GDP ratio, elevated levels of unemployment, and weakening revenue collections. Domestic conditions are further weighed by increased risks to global growth, with lower commodity prices and waning international trade conditions. Within this context, South Africa's commitments to the MDBs and the CMA are forecast to steadily increase over the next Medium-Term Strategic Framework (MTSF) period.

Therefore, the **purpose** of this spend review is to review the benefits and costs of South Africa's membership of the Multilateral Development Banks (MDBs) and the CMA in the context of South Africa's current fiscal pressures.

Included in this review are transfers to the African Development Bank (AfDB), the World Bank Group (WBG), and the New Development Bank (NDB) for the buying of shares and contributing to the general and selective capital increases in the institutions' authorised capital. Also included are contributions are also made to the African Development Fund (ADF) and the International Development Association (IDA) the concessional funds of the AfDB and WBG respectively. The Spending Review also assesses South Africa's involvement in a multilateral relationship with several countries that together form the Common Monetary Area (CMA).

The study is driven by the need to demonstrate that funding to Multilateral Development Institutions has a high impact and is not simply the unnecessary depletion of financial resources given the difficult fiscal environment that South Africa is facing. In particular, the review sort to identify the (i) **tangible and intangible costs** against the benefits derived from subscriptions, transfers, and contributions to the MDBs and the CMA, as well as (ii) the **possible savings** that could be realised.

Background and context to South Africa's involvement in the MDBs and CMA

Greater involvement in international multilateral institutions has been a prominent feature of South Africa's post-apartheid foreign policy, and has contributed to build a strong reputation for the country. Since the end of apartheid, the country has emerged as a promoter of established international norms and has sought to play a leading role in reforming the global political economy and North-South relations in favour of a "fairer distribution of power and resources". South Africa's role in the Southern African Customs Union and the Common Monetary Area has been central to its quest to promote regional integration, peace, security, and development.

This foreign policy position has underpinned South Africa's continued participation and shareholding in Multilateral Development Banks (MDBs), such as the World Bank Group (WGB), the African Development Bank (AfDB) and the Common Monetary Area (CMA).

The National Treasury, as mandated by Chapter 13 of the Constitution, Chapter 2 of the Public Finance Management Act (PFMA), and Priority 7 of the Medium Terms Strategic Framework (MTSF), namely “A Better Africa and World” manages South Africa’s relationships with these institutions. This role is further concretised in the Strategic Plan of the National Treasury 2020-2025 which requires the International and Regional Economic Policy (IREP) Division to monitor the uptake of development finance from the AfDB, WBG and the New Development Bank (NDB), in support of the National Treasury’s mandate of promoting national government’s fiscal policy and the coordination of its macroeconomic policy at a global level.

MDBs provide financial assistance to developing countries in order to promote economic and social development. The MDBs primarily fund large infrastructure and other development projects and provide loans tied to policy reforms by the government. The MDBs provide non-concessional financial assistance to Middle-Income Countries (MICs) and some credit worthy Low-Income Countries (LICs) on market-based terms, typically in the form of loans, but also through equity investments and loan guarantees. They also provide concessional assistance, including grants and loans at below market interest rates, to LICs.

As a member of the MDBs, South Africa is required to make capital contributions towards each of the Banks in the form of both paid in capital instalments and callable capital, which are based on the shares allocated for either the establishment of the MDB (*e.g.*, the NDB), or the recapitalisation of the MDBs (*e.g.*, WBG and AfDB). The calls for the recapitalisation of the MDBs are mainly triggered by developments in the global economy and the increase in demand for financial support from member countries, driven by the need to eradicate poverty, achieve sustainable development goals and grow economies worldwide. South Africa’s investment in the MDBs assumes that the financing will be made available to South African public and private sectors and that viable projects be presented to the MDBs.

To date the paid in capital to the AfDB and the WBG, based on the shares allocated for recapitalisation that take place every eight or ten years, has not been significant. The NDB, on the other hand, has not required recapitalisation as it is concluding its paid in capital contribution schedule as a newly established MDB.

South Africa’s participation in the CMA, speaks directly to Outcome 2 of the Strategic Plan of the National Treasury 2020-2025 regarding *‘Coherent Economic Policy Advocated’,* specifically relating to the *facilitation of regional and international cooperation*. Additionally, South Africa’s participation in the CMA is also in furtherance of Outcome 1 related to *“sustainable public finances”.* Through the Multilateral Monetary Agreement (MMA) as revised in 2021, South Africa has advocated for the inclusion of financial regulation and banking supervision to ensure that within the CMA *illicit financial flows and money laundering* are combatted. As the MMA, that underpins the CMA, calls for South Africa to compensate Eswatini, Lesotho and Namibia for the loss seigniorage resulting from the Rands circulating in their economies and displacing their national currencies. The CMA payments made to the above-mentioned countries have been increasing steadily since 2008.

Key findings and recommendations

The Spending Review **did not reveal any savings that could be yielded** within the commitments to the Multilateral Development Banks (MDBs); the Common Monetary Area (CMA) and the New Development Bank (NDB).
Although the payments in subscriptions and shares to the **Multilateral Development Banks** and **Institutions** appear to be a very large burden on the fiscus, the opposite is actually true. The **African Development Bank** and **World Bank Group** shareholding, enables South Africa to not only be Board members in these Banks, but also influence the policy direction that these Banks develop.

In the **New Development Bank**, the benefit of being a founding member resulted in South Africa being a 20 percent equal shareholder in the institution. This shareholding position not only provides the country representation at the Board of Directors, a NDB Africa Regional Centre, a Vice President position, but also the voice to ensure that the institution's policies are closely aligned with the country's developmental imperatives. The NDB has provided project approvals of approximately R81 billion to South Africa in the 6 years of the Bank's operation. Sovereign and non-sovereign project financing as well as rand denominated loans has been received by government and its private sector.

In the case of the **Common Monetary Area** payments, the value of being part of this grouping is that it has close ties to the Southern African Customs Union and establishes an Area whereby, through trade, all member states can have the same development and equitable economic advancements.

Therefore, South Africa's membership in the MDBs and the CMA continues to be of **strategic importance** and can be seen as supporting the country to achieve its **national development objectives**, to **reform the global political-economy** and **strengthen regional integration**. This is also **in support of the National Treasury's mandate** of promoting national government's fiscal policy and the coordination of its macroeconomic policy at a global level. The MDBs have the potential of **providing South Africa** with **finance at more competitive rates** than the markets can offer, that can be utilised for projects, programmes, and budget support. The retention of South Africa's shareholding in the MDBs also supports the country's efforts to reform the global political economy, by ensuring that South Africa has direct representation in the governance structures of these institutions, thereby also **increasing the voice** of developing countries and the Global South.

Notwithstanding the above, South Africa can adopt the following measures to increase the value for money from its contribution to the MDBs as well as improve its financial management associated with making these payments:

1. Increase the role of MDB’s in South Africa’s current funding strategy for the fiscus.
2. Maintain or increase its shareholding in the MDB.
3. Place the funding to the CMA as a direct charge from the NRF.

<u>To increase the role off MDB’s in South Africa’s current funding strategy for the fiscus</u>
During 2020, the National Treasury increased its borrowing from MDB/I as a result of the Covid-19 pandemic. This is the first time South Africa has borrowed as a sovereign and thus a number of lessons were learnt during the experience. Going forward, the proposed **Funding Strategy** should include MDBs as a source of finance in its funding mix, to ensure that South Africa takes full advantage of the opportunities that its capital contributions and membership offers, as well as to fund Government’s deficit in the most economically favourable way possible.

The **lending terms** from these institutions are **more favourable** compared to market rates e.g., longer grace period and maturities; below-market interest rates and embedded technical assistance. This may be a possible avenue that would result in the reduction of **the level of debt service cost** of government. National State-Owned Entities have been using this option to address liquidity challenges given persisting fiscal challenges in the country.

Considering the above recommendation, the actions that would have been suggested was for IREP to engage with ALM and P.F. regarding the benefits identified in this report. However, it is clear that the spend review may have been overtaken by actual events. Based on several previous interactions during 2020 with ALM, where they borrowed from the AfDB, NDB and the IMF, this point seems to be confirmed by the real situation in which IREP and NT finds themselves. With the advent of the Covid-19 pandemic, borrowing from MDBs has subsequently been integrated into the funding strategy of the Treasury. Currently negotiations are underway to source Vaccine funding as well as funding for Budget Support from the World Bank, as part of the implementation of the borrowing strategy. Continuous engagement between IREP; ALM and P.F. will inform all future borrowing.

<u>To maintain or increase shareholding</u>
South Africa should **maintain or increase its shareholding** (**recapitalisation**) in the MDBs, since the shareholding links directly to the **voting power and voice** of the country in order to bring **African issues** to the forefront in MDBs.

To **ensure balanced continental representation** in the MDBs, South Africa should aim to retain its seat as one of the top three African (Nigeria, Egypt and South Africa) shareholders in the World Bank Group (WBG) and the African Development Bank (AfDB). For example, within the AfDB, Nigeria is the largest shareholder regionally, followed by Egypt and then South Africa. There is a Cabinet mandate for South Africa to strive towards increasing its shareholding within the Bank to 6%. Additionally, there is a very real **reputational risk** for South Africa in the Constituency at the World Bank, as Nigeria and Angola are increasing their shareholding, and are up to date with their capital subscriptions for the 2018 recapitalisation of the International Bank for Reconstruction and Development.

Actions to bring fourth the above recommendation will include: IREP will continue to engage with Public Finance, Budget Office (Fiscal Policy unit); Assets and Liabilities and the CFO, prior to seeking Cluster and Cabinet approval via a submission. Public Finance will be alerted as soon as a recapitalisation process is triggered by an MDB, to ensure alignment with internal planning and budget process. Considering the aforementioned, P.F. together with B.O. can then develop a strategy on how to deal with this unique process

<u>To place the funding to the CMA as a direct charge from the NRF</u>

South Africa **should not pursue the amendment of the CMA payment formula** and the CMA payments should be viewed as policy instruments that must be used to ensure that the CMA can be a foundation for long-term development towards a monetary union in Southern Africa. Thus, any potential savings should be weighed against possible impact on trade and investment. Other considerations are the immediate political fallout and likely spill-over to bodies such as the African Union (AU), Southern African Customs Union (SACU) and the Southern African Development Community (SADC). Given that the standards of living in the region have not converged over the past 19 years, South Africa's case to review the CMA payment formula will be difficult to negotiate successfully.

The option that is being pursued to affect this recommendation, is for IREP to coordinate with P.F. to make inputs into the ongoing process to amend the PFMA, in order for the CMA expenditure to be charged as a **direct charge against the National Revenue Fund**. IREP and P.F. have made submissions to the Legislation Unit regarding the proposal made above. At this point, IREP and P.F. are awaiting the conclusion of the PFMA review to find out if the submission made was successful and await the process to amend the PFMA to conclude and see if the proposal has been considered favourably.

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1. Introduction to Spending Review

The purpose of this spend review is to review the benefits and costs of South Africa's membership of the Multilateral Development Banks (MDBs) and the CMA in the context of South Africa's current fiscal pressures.

Included in this review are transfers to the African Development Bank (AfDB), the World Bank Group (WBG), and the New Development Bank (NDB) for the buying of shares and contributing to the general and selective capital increases in the institutions' authorised capital. Also included are contributions are also made to the African Development Fund (ADF) and the International Development Association (IDA) the concessional funds of the AfDB and WBG respectively. The Spending Review also assesses South Africa's involvement in a multilateral relationship with several countries that together form the Common Monetary Area (CMA).

The study is driven by the need to demonstrate that funding to Multilateral Development Institutions has a high impact, and is not simply the unnecessary depletion of financial resources given the difficult fiscal environment that South Africa is facing.

2. Programme Description

Overview of the MDB programme and associated expenditure obligations

South Africa is a member of three (3) MDBs – Africa Development Bank (AfDB), the World Bank (aka the International Bank for Reconstruction and Development-IBRD), the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA), and the New Development Bank (BRICS). With the exception of the IFC and the MIGA, the intended beneficiaries of these MDBs are the Public Sector.

Table 1: Overview of South Africa's membership in MDB

Institution	*Purpose of Component*	*Beneficiaries*
AfDB	SA is the third largest shareholder at the AfDB at 5% (currently valued at \$4,6 billion (R69 billion). The Bank's active project portfolio in South Africa as of 31 March 2021 is comprised of 28 operations valued at US\$ 5.35 billion (ZAR 75 billion). The Portfolio is dominated by the energy sector having the highest share of total commitments at 59%, followed by finance (23%), transport (9%), multisector (6%), industry (2.7%) with the remaining 0.3% in water and agriculture. In June 2020, the AfDB approved a budget support loan of R5 billion for Covid-19 response to the National Treasury.	Public Sector
World Bank (International Bank for Reconstruction and Development-IBRD)	SA's shareholding at the World Bank is 0.7% valued at \$2.1 billion (R31 billion). The total current lending portfolio to South Africa is valued at US\$3.8 billion (R53 billion) as of 31 March 2021. 93% of the funding is concentrated to Eskom Medupi Investment Support Project (US\$3.4 billion). The other two noticeable projects are the Eskom Climate Technology Fund (US\$250 million) and Land Bank (US\$93 million).	Public Sector
International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA)	South Africa is IFC's second largest client in Sub-Saharan Africa and is MIGA's largest client in Africa and has the third largest Worldwide portfolio of \$1.6 billion (R22.4 billion) through loans, equity and risk cover supporting the private sector in the country. The current IFC portfolio is valued at US\$ 2.1 billion (28 billion). The Multilateral Investment Guarantee Agency portfolio is valued at US\$1.6 billion.	Private sector
New Development Bank (BRICS)	SA has 20% shareholding at the NDB which is currently the same as the other four-member countries (Brazil, China, India and Russia) This is equivalent to 100,000 (one hundred thousand) shares, in a total of ten billion dollars (US\$10,000,000,000), of which 20,000 (twenty thousand) shares correspond to paid in capital, in a total of two billion dollars (US\$2,000,000,000) and 80,000 (eighty thousand) shares correspond to callable capital, in a total of eight billion dollars (US\$8,000,000,000). The total portfolio extended by the New Development Bank to South Africa is valued at R76 billion. The main sectors that have received funding from the NDB include transport, energy, water and more recently health and fiscal support.	Public Sector

The Multilateral Development Banks (MDBs) provide financial assistance to their member countries, in order to promote economic and social development. They primarily fund large infrastructure projects and other development projects, and also provide grants and loans often tied to policy reforms or performance by the government. They also provide:

- Non-concessional financial assistance to their middle-income countries[1] and some credit worthy low-income countries[2] on terms which are relatively more competitive than the market, typically in the form of loans, equity investments, and loan guarantees.
- Concessional assistance, including grants and loans at below market interest rates, to low-income countries – most of which are on the African Continent.

Shareholding is a pre-requisite for membership and access to finance. Whilst there are no eligibility criteria for funding, funding is determined by the lending envelope available for the MDBs and is based on the Agreements or Articles establishing the institutions and their lending policies

Each type of assistance places different types of payment obligations on its members.

Expenditure obligations to fund the MDB's non-concessional loans

The expenditure obligation that results for non-concessional loans arise when member countries subscribe to shares as a consequence of their membership in each of these MDBs. However, only a small portion (typically between 10% and 20%) of the value of these shares is actually paid to the MDB ("as paid in capital"). The rest of the contributions is callable capital which the Banks call upon its members to pay if their resources are exhausted and they still need funds to repay bondholders. To date, no MDB has ever had to draw on its callable capital.

A second obligation may arise when MDBs negotiate the recapitalisation of their capital with their Board of Governors every eight to ten years as their resources get depleted. This recapitalisation follows the subscription process outlined above. It has a paid-in portion which ranges from between 10% and 20%; and the rest (80-90%%) is the callable portion. If the recapitalisation is approved the callable portion increases according to the shares allocated to each member country. The callable capital from the previous subscriptions does not lapse after the negotiations.

The MDBs use the capital subscriptions from their member countries to borrow money from international capital markets competitively due to their AAA credit rating and then on-lend the money to their member countries. MDBs are able to competitively borrow from international capital markets because most of the loans to the member countries are backed by the guarantees from governments.

The NDB has not negotiated a recapitalisation so far.

[1] According to the world bank, middle income countries are those with a gross national **income** (GNI) per capita between $1,036 and $12,535. South Africa is considered as a MIC due to its GNI that was $12.670 in 2019 classification.

[2] As of 1 July 2019, low-income economies are defined as those with a GNI per capita, calculated using the World Bank Atlas method, of $1,025 or less in 2018.

Expenditure obligations to fund the MDB's Concessional Lending Windows

Expenditure obligations may also arise if South Africa decides to fund concessional lending windows. These lending windows are generally not funded by the market through the issuing of bonds. Rather, their funds have generally come from direct financial contributions made by member countries. Most of the money comes from more prosperous countries, while contributions from borrowing countries are generally more symbolic than substantive. The MDBs also use some of the net income from their non-concessional windows to fund the concessional lending windows. In 2018, the World Bank's International Development Agency (IDA) started issuing bonds to help finance its programmes, similar to the bonds issued by the non-concessional windows.

As the MDBs extend concessional loans and grants to low-income countries, the Windows's resources become depleted. Thus, the donor countries meet together periodically to replenish these resources. These increases in resources are called replenishments, and mostly occur on a planned schedule ranging from three to five years. If these facilities are not replenished on time, they will run out of lendable resources and have to reduce their levels of aid to poorer countries.

Additional rationale for South Africa's participation in the MDBs includes:

- South Africa as a member directly benefits through accessing competitive funding compared to capital markets from the MDBs, to augment its budget (budget support) or provide guarantees to support infrastructure programmes for State Owned Companies (SOCs).
- In general, as a Country we support the global agenda of these institutions (e.g., SDGs 2030) which aim to reduce global poverty through supporting critical long-term development projects and programmes in sectors ranging from infrastructure, social sectors, and the environment in developing countries.
- South Africa, through the National Treasury has a voice and effectively participates in global financial discussions at the MDBs where decisions are taken on specific policy issues such as the debt problem which particularly affects African Countries, climate change – which affects South Africa directly considering its high carbon/fossil fuel dependent energy production, and currently - resource mobilisation for vaccine access for developing countries including South Africa and the rest of the African Continent.

Overview of the CMA programme and associated expenditure obligations

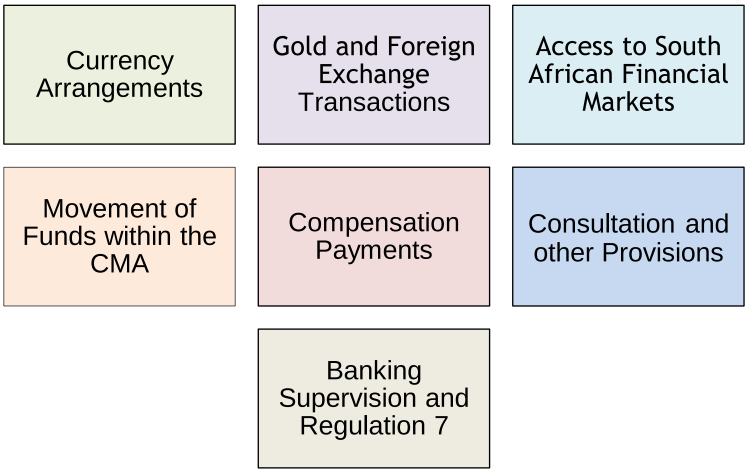
Separate from its participation in the MBDs, South Africa is a member of a Common Monetary Area (CMA) with Namibia, Lesotho, and Eswatini. The CMA derives its mandate from the Multilateral Monetary Agreement (MMA) which was approved and signed into law by the respective CMA Ministers of Finance in 1992. The MMA seeks to advance and sustain economic development within the CMA region through the formalisation of the monetary arrangements in the CMA. It seeks to do so by ensuring that all of its major features depicted in figure 1 and summarised in annexure 1 are adopted and implemented.

The expenditure obligation arising from South Africa's membership of the CMA are the compensatory payments that the Government of South Africa must make to the other contracting parties. These payments represent a return on the rand currency circulating as legal tender in their respective areas. These payments are made from the National Treasury's departmental budget.

South Africa's Rationale for participating in the CMA include:

- The CMA advances monetary integration through the free movement of funds, foreign exchange transactions, ELN countries access to South African Financial Markets as well as banking supervision and regulations.
- The resultant an exchange of statistical and other data required for the efficient implementation of monetary and exchange control policies.

Figure 1: Institutional Arrangements of the CMA



Policy and Institutional Information

South Africa's participation in international development institutions is guided by a number of foreign policy pronouncements. These include:

- The White Paper on South Africa's Foreign Policy (2011) which states that *"South Africa will continue to engage internationally on aid effectiveness, increased global development assistance, and strengthening development partnerships"*.
- The National Industrial Policy Framework (NIPF) and the Industrial Policy Action Plan (IPAP) which aim to *"contribute to industrial development in Africa, with a strong emphasis on regional integration and building regional capabilities"*.
- The National Development Plan (NDP) which is the policy premise of South Africa's international engagement for its economic benefit across all sectors in global fora. It emphasizes that one of the specific objectives for South Africa's international engagement is to *"advance South Africa's national interest and safeguard South Africa's national positions within all international engagements and promote an equitable rules-based multilateral system, which includes institutions such as MDBs amongst others".*
- Chapter 4 of the NDP also calls for increased investment in: transport (rail, road, ports); energy (generation and distribution); and information & communications infrastructure, and infrastructure is the main priority of Multilateral Development Institutions.

The current policy guidance for the country's participation in the multilateral system is the Medium-Term Strategic Framework for 2014-2019 (MTSF 2019-2024), which is a Cabinet Strategy to implement the National Development Plan (NDP). With specific reference to the previously used Outcome 11: *"Creating a better South Africa and contribute to a better and safer Africa and World*", which is now encapsulated in Priority 7 *"A better Africa and World*", South Africa will continue "*working towards global peace, people-centred development, and prosperity for all*".

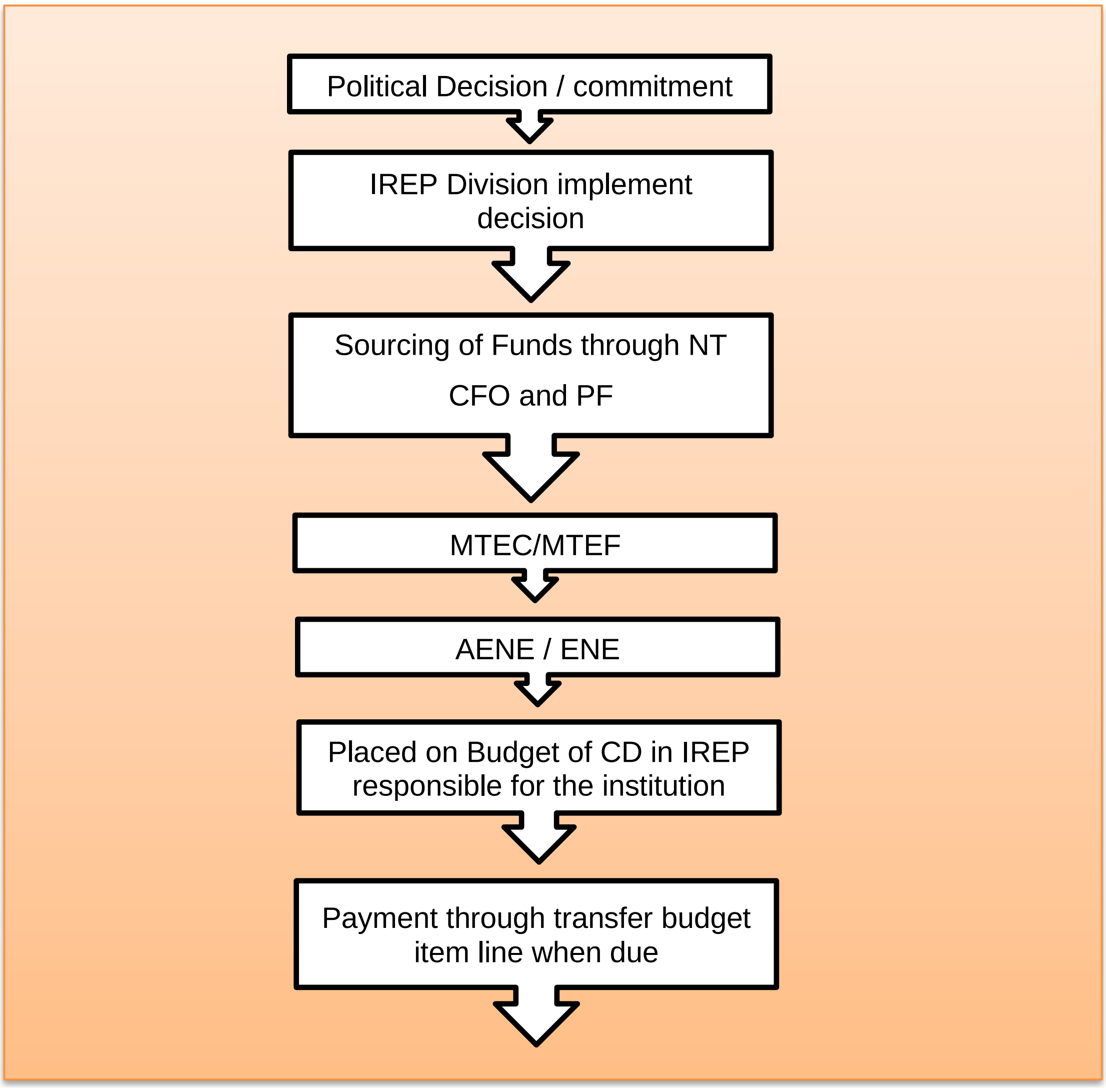
The Minister of Finance supported by the National Treasury represents South Africa in the MDBs, in line with the Finance mandate. The PFMA assigns responsibility to the Minister of Finance to engage on any foreign borrowing including with Multilateral Development Institutions. The Minister of Finance is therefore a MDB Governor and participates in the MDB governance matters related to lending policies, capital contributions, determination of priority sectors for lending, regional lending allocations, representation at board level. The MoF thus contributes to the strategic direction, of these global financial institutions, to advance South Africa and Africa's interests.

For the advancement of our key interests at the Boards of these institutions, South Africa has a permanent seat on the Board of Directors of the AfDB, New Development Bank and shares a constituency office with Eswatini and Lesotho at the AfDB. At the World Bank, South Africa shares the seat in the Board of Directors with Angola and Nigeria. These offices report to the Minister of Finance of South Africa.

The Minister of Finance supported by the Central Bank Governor represents South Africa in the CMA.

The flow of funds to the MDBs and the CMA are depicted in **figure 2** below.

Figure 2: Flow of Funds



3. Programme Chain of Delivery

MDB Programme Chain of Delivery

Key role players in determining and managing South Africa's participation in MDB is summarised as follows:

- *The President of the Republic of South Africa* who authorises the decision to join through the Cabinet and authorises the Minister of Finance (MoF) to sign the Agreement or Articles establishing the institutions through a Presidential minute. The President also approves the request of shareholding to be taken based on affordability and strategic objectives.
- *Cabinet* who authorise the recommendation by made by the MoF to join, provided the request for joining is based on affordability and strategic objectives. Cabinet also approves SA's participation in the recapitalisation of these institutions.
- *Parliament* who gazettes the signed Agreement or Articles establishing these institutions.

- *The Minister of Finance* who, supported by National Treasury, approves and recommends the request to join or participate in the recapitalisation to Cabinet.
- *The Fiscal Liability Committee (FLC) or the CFO* who ensure that the prescribed processes as per Public Finance's requirements are followed (e.g., the Chief Financial Officer (CFO) will confirm the availability of funds to pay the paid in portion and the FLC will confirm the affordability of the callable capital). The payments are done by IREP once the ratification process has been finalised and subject to the payment calendar of each institution.

In joining the institution, the DG and Minister of Finance recommend to Cabinet that the Government of South Africa joins the institutions based on a due diligence conducted and the strategic importance of that particular institution. The due diligence includes a legal opinion from the NT Legal Services and the Office of Chief State Law Advisor at DIRCO. Cabinet will then deliberate on the matter and a decision will be made. Once approved, The Minister of Finance will sign the Presidential Minute and Parliament will Gazette.

The Country Partnership Frameworks or Strategies that Government has with these institutions will then determine how reporting is done and performance is measured. Internally, key matters are periodically placed on the National treasury's Exco's Policy Group Meeting Agenda. Memorandums are drafted for the DG and Ministerial consideration and approval. Where applicable, the Cluster Inter-governmental Co-ordination platform is utilised for inter-departmental consultation from official/technical level, DGs level and Cabinet level. Programme performance monitoring takes place through the standard quarterly reporting through the APPs and periodic reports through the MTSF reporting process.

The cost of financing or joining the institution is determined during the due diligence on the rationale to join. By the time it goes to the principal (President; Cabinet; Minister of Finance), an assessment of whether the subscriptions or capital contributions (i.e., paid in capital and callable capital) will be affordable and where the resources will come from should also be done. The paid-in capital is done in consultation with the CFO's office, the cost of callable capital is presented to Fiscal Liability Committee (process is led by ALM) for consideration.

The above process steps are summarised in the process map and log frames shown **in figures 3**; **4** and **5** below.

Figure 3: Generic Process Map

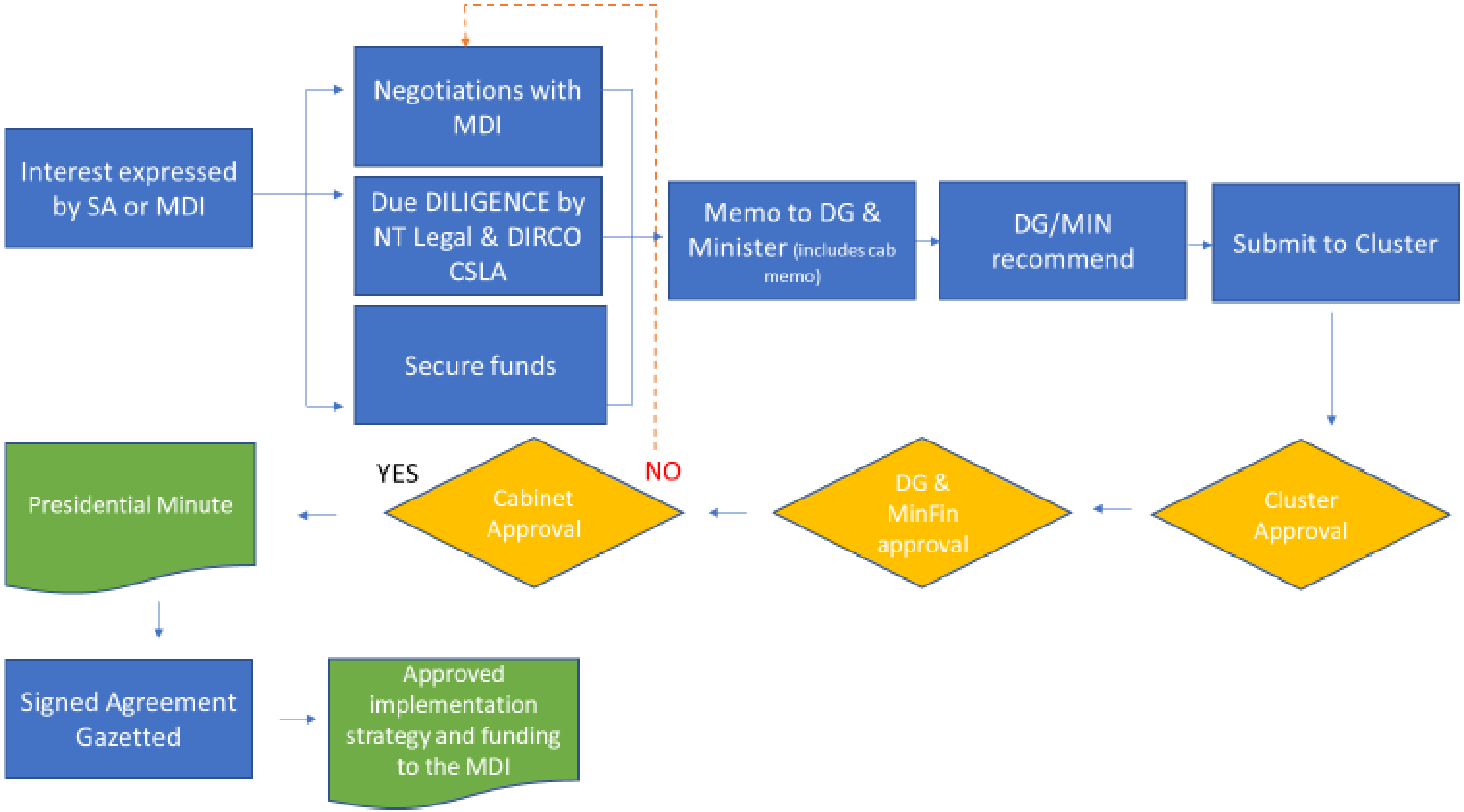


Figure 4: Combined Log Frame MDBs

IMPACT	A better Africa and World "South Africa will continue to engage internationally on aid effectiveness, increased global development assistance, and strengthening development partnerships"			
OUTCOME	Increase access to development finance		Support received from MDBs for developmental projects in line with NDP chapter 7	Increased investment in development projects including infrastructure
Performance Indicators	Participation or Subscription are paid		Alignment of Country Partnership Framework (CPF) priorities (identified projects and programmes) to government strategic objectives	Effective implementation of projects
Outputs	Membership and funding for capital subscriptions attained	Decision to participate in the recapitalisation approved	Develop a Country Partnership Strategy (CPS)	Implement the Country Partnership Strategy (CPS)
Performance Indicators	Within 2 years subject to Cabinet/political processes	South Africa's recapatalisation process concluded within the provided timeframe	Country Partnership Strategy (CPS) developed	Country Partnership Strategy (CPS) implemented
Responsibility	IREP	IREP	IREP	IREP
Related activities per output				
Activity 1	Draft a letter expressing interest by Minister of Finance informed by political/cabinet decisions to join	Mid-way through period of subscription, negotiations for recapitalisation will start by the institution (size of package) OR a based external trigger	Coordinate government's participation in the MDB Systematic Country Diagnostics (SCD) to identify key challenges and opportunity for the country	Facilitate implementation of the CPS through the processing of grants and technical assistance received from the institutions
Activity 2	Undertake negotiations and technical discussions with MDB and ALM on general conditions of membership	Negotiate with CFO, ALM, Public Finance and BO to secure funds	Coordinate consultations for the development of the Country Partnership Framework (CPF) with the MDB, informed by the SCD	Coordinate the supervision missions
Activity 3	Negotiate with CFO, ALM, Public Finance and BO to secure funds	Board of Governors negotiate based on the case for recapitalisation and scenarios	Organise the Consultation Workshop to develop the CPF	Participate in supervision missions and sign acknowledgement of outcome reports
Activity 4	Undertake due diligence of legal agreements and implications for the purposes of ratification by NT Legal, DIRCO OCSLA and DoJ&CD	Agreement of a specific scenario	Receive and comment on the Draft CPF	Request implementation status from the MDB and the implementing agencies
Activity 5	Draft memo to DG & FINMIN (includes draft cab memo)	Letter from Institution to Governors to vote on resolutions (adopt size of recap)	Send comments on the Draft CPF to the MDB	Liaise with different stakeholders to address delays or challenges in the implementation of projects
Activity 6	Receive approval from DG & FINMIN	Draft memo to DG & FINMIN (includes draft cab memo)	Submit Draft CPF for endorsement by DG and Minister	Coordinate the midterm review to assess the implementation of CPF
Activity 7	Submit to Cluster for recommendation to submit to Cabinet	Receive approval from DG & FINMIN	Present draft CPF to relevant stakeholders for endorsement	Finalise and sign outcome report for the midterm review
Activity 8	Submit to Cabinet for ratification and prepare a presentation for Minister	Ratification process start: OCSLA & DoJ&CD for legal opinions		
Activity 9	Receive Presidential Minute authorising Minister of Finance to sign on behalf of SA government	Submit to Cluster for recommendation to submit to Cabinet		
Activity 10	Parliament gazettes the signed Agreement	Submit to Cabinet for ratification and prepare a presentation for Minister		
Activity 11		Legal opinions and instrument of subscription sent back to Institutions		
Activity 12		Receive Presidential Minute authorising Minister of Finance to sign on behalf of SA government		
Activity 13		Receipt of payment schedule from the Institution		
Activity 14		Payment of the subscription according to schedule		
Key programme inputs				
Input 1	Human Capital: Internal (ALM, EP and Legal Services); External (OCSLA, DoJ, DIRCO, MDBs)	Human Capital: Internal (ALM, EP and Legal Services); External (OCSLA, DoJ, DIRCO, MDBs)	Human Capital: internal (ALM, BO, PF, OCPO, OAG and EP); external (government departments, SOEs, DFIs and MDBs) consultations	Human Capital: internal (ALM, BO, PF, OCPO, OAG and EP); external (government departments, SOEs, DFIs and MDBs)
Input 2	Financial resources (ALM, BO, PF and CFO)	Financial resources (ALM, BO, PF and CFO)	Secure venue for the Workshop	Financial resources from the Multilateral Development Bank: Budget support related funding and grant funding for technical support

CMA Programme Chain of Delivery

Key role players in determining and managing South Africa's participation in CMA are summarised as follows:

- The Minister of Finance is responsible for the ratification of the Multilateral Monetary Agreement (MMA).
- The National Treasury and the South African Reserve Bank (SARB) lead the implementation responsibilities including the coordinating and dissemination of relevant information between the Ministries of Finance and Central Banks within the CMA. The South African Reserve Bank (SARB) also coordinates the quarterly meetings of CMA Central Banks.
- South African Reserve Bank (SARB) is the lead institution in decision-making between South Africa and ELN countries in respect of any national currency issues other than the rand.
- The national arrangement in South Africa is for the National Treasury to make compensatory payments. These annual payments are paid directly from the National Treasury budget on the last day of February for each succeeding year. The determination/calculation of the payments is done by the SARB with inputs from National Treasury (in terms of estimates of the government's 10-year bond yields).

Figure 5: Logframe for the CMA

IMPACT	A better Africa and World "South Africa will continue to engage internationally on aid effectiveness, increased global development assistance, and strengthening development partnerships"	
OUTCOME	Increased trade and investment between CMA member states	
Performance Indicators	Free movement of capital within the CMA	
Outputs	Compesatory payments made to ELN	Policy coordination within the CMA
Performance Indicators	Annual exports and outward investment levels vs total CMA payments to ELN; reduced transaction costs for capital movement	CMA Finance Ministers Central Bank Governors communique of commitments
Responsibility	**IREP**	**IREP**
Related activities per output		
Activity 1	Facilitate increased outward investments and exports of RSA goods and services by making payments to ELN countries for use of rand	Coordinating and prepare Minister for the joint CMA FMCBG meeting
Activity 2	Request annual yield estimates on Government long term bonds from Economic Policy	Monitoring implementation of commitments
Activity 3	Share yield estimates with the SARB for the determination of CMA Payments	Provision of secretarial services (24 months)
Activity 4	Receive payment request from the SARB with actual payment calculations for the current FY and estimates for the upcoming three FY	
Activity 5	Liase with Finance to determine availability of funds	
Activity 6	Draft a payment submission request to Finance to make the payments	
Activity 7	Receive proof of payments and share with ELN	
Key programme inputs		
Input 1	Human Capital: internal (CFO and EP); external (SARB)	Human Capital: internal (CFO and EP); external (SARB)
Input 2	Financial resources to make payments	Financial resources to make payments

4. Expenditure Analysis

With reference to Appendix D: CMA payments (Eswatini; Lesotho and Namibia) and trade benefits as well as Appendix C: MDBs contributions; benefits and projects per MDB (i.e. AfDB; IBRD; IFC; MIGA and NDB) attached to the document, the data captured in the Appendices has been interpreted in the sections hereafter.

World Bank Group Financial Contributions and Benefits 2010-2020

The overall financial contributions from 2010-2020 to the World Bank Group (including IBRD, IFC and IDA) amount to **R1.08 billion** in that period. The overall financial benefits amount to **US$8.48 billion** (equivalent of R120 billion at the current exchange rate**)**. This is made up of funding mobilized in loans, equity, guarantees, and grants. Key sectors that were supported included energy, agriculture, manufacturing, mining, finance, pharmaceutical, property and infrastructure.

African Development Bank Financial Contributions and Benefits 2010-2020

South Africa's financial contribution to the African Development Bank over the 2010-2020 period amounted to R3.3 billion (including US$192 million for shares and R469 million for concessional lending windows). In the same period, data was further collected regarding the financial benefits derived from the African Development Bank in terms of overall funding mobilized in the form of loans, equity, and grants. The overall financial benefits amount to US$11.58 billion (equivalent of R165 billion in current exchange rate). Key sectors that were supported included energy, finance, and transport.

New Development Bank (NDB) Financial Contributions and Benefits 2010-2020

South Africa has been a member of The New Development Bank since its operationalized in 2016. South Africa has contributed R24.75 billion (USD/Rand – 15.00) to the establishment of the Bank from 2016 – April 2021 period. In the same period, the NDB approved R81.33 billion (USD/Rand – 15.00) of project loans to the country. The 11 approved projects supported the clean energy, ports, water, transport, and health sectors.

Table 5 below provides a status of South Africa's loan portfolio at the NDB. Approved loans are in the transport, energy, water sectors and more recently COVID-19 loans to provide health and social safety nets as well as to support economic recovery and contain the economic fallout of the pandemic.

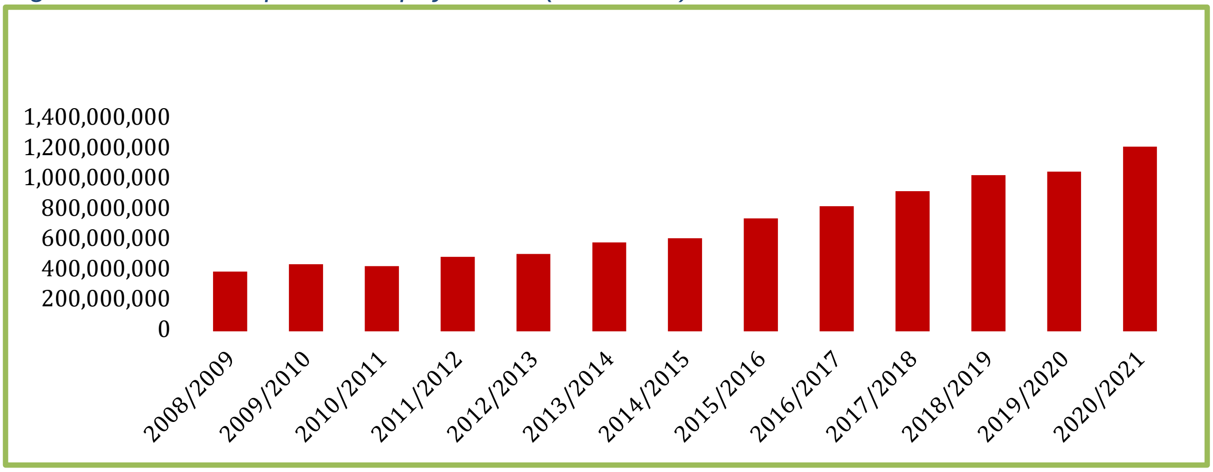
Table 2: Approved South African Projects by the NDB

Entity	Sector	Project
Eskom SOC Limited	Energy	Transmission Lines Infrastructure Program
Transnet SOC Limited	Transportation	Durban Container Terminal Port
Development Bank of Southern Africa (DBSA)	Energy	Renewable IPP Programme
TCTA SOC Limited	Water	Lesotho Highland Water Project, Phase 2
Eskom SOC Limited	Energy	Medupi power station FGD retrofit Project
Industrial Development Corporation (IDC)	Energy	Renewable IPP Programme
SANRAL SOC Limited	Transportation	Toll Road Portfolio
Eskom SOC Limited	Energy	Battery Storage (Phase 1 and Phase 2)
National Treasury	Health	Emergency Program COVID-19 (Health)
SANRAL SOC Limited	Transportation	Non-toll Road Portfolio
National Treasury	Fiscal stimulus	COVID-19 Economic Recovery Loan

CMA Compensatory Payments 2009 - 2021

South Africa makes compensatory payments to ELN countries in terms of the MMA and over the years, the total payments have grown noticeably. For example, between 2008/09 and 2020/21 payments increased at an average annual rate of 10.6 per cent. This increase has been influenced by the growth in South African Rands circulating in ELN.

Figure 6: CMA Compensation payments, (R millions)



Source: SARB CMA payment letters

Article 8 [Compensatory Payments] of the MMA makes provision for the calculation of compensatory payments to ELN countries as follows:

Compensation = 2/3 * (X*Y(R)) ……………………………… (1)

Two thirds (2/3) of X percent of Y (R),

where X represents the annual yield to redemption of domestic long-term South African government bonds in issue with outstanding maturity of 10 years and longer for the months of October, November and December (quarter 4 of the year) preceding the annual payment; and

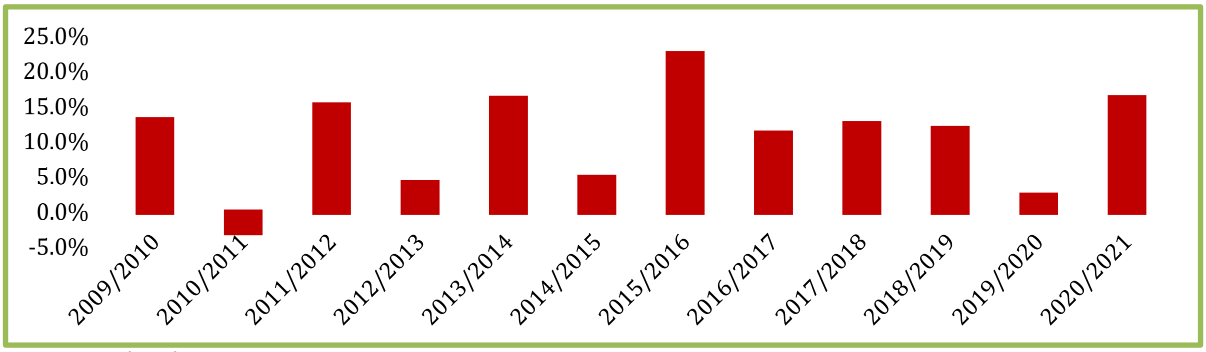
Y (R) represents the relevant agreed amount of South African rand calculated to have been in circulation in the respective member.

The CMA formula consists of two main elements which directly impacts total compensatory payments made by South Africa to ELN countries. The two elements include: (a) Money supply stock (total notes and coins in circulation outside South Africa. The total South African rand in Eswatini, Lesotho and Namibia are determined by scaling up total money stock in circulation by a factor of 1.2 and then deducting total local currency from the total money stock to estimate total South African rand in circulation and (b) Yield to redemption of domestic South African government bonds in issue with outstanding maturity of 10 years and longer for the months of October, November, and December. Eswatini, Lesotho and Namibia are compensated two-thirds of the average yield of the fourth quarter for the loss in monetary policy space due to the use of the South African rand.

The upward trend in CMA payments has mainly been due to the fact that the total amount of South African rand in ELN grows faster than the rate of growth in rand circulating in South Africa. In the period under consideration, the total amount of South African Rands circulating in ELN grew by an average nominal rate of 9.3 per cent. This consistent growth has resulted in the rand being the dominant currency ELN, which implies that the South African monetary policy regime has become more entrenched overtime.

As a result, CMA payment grew in line with this increased influence by the South African Reserve Bank (SARB). Between 2008/10 and 2020/21, CMA payments grew by an average nominal annual rate of 10,6 percent. This above-inflation growth makes it difficult for the National Treasury to effectively plan for these payments, especially because the budget baseline increases are aligned to inflation. This challenge is further exacerbated by the unpredictable fluctuations in annual growth rates **(see figure 7).**

Figure 7: CMA payments (Year on Year growth)



Source: National Treasury

While the total stock of rand in ELN grew robustly over this period, the average annual growth rate in government bond yield for quarter four of the year changed modestly at 1.7% over the same period. The contribution of bond yield to the total payments remains insignificant given that only two-thirds is paid to ELN. In this case, South Africa has paid only two thirds of the 1.7% average annual growth rate to ELN over the period 2009/10 and 2020/21.

5. Benefit and Value Analysis

This section discusses the **non-tangible value and benefits** derived from the MDBs compared to expenditure presented in the expenditure analysis section.

Benefits derived from Multilateral Development Banks

South Africa derives a number of benefits from its MDB membership. These include, but are not limited to:

i. Favourable lending terms
ii. Access to technical assistance
iii. Voting power and a voice to advance African issues
iv. A day in the MDB strategic direction and governance

The following paragraphs provide a description of these benefits.

The **lending terms** from to these institutions are more favourable compared to market rates (longer maturity and lower interest rates). This is another avenue which State Owned Entities are using to address liquidity challenges in the context of government fiscal consolidation and commitment to a reduction of government debt. Since 2020, the National Treasury has begun borrowing from the MDBs in order to address to economic challenges presented by the Covid-19 pandemic, as well as to invest in infrastructure for economic growth and job creation. The MDBs should form part of the government funding strategy in the medium-term.

Table 3: MDBs Loans Vs the Market Rates

USD million (2020)	**NDB Loan**	**AfDB Loan**	**NDB Loan**	**Average**
Amount	1000	288	1000	
Tenor*	30	20	30	**26.6**
Rate	2,08%	4,45%	1,43%	**2.6%**
Market Rates (indicative)				
Min	6,50%	6,00%	6,50%	**6,33%**
Max	6,63%	6,13%	6,63%	**6,46%**
Difference				
Min	4,42%	1,55%	5,07%	**3,60%**
Max	4,55%	1,68%	5,20%	**3,81%**

Source: ALM Unpublished Notes

- It has to be noted that MDBs loans come with 5-7-year grace period.
- NB: these rates were for Covid-19 loans received in 2020
- The average lending rate of an MDB is 2.6%, while the market rate is at 6.3%.
- The Difference between the MDB rate vs the market rate is at 3.6%.
- Although the MDBs loans are cheaper, the Cons for the MDB loans is that they usually take longer to negotiate and disburse the funds and the reporting requirements can be laborious.

MDBs have provided **technical assistance** to assist the Government of South Africa to implement key government policy areas. Over the last year the following projects have been approved:

- Agri-Parks Programme with Department of Agriculture
- Air Quality Management in Johannesburg with Environment Department
- Public Expenditure Review with Department of Basic Education
- Bio-diversity Economy Project with Environment Department

South Africa's participation in MDBs gives the country the shareholding, **voting power and voice to bring African issues** to the forefront in the IBRD as well as IDA, resulting in linkages between continental and global agendas. South Africa's participation in these institutions has the potential to support Africa's Development in the following ways:

- South Africa is strategically placed to influence the strategic direction of IDA and can exert influence to ensure that African developmental priorities are prioritized on the IDA Agenda.
- Being one of the few African countries that consistently contributes to IDA provides South Africa with the opportunity to influence discussions and highlight Africa's key developmental needs.
- The Covid-19 pandemic has placed many African countries on a trajectory of depleting public finances, therefore avenues such as IDA become very critical in assisting countries achieve their developmental goals and provide significant infrastructure project and budgetary support. If any African country were to collapse, particularly countries in SADC and SACU, this would have devastating effects for South Africa as the expectation would be that South Africa needs to play a leadership role to assist, putting further pressure on its diminishing finances.

South Africa's subscriptions in the World Bank and shareholding in the AfDB allow South Africa a say in the institutions' **Strategic Direction and Governance**.

- At the World Bank, South Africa shares a constituency with Nigeria and Angola and rotates the position of Executive Director and Alternate Executive Director every two years according to a pre-determined scheduled. South Africa and Nigeria have the largest shareholding in the constituency compared to Angola. As a result, there are positions in the Constituency that are only shared by the two countries. For the constituency to exist and be able to vote in the Board, it needs a voting power of above 2 percent of the total subscriptions of the elected Executive Directors. South Africa's failure to fully subscribe to the shares poses a potential risk to the Constituency to lose the seat at the Board of Directors. Furthermore, there is a reputational risk for South Africa in the Constituency, as Nigeria and Angola are increasing their shareholding and are up to date with their capital subscriptions for the 2018 World Bank recapitalisation. South Africa hosts the regional office for the Bank which serves six countries in the region. The IFC regional office is also hosted in Johannesburg.
- South Africa's shareholding at the African Development gives the country access to a permanent seat on the Board of Directors. South Africa shares a constituency office with Eswatini and Lesotho and can appoint and alternate the positions of Alternate Executive Director, Senior advisor and advisor within the Constituency. South Africa hosts one of the largest regional resource centres of the Bank and services 12

countries. The office also serves as the back-up office should anything happen in the Bank Headquarters in Abidjan, Cote d'Ivoire.

Benefits derived from the Common Monetary Area

The main value addition for South Africa from the CMA relates to the fact that the SARB effectively formulates monetary policy for the CMA, although ELN have their own central banks. The member states consequently also indirectly adhere to an inflation targeting monetary policy framework owing to South Africa's adoption of inflation targeting in 2000. There are no restrictions on capital transfers between member states, whether for current or capital purposes. It means that there is no restriction of cross-border investments from South Africa, and this contributes to economic development and economic integration. The four CMA member states also belong to the Southern African Customs Union wherein capital and goods are highly mobile. The use of a single currency thus further facilitates trade integration. Lesotho, Namibia and Eswatini depend heavily on trade from South Africa, a major benefit from the CMA arrangements is the fixed and predictable exchange rate with the rand.

The resultant benefits from the above include but are not limited to:

i. High intra-CMA trade and investment linkages
ii. Higher trade integration between CMA members compared to other SADC countries.

The following paragraphs expand on each of these benefits.

Intra-CMA trade and investment linkages

The existence of a currency union such as the CMA improves intra-CMA trade. South Africa on average, accounts for 85 per cent of the ELN countries' imports, which are free from tariffs and virtually all other trade barriers, as well as low transaction costs due to the use of a single currency. The CMA has provided the benefits of lower and falling interest rates to its member countries (Including South Africa). This is an important benefit, owing importantly to the monetary policy of the SARB. Financial stabilisation in South Africa has successfully brought down inflation expectations, contributing to lower interest rates throughout the region. South African financial institutions play a dominant role in Lesotho, Namibia, and Eswatini, creating a virtually unified banking system within the CMA. There has been evident macroeconomic convergence within the CMA region, this convergence may be attributable to similar macroeconomic policies being pursued by member states.

The benefits of the CMA for South Africa and the region dwarf the perceived costs when assessed through trade and investment linkages. As has been shown by ***Table 1*** below; total trade within the CMA remained robust. South Africa maintained its trade surplus throughout the period 2013/14 to 2019/20. However, the trade surplus declined from R70 billion in 2013/14 to R45 billion reflecting the slowdown in economic activity in the South African economy since 2008. Despite the weakness in economic activity, the application of the rand within the CMA significantly reduced transaction costs and continued to support trade within the region.

Table 4: South Africa's trade with ELN countries 2013/14 – 2019/20 (R millions)

	Total exports	Total Imports	Trade Balance
2013/ 2014	90 265	19 930	70 335
2014/ 2015	76 966	22 338	54 628
2015/ 2016	78 260	23 991	54 269
2016 /2017	79 064	26 180	52 884
2017/ 2018	76 722	32 031	44 691
2018/ 2019	77 170	33 082	44 088
2019/ 2020	80 841	35 586	45 255

Source: SARS

On the investment side, ***Table 2*** shows that South African firms expanded their footprint into the region diversifying their exposure to South Africa and taking advantage of better economic performance outside South Africa. Total investment[3] by South African firms in the ELN countries more than doubled between 2012 and 2019, increasing from R25 billion to R55 billion.

Table 5: RSA total investment in ELN countries

R millions	Eswatini	Lesotho	Namibia
2012	4 904	2 624	17 721
2013	5 111	2 781	19 790
2014	5 555	3 230	19 500
2015	8 435	4 617	27 476
2016	7 282	5 488	23 678
2017	8 147	6 152	27 776
2018	8 171	6 400	31 148
2019	9 089	8 157	38 238

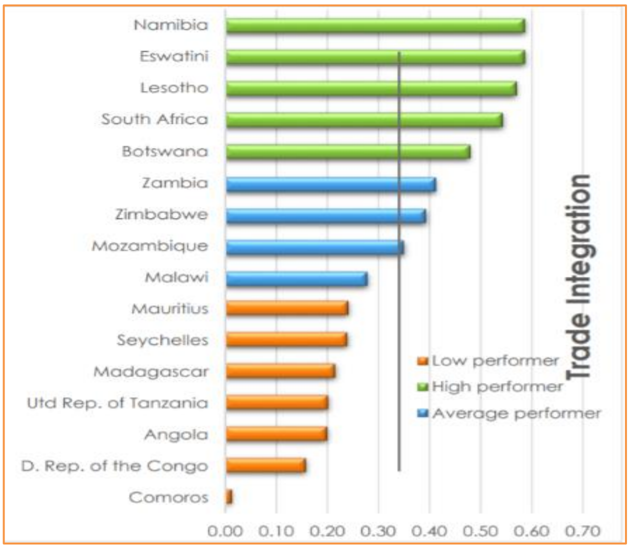
Source: SARB Quarterly Bulletin

Comparison of Trade Integration between the CMA and other SADC countries

The level of trade integration with Southern African Development Community (SADC) countries is generally low according to the African Development Bank (2019). However, there is noticeable variation amongst countries due to overlapping membership. Some countries belong to a customs union in SACU, and some in a currency union in CMA. **Figure 8** below ranks SADC member states according to their levels of trade intensity/activity within the region and finds that trade integration is higher for countries that belong to SACU. Additionally, it is notable from Figure 7 below that countries that perform the best within the SACU group also belong to the CMA i.e. Namibia, Eswatini, Lesotho and South Africa.

[3] Includes total direct and portfolio investments

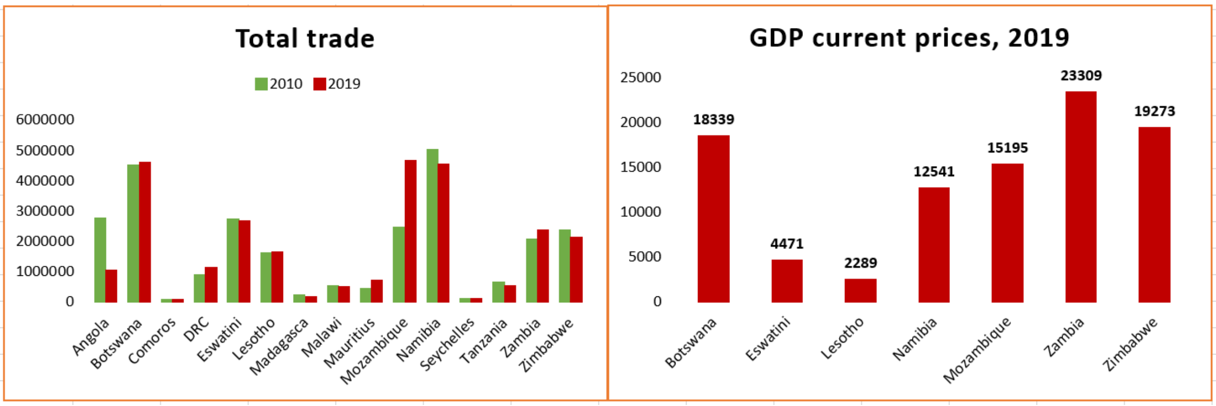
Figure 8: Trade Integration in SADC



Source: African Development Bank, 2019

Figure 9 below depicts countries that traded the most with South Africa for the years 2010 and 2019. The data confirms that CMA countries (ELN) are amongst the top trading partners for South Africa. Although CMA economies, especially Eswatini and Lesotho, have modest economic sizes relative to Mozambique, Zambia, Botswana and Zimbabwe, their trade intensity/activity with South Africa is higher. It does not reflect their economic size but perhaps this could be attributed to the ease of doing business, especially trade facilitated by their position in SACU and the CMA. These findings indicate that economic size is only significant when the trading environment is homogenous. For instance, if all member states belong to a free trade area or the customs union. The findings also indicate that a customs union has better economic returns than FTA.

Figure 9: Total Trade & Trade Activity



Source: ITC, 2021

6. Options to reduce MDB and CMA Payment Obligations

Options to reduce payment obligations at the World Bank Group and AfDB

The biggest challenge faced by National Treasury (IREP) is that the cost implications for the allocated shares for the World Bank and the African Development Bank recapitalisation are above the allocated budget. The reason is that shares are allocated based on the size of shareholding of the country in these institutions. At the AfDB, South Africa is the third largest shareholder regionally at 5%, hence more shares are allocated. At the World Bank at the South Africa's shareholding is 0.73% and accordingly shared allocated are quite small.

There are currently no risk-free options that can yield savings for South Africa at the World Bank Group and the AfDB. However, South Africa could consider the options below for the country's participation in the future recapitalisation of these institutions and these could come at a big risk or power implications for the country and region's position at these institutions.

Option 1: Only subscribe to shares based on available budget baselines

One option going forward could be for South Africa to only subscribe based on the allocated budget. This would mean that South Africa will only subscribe to a portion of allocated shares from these institutions. According to the Articles of Agreement establishing these institutions, it is not mandatory for member countries to subscribe to the allocated shares. The Articles states that "*in the event of an increase of the capital stock, no member, however, shall be obligated to subscribe to any part of such increased stock.*"

The risk associated with this option is that relinquished or unallocated shares for South Africa will be reallocated to other countries that are interested to increase their shareholding at the institution. In the **African Development Bank,** shareholding directly links to a country's political influence within the region and Continent. In the Bank, Nigeria (West Africa region) is the largest shareholder, followed by Egypt (north-eastern region of Africa) and then South Africa (sub-Sahara Africa - SSA). South Africa's shareholding within the Bank further gives it a strong position of influence in the Africa Union (AU) as the largest shareholder in the SSA region. This enables South Africa to strategically influence the policy direction of the Bank as well as the AU. Relinquishing or not taking up available shares will thus have a negative political implication for the country in the region and on the continent.

Further, there is currently a Cabinet mandate to increase South Africa's shareholding to 6% at the African Development Bank, which means that the country should take up shares whenever they become available. South Africa's current shareholding is at 5%, but due to the current fiscal situation, no additional shares can be taken up. The financial implications of an increase in shares is not known beforehand, as the costs linked to that is only declared at the moment in time when the shares are announced.

Option 2: Requesting Extended Payment Periods

This option only applies to the World Bank. The rules at the World Bank allow countries to extend the payment period by two-years, moving the current schedule from a 5-year payment schedule to 7-year period. With this option, we will continue to pay using the allocated budget. A formal application by the country is needed for that extension to be granted. For example, IREP intends to formally apply for extension during the current recapitalization of 2019-2023 at the World Bank in 2022 to move the payment period to 2025.

This option is not applicable to the African Development Bank. South Africa is the middle-income country at the AfDB and is allocated an 8-year payment schedule. During the negotiations for recapitalisation, National Treasury requested to extend the payment of SA's subscription over a 12-year period instead of 8 years. This was rejected by the AfDB due to the fact that SA is a middle-income country and a payment period over 12 years is only allowed for low-income countries.

Option 3: Being more selective about which institution to recapitalise

Due to the current fiscal and economic challenges facing the country, South Africa will have to prioritise which institutions it wants to participate in their recapitalisation in the future. South Africa might have to consider reducing some subscriptions by not participating in the recapitalisation of certain institutions without significantly reducing the country's subscription.

For example, in 2020 South Africa did not participate in the recapitalisation of the International Finance and Corporation (IFC), an organ of the World Bank due to fiscal constraints.
The allocated shares were valued at US$60.2 million (R993 million) payable over a 5-year period. The National Treasury officially notified the IFC management that the country will not subscribe to its allocated shares and IFC has noted the decision. Due to this decision, the country's shareholding at the IFC will decrease to 0.53% from 0.68%. Unsubscribed shares will be returned to the pool of unallocated shares after the end of 2023.

The **portfolio** envelope at the institution is not linked with the size of shareholding nor affected by the decision of not subscribing to allocated shares. South Africa has the biggest IFC portfolio on the African continent and will continue to access funding from the IFC. The IFC noted SA situation and kept the door open for possible future recapitalisation.

Expected results

While the reprioritisation of SA's participation in the **World Bank** and **AfDB** recapitalisation could save money for the country, this will have serious implications and poses risks to the country. Firstly, South Africa's influence in these institutions could diminish with serious implications on the power dynamics and geopolitics in the continent and globally. Secondly, this could, over time, lead to the erosion of the country's shareholding in these institutions. In the World Bank, It should be noted that there is a very real reputational risk for South Africa in the Constituency, as Nigeria and Angola are increasing their shareholding and are up to date with their capital subscriptions for the 2018 World Bank recapitalisation.

Options available to yield savings in the NDB

There are currently no risk-free options available to yield savings. South Africa is due to make its 7th and final capital contribution to the NDB in 2021/22. Provision for this has been made in the budget. The Bank remains adequately capitalised with a capital utilisation ratio (CUR) of 12.00% (as 28 June 2021). Considering the recent trend and the projected increase in approvals and disbursements, the CUR values are still at comfortable levels. The ratio could improve although marginally following final capital subscriptions by member countries. It is therefore highly unlikely that the Board of Governors will call on additional capital from founding members in the near-term.

Option 4: Making use of the bank's Project Preparation Funds to increase the number of bankable projects in its pipeline

There is still scope for South Africa to maximise and leverage its membership at the New Development Bank. There is no limit to what each member country can access from the NDB. The total portfolio extended by the New Development Bank to South Africa is valued at R81 billion. South Africa can raise more funding from the NDB through increasing the number of bankable projects in its pipeline. That is, improving the risk profile of project concepts early in the project development stage leading to better risk allocation amongst parties. This will have the consequence of improving the attractiveness of the project to funders and investors. A project is deemed bankable when all risk factors are considered, and the project readiness has been determined based on its ability to generate sufficient and sustainable returns to justify the risk. One of the means that can assist member countries to develop bankable, investment-ready projects are Project Preparation Funds (PPFs). PPFs provide technical support, such as project feasibility studies, including value-for-money analysis, developing procurement documents and project concessional agreements, as well as undertaking social and environmental studies. The NDB established a PPF which South Africa can benefit from once a contribution has been made. Worth noting is that there is no limit to how much a member country can benefit from the PPF, regardless of the contribution made.

Options to reduce payment obligations to the CMA

The growth in CMA payments is explained by the trajectory in both the average yield on government's 10 years and older bonds and the total rand circulating in ELN. As indicated earlier in this document, the growth in rand circulating in ELN countries significantly explains the growth in CMA payments because total money stock is scaled-up by a factor of 1.2 to ensure that there is no disincentive in the continuation and durability of the CMA. This assumption was also founded on the basis that due to their underdevelopment, ELN will likely grow faster than South Africa as the region gradually integrates and income levels converge.

Against these considerations, there is no risk-free option for savings.

Option 5: Amending the CMA payment formula

Amending the CMA payment formula is both a policy and political decision that requires balancing the costs and benefit of this arrangement for South Africa but also for the region. It involves not only South Africa, but the entire balance of CMA countries. Also, it is important that the potential savings out of a R1 billion cost to South Africa is balanced against the trade and investment benefits outlined above; but also, the wider cost implications especially in terms of damaging foreign relations that may spill over to other regional bodies such as the Southern African Customs Union (SACU) and the Southern African Development Community (SADC).

For South Africa, the CMA payments are policy instruments that must be used to ensure that the CMA can be a foundation for long-term development towards a monetary union in Southern Africa. Thus, ***Table 3*** below presents the standard of living in the region, measuring through gross domestic product per capita, and finds that the standard of living improved markedly between the years 2000 and 2019 in the region.

However, the convergence envisioned in the CMA payments has not materialised as expected. For instance, differences in standards of living narrowed marginally between South Africa, Namibia and Eswatini but worsened between South Africa and Lesotho. The fact that standards of living have not converged as significantly as would have been expected over the past 19 years will make South Africa's case to review the CMA payment formula difficult to negotiate successfully.

Table 6: Standard of living in the CMA (GDP per Capita USD)

	2000	2019
Eswatini	1819	4 010
Lesotho	453	1117
Namibia	2140	5100
RSA	3039	5977

Source: IMF

It must be noted that while CMA payments have increased above inflation since 2008, when contextualised, the payments are only significant when assessed against a divisional budget in the National Treasury. According to the 2021 Estimates of National Expenditure, National Treasury's total expenditure budget in 2019/20 amounted to R29.7 billion while programme 6's budget under which the CMA falls resides spent R5.4 billion. When assessed against these outcomes, CMA payments accounted for 3 per cent of National Treasury's 2019/20 budget and 18 per cent of the budget of Programme 6.

Option 6: Making CMA Payments direct from the National Revenue Fund as opposed from National Treasury's budget

CMA payments are paid annually on the last business day of February of each succeeding year in line with Article 8 of the revised Multilateral Monetary Agreement (MMA). National Treasury uses estimations for the expected yield on government long term bonds (sourced from Economic Policy Division); and estimations for expected total amounts of South Africa Rands in Eswatini, Lesotho and Namibia for the next years (sourced from SARB). The estimations are generated twice a year: in January and June each year to project the baseline expenditure for the National Treasury.

The main challenge is that the projections are unreliable because they are affected by unpredictable changes in government bond yields and total amount of South African rand circulating in ELN. National Treasury incurs perpetual shortfalls as the uncertainties make it difficult to plan for the CMA payments. There is currently no process in the budget to manage such significant deviations (surpluses and deficits). Therefore, it is against this background that a recommendation is being made for this expenditure line to be charged directly against the National Revenue Fund instead of the National Treasury budget.

Expected results

The revised MMA has been signed by all **CMA** Finance Ministers in August 2021, which implies that if South Africa wishes to review the payment formula it would need to submit a formal notice to CMA members. In the meantime, National Treasury remains obligated to make annual payments in line with Article 8 of the MMA. If National Treasury's request for the

CMA payments to be charged directly from the National Revenue Fund is successful, the perpetual shortfalls the department incurs due to the unpredictable changes in total South African Rands circulating in ELN would be addressed.

7. Recommendations

Based on an assessment of the options and the associated risks and expected results, the following recommendations are made.

1) To increase the role of MDB's in South Africa's current funding strategy for the fiscus
   - During 2020, the National Treasury increased its borrowing from MDB/I as a result of the Covid-19 pandemic. This is the first time South Africa has borrowed as a sovereign and thus a number of lessons were learnt during the experience. Going forward, the proposed **Funding Strategy** should include MDBs as a source of finance in its funding mix, to ensure that South Africa takes full advantage of the opportunities that its capital contributions and membership offers, as well as to fund Government's deficit in the most economically favourable way possible.

   - The **lending terms** from these institutions are **more favourable** compared to market rates e.g., longer grace period and maturities; below-market interest rates and embedded technical assistance. This may be a possible avenue that would result in the reduction of **the level of debt service cost** of government. National State-Owned Entities have been using this option to address liquidity challenges given persisting fiscal challenges in the country.

2) To maintain or increase shareholding
   - South Africa should **maintain or increase its shareholding** (**recapitalisation**) in the MDBs, since the shareholding links directly to the **voting power and voice** of the country in order to bring **African issues** to the forefront in MDBs.

3) To place funding to the CMA on direct charge from the NRF
   - South Africa **should not pursue the amendment of the CMA payment formula** and the CMA payments should be viewed as policy instruments that must be used to ensure that the CMA can be a foundation for long-term development towards a monetary union in Southern Africa. Thus, any potential savings should be weighed against possible impact on trade and investment. Other considerations are the immediate political fallout and likely spill-over to bodies such as the African Union (AU), Southern African Customs Union (SACU) and the Southern African Development Community (SADC). Given that the standards of living in the region have not converged over the past 19 years, South Africa's case to review the CMA payment formula will be difficult to negotiate successfully.

8. Actions

Increased role of MDB's in South Africa's current funding strategy for the fiscus

- With the advent of the Covid-19 pandemic, borrowing from MDBs has subsequently been integrated into the funding strategy of the Treasury.
- Currently, negotiations are underway to source Vaccine funding as well as funding for Budget Support from the World Bank, as part of the implementation of the borrowing strategy.

Maintain or increase shareholding

- Continue to engage with Public Finance, Assets and Liabilities and the CFO, prior to seeking Cluster and Cabinet approval via a submission.
- Alert Public Finance as soon as a recapitalisation process is triggered by an MDB, to ensure alignment with internal planning and budget process.

Place the funding to the CMA on direct charge to the NRF

- Coordinate with PF to make inputs into the ongoing process to amend the PFMA for the CMA expenditure to be charged as a direct charge against the National Revenue Fund.
- Engage the Legislation unit regarding this proposal and await the process to amend the PFMA to conclude and see if the proposal has been considered favourably.

IREP and PF have made submissions to the Legislation Unit regarding the proposal made above. At this point, IREP and PF are awaiting the conclusion of the PFMA review to find out if the submission made is successful

9. Appendices

The CMA log frame **and** CMA payments (Eswatini; Lesotho and Namibia) and trade benefits attached as attached as **Appendix A**.

MDBs combined log frame attached as **Appendix B**.

MDB contributions; benefits and projects per MDB (i.e. AfDB; IBRD; IFC; MIGA and NDB) attached as attached as **Appendix C**.

Presentation attached as **Appendix D**.