SOUTH AFRICA YEARBOOK 2012/13

Finance

South Africa has demonstrated resilience in the face of the global financial and economic crisis that started in 2008. The economy is growing, though more slowly than originally projected. More jobs are being created, household spending is robust and private-sector investment is gathering pace.

This underscores the fundamental importance of supportive, efficient and sustainable public financial management to the promotion of economic development, good governance, social progress and a rising standard of living for all South Africans.

The Ministry of Finance is at the heart of South Africa 's economic and fiscal policy development. The Minister of Finance and Deputy Minister of Finance are responsible for a range of state entities that aim to advance economic growth and development, and to strengthen South Africa's democracy.

National Treasury is responsible for managing South Africa's national government finances.

The Constitution mandates National Treasury to ensure transparency, accountability and sound financial controls in the management of public finances.

National Treasury is furthermore mandated to promote government's fiscal policy framework; to coordinate macro-economic policy and intergovernmental financial relations; to manage the budget preparation process and preparing a sound and sustainable national budget; to facilitate the Division of Revenue Act, 2009 (Act 12 of 2009) which provides for an equitable distribution of nationally raised revenue between national, provincial and local government; and to monitor the implementation of provincial budgets.

It will also continue to support the optimal allocation and use of financial resources in all spheres of government to reduce poverty and vulnerability among South Africa's most marginalised.

It has also created an independent Auditor-General (AG) and an independent central bank, the South African Reserve Bank (SARB), and sets out the principles governing financial accountability to Parliament, as well as the annual budget process.

Financial expenditure

National Treasury plays a pivotal role in managing government expenditure.

It determines financial-management norms and standards, and sets reporting policy that guides the AG's performance. It also assists Parliament, through the Standing Committee on Public Accounts, with its recommendations and the formulation of corrective actions. National Treasury closely monitors the performance of national departments and is obliged to report any deviations to the AG.

The department maintains transparent and fair bidding processes, as well as accounting, logistic and personnel systems. It sets and maintains standards and norms for treasury and logistics, acts as a banker for national departments and oversees logistical control of stocks and assets.

National Treasury draws its mandate from Chapter 2 of the Public Finance Management Act (PFMA), 1999 (Act 1 of 1999), based on Chapter 13 of the Constitution. It is mandated to:

- coordinate macro-economic policy
- promote government's fiscal policy framework
- manage the budget preparation process
- coordinate intergovernmental financial relations
- facilitate the Division of Revenue Act, 2009, which provides for equitable distribution of nationally raised revenue between national, provincial and local government
- monitor the implementation of provincial budgets
- create an enabling regulatory environment for the financial sector
- defend the integrity of the financial system
- ensure efficient and effective revenue collection
- oversee the programmes of development finance institutions (DFIs).

> More than R1,87 billion in grant funding was approved by the R9-billion Jobs Fund in its first year, and complemented by a further R1,78 million from the private sector, to support 41 projects.
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> In all, more than R3,6 billion was committed to Jobs Fund projects between April 2012 and February 2013. The fund, which is managed by the Development Bank of South Africa (DBSA), will run until 2014.
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> By the end of September 2012, R320 million would have been transferred by National Treasury to the DBSA. The R1,8 billion approved by the DBSA will be disbursed in tranches over the agreed terms of the projects.
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> The Jobs Fund was announced by President Jacob Zuma in 2011 to create jobs and fight poverty.

Fiscal policy framework

Government's fiscal policy seeks to encourage and support structural reform of the South African economy consistent with long-run growth, employment creation and equitable distribution of income.

Fiscal policy seeks to:

- present a fuller picture of government finances and the effects of policy decisions
- ensure a sound and sustainable balance between government's spending, tax and borrowing requirements
- improve domestic savings to support a higher level of investment and reduce the need to borrow abroad
- keep government consumption spending at an affordable level
- contribute to lower inflation and a sustainable balance of payments
- support an export-friendly trade and industrial strategy to improve South Africa's competitiveness.

Meeting the country's social and economic goals requires sustainable increases in real expenditure over the decades to come. To achieve this goal, the principles of countercyclicality, debt sustainability and intergenerational equity will continue to anchor fiscal policy choices.

Budget framework

Over the past decade, government has advanced a broad array of social and economic programmes as declining debt-service costs, healthy levels of tax revenue and sound policy choices supported significant increases in public expenditure.

The budget of more than R1 trillion in 2012/13 maintains the state's contribution to growth and social development, while taking steps to ensure fiscal sustainability.

In line with the countercyclical fiscal stance, the budget deficit remains substantial at 4,6% of gross domestic product (GDP) in 2012/13, but narrows to 3% in the outer year as economic activity accelerates.

Over the medium term, slower growth in public spending, combined with rising revenue, will strengthen the sustainability of the fiscus. The stabilisation of public debt will arrest the growth of debt-service costs.

Government will begin to shift the composition of spending from consumption towards capital investment. Moderating growth in the public-sector wage bill and stabilising the growth in interest payments will allow more funds to be spent on infrastructure and social spending.

The consolidated budget includes the national budget, social security funds, Reconstruction and Development Programme (RDP) funds, provincial budgets and extra-budgetary institutions such as the South African National Roads Agency Ltd and the Trans-Caledon Tunnel Authority.

Average annual real revenue growth of 4,8% is projected to outpace GDP growth of 3,7% over the next three years, while expenditure will grow by an average of 2,9% in real terms over this period.

A large share of expenditure growth is absorbed by debt-service costs, which will amount to R109 billion in 2014/15. An improvement in the deficit from 4,8% of GDP to 3% in 2014/15 will stabilise growth in debt-service costs as a percentage of GDP.

Fiscal outlook

Total spending is expected to reach R1,1 trillion in 2013, representing some 32% of GDP. During a period of global uncertainty, the 2012 Budget provided conitinued support for growth, investment and job creation; and maintained the value of social wages. Key features of the fiscal outlook included:

- real growth in non-interest expenditure averaging 2,6% over the medium term, bringing spending in line with long-term revenue trends
- additional allocations of R55,9 billion over the next three years, including R9,5 billion for an economic support package
- tax revenue levels stabilising at about one quarter of GDP
- a reduction in the budget deficit from 4,8% in 2011/12 to 3% in 2014/15
- a shift from consumption to capital spending so that, from 2014/15, new borrowing will support productive investment.

The fiscal position will consolidate in line with improved economic performance and rising revenue over the medium term.

As the economy grows, government will build fiscal space to respond to future crises.

Macro-economic outlook

Government maintains prudent macro-economic policies that promote a favourable environment for investment and job creation through low and stable inflation and interest rates, a competitive real exchange rate and measures to support financial stability.

Policies further seek to create a climate conducive to dynamic private-sector investment, entrepreneurship and growth by removing bottlenecks to trade, reducing red tape and business costs, increasing competition, raising productivity and expanding exports.

The South African economy remains vulnerable to slow global recovery (slowdown in China's economic growth and decreased demand for South African exports by the European Union, which is South Africa's largest trading partner), as well as to domestic factors such as the recent labour unrest.

Economic growth (in real terms) decreased from 2,8% in 2010 to 2,5% in 2012. However, the economy still managed to register moderately positive growth for the third year in a row following the 2009 recession.

The subdued growth rate perpetuates the trajectory of sub-optimal growth. This implies that even though the economy may be performing reasonably and is certainly not collapsing, it is also not performing well enough to make a meaningful dent in the country's high unemployment rate. Furthermore, even though the economy is expected to slowly recover in the medium term, the economic growth forecasts fall below the 5,4% economic growth cited in the National Development Plan (NDP) document, which is necessary to achieve government's job-creation and poverty reduction goals.

Revenue estimates and tax proposals

The tax system raises the revenue needed to fund government programmes and deliver services.

While the South African economy has continued to grow since the 2009 recession, the moderate pace of economic growth has adversely affected revenue performance.

The revised tax revenue estimate for 2012/13 is R810,2 billion, R16,3 billion lower than the estimate made in the 2012 Budget. This underperformance is largely the result of weak economic growth during the second half of 2012, labour unrest and lower commodity prices.

Tax revenues are expected to improve over the Medium Term Expenditure Framework (MTEF) period in line with higher economic growth and the stabilisation of key commodity prices at marginally higher levels.

The main tax proposals for 2013 include:

- personal income tax (PIT) relief of R7 billion
- reforms to the tax treatment of contributions to retirement savings
- an employment tax incentive targeted to support young workers and those employed in special economic zones
- tax relief for small businesses
- requiring foreign businesses selling digital goods in South Africa to register as value-added tax (VAT) vendors
- increases in fuel and excise taxes
- alignment of the proposed carbon tax, energy-efficiency savings tax incentive and the electricity levy.

Over the next year, a tax review will assess whether present tax policy is appropriate to support government's objectives of inclusive growth, employment, development and fiscal sustainability.

The NDP notes that the best way to generate resources to implement the national vision is to grow the economy more rapidly.

The *Open Budget Index Survey* results put South Africa second out of 100 countries in the transparency of its budget processes.

The Washington-based International Budget Partnership has placed South Africa in second place in its *Open Budget Index Report* of 2012, with a score of 90 points out of a possible 100 points.

South Africa is one of only six countries worldwide that release extensive budget information to the legislature and the public in general.

The Institute for Democracy in Africa cooperates with the International Budget Partnership on the Open Budget Index, which is the only independent, comparative and regular measure of budget transparency and accountability around the world. It is produced by independent experts not beholden to national governments.

Spending on public services

Allocations for employment programmes will increase by 13,5% a year over the next three years.

Consolidated spending on health and social protection for 2013/14 is R268 billion. Health infrastructure remains a priority. In 2012, 1 967 health facilities were in stages of planning, construction and refurbishment.

Substantial improvements in the social assistance payments system are in progress, providing easier access by recipients to grants. The cost of social grants payments has been reduced from R32 to R16 per disbursement.

Spending on education, sport and culture amounts to R233 billion in 2013/14. Over the period ahead, the basic education sector will focus on improving numeracy and literacy, expanding enrolment in Grade R and reducing school infrastructure backlogs. Together with the broader education infrastructure grant, R23,9 billion is available to provincial education departments for infrastructure over the next three years.

R700 million has been allocated over the MTEF period for the Technical Secondary Schools Recapitalisation Grant. This will finance the construction and refurbishment of 259 workshops and training of over 1 500 technology teachers. Transfers to higher education institutions increase from R20,4 billion in 2012/13 to R24,6 billion in 2015/16.

Expenditure on economic services in 2013/14 will amount to R48 billion, including R5,3 billion for the Manufacturing Competiveness Enhancement Programme and R2,9 billion for special economic zones.

Expenditure on transport, energy and communications will amount to R89 billion in 2014.

Additional allocations include R450 million over three years to the Economic Development Department for the Small Enterprise Finance Agency.

The allocation to the Department of Science and Technology includes R2 billion to support the Square Kilometre Array Project.

The allocation to the Department of Transport increases from R42,3 billion in 2014, to R53,4 billion in 2015/16.

Local government, community amenities and housing are allocated R132 billion in 2013/14. The largest increases will go to bulk water, water treatment and water distribution projects, and allocations to the Local Government Equitable Share.

R4,3 billion is allocated to a new grant to be administered by the Department of Water Affairs, providing for water treatment, distribution, demand management and support for rural municipalities. The Municipal Infrastructure Support Agency of the Department for Cooperative Governance receives R820 million to provide technical assistance to rural and low-capacity municipalities.

Funding for improving human settlements will grow from R26,2 billion to R30,5 billion over the next three years, including R1,1 billion to support the informal settlement upgrading programme in mining towns. Social housing receives an additional allocation of R685 million.

The general public services function is allocated R57 billion in 2013/14. This includes the South African Revenue Service (Sars) budget of R9,5 billion, which is just over 1% of revenue to be collected.

The Department of Public Works reprioritised R464 million over the medium term to fund its turnaround strategy, which focuses on lease and property management portfolios. The Public Service Commission receives R71,4 million to combat corruption and address grievances.

Over the MTEF period, the Department of Home Affairs will spend R1 billion on its Information Systems Modernisation Programme.

The allocations for defence, public order and safety amount to R154 billion in 2013/14.

The Department of Police has reprioritised R2,5 billion over the MTEF to improve detective and forensic capability. The Department of Justice and Constitutional Development receives R1,2 billion for the Criminal Justice Sector Revamp and Modernisation Programme.

Debt management

Government's borrowing requirement has increased significantly over the past five years as a countercyclical response to the global economic crisis. The nett borrowing requirement is expected to peak at R168,8 billion in 2012/13 before declining to R158 billion in 2013/14. In 2014/15, the nett borrowing requirement is projected to decease further to R140,8 billion owing largely to economic recovery.

Despite elevated borrowing requirements, the funding cost in the domestic markets has declined significantly in 2011/12 relative to the preceding year. Sound economic and fiscal policies coupled with deep and liquid domestic capital markets continue to underpin demand by non-residents and local investors. Consequently, government is able to fund the bulk of its borrowing requirement in the domestic capital markets.

The holdings of domestic government bonds by non-residents increased to 29,1% in 2011 up from 21,8% in 2010. In addition, a successful issuance of US$1,5 billion global bond in January 2012 served as a sign of confidence in the country's story.

National government debt amounted to R1,2 trillion on 31 March 2012 and is expected to reach R1,7 trillion in 2014/15.

Debt-service costs for 2011/12 were 2,6% of GDP. Debt-service costs are expected to peak at 2,8% of GDP in 2013/14 before decreasing slightly to 2,7% of GDP in 2014/15.

Treasury norms and standards

In terms of the Constitution, National Treasury must prescribe measures to ensure both transparency and expenditure control in each sphere of government, by introducing uniform treasury norms and standards.

These aim at deregulating financial controls by granting spending agencies' accounting officers more autonomy in financial decision-making within the ambit of impending financial legislation.

Budget evaluation

National Treasury plays an important role in supporting the economic policy to which government has committed itself. It determines the macro-limit on expenditure, which is then matched with requests from departments, in line with the affordability and sustainability of services.

Based on this limit, all national departments are requested to submit budget proposals annually to National Treasury for the next financial year.

Budget Council

The Budget Council comprises the Minister of Finance and the nine provincial members of the executive councils responsible for finance.

The Budget Forum extends the Budget Council to include representatives of organised local government. These forums ensure cohesion between national policy priorities, the division of nationally raised revenues, and planning and budgeting in provincial and local spheres of government.

The forums also allow the leadership of the three spheres of government to evaluate government's execution of key national programmes and, where necessary, to agree on support initiatives that will ensure the attainment of national goals.

The National Treasury and representatives of the Banking Association of South Africa (Basa) – representing Absa, Standard Bank, FirstRand, Nedbank, African Bank and Capitec – signed an agreement in October 2012 aimed at improving responsible lending and preventing households from being caught in a debt spiral. In a joint statement, the parties expressed concern at the excessive lending to households even when such loans were not affordable or involved unethical practices.

The parties agreed to support the National Credit Regulator (NCR) in enforcing the law and stamping out poor market conduct practices. Going forward, National Treasury, Basa and the NCR are expected to discuss how the current system of debt counselling can be improved to remove unethical incentives and eliminate abuses.

Early Warning System

The Early Warning System was established in 1997. Any likely under- or over-expenditure is brought to the attention of Cabinet, so that the relevant Minister can ensure that appropriate action is taken.

The system assists in monitoring provincial departments' expenditure trends monthly, by having provincial treasuries report to National Treasury in a prescribed format. The information derived from early warning reports is used for advising the Minister of Finance, Budget Council and Cabinet.

Financial systems

National Treasury is responsible for the development, maintenance and support of financial management systems (Basic Accounting System or Bas, Persal, Logis and Vulindlela) that support:

- payment of government employees' salaries and service providers
- financial reporting and management for government departments.

In 2005, Cabinet approved the development of the Integrated Financial Management System (IFMS).

Annual spending on infrastructure for the IFMS has remained stable at approximately R177 million and is expected to increase marginally to R180,3 million over the medium term.

The main purpose of the IFMS is to replace the existing legacy financial management systems. The project has already spent R603,9 million on the development and implementation of the business intelligence, human resources management, procurement management and asset management modules by 2012/13.

The first phase of the business intelligence module has been completed and the module is currently undergoing testing before being rolled out. The rollout of the human resources management module has progressed well at the Department of Public Service and Administration lead site, while the progress at the Free State Department of Education has been hampered by delays in the development of the payroll module.

The rollout of the procurement management module at the lead sites, National Treasury and the Department of Defence has progressed although there are systems integration issues at the latter. This module automates the procurement process and correctly classifies commodities to ensure appropriate and effective demand-planning.

The asset management module had been successfully implemented at five departments in the Limpopo provincial government by the end of 2012 and these departments can now account for all their assets.

However, capacity challenges within the province are likely to impact negatively on its ability to adequately maintain this positive outcome. The cost of this rollout up to March 2012 was R150,4 million, which included software licences and maintenance. The development of the financial management, payroll management and inventory management modules is estimated to cost R650 million.

Supply chain management (SCM)

SCM is an integral part of financial management. The SCM Framework, issued in terms of Section 76 of the PFMA, 1999 replaced outdated procurement and provisioning systems in government.

The Preferential Procurement Policy Framework Act (PPPFA), 2000 (Act 5 of 2000), and its related regulations are being aligned with the aims and strategies of the Broad-Based Black Economic Empowerment (BBBEE) Act, 2003 (Act 53 of 2003).

A phased approach is envisaged. The first phase will be alignment through the amendment of the current preferential procurement regulations as an interim measure.

The second phase will be the comprehensive review of primary procurement, namely the PPPFA, 1999.

The current Act prescribes that tenders must be evaluated on a preference point system where 80 or 90 points are allocated for the price of the lowest acceptable tenderer, and a maximum of 10 or 20 points are allocated for ownership by historically disadvantaged individuals and for promoting specified RDP goals.

Cabinet has approved for promulgation, subject to legal refinement, the draft revised preferential procurement regulations, aligning the preferential procurement policy with the aims of the BBBEE Act, 2003.

Once promulgated, tenders will be evaluated in terms of the generic black economic empowerment scorecard and where sectoral charters exist, evaluation will be done in terms of them.

It is also proposed that local content be considered as an important element of the evaluation criteria. The revised preferential procurement regulations were expected to be promulgated during 2011.

Legislation and policies

Public Finance Management Act (PFMA), 1999

Transforming public-sector financial management is one of National Treasury's key objectives. To this end, National Treasury has been implementing the PFMA, 1999 since 1 April 2000.

The Act changed the approach to the way in which public funds are managed by introducing a less rigid environment for financial management, with a stronger emphasis on the prudent use of state resources, improved reporting requirements and the use of management information to enhance accountability.

Since its introduction, the PFMA, 1999 has contributed towards measurable improvements in financial management in both the national and provincial spheres of government, which include:

- an improved linkage between planning and budgeting, whereby departments are required to compile and table strategic plans consistent with their budget envelope
- strategic plans and budget documentation containing improved information on measurable objectives expressed in terms of quantity, quality and timeliness
- the submission by departments of monthly expenditure reports on actual expenditure incurred, and on projected expenditure for the remainder of the financial year
- risk-management processes
- establishing internal-audit functions and audit committees in all departments
- setting accounting standards in accordance with best accounting practices
- finalising and submitting financial statements to the AG within two months of the end of the financial year
- tabling annual reports in the legislature within six months of the end of the financial year.

Municipal Finance Management Act, 2003 (Act 56 of 2003)

The Act applies to all municipalities and municipal entities, and national and provincial organs of state, to the extent of their financial dealings with municipalities.

The objective of the Act is to secure sound and sustainable management of the fiscal and financial affairs of municipalities and municipal entities by establishing norms, standards and other requirements for:

- ensuring transparency, accountability and appropriate lines of responsibility in their fiscal and financial affairs
- managing their revenues, expenditures, assets and liabilities, and handling their financial dealings
- budgetary and financial-planning processes and coordinating processes for borrowing by organs of state
- handling financial problems and other financial matters.

Co-Operative Banks Act, 2007 (Act 40 of 2007)

The Co-Operative Banks Act, 2007 came into effect on 1 August 2008. Its functions include:

- promoting and advancing the social and economic welfare of all South Africans by improving access to banking services
- promoting the development of sustainable and responsible co-operative banks
- establishing an appropriate regulatory framework for co-operative banks that protects members of co-operative banks.

The Act provides for the establishment of the Co-Operative Banks Development Agency as a public entity under the executive authority of the Minister of Finance.

The agency's responsibility's include:

- supervising and registering deposit-taking financial services co-operatives as co-operative banks
- capacitating, promoting and informing communities and groups about co-operative banking
- registering and regulating representative bodies and support organisations
- establishing the Deposit Insurance Fund for Co-Operative Banks
- liquidity/solvency management through loans and grants

- formalising approaches to developing co-operative financial institutions.

Financial institutions

Financial Intelligence Centre (FIC)

The FIC is a national agency that develops and provides financial intelligence for law-enforcement authorities, the intelligence services and the South African Revenue Service (Sars). The FIC was established by the FIC Act, 2001 (Act 38 of 2001), which came into effect in February 2003. The FIC Act, 2001 is aimed at maintaining the integrity of South Africa's financial and economic system. FIC reports directly to the Minister of Finance and to Parliament.

The FIC's mandate is to:

- monitor the compliance of designated businesses (accountable institutions) and supervisory bodies regarding their anti-money laundering and terror financing obligations
- receive and analyse transactional data from a range of businesses to identify the proceeds of crime, money laundering and the financing of terrorism
- provide financial intelligence reports to the law-enforcement authorities, intelligence agencies and the revenue service as a result of the analysis conducted
- formulate and lead the implementation of policy regarding money laundering and the financing of terrorism
- advise to the Minister of Finance
- uphold the international obligations and commitments required by the country in respect of anti-money laundering and combatting financing of terrorism (AML/CFT).

The FIC Act, 2001 introduces a regulatory framework of measures that require that certain categories of business take steps regarding client identification, record-keeping, reporting of information and internal compliance structures.

All businesses have to report various suspicious transactions to the FIC. The FIC also receives additional financial data from accountable and reporting institutions.

From October 2010, the FIC requires that all accountable and reporting institutions report on cash transactions exceeding R25 000.

In December 2010, amendments to the FIC were promulgated, which required that all accountable and reporting institutions be registered with the FIC. Furthermore, the Act gave the FIC and supervisory bodies the authority to inspect and impose administrative penalties on non-compliant businesses. The Act also introduced an appeals process and appeals board.

South Africa is a member of the Financial Action Task Force, a body which sets international standards and policy on AML/CFT. It is also an affiliate of the 14-member Eastern and Southern Africa Anti-Money Laundering Group, which aims to help countries to implement the global AML/CFT standards.

The FIC is a member of the Egmont Group, consisting of the financial intelligence units of 126 countries, which aims to facilitate international cooperation, and the sharing of information and expertise among its members.

Financial and Fiscal Commission (FFC)

The FFC is an independent, objective, impartial and unbiased constitutional advisory institution. It is a permanent expert commission with a constitutionally defined structure, a set of generic responsibilities and institutional processes.

The FFC submits recommendations and advice to all spheres of government, based on research and consultations on a range of intergovernmental fiscal issues.

The research includes:

- developing principles for intergovernmental fiscal relations, based on analysis of international best practice
- analysing local, provincial and national government budgets to understand revenue and expenditure trends
- identifying and measuring factors influencing provincial and local revenues and expenditures
- assessing fiscal policy instruments, such as conditional grants, equitable share transfers and taxes.

Government is required by the Constitution and other legislation to consult with the FFC on issues such as provincial and local government revenue sources, and provincial and municipal loans.

Consultation about the fiscal implications of assigning functions from one sphere of government to another is also required.

Public Investment Corporation (PIC)

The PIC's clients are public-sector entities, most of which are pension, provident, social security, development and guardian funds.

The PIC's role is to invest funds on behalf of these clients, based on investment mandates set by each client and approved by the Financial Services Board (FSB), with which it is registered as a financial services provider (FSP).

The PIC is wholly owned by the South African Government, with the Minister of Finance as the shareholder representative.

The PIC was established as a corporation on 1 April 2005 in accordance with the PIC Act, 2004 (Act 23 of 2004).

Corporatisation has enabled the PIC to structure its investment activities and operations in a manner comparable to that of private-sector investment managers.

Some 1 001 162 income tax returns for the 2012 tax season were submitted in record time, exceeding the South African Revenue Service's (Sars) expectations. In the corresponding period during the 2011 tax season, Sars received only 681 497 tax returns.

The higher rate of submissions and much faster turnaround times in processing tax returns enabled Sars to pay R3,07 billion in refunds to 501 096 taxpayers over 22 days.

Some 620 564 returns were submitted via e-Filing, which is 32% higher for e-Filing than the same period during the 2011 tax season.

At branch offices, Sars assisted taxpayers across the country to submit 376 802 returns electronically, which is 82% higher than for the same period during the 2011 tax season.

Apart from pursuing FSB-compliant mandates, the PIC benchmarks its investment performance against market-driven indices, enabling clients and the shareholder to compare PIC's returns with those achieved in the marketplace.

South African Revenue Service (Sars)

In accordance with the Sars Act, 1997 (Act 34 of 1997), Sars is an administratively autonomous organ of state.

It aims to provide a world-class, transparent and taxpayer-centred service, ensuring optimum and equitable revenue collection.

Its main functions are:

- collecting and administering all national taxes, duties and levies
- collecting revenue that may be imposed under any other legislation, as agreed upon between Sars and an organ of state or institution entitled to the revenue
- advising the Minister of Finance on all matters concerning revenue and the exercise of any power or the performance of any function assigned to the Minister of Finance or any other functionary in the national executive in terms of the above mentioned legislation
- facilitating trade
- providing protection against the illegal import and export of goods
- advising the Minister of Trade and Industry on matters concerning control over the import, export, manufacture, movement and storage or use of certain goods.

Tax administration

National Treasury is responsible for advising the Minister of Finance on tax policy issues that arise in local, provincial and national government. As part of this role, the department must design tax instruments that can optimally fulfil their revenue-raising function, and that are aligned to the goals of government's economic and social policy. National Treasury and Sars cooperate in compiling tax policies.

A Modernisation Programme begun in 2006 resulted in the successful introduction of electronic platforms for taxpayers and employers to interact with Sars across major tax products like PIT, withholding of employee's tax, VAT and Customs. As a result, individual taxpayers, employers, customs traders and VAT vendors can submit returns, make declarations and pay dues to Sars electronically. The electronic take-up by taxpayers and employer of these electronic channels are amongst the highest in the world, surpassing most tax administration jurisdictions in developed economies.

The Modernisation Programme is based on:

- automating basic tax processes
- using the latest computer technology
- rethinking how better to use the Sars pool of skills
- accessing third-party data and enhanced risk management.

The automation of tax processes is continuously enabling faster processing of taxpayer and employer declarations. The majority of individual tax returns are assessed within minutes and refunds, where applicable, are paid out within three days in more than 77% of cases. Third-party information enables Sars to pre-populate most PIT returns, and also serves to verify information supplied by taxpayers in their returns. In turn, this enables Sars to more accurately focus on areas of non-compliance.

The new Tax Administration Act, (Act 28 of 2011) was promulgated into law in September 2012 and commenced in October 2012. The Act simplifies and provides greater coherence in South African tax administration law. It eliminates duplication, removes redundant requirements and aligns disparate requirements that currently exist in the different Tax Acts administered by Sars. It creates a single, modern framework for the common administrative provisions of the various Acts.

The Act provides for common procedures across the tax products, and provides for the appropriate balance between the rights and obligations of Sars and the rights and obligations of taxpayers in a transparent relationship.

South African tax system

South Africa has a residence-based tax system, which means residents are – subject to certain exclusions – taxed on their worldwide income, irrespective of where their income was earned. Non-residents are, however, taxed on their income from a South African source, but subject to the provisions of International Agreements for the Avoidance of Double Tax.

In broad terms, tax is levied on taxable income, which is calculated by reference to gross income less certain income of a capital nature, exemptions and permissible deductions.

The main tax products are corporate income tax (CIT), VAT, PIT and customs and excise duties.

The South African Revenue Service (Sars) exceeded its target when it collected more than R814 billion in taxes for the 2012/13 fiscal year. This is R4 billion (0,5%) more than what Finance Minister Gordhan projected when he delivered the National Budget in February 2012.

It is the first set of results after the introduction of Sars's new five-year Compliance Programme in 2012. The programme was introduced to help Sars achieve high levels of compliance with tax and customs legislation.

An increase of 8,8% in the compensation of employees contributed positively to the growth in personal income tax. Personal income tax collection grew by R25 billion to R276,8 billion compared to the R251 billion Sars managed to collect in the previous financial year, while value-added tax accounted for R215 billion.

Corporate income tax (CIT)

Corporate institutions are subject to a flat tax rate, currently 28% of taxable income. An exception to the rule is the relief provided to small and micro businesses.

Value-added tax (VAT)

VAT is currently levied at a rate of 14% on the value-added supply of all goods and services rendered by persons (certain supplies are zero-rated) and contributes approximately 33% to the national budget. The quoted or displayed price of goods and services must be VAT-inclusive. A person who supplies goods or services is liable to register for VAT if the income earned from supplying such goods or services is more than R1 million in a 12-month period, or when there is a reasonable expectation that the income will exceed this amount.

A person can also register voluntarily for VAT if the income earned from supplying goods or services for the past period of 12 months exceeded R50 000 or where the turnover is likely to exceed R50 000 only after a period of time as a result of the nature of activity being conducted.

Personal income tax (PIT)

PIT mainly focuses on the taxation of non-corporate income. The main contributor to PIT is employment income, but it also includes income generated from sole-proprietor ventures.

The tax rate applicable to PIT-related taxable income is progressive of nature, currently ranging from marginal rates of 18% to 40%.

Employees' tax (commonly referred to as Pay As You Earn or PAYE) is withheld by employers from salary and wage income on a monthly basis, and reconciled at year-end or on assessment to the final tax liability of the taxpayer.

Other tax products administered by Sars

Excise duty

Excise duty is levied on certain locally manufactured goods and their imported equivalents, such as tobacco and liquor, and as an *ad valorem* duty on cosmetics, audio-visual equipment and motor cars.

Relief from excise duty is available where excisable products are exported, for example specific farming and forestry equipment, and certain manufacturing activities.

Transfer duty

Transfer duty is payable on the acquisition of property. With effect from 23 February 2011, property costing less than R600 000 attracts no duty. A 3% rate applies to properties costing between R600 000 and R1 million.

In respect of property with a value between R1 million and R1,5 million, the duty is R12 000 plus 5% of the value above R1 million.

In respect of property above R1,5 million, the duty is R37 000 plus a rate of 8% of the value exceeding R1,5 million.

Estate duty

Estate duty is levied at a flat rate of 20% on property of residents and South African property of non-residents.

A basic deduction of R3,5 million is allowed in the determination of an estate's liability for estate duty as well as deductions for liabilities, bequests to public benefit organisations and property accruing to a surviving spouse.

Dividend-withholding tax

With effect from 1 April 2012 a dividend-withholding tax is levied on shareholders on payment of a dividend at a rate of 15%.

The tax is withheld by either the institution paying the dividend or by a regulated intermediary distributing the dividend. The dividend-withholding tax replaces the secondary tax on companies.

Securities transfer tax

Securities transfer tax is levied at a rate of 0,25% on the transfer of listed or unlisted securities. Securities consist of shares in companies or member's interests in close corporations.

Skills-development levy

The Skills Development Fund is intended to be used for employee training and skills development.

The levy, which is an amount paid by all employers to Sars, goes into a government body responsible for organising education and training programmes within a specific sector. Each sector has its own Sector Education and Training Authority.

The rate, as from 1 August 2005, is 1% for employers with an annual payroll in excess of R500 000.

Unemployment Insurance Fund (UIF)

The UIF insures employees against the loss of earnings due to termination of employment, illness or maternity leave. The contribution to the UIF is shared equally by employers and employees at a rate of 1% of remuneration each. The employee share of 1% is withheld by the employer and paid to Sars together with the employer share of 1% on a monthly basis.

Tax on international travel

This tax is levied as follows: R190 per passenger departing on international flights, excluding flights to Botswana, Lesotho, Namibia and Swaziland, in which case the tax is R100.

Rates on property

Property-related taxes include municipal rates (sometimes referred to as "property taxes") and charges for refuse and sewerage, although the latter apply mainly to those in urban areas; there are no refuse or sewerage services in some rural areas.

The calculation of municipal rates was changed in March 2004, when the Local Government Municipal Property Rates Bill became law.

Customs duty

The policy on tariffs applicable to importation into South Africa is set by the International Trade Administration Commission under the authority of the Department of Trade and Industry.

The duties levied on imported goods can be separated mainly into customs duties, which include additional customs duties (*ad valorem*) on certain luxury or non-essential items, and anti-dumping and countervailing measures. In addition, VAT is also collected on goods imported and cleared for home consumption and certain other levies are imposed on specific products.

Southern African Customs Union (Sacu)

South Africa, Botswana, Lesotho, Namibia and Swaziland are signatories to the Sacu agreement. They apply similar customs and excise legislation and the same rates of customs and excise duties on imported and locally manufactured goods. The uniform application of tariffs and harmonisation of procedures simplify trade within the Sacu area by enabling free movement of goods for customs purposes. However, all other national restrictive measures such as import and export control, sanitary and phytosanitary requirements and domestic taxes apply to goods moved between member states.

The 2002 Sacu Agreement is in force and provides a new dispensation for calculating and effecting transfers based on customs, excise and a development component of the Revenue Sharing Formula.

The Sacu Heads of State and Government endorsed an ambitious Sacu regional trade facilitation programme that is focused on creating common information technology platforms to allow:

- interconnectivity
- harmonising enforcement strategies to curb illicit trade
- improving border efficiencies to facilitate seamless trade
- developing partnerships with traders through the establishment of a formalised Customs-Trader Forum
- developing similar customs legislation
- establishing one-stop border posts.

South Africa and all Sacu countries are working towards implementing the programme.

Border posts

South Africa is automating most of its border processes to bring the country in line with the international standards of the World Customs Organisation and world-class immigration processes.

The latest technology is now being used to enable cargo to be cleared electronically, while allowing customs and immigration officials to scan passports and release notifications at ports of entry. The intention is to have a seamless process for compliant travellers and traders while making it difficult for illegitimate travellers and traders.

Visitors to South Africa need to ensure that they are familiar with the list of goods (and quantities) that can be imported without payment of customs duty and VAT and those for which customs duty and VAT are payable. This information is available on the Sars website.

International tax agreements for the avoidance of double taxation

International tax agreements are important for encouraging investment and trade flows between nations, by providing certainty about the tax framework.

By reaching agreement on the allocation of taxing rights between international investors' residence and source countries, double-taxation agreements provide a solid platform for growth in international trade and investment. South Africa has tax agreements with over 60 countries.

African Tax Administration Forum (ATAF)

The ATAF is a platform to promote and facilitate mutual cooperation among African tax administrations (and other relevant and interested stakeholders) with the aim of improving the efficacy of their tax legislation and administrations.

The forum brings together heads of African tax administrations and their representatives to discuss the progress made, challenges faced and a possible new direction for African tax policy and administration in the 21st century.

In implementing its mission, ATAF will:

- improve the capacity of African tax administrations to achieve their revenue objectives
- advance the role of taxation in African governance and state building
- provide a voice for African tax administrations
- develop and support partnerships between African countries and development partners.

The ATAF has 36 member countries. South Africa's Sars Commissioner, Oupa Magashula, was unanimously elected as the first chairperson of the ATAF at the inaugural conference and re-elected at the ATAF General Assembly in July 2011.

Organisational performance

In 2011/12, Sars collected R3,9 billion more than the targeted R742,7 billion, representing an increase over the previous financial year of R68,5 billion or 10,2%.

Of the R3,9 billion surpluses against the revised estimate, the most significant contributors are secondary tax on companies (R2,5 billion) and custom duties (R1,9 billion). CIT amounted to R153 billion. While showing steady growth it has remained below the pre-crisis levels that were achieved in 2008/09.

PIT collection rose to R251,3 billion from R228,1 billion in 2010/11. Of the R742,7 billion collected, R595,6 billion (80%) came from PIT, CIT and VAT. Historically these three taxes have always contributed around 80% of the total tax revenue.

The revenue collected from the fuel levy earned Sars R36,6 billion, which was -2% below target, and contributed 4,9% to the overall revenue collected. This decreased from 5,1% in 2010/11 to 4,9% in 2011/12.

e-Filing

Sars introduced its Internet service, e-Filing (*www.sarsefiling.co.za*) as an electronic gateway for taxpayers to interact with Sars, as well as the facility to file electronically at Sars branches.

The e-Filing gateway is a secure and free service, enabling taxpayers to submit their tax returns online from the comfort of their home or office, at any time. It removes the risks and inconvenience of submitting paper tax returns. Not only can returns be submitted via the Internet, but users can also make secure tax payments online. There is also a facility to apply for tax directives, which can be obtained within 24 hours.

The e-Filing service is equal to international standards, being comparable with services offered in the United States of America, Australia, Singapore, Ireland, Chile and France.

Tax calendar

Sars has instituted three critical filing seasons in the tax year that runs from March to Febru-

The Nelson Mandela Metropolitan University's (NMMU) business school has been named an international business leader at the third annual Asia's Best Business Schools award ceremony, held in Singapore in July 2012.

The awards are organised by the World Brand Congress and CMO Asia, which is an arm of the California-based CMO Council, a peer network of marketing executives and brand decision-makers from around the world. It promotes global best practices, knowledge sharing, market transformation and relationship building among its more than 20 000 individual members located in 100 countries.

Based in Port Elizabeth in the Eastern Cape, the NMMU Business School was founded in 2005, and is the youngest such institution in southern Africa.

It was one of 12 award recipients in the business leadership category, and it was the only African institution recognised. Most winners were drawn from the highly competitive Indian and Southeast Asian tertiary education systems.

ary. The first one is Tax Season for Employers, when employers file their annual PAYE reconciliations. This runs from April to May every year.

This is followed by Tax Season for Individuals, when individual taxpayers file their income tax returns. This runs from July to the end of November for non-provisional taxpayers who submit via e-Filing.

Provisional taxpayers who submit via e-Filing have until 31 January the following year to submit their returns. Provisional tax is a system that allows qualifying taxpayers to pay at least two amounts in the course of the year of assessment. Final liability, however, is determined upon assessment.

For the 2012 Tax Season for individuals, Sars received 3 057 296 returns by 3 October, compared to 2 368 928 returns by 3 October 2011, representing a 29% increase.

Employers then have an interim filing season when they file reconciliations for the first six months of the tax year, and this is in effect during September and October.

All three filing seasons are accompanied by innovative communication and marketing campaigns aimed at the relevant taxpayer segments, in line with Sars' segmentation approach. There has been a steady increase in taxpayer compliance as a result of the predictable filing seasons, combined with Sars' improved service offering and taxpayer education.

The Taxpayer Education Campaign focuses on helping all eligible taxpayers to complete their tax returns correctly, honestly and on time.

People who owe Sars tax are charged interest at a rate as published in the *Government Gazette*.

National Gambling Board (NGB)

The NGB was established in terms of the National Gambling Act (NGA), 1996, (Act 33 of 1996), which was repealed on 1 November 2004 by the NGA, 2004 (Act 7 of 2004).

The vision of the board is to position South Africa as the pre-eminent jurisdiction with an effectively regulated industry. The NGB is committed to effective regulation and supervision of the South African gambling industry, a significant economic sector, by upholding internationally recognised standards of compliance.

The emergence of illegal Internet gambling raises challenges to the regulatory regime concerning when, how and what the framework of interactive gambling will be, and what the challenges are.

Statistics

The NGB maintains a national gambling database that contains information on national gambling statistics such as turnover, gross gambling revenue (GGR), gambling taxes and levies, as well as returns to players and punters.

Provincial licensing authorities are required to submit statistics to NGB on a quarterly basis for consolidation and reporting on the national status.

The results for 2011/12 continued to show an increase in GGR and the collection of taxes. In current prices, the GGR increased by 7,5% from R17 140 million to R18 417 million, whereas taxes/levies paid increased by 9,8% from R1 670 million to R1 834 million. In constant (2008/9 financial year) prices, GGR increased with 2,6% and taxes/levies with 4,9%.

Responsible gambling

The NGB has a legislated responsibility to educate the public on the odds of gambling and the negative socio-economic impact of the gambling industry on society.

The National Responsible Gambling Programme (NRGP) is a resource that integrates research and monitoring, public education and awareness, training, treatment and counselling.

The NRGP is managed by the South African Responsible Gambling Foundation, which comprises a board of directors, representing regulators and industry. The main thrust of the NRGP's prevention programme is to educate gamblers and potential gamblers and society as a whole about responsible gambling.

The NRGP has a toll-free Problem Gambling Counselling Line that is staffed by multilingual telephone counsellors. It also has a national network of treatment professionals who provide free and confidential treatment and counselling.

The NRGP has various operational components, e.g. public awareness and prevention, a toll-free counselling line, a countrywide treatment network for outpatient counselling and therapy, research and monitoring initiatives, training for regulators and industry employees, a crisis line service available to gambling industry employees and management, as well as a life skills programme called Taking Risks Wisely – a teaching resource for grades 7 to 12.

Key highlights of the NRGP's activities in 2012 included:

- Problem gambling numbers have remained stable over the past three years at between 3% and 4,7% with 0,5% experiencing severe problems, in line with international trends.
- Available evidence suggests that regular gambling at casinos constitutes no greater risk than other forms of regulated gambling, but that illegal gambling on games such as Fafi, dice and cards does significantly increase the risk of problem gambling. Internet gambling, although not yet legal, constitutes a serious potential threat.
- The multilingual treatment network has more than 70 treatment professionals and has been extended to over 50 towns and cities in southern Africa.
- Over 27 000 gambling industry workers, along with staff from government regulatory authorities, have received formal training on the subject of compulsive and problem gambling.
- The website *www.responsiblegambling.co.za* enjoys up to 1 000 hits monthly.
- The NRGP's services are advertised widely in the media and through collateral displayed in all gambling venues.
- The NRGP is funded by voluntary contributions from the private sector which includes the casino, horse racing, bingo and limited payout machines industries. This comprises 0,1% of the industry's GGR or company winnings. Some R123 million has been invested in the programme by the private sector up to February 2012.

> From its inception to December 2011, the National Responsible Gambling Programme's toll-free counselling line – 0800 006 008 – operating 24 hours a day and seven days a week, has received more than 316 148 calls; 13 661 callers were referred for free treatment to a medical professional (about 100 per month on average); and more than 3 830 received assistance telephonically.

Gambling Review Commission (GRC)

To consider questions about the appropriateness of current gambling policy, regulation, and the proliferation of gambling opportunities and challenges around the regulation of particular forms of gambling, the Minister of Trade and Industry appointed the GRC in December 2009. The commission was to review the gambling industry in terms of framework policy, structural efficiency and socio-economic consequences, from the period 1996 onwards.

In 2011, the Department of Trade and Industry released the committee's findings. These included:

- 68,2% of the South African population does not engage in any gambling activity (based on a representative sample of 3 500 respondents drawn from rural, semi-rural and metro areas). Data includes all variables such as race, household income, education, gender, age and working status.
- Critical to regulate in a manner that balances the growth of this industry while ensuring communities are protected from excessive gambling activities that impact negatively on households. The data affirms the benefits of a well regulated gambling regime.

Recommendations included:

- There is a need to ensure that horseracing is brought within the regulatory framework. Review of work already done in this area should be revisited and this industry should be regulated nationally, to be inclusive of the National Horseracing Authority.
- Regulation of betting exchanges – however, government has to determine implications thereof and policy in this area. Critical to maintain a regulatory national advisory and oversight body with oversight powers and authority to create harmonisation and uniform gambling norms and standards.
- Regulating interactive gambling required mutual cooperation across multidisciplinary institutions with broader knowledge involving movement of money; verification of players; Regulation of Interception of Communications and Provision of Communication-related Information Act, 2002 (Act 70 of 2002) and Consumer Protection Act, 2008 (Act 68 of 2008); cybercrime and communication strategies to ensure monitoring and verifying punters.
- Regulatory framework must accommodate innovations and emerging trends without necessarily allowing for a penetration of illegal activities.
- Any additional gambling modes should be informed by research, national policy and comprehensive legislative framework.
- The NGB facilitates processes of aligning legislations notwithstanding provincial gambling boards retaining their provincial permutations.
- There is a need to introduce a regulatory framework intended to level the playing fields between all forms of gambling activities – no sector should be granted significant competitive advantage over others.
- NGB facilitates processes of aligning legislations notwithstanding provincial gambling boards retaining their provincial permutations.
- There is a need to introduce a regulatory framework intended to level the playing fields between all forms of gambling activities – no sector should be granted significant competitive advantage over others.

Conclusions made going forward in the regulation of the gambling industry included:

- A proposed merger of the NGB and the National Lotteries Board (NLB). Currently, these boards have two entirely different mandates derived from different legislations.
- There is a need for collaboration to effectively regulate and research responsible gambling; register advertisements and promotions; registration of machines and devices; and the probity registers.
- The current Act requires a complete over-

The Financial Services Laws General Amendment Bill, 2012, was tabled in Parliament in September 2012.

The Bill, which was released for public comment in March, addresses urgent issues in 11 financial sector laws, including legislative gaps that were highlighted after the 2008 financial crisis and to align these laws with the new Companies Act, 2008, and other legislation.

Among other things, the Bill seeks to make the Financial Services Board the lead regulator where there is concurrent jurisdiction, as well as eliminate overlaps caused by the Consumer Protection Act, 2008; Companies Act, 2008; and Competition Commission Act, 2009.

Brand Finance, together with Brand South Africa and Brand Africa, launched Brand Finance South Africa 50, a study of the most valuable brands from South Africa, in early 2012.

Brand Finance South Africa measured the financial value of the 50 most valuable brands from South African companies that operate both within and outside South Africa.

MTN topped the list as the Most Valuable South African Brand, with a global value of R43,3 billion and is also the only South African brand in the Brand Finance Global 500, the definitive guide to the world's top 500 brands.

South African banks also had a successful year in 2012, with Standard Bank ranked as the Most Valuable Banking Brand. Banks make up the majority of the Top 10 with Absa, Nedbank and First National Bank also securing high places in the South African ranking.

Vodacom and Standard Bank were found to be the second and third most valuable brands in South Africa (at R18,7 billion and R18 billion respectively), while MTN and First National Bank were found to be the strongest brands, with both having a brand rating of AAA-.

haul to address all identified lacuna, and all approved new forms of gambling.
- Expediting the promulgation of additional national norms and standards.

The commission established that online gambling was unlikely to disappear, as the world was driven by technology. It recommended that a holistic view of online gambling should be taken to its regulation that includes interactive gambling and all forms of remote gambling such as telephone or cellphone gambling.

National Lotteries Board (NLB)

The NLB was established in October 1998 in terms of the Lotteries Act, 1997 (Act 57 of 1997). The board's main activities include:
- advising the Minister of Trade and Industry on the issuing of the licence to conduct the National Lottery
- ensuring that the National Lottery and sports pools are conducted with all due propriety
- ensuring that the interests of every participant in the National Lottery are adequately protected
- ensuring that the nett proceeds of the National Lottery are as high as possible
- administering the National Lottery Distribution Trust Fund and hold it in trust
- advising the Minister on percentages of money to be allocated in terms of the Lotteries Act, 1997
- advising the Minister on establishing and implementing a social-responsibility programme in respect of lotteries
- administering and investing the money paid to the board in accordance with the Lotteries Act, 1997.

The National Lottery operator is Gidani, a 89,2% black-majority-owned private company.

Between 1 April 2011 and 31 March 2012, 68 players won more than a million rand. 49 Lotto players, 18 PowerBall players and one SportStake player became millionaires. Since the lottery began in March 2000, 1 112 millionaires have been created.

More than R2 billion in funding was disbursed to non-governmental organisations countrywide during 2011/12, against a backdrop of an increasing number of applications from eligible organisations.

In 2011, the Department of Trade and Industry launched a review of the Lotteries Policy Framework. The *Lottery Policies Review,* detailing proposed amendments to the Lotteries Act, 1997, was published for public comment in the *Government Gazette* in October 2012. A draft Bill will flow from the policy proposals following consultations with various stakeholders.

Auditor-General of South Africa

The AG strengthens South Africa's democracy by enabling oversight, accountability and governance in the public sector through auditing, thereby building public confidence.

The AG is one of the Chapter-9 institutions mandated by the Constitution to fulfil certain functions. These institutions are not part of government and do not have a duty to be part of the mechanisms of cooperative government. The independence of the AG is thus respected and strengthened.

As mandated by the Constitution and the Public Audit Act, 2004 (Act 25 of 2004), the AG is responsible for auditing national and provincial state departments and administrations, all municipalities and any other institution or accounting entity required by national and provincial legislation to be audited by the AG.

Various business units provide auditing services, corporate services and specialised audit work, such as performance audits, information system audits and audit research and development. The AG also boasts an impressive international auditing complement.

The AG has been presented with the Jörg Kandutsch Award by its peers, in recognition of its efforts to enhance public auditing. The organisation has benefited from the shared experiences and knowledge gained as a member of several working groups, subcommittees and regional working groups of the International Organisation of Supreme Audit Institutions.

In addition, the AG contributed directly to the development of the International Standards of Supreme Audit Institutions, which were officially re-launched as a whole during the 20th International Congress of Supreme Audit Institutions held in Johannesburg in 2010. The next congress will take place in Beijing, China, in October 2013.

Financial sector

South African Reserve Bank (SARB)

The Reserve Bank is the central bank of South Africa. It was established in 1921 in terms of a special Act of Parliament, the Currency and Banking Act, 1920 (Act 10 of 1920), which was the direct result of abnormal monetary and financial conditions that had arisen during and in the period immediately following World War I.

The Reserve Bank is governed by the SARB Act, 1989 (Act 90 of 1989). In terms of the Constitution, it has been given an important degree of autonomy in the execution of its duties.

Since its establishment, the Reserve Bank has always been privately owned. It has more than 600 shareholders. Its shares are traded on the over-the-counter share-trading facility managed by the Reserve Bank.

Its operations are not motivated by a drive to return profits, but to serve the best interests of all South Africans.

The Reserve Bank has branch offices in Johannesburg, Bloemfontein, Cape Town, Durban, East London, Port Elizabeth and Pretoria North.

The bank must submit a monthly statement of its assets and liabilities to National Treasury and an annual report to Parliament. The Governor of the Reserve Bank holds regular discussions with the Minister of Finance and appears before the Parliamentary Portfolio and other select committees on finance from time to time.

The Reserve Bank has a unique position in the economy, as it performs various functions and duties not normally carried out by commercial banks. Although the functions of the Reserve Bank have changed and expanded over time, the formulation and implementation of monetary policy has remained one of the cornerstones of its activities.

The Reserve Bank has used different monetary-policy frameworks over time, such as credit ceilings and credit controls in the 1970s, money-supply growth targets in the 1980s, money-supply growth guidelines in the early 1990s and an eclectic monetary policy with an informal inflation target from the mid-1990s.

In February 2000, an inflation target was specified for the first time, and the adoption of this target entrusted a single objective to the Reserve Bank: price stability. This target was set for the first achievement in 2002. The target is to keep the headline consumer price index between 3% and 6% per year.

The Reserve Bank publishes monetary-policy reviews, while regular regional monetary-policy forums are held to provide a platform for discussions of monetary policy with broader stakeholders from the community.

System of accommodation

The Reserve Bank's refinancing system is the main mechanism used to implement its monetary policy. Through its refinancing system, the Reserve Bank provides liquidity to banks, enabling them to meet their daily liquidity requirements.

"Liquidity" refers to the banks' balances at the central bank that are available to settle their transactions with one another, over and above the minimum statutory level of reserves that they have to hold.

The main instrument for managing liquidity in the money market is repo transactions. The refinancing system, based on repo transactions, was introduced in March 1998.

The repo rate is the price at which the Reserve Bank lends cash to the banking system and is the key operational variable in the monetary-policy implementation process. It represents the most important indicator for short-term interest rates.

The refinancing system also provides for supplementary and standing facilities to bridge the banking sector's overnight liquidity needs, as well as a concession to banks to use their cash-reserve balances with the Reserve Bank to square off their daily positions.

Creating a liquidity requirement

In terms of its monetary-policy implementation framework, the Reserve Bank has to compel banks to borrow a substantial amount (the liquidity requirement or the money-market shortage) from the Reserve Bank.

The Reserve Bank, therefore, creates a liquidity requirement (or shortage) in the money market, which it then refinances at the repo rate – a fixed interest rate determined by the Monetary Policy Committee (MPC), comprising the bank's governors and other senior officials. After each meeting, the MPC issues a statement indicating its assessment of the economy and announces policy changes, if necessary.

The Reserve Bank's repo rate influences the interest rates charged by banks, the general level of interest rates in the economy and therefore other economic aggregates such as money supply, bank-credit extension and, ultimately, the rate of inflation. The repo rate influences market rates in two ways: it directly influences the bank's marginal cost of funding and it reflects the bank's stance on monetary policy.

The Reserve Bank has to intervene regularly in the money market to create a shortage that would drain excess liquidity. In addition to the liquidity-management operations, the Reserve Bank uses other open-market operations to achieve its monetary-policy objectives.

The open-market operations refer to the selling of Reserve Bank debentures, longer-term reverse repos, money-market swaps in foreign exchange and the movement of public-sector funds, for example, the Corporation for Public Deposits and central government funds, as well as changes in the cash-reserve requirements for banks, which by mid-2009 amounted to 2,5% of banks' liabilities.

Functions

The functions of the Reserve Bank can be grouped into the following major areas of responsibility:

- Formulation and implementation of monetary policy (aimed at achieving the inflation target).
- Refinancing system and interest rates: The essence of the bank's monetary-policy implementation framework and the transmission of monetary policy is its influence on the level of interest rates through its refinancing system.
- Open-market operations: These operations are conducted for two reasons: Firstly, to neutralise or smooth the influence of exo-genous factors on the liquidity position in the money market. Secondly, to maintain an adequate liquidity requirement in the market, which has to be refinanced from the bank. Through this mechanism, the bank can exert influence over interest rates in the market.

- Service to government:
  - Gold and foreign-exchange reserves: The bank is the custodian of the country's offi-

cial gold and foreign-exchange reserves. Subsequent to the conversion of the nega-ive nett open foreign currency position in May 2003 into a positive position, foreign reserves have been growing.
  - Banker and adviser to government: The main services provided are administering the auctions of government bonds and National Treasury bills, participating in the joint standing committees between the bank and National Treasury, and managing the flow of funds between the exchequer.
- Account and tax and loan accounts.
  - Administration of exchange control: The bank is responsible for the administration of government's exchange-control policy.
  - Provision of economic and statistical serv-ices: The bank collects, processes, inter-prets and publishes public information, economic statistics and other informa-tion, and uses this information in policy formulation.
- Bank supervision: The purpose is to achieve a sound and effective banking system in the interest of depositors of banks and the economy as a whole.
- The national payment system: The bank is responsible for overseeing the safety and soundness of the national payment system. The main aim is to reduce interbank settle-ment risk with the objective of reducing the potential of a systemic risk crisis emanating from settlement default by one or more of the settlement banks.
- Banker to other banks: The bank acts as custodian of the cash reserves that banks are legally required to hold or prefer to hold voluntarily with the bank.
- Banknotes and coins: The South African Mint Company, a subsidiary of the bank, mints all coin on behalf of the bank. The South African Bank Note Company, another subsidiary of the bank, prints all banknotes on behalf of the Reserve Bank. Currency is distributed through the bank's seven branches to com-mercial banks. It is the responsibility of the branches to ensure that there is an adequate supply of new notes available to meet the demand, and to replace unfit notes. The branches are responsible for the quality of banknotes in circulation in their respective regions.
- Lender of last resort: In terms of its "lender-of-last-resort" activities, the bank may, in certain circumstances, provide liquidity assistance to banks experiencing liquidity problems.
- Monitoring financial stability: In view of the interrelationship between price and finan-cial-system stability, the bank monitors the macro-prudential aspects of the domestic financial system. The objective of financial stability is to prevent costly disruptions in the country's financial system.
- Provision of internal corporate support serv-ices and systems.
- To ensure smooth operations and admin-istration, the bank provides its own inter-nal services, supported by information, commutation and technology, and human resources.

Monetary policy

Global economic developments had a major impact on the conduct of monetary policy in 2011, as a series of negative shocks resulted in slower economic growth and higher inflation outcomes.

> The Reserve Bank launched a national campaign on a new range of banknotes honouring former president Nelson Mandela.
>
> The range was themed *One of a Kind* and the campaign was aimed at educating the public about the banknotes, which entered circulation at the end of 2012.
>
> The new R200, R100, R50, R20, and R10 notes show Mandela's face on the front, and the Big Five group of mammals, which appear on the existing notes, on the back.
>
> Security features include watermarks, micro-printing, and unique numbering. The notes also feature raised printing for the visually impaired.
>
> The new banknotes are the same size as the previous one that are in circulation to avoid con-fusing the visually impaired.

The South African rand was relatively strong for most of the first half of 2011, which helped contain negative price trends. The second half of the year was dominated by the sovereign debt and banking crises in the eurozone and heightened risk aversion resulted in a depreciation of the rand, which exacerbated the impact of higher international oil prices and posed an increased risk to the domestic inflation outlook.

Monetary policy in South Africa was significantly influenced by this global backdrop, alongside a range of key domestic factors. At the time of the March 2011 MPC meeting, the domestic growth prognosis had improved but upside risks led to an upward revision of the inflation forecast. By the May 2011 MPC meeting, the Reserve Bank's forecast for domestic economic growth was reduced slightly and the inflation forecast was again revised upwards.

By the time of the May 2012 MPC meeting, the outlook for domestic economic growth remained unchanged, whereas the inflation outlook improved. A stable interest rate environment was preferred given the conflicting pressures on monetary policy and during the entire period under review, the repurchase rate remained unchanged at 5,5% in support of the real economy despite the temporary breach of the target. Since then, there have been further indications of a generalised slowdown in the global economy and at the July meeting the growth and inflation forecast was revised down. In light of these developments, the repurchase rate was reduced by 50 basis points to 5% a year.

The banking industry

As at the end of December 2011, 31 banking institutions – 10 locally controlled, six foreign-controlled, 13 registered branches and two mutual banks – were reporting data to the Bank Supervision Department of the Reserve Bank. There were also 43 authorised representative offices of international banks in South Africa.

The banking industry is characterised by a high degree of concentration, with four banks, namely Absa Bank Ltd, Standard Bank of South Africa Ltd, FirstRand Bank Ltd and Nedbank Ltd, dominating the sector. The domestic banking sector's operating environment remained challenging during 2011; however, signs of improvement were evidenced compared to 2010.

Total banking-sector assets amounted to R3 409 billion at the end of December 2011, compared to R3 126 billion at the end of December 2010, representing year-on-year growth of 9,0%. Total assets of the four largest banks accounted for 84,1% of total banking-sector assets as at December 2011 (December 2010: 84,6%). Gross loans and advances increased by 8,8% from R2 312 billion at the end of December 2010 to R2 516 billion at the end of December 2011.

Home loans remained the largest component of gross loans and advances, representing about 32,9%, followed by term loans at 17,4% and other loans and advances at 12,8%. At the end of December 2011, banking-sector total equity and liabilities amounted to R3 409 billion (December 2010: R3 126). Total deposits, amounting to R2 710 billion, represented 85,7% of the banking sector's liabilities of R3 161 billion at the end of December 2011 (December 2010: 85,6%).

Deposits from corporate customers (including financial institutions) constituted the largest portion of total banking-sector deposits (46,3%). The total capital-adequacy ratio of the banking sector increased marginally from 14,9% at the end of December 2010 to 15,1% at the end of December 2011.

The banking sector operating profit increased by 30% to R49 billion for the year ending December 2011 (December 2010: R38 billion). The return on equity and return-on-assets ratios improved during 2011 to 16,4% and 1,2%, respectively, at the end of December 2011 (December 2010: 14,6% and 1%, respectively).The ratio of liquid assets to liquid assets held by the banking sector increased during 2011, rising from 174,8% in December 2010 to 193,5% in December 2011.

Impaired advances to gross loans and advances improved throughout 2011 and amounted to 4,7% at the end of December

2011 (December 2010: 5,8%). In line with the general improvement in the quality of the loan books of the banks, the ratio of specific credit impairments as a percentage of gross loans and advances decreased from 1,9% in December 2010 to 1,6% in December 2011.

The microlending industry

The Department of Trade and Industry introduced the National Credit Act (NCA), 2005 (Act 34 of 2005), to allow the credit market to function in a robust and effective manner.

The NCA, 2005 replaced the Usury Act, 1968 (Act 73 of 1968), and the Credit Agreements Act, 1980 (Act 75 of 1980). The NCA, 2005, which became effective on 1 June 2007, aims to regulate the granting of consumer credit by all credit-providers, including microlenders, banks and retailers.

It created the National Credit Regulator (NCR) and the National Consumer Tribunal, which play a vital role in ensuring enforcement, promoting access to redress and adjudicating contraventions of the Act.

Out of a population of close to 50 million, South Africa has just over 18 million credit-active consumers.

The NCR is responsible for regulating the South African credit industry. It carries out education, research and policy development; registers industry participants; investigates complaints; and ensures that the Act is enforced.

In terms of the Act, the NCR has to promote the development of an accessible credit market to meet the needs of people who were previously disadvantaged, earn a low income or live in remote, isolated or low-density communities.

The National Consumer Tribunal adjudicates various applications and hears cases against those who contravene the Act.

The Act provides for the registration of debt counsellors to assist overindebted consumers. Debt counsellors are required to undergo training approved by the NCR through approved training service providers appointed by the regulator.

Other financial institutions

Co-Operative Banks Development Agency

The Co-Operative Banks Development Agency was established in 2009 in terms of the Co-Operative Banks Act, 2007.

Its objectives are to provide for the registration of deposit-taking financial service co-operatives, savings and credit co-operatives, community banks and village banks, and their regulation and supervision. The agency also facilitates, promotes and funds the education and training of co-operative bank personnel.

Access to financial services is a precondition for economic development. As 37% of South Africans have no access to regulated financial services, National Treasury is committed to a range of initiatives to increase access.

Financial co-operatives are owned and controlled by members. The agency provides training and support to ensure that the members' savings and assets are properly managed, and not exposed to undue risk.

In line with government's responsibility for regulating banking and developments in the co-operative banking sector, the department developed appropriate legislation to supervise and support the sector.

Development Bank of Southern Africa (DBSA)

The DBSA Act, 1997 (Act 13 of 1997), stipulates that the DBSA's main role is to promote economic development and growth, human-resource development and institutional capacity-building. The bank achieves this by mobilising financial and other resources from the private and public sectors, both nationally and internationally, for sustainable development projects and programmes.

The DBSA's annual financial results for the year ended 31 March 2011 showed an enhanced contribution to development (loan and equity disbursements plus developmental initiatives) amounting to R8,9 billion. This was achieved despite the financial year being dominated again by economic and market conditions, characterised by lower short-term interest rates and increased long-term interest rates on investments.

During 2010/11, the DBSA spent R518,9 million (2009/10: R550,2 million) on developmental initiatives, representing 60,8% (2010: 66,9%) of its sustainable earnings.

In June 2011, National Treasury's R9-billion Jobs Fund, which aims to create 150 000 jobs over three years, was accepting applications from companies and non-governmental organisations with innovative job-creation projects.

The aim was to give R2 billion in grants in 2011/12 to those companies in the private sector that create jobs. The fund will run for three years and be administered by the DBSA. The department chose the DBSA to administer the fund because of its footprint, which covers over 200 municipalities across the country, and its experience in funding community development projects.

The fund targets established companies with a good track record that plan to expand existing programmes or pilot innovative approaches to employment creation, with a special focus on opportunities for young people.

The fund will target four areas, namely enterprise development, local infrastructure development, support for work seekers and institutional capacity-building.

The DBSA is an implementing agent of the Siyenza Manje Project, an initiative to build capacity and support programmes within local government by hiring experts and young professionals in areas where there are skills shortages.

In 2012, South Africa's former secret service head Mo Shaik was appointed as chief executive of the Development Bank International, to be launched as a subsidiary of the DBSA.

Land and Agricultural Development Bank (Land Bank)

The Land Bank operates as a DFI within the agricultural and agribusiness sectors, and is regulated by the Land and Agricultural Development Bank Act, 2002 (Act 15 of 2002).

The Land Bank provides a range of financing products to a broad spectrum of clients within the agricultural industry. Financing products include wholesale and retail financing to commercial and developing farmers, co-operatives and other agriculture-related businesses.

The Land Bank's objectives are defined within its mandate, which requires that it should achieve:

- growth in the commercial market
- growth in the development market
- business efficiency
  - service delivery
  - resource management
- sustainability.

The Land Bank is the sole shareholder in the Suid-Afrikaanse Verbandversekeringsmaatskappy Beperk, which provides insurance to people indebted to the bank through mortgage loans.

A key recent achievement was the diversification of investors to fund the growing loan book.

Financial Services Board (FSB)

The FSB is a regulatory institution established in terms of the FSB Act, (Act 97 of 1990). The functions of the board include:

- supervising the compliance with laws regulating financial institutions and the provision of financial services
- advising the Minister on matters concerning financial institutions and financial services, either of its own accord or at the request of the Minister
- promoting programmess and initiatives by financial institutions and bodies representing the financial services industry to inform and educate users and potential users of financial products and services.

Collective investment schemes (CIS)

CIS are investment structures whereby individual investor funds are pooled with those of other investors. Qualified asset managers regulated under the Financial Advisory and Intermediaries (FAIS) Act, 2002 (Act 37 of 2002), invest these funds on behalf of the investor. Each investor owns units (participatory interest) in the total fund.

The South African CIS industry has recovered well after the financial crisis. The industry continued to benefit from strong investor confidence in the first quarter of 2013, attracting nett inflows of R47 billion – the second highest quarterly nett inflows ever. The highest ever nett quarterly inflows of R63 billion were recorded in the third quarter of last year and the third highest of R41 billion were achieved in the fourth quarter of 2012.

The three consecutive quarters of record-breaking nett inflows for unit trusts and other local CIS resulted in the highest ever nett inflows for any rolling 12-month period. R166 billion in nett inflows was recorded for the year ended March 2013.

At the end of the first quarter in 2013, the local CIS industry managed assets of R1,28 trillion and offered investors 988 funds. In comparison, total assets under management at the end of December 2012 stood at R1,20 trillion.

The industry's assets under management almost doubled over the past five years.

Financial advisers and intermediaries

The purpose of the FAIS Act, 2002 is to regulate, in pursuance of consumer protection, the provision of advice and intermediary services to certain clients in respect of a range of financial products and services.

The FSB, through the FAIS Division, is responsible for the regulation of the rendering of financial advisory and intermediary services to clients by FSPs in respect of a wide range of financial products.

The provisions of the FAIS Act, 2002 became effective on 30 September 2004. In terms of this Act, before conducting any transaction, consumers should ensure that the FSP they are dealing with has obtained a licence from the FSB. Information on authorised FSPs can be obtained from the FSB website.

Recognised representative bodies

Section 6(3)(iii) of the FAIS Act, 2002 provides for the Registrar of FSPs to delegate any of its powers in terms of the Act to anybody recognised by the Act. Two such functions, the consideration of applications for licences under Section 8 and the consideration of applications for approval of compliance officers under Section 17(2) of the Act, were delegated to two recognised representative bodies. As recognised examination bodies, another four bodies are responsible for developing and delivering the regulatory examination.

Advisory Committee on Financial Services Providers

The Minister of Finance appoints the Advisory Committee on FSPs, whose function is to investigate and report or advise on any matter covered by the FAIS Act, 2002.

The advisory committee consists of a chairperson and other members, including a rep-resentative of the Council for Medical Schemes established by Section Three of the Medical Schemes Act, 1998 (Act 131 of 1998), and persons representative of product suppliers, FSPs and clients involved in the application of this Act, appointed by the Minister after consultation with the board.

The members of the advisory committee, except for the Registrar and Deputy Registrar, who are ex officio members, hold office for a period determined by the Minister.

Licensing of financial services providers

The Registrar of FSPs authorises and renders ongoing supervision of five categories of FSPs. Category-1 consists of financial advisers and intermediaries who provide financial services without discretion. Category-2 FSPs offer discretionary intermediary services in terms of financial product choice, but without implementing bulking. Category-2A FSPs are hedge-fund managers. Category 3 FSPs are investment administrators specialising mainly in the bulking of collective investments on behalf of clients (linked investment services providers). Category 4 FSPs represent assistance business administrators who render intermediary services in terms of the administration of assistance business (funeral policies) on behalf of an insurer to the extent agreed to in a written mandate between the two parties.

Insurance companies

Insurance is divided into long- and short-term insurance. Insurance is an agreement between a policy holder and the insurance company. Under a short-term insurance policy, the insured is entitled to be compensated by the insurer for the loss of or damage to assets caused by the event against which they are insured.

The aim of short-term insurance is to put the insured in the same position they occupied immediately before the loss, depending on the terms and conditions of the policy contract. Examples of short-term insurance include motor-vehicle, household, theft and fire insurance. By 31 March 2011, there were 108 short-term insurers in South Africa.

Long-term insurance includes life and assistance policies that pay a benefit to dependants on the death of the insured person(s), endowment (savings) policies payable at a predetermined date, disability policies, pensions and retirement policies, or even a combination of these. By 31 March 2011, there were 87 long-term insurers in South Africa.

In terms of the Long-Term Insurance Act, 1998 (Act 52 of 1998), and the Short-Term Insurance Act, 1998 (Act 53 of 1998), all insurance companies must be registered by the FSB and must comply with the provisions of these Acts.

The insurance industry has appointed a short-term and long-term insurance ombudsman to mediate dispute resolution between insurers and policy holders.

Market abuse

The Directorate: Market Abuse is an FSB committee responsible for combatting market abuse in the financial markets in South Africa. The three forms of market abuse prohibited in South Africa are insider trading, price manipulation and publication of false or misleading statements. The members of the directorate are representative of the legal and accounting professions, financial markets, the banking industry, the fund managers industry, the Reserve Bank and investors.

All three forms of market abuse are criminal contraventions. In addition, an offender may be referred to the FSB Enforcement Committee, which can impose unlimited penalties. In the case of insider trading contravention, such penalties are distributed to people who were prejudiced by the offending transactions.

Retirement funds

The Minister of Finance announced proposals in the 2013 Budget Speech to reform the retirement industry, with a focus on governance, preservation, annuitisation and harmonisation of retirement funds.

These proposals follow a series of technical discussion papers with draft proposals that were issued in 2012, after the 2012 Budget announcements by the Minister.

Over the course of 2012, both formal and informal consultations were held in respect of these papers with stakeholders, including unions, industry associations, product providers, intermediary associations, and members of the public. Following on from these consultations, government has developed revised policy proposals for further consultation.

The overall approach of these policy proposals is to alter the defaults implicit in retirement fund design, where appropriate, to nudge, rather than force, individuals into making decisions which serve their long-run interests.

From an effective date, on or after 2015, called T-day, employer contributions to retirement funds will become a fringe benefit in the hands of employees for tax purposes. Individuals will be able to receive a tax deduction on employer and employee contributions to a pension fund, provident fund or retirement annuity fund up to 27,5% of the greater of remuneration and taxable income. A ceiling of R350 000 will apply.

In addition, government is exploring ways to increase retirement fund coverage to all workers.

Enforcement

The Enforcement Committee of the FSB is adjudicates on all alleged contraventions of legislation, regulations, codes of conduct, etc. administered by the FSB within the South African non-banking financial services industry.

The FSB administers the following Acts:

- CIS Control Act, 2002 (Act 45 of 2002)
- FSB Act, 1990, the FAIS Act, 2002
- Financial Institutions (Protection of Funds) Act, 2001 (Act 28 of 2001)
- Financial Supervision of the Road Accident Fund Act, 1993, (Act 8 of 1993)
- Friendly Societies Act, 1956 (Act 25 of 1956)
- Inspection of Financial Institutions Act, 1998 (Act 80 of 1998)
- Long-Term Insurance Act, 1998
- Pension Funds Act, 1956 (Act 25 of 1956)
- Short-Term Insurance Act, 1990
- Supervision of the Financial Institutions Rationalisation Act, 1996 (Act 32 of 1996)
- Securities Services Act, 2004 (Act 36 of 2004).

The committee considers cases of alleged contraventions of legislation administered by the FSB. The industries regulated by the FSB include CIS; FSPs; insurance; nominee companies; retirement funds and friendly societies. The committee may impose unlimited penalties, compensation orders and cost orders. Such orders are enforceable as if it were a judgment of the Supreme Court of South Africa.

Financial markets

Capital markets were characterised by high levels of capital inflows into emerging markets and the sovereign debt crisis in Europe from 2010 to 2012.

Attractive returns in emerging debt markets coupled with higher growth prospects impelled investors around the globe to seek higher-yielding emerging market assets, particularly in the second half of the year.

The South African capital market had its fair share of capital inflows, with a substantial amount finding its way to the local currency government bond market.

Government bonds

Retail bonds

Retail bonds can be purchased from National Treasury, the South African Post Office and Pick n Pay stores countrywide. Since the introduction of RSA fixed-rate retail savings bonds in May 2004 and inflation-linked retail bonds in April 2007, the cumulative amount reached R17,2 billion on 31 May 2012.

Government first issued these bonds to encourage South African citizens to save. These bonds are easily accessible through various distribution channels across the country. The number of investors has increased over the past eight years.

Due to general familiarity with fixed deposits as made available by the commercial banks, investors in the RSA retail bonds are more inclined to invest in a predictable product such as fixed-rate investment. There has been increased investment in inflation-linked bonds, mainly due to the decline in stereotype associated with fixed-rate investments.

Domestic capital market bonds

Increased global demand for emerging market's higher-yielding debt has led to rising international interest in South African government bonds. Non-residents' purchases of domestic bonds declined somewhat from a nett annual high of R52 billion in 2010 to a nett R42 billion in 2011. In the first six months of 2012, non-residents purchased a nett of R49 billion worth of domestic bonds, which contributed to the noticeable decline in bond yields.

Among the most traded bonds in the market are the R157 (13,5%: 2015) and the R186 (10,5%: 2026). The daily yields on the R157 government bond averaged 6,555% in 2012 to June, after closing 2011 at the average of 7,271%, from a daily average of 7,751% in 2010. The R186 government bond averaged 8,297% in 2012 to June, after closing 2011 at the average of 8,511% as opposed to 8,614% in 2010. The average spread between the R157 and the R186 widened to the 170 basis points level from 2010's average of about 88 basis points.

The break-even inflation rate – calculated as the differential between fixed-interest bond yields and the real yields of inflation-linked government bonds within the one-year maturity range – increased from an average of 5,56% in June 2011 to 5,95% in June 2012. The long-term break-even inflation rate (21-year) increased from an average of 6,03% in June 2011 to 6,21% in June 2012, owing to stronger real yields being driven down by the demand for inflation-linked bonds.

Primary market

Government funding in the domestic primary market is done through long-term market loans, which comprise fixed-income bonds, inflation-linked bonds, floating-rate notes and retail bonds.

Fixed-income bond issuances constitute most of the total bond issuance, and were issued at a weighted average nominal yield of 8,3%, while inflation-linked bonds were issued at a weighted average real yield of 2,9% in the previous year.

Five new domestic bonds were issued in 2012 – the two new fixed-income bonds, R2023 (7,75%; 2023) and R2048 (8,75%; 2047/48/49), and three new inflation-linked bonds, I2025 (2%: 2025), I2038 (2,25%: 2038) and I2050 (2,5%: 2049/50/51). All were well received by market participants and their volume has increased to contribute to the improved market turnover.

International bonds

South Africa priced a US$1,5 billion 12-year global bond in the international capital markets on 9 January 2012. The bond was priced at a yield of 4,715%, a coupon (interest) of 4,665% and a spread of 270 basis points above the 10-year United States of America (USA) Treasury's benchmark bonds. The coupon (interest) of 4,665% was 159 basis points lower than the coupon of the 30-year global dollar coupon issued in 2011 at 6,25.

After reaching a spread of 129 basis points over the underlying US Treasury bond on 29 June 2011, the spread on the RSA global bond maturing in 2041 widened to 290 basis points on 23 September 2011 before narrowing to 177 basis points, while the new 2024 narrowed to 208 basis points at end of June 2012.

After recording nett redemptions in 2009 and 2010, gross issues of rand-denominated bonds by non-residents in the European and Japanese Uridashi bond markets exceeded gross redemptions in 2011, resulting in nett issues of R20 billion over the period.

While issuances in the Japanese Uridashi bond market remained broadly on the same level, issuance activity in the European bond markets more than doubled in 2011 when compared with 2010.

Although rand-denominated bond issuances by non-residents continued steadily in 2012, they were at a somewhat lower level, possibly in part as a result of fragile market conditions amid the political and financial problems in Europe, and the downgrading of sovereign debt credit ratings in Japan and a number of European countries.

In the first half of 2012, nett redemptions of rand-denominated bonds in the European bond markets amounted to R1,3 billion, while nett issuances of R1,4 billion were recorded in the Uridashi bond market.

Secondary market

The local bond market continued to benefit from prudent macro-economic policies, which saw the country through the global financial crisis in 2008. The nominal turnover on the domestic bond market reached a high of R19,3 trillion in 2008 before declining significantly to R13,4 trillion in 2009. In 2010, turnover increased to R16,9 trillion and continued higher to a record high of R20,9 trillion in 2011 with support from non-residents.

Non-residents contributed about 10% to total turnover in June 2012, while local investors added the remaining 90%. The bond market capitalisation on the JSE Ltd amounted to

R1,7 trillion in June 2012, with government contributing the largest share of 61% to the total market capitalisation, followed by public and private corporations at 38%. Fixed-rate (including zero-coupon) bonds accounted for 67% of the total listing on the exchange in terms of instrument composition while inflation-linked and floating rate contributed 21% and 12% respectively.

Exchange rates

Uncertainty about the sovereign debt crisis in peripheral European countries to an important extent dominated foreign-exchange markets over the past 18 months, although factors such as political turmoil in North Africa and the economic impact of the natural disaster in Japan also had a bearing on currencies.

Subsequent to an increase of 0,7% in the final quarter of 2011, the nominal effective exchange rate of the rand increased by 4,4% from the end of December 2011 to the end of March 2012.

The rand appreciated in the first quarter of 2012 most notably against the US dollar, Chinese yuan and the Japanese yen. The appreciation in the external value of the rand in the first quarter of 2012 was supported by an improvement in international investor sentiment and risk appetite following the approval of Greece's second bailout package of €130 billion, alongside sustained low interest rates in developed economies.

However, from the end of March 2012 to the end of May 2012, the nominal effective exchange rate of the rand lost momentum and declined by 6,6%. The depreciation in the exchange value of the rand over this period could largely be ascribed to risk aversion following inconclusive Greek elections and renewed uncertainty in the global financial markets.

Subsequent to a 2,4% increase in December 2011, the real effective exchange rate of the rand rose by a further 0,8% up to March 2012, dampening the price competitiveness of local exporters. However, this trend reversed on account of the decline in the exchange rate of the rand in April.

The average nett daily turnover in the domestic market for foreign exchange increased by 34,3% from US$16,5 billion in 2010 to US$22,1 billion in 2011 and approximately US$20 billion in the first five months of 2012. The higher turnover in the domestic market for foreign exchange could largely be attributed to increased activity by non-resident investors in the swap market. The value of transactions in the market for third currencies also rose firmly in 2011 compared with the preceding year before levelling out in the early months of 2012.

Exchange controls

Exchange-control regulations are administered by the Reserve Bank on behalf of the Minister of Finance. The Minister of Finance has also appointed certain banks to act as authorised dealers in foreign exchange, as well as authorised dealers with limited authority in foreign exchange, which gives them the right to buy and sell foreign exchange, subject to conditions and within limits prescribed by the Financial Surveillance Department of the Reserve Bank. Authorised dealers are not agents of the Financial Surveillance Department, but act on behalf of their customers.

Since 1994, there have been gradual exchange-control reforms concerning individuals, corporates and institutional investors. The liberalisation has been focused on progressively increasing the individual foreign capital allowance, increasing institutional investors' foreign exposure and allowing South African firms to raise capital and expand their operations offshore from a domestic base.

Under current exchange control regulations there are no limitations as to how much money can be brought into South Africa, but there are limitations on the amount of money that can be transferred out of South Africa.

South Africans are currently, for example, able to transfer up to R4 million out of the country and invest it overseas. This is their lifetime allowance; additional allowances are available for travelling and other defined activities.

For all non-South Africans, their exchange control status is vital in deciding if there will be limitations on transfering money out of South Africa that was introduced previously.

Johannesburg Stock Exchange (JSE) Ltd

The JSE Ltd is privately owned and funded, and governed by a board of directors. Its activities are licensed and regulated by two Acts of Parliament, namely the Stock Exchanges Control Act, 1985 (Act 1 of 1985), which governs the equities markets, and the Financial Markets Control Act, 1989 (Act 55 of 1989), which governs the derivatives markets.

In keeping with international practice, the JSE Ltd also acts as regulator of its members and ensures that markets operate in a transparent way, ensuring investor protection. Similarly, issuers of securities must comply with the JSE Ltd listings requirements, which aim to ensure sufficient disclosure of all information relevant to investors.

The JSE Ltd's roles include regulating applications for listing and ensuring that listed companies continue to meet their obligations. The JSE Ltd monitors applications for alterations to existing listings, and scrutinises company disclosures to the public. It also provides a Stock Exchange News Service through which company news, including price-sensitive in-formation, is distributed to the market.

The JSE Ltd has been bold in restructuring in view of increasingly tough global competition, adopting new technologies and outsourcing aspects of its business.

The traditional open outcry market in which traders jostled for deals on a noisy trading floor has now disappeared, replaced by a less colourful, but faster, computer-driven trading system (the Johannesburg equities trading screen-based system).

The JSE Ltd has been opened to corporate membership, resulting in a stampede by foreign banks, who have bought out most of the major local broking firms, using these as platforms for other financial services, such as corporate and government advisory work.

The introduction of an electronic settlement system called Strate (Share Transactions Totally Electronic), replaced the previous manual settlement method. Strate Ltd is the licensed Central Securities Depository for the electronic settlement of financial instruments in South Africa.

The Johannesburg Stock Exchange (JSE) was established in 1887 and became a member of the World Federation of Exchanges in 1963. It is currently the largest stock exchange in Africa, and the 16th largest in terms of market capitalisation and trading volume in the world. It has some 480 listed companies on the exchange with a total market capitalisation of approximately $580 billion.

The JSE Ltd's trading and information systems were replaced with the London Stock Exchange's (LSE) Sequence and the London Market Information Link or LMIL systems, branded JSE SETS and InfoWiz, respectively. The trading engine and information dissemination feed-handler is hosted in London and connected remotely to the JSE Ltd. The connection takes place over a 9 000-km transcontinental undersea cable and an innovative, integrated solutions design. More than 1 500 traders and information users access the system via a sophisticated application service provider with sub-second response time.

The JSE Ltd also aligned its equities trading model with that of Europe, and reclassified their instruments in line with the FTSE Global Classification System. This has led to the introduction of the FTSE/JSE Africa Index Series that makes the South African indices comparable to similar indices worldwide.

The investment community is now served by one of the most reliable trading platforms worldwide. Trade information of instruments listed on the JSE Ltd can be disseminated by the LSE to more than 104 000 trading terminals around the world, raising the profile of the JSE Ltd among the international investor community.

Conclusion

Over the next 10 years, National Treasury's priorities include increasing investment in infrastructure and industrial capital; improving education and skills development to raise productivity; improving the regulation of markets and public entities; and fighting poverty and inequality through efficient public service delivery, expanded employment levels, income support and empowerment.

During the next five years, National Treasury will continue to contribute to the design of social and economic reforms, especially in the areas of transport, energy, telecommunications and health.

It will also continue to focus government's financial resources on the stimulation of economic growth and job creation, and take a more hands-on approach to ensuring that government realises greater value for public funds spent. In this regard, some of the shortcomings in the management and monitoring of public finances will be addressed. A multifaceted approach has been adopted, including changes to supply-chain policy and selected expenditure reviews, as well as technical support where required.

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

As part of its commitment to transparency, National Treasury will start publishing yearly reports on the management of public debt. These reports are intended to complement regular domestic and international road shows, as well as the investor relations website.

On the international front, National Treasury will continue to focus on influencing regional and global policies to advance the economic, financial and development objectives of South Africa and that of Africa more generally.

During the next five years, member states of Sacu – Botswana, Lesotho, Namibia, South Africa and Swaziland – are expected to reach an agreement on a new revenue-sharing arrangement for the customs union. National Treasury will also engage in multilateral efforts to ensure the full implementation of SADC's Finance and Investment Protocol.

In view of current global economic uncertainty, G20 member states have been working to intensify international cooperation, giving particular consideration to the processes and institutions of global governance. National Treasury will play a leading role in developing, coordinating and negotiating South Africa's positions with respect to this agenda, in close collaboration with The Presidency, the Department of International relations and Cooperation and other core departments.

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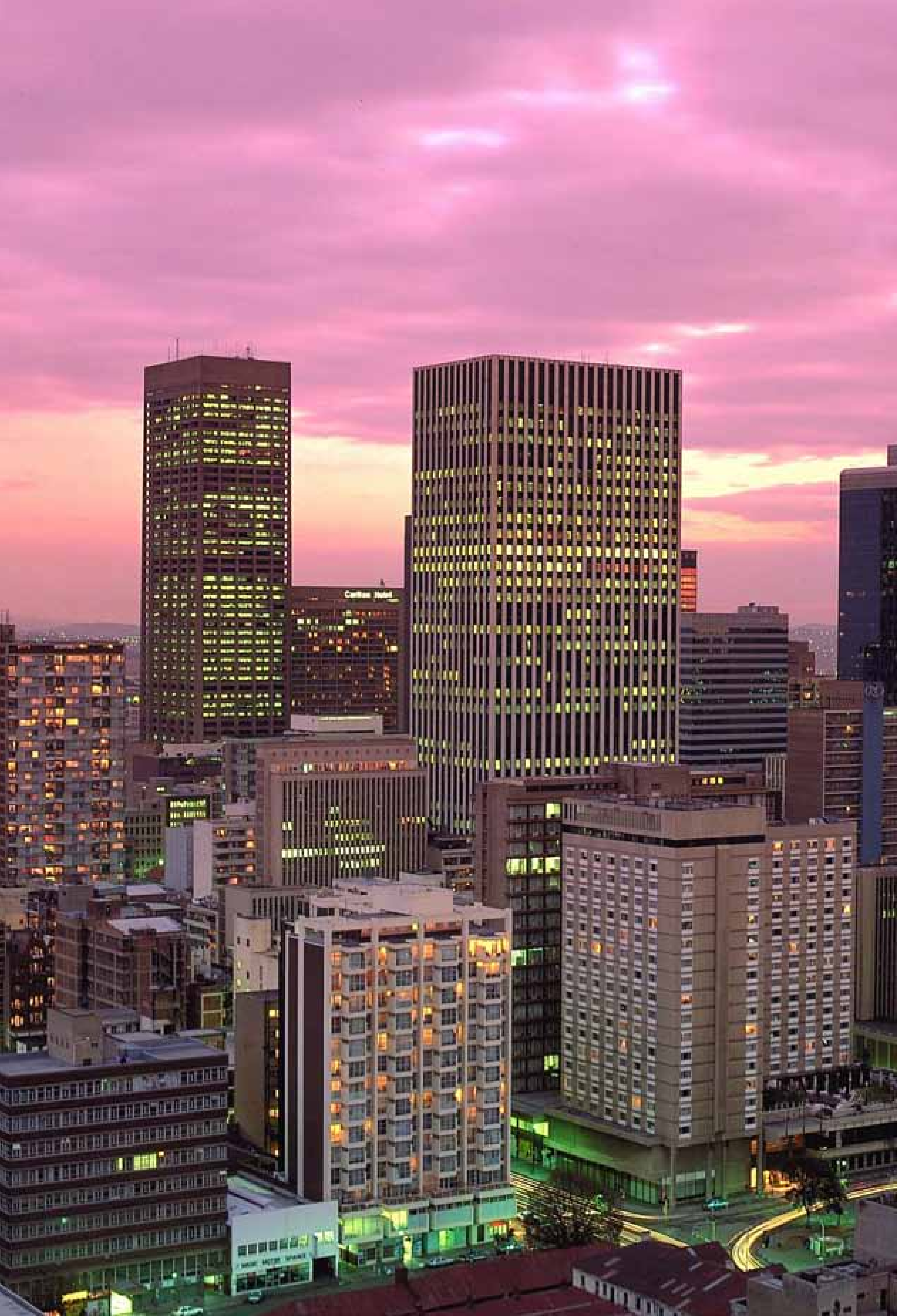
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