National finances

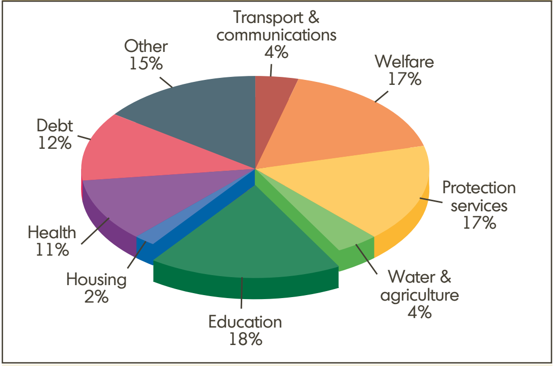
South Africa's debt, both domestic rand-denominated bonds and foreign debt issues, enjoys increasing recognition on international capital markets. The South African economy grew by 3,7% in 2004, and is set to grow by over 4% a year for the next three years. The economy is growing more strongly than at any time in the past 20 years.

This reflects:

- the country's macro-economic success
- sustainable fiscal and macro-economic policies
- a sound and transparent approach to debt management
- a healthy balance-of-payments position
- the maturity of South Africa's financial markets.

South African foreign debt continues to trade at tighter spreads than the Emerging Market Bond Index.

Government expenditure



Source: *A People's Guide to the Budget 2005*

The primary objective of domestic debt management has in recent years shifted to reducing the cost of debt to within acceptable risk limits, with diversification of funding instruments and ensuring flexible government access to markets as secondary goals. Recourse to foreign borrowing has been stepped up, allowing the fiscus to contribute to reducing the foreign currency exposure of the South African Reserve Bank in its forward market portfolio.

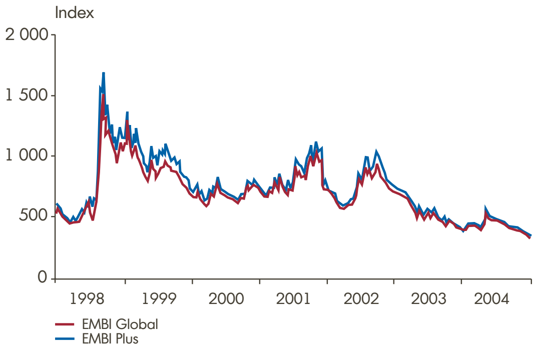
State debt costs continue to fall as a share of government expenditure. It was expected to be 2,3% of gross domestic product (GDP) in 2005/06, while debt service costs were expected to total 3,5% of GDP according to the Budget speech delivered early in 2005. Debt service accounted for 5,6% of GDP in 1999. The liquidity in the domestic government bond market, measured by the increase in nominal trades, has improved substantially in recent years.

Financial markets

Primary capital market

Although primarily a government-bond market, the Bond

Emerging-market bond indices



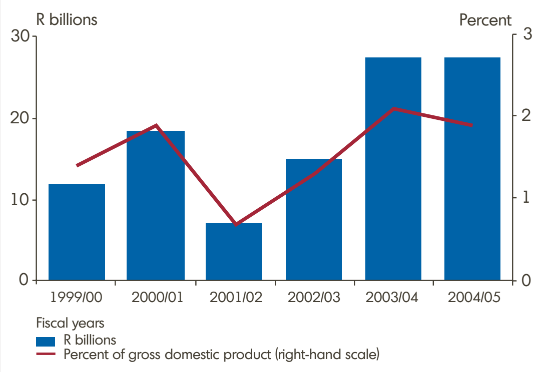
Source: South African Reserve Bank

Exchange of South Africa (BESA) also lists rand-denominated debt securities issued by local government, public enterprises and major corporates. At 31 December 2004, BESA had 378 fixed-income securities outstanding, issued by 65 borrowers, with a total nominal value of R572 billion. Just over 70% of this debt had been issued by central and municipal government, with a further 11% issued by parastatal and utility organisations. The remaining listed debt had been issued by companies in a wide range of sectors: banking, gold mining, chemical, food, household goods and textiles, telecommunications and transport. Securitisation issues include vehicle, credit card, loan receivables, equipment receivables and mortgage products.

Market performance

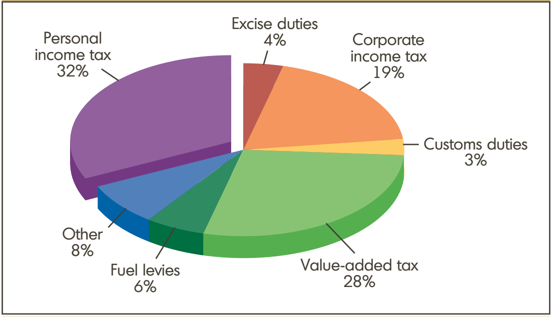
The South African bond market is one of the most liquid emerging bond markets in the world. Turnover in listed debt declined in 2004, with volumes decreasing from R10,7 trillion nominal in 2003 to R8,4 trillion nominal, representing a drop of 21%. The decrease in nominal turnover was also reflected in the lower number of matched

Non-financial public-sector borrowing requirement



Source: South African Reserve Bank

Tax revenue



Source: *A People's Guide to the Budget 2005*

trades for the year, which decreased from 356 000 in 2003 to 328 000 in 2004. Turnover in the spot market increased from 33,6% of total turnover in 2003 to 34,1% in 2004.

Although turnover figures for 2004 dropped significantly, the turnover velocity of listed debt instruments remained healthy at 14 times the market capitalisation for 2004.

While 94% of market turnover in 2004 was in government and utilities stock, there has been an ever-increasing amount of listings and turnover in corporate issuances and securitisations which together, in 2004, accounted for 6% of total turnover.

Offshore turnover in listed debt that was settled locally amounted to R2 trillion, or 23,6% of total turnover, indicating that South Africa's local debt has significant attraction for international investors.

Secondary capital-market activity

South African bond yields declined considerably from May 2004 until February 2005. The yields on government bonds declined to historically low levels, with the yields on two-year R194, five-year R153 and 20-year R186 government bonds declining to 7,22%, 7,40% and 6,98%, respectively, by 28 February 2005.

Factors that contributed to this decline in local yields include the firmer Rand-Dollar exchange rate, reductions in the repo rate, low yields in the developed countries, and a ratings upgrade by Moody's in January 2005. In addition, the inflation outlook has remained promising, with CPIX moving to historically low levels, and not expected to breach the upper band of the Reserve Bank's 3% to 6% guideline range over the forecast period. Improved investor sentiment towards the country's political and economic policies also contributed to the decline in bond yields, as reflected by non-resident interest in the local bond market. After being net sellers of South African bonds to the value of R8,1 billion in 2003, foreigners were net purchasers of bonds to the value of R450 million in 2004.

During March 2005, bond yields increased by an average of 80 basis points, in reaction to external factors, such as increasing United States (US) Treasury yields.

Managing public finances

The Public Finance Management Act, 1999 holds heads of departments accountable for the use of resources and emphasises regular financial reporting, independent auditing and measuring output and performance.

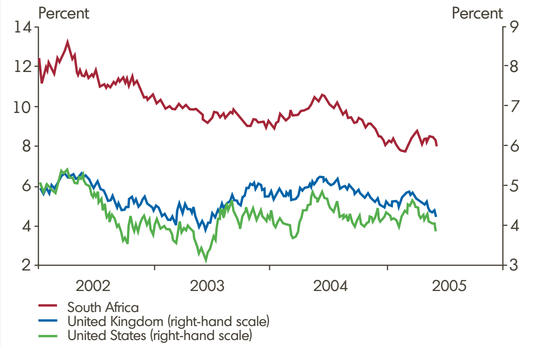
State departments are closely monitored by the National Treasury and any deviations are referred to the Auditor-General for investigation.

Taxation

The South African Revenue Service (SARS) collected

The Auditor-General has a budget of more than R712 million and 1 598 employees. These are divided into various centres of excellence that provide auditing services, corporate services and specialised audit work, namely performance, forensic auditing, computer auditing and technical support. It also boasts an impressive international auditing complement.

Yields on long-term government bonds



Source: South African Reserve Bank

R354,9 billion in taxes during 2004/05, exceeding its revised target of R333,7 billion by almost R10 billion and its original target of R345,3 billion by R21 billion. The revenue haul will help trim South Africa's budget deficit for 2004/05 from 2,3% to 1,6% of GDP.

South African residents are (subject to certain exclusions) taxed on their worldwide income.

Companies are taxed at a rate of 29% after a 1% reduction for 2005/06 to stimulate investment and job creation. In addition, secondary tax on companies is levied on companies at a rate of 12,5% on dividend distributions. A formula tax applies to gold-mining companies. A number of administrative interventions as well as tax-relief measures were announced in the Budget to regularise and to stimulate growth for small businesses. Small business corporations (annual turnover limit increased to R6 million) benefit from a revised graduated tax rate of 0% on the first R35 000 of taxable income and 10% up to R250 000 of taxable income. They are eligible for accelerated depreciation allowances, and can write off investments in manufacturing plant and equipment in the year in which it is incurred.

Value-added tax is levied at a standard rate of 14%. Transfer duty, estate duty, stamp duty, marketable securities tax, customs duty and excise duty are also levied. Local governments levy rates on the value of fixed property.

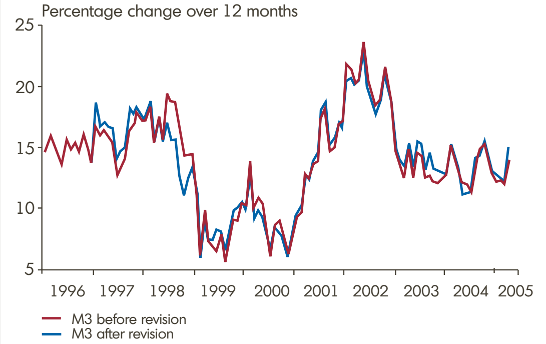
A skills development levy applies at the rate of 1% of payroll, for employers with an annual payroll of more than R250 000.

The Minister of Finance, Mr Trevor Manuel, presented the Budget for 2005/06 on 23 February 2005.

Highlights included:

- R6,8 billion in tax relief for individuals and households, directed mostly at those earning below R200 000 a year
- people earning below R35 000 a year (R60 000 for over 65s) would not pay personal income tax
- a change in the tax treatment of medical scheme contributions to reduce costs of membership for lower-income families
- scrapping of transaction tax on debit entries to credit card and bank accounts, to keep banking services affordable
- beer went up 11c a bottle, and 5c a can, while a packet of 20 cigarettes cost 52c more
- levies on petrol and diesel increased by 10c a litre
- tax relief of R1,4 billion for small business, to free up resources for growth
- measures to reduce tax-compliance costs and red tape for small business
- a drop in the company tax rate from 30% to 29%
- changes to the tax on travel allowances to remove unwarranted benefits for higher-income earners
- a R40 increase in the maximum monthly old age, disability and care dependency grants to R780, and a R10 increase in the monthly Child Support Grant to R180
- a R6-billion allocation to allow the land restitution programme to complete its work over the next three years
- eliminating regional services council levies in 2006

Growth in M3



Source: South African Reserve Bank

- R2 billion for the new comprehensive housing strategy and R3 billion for related community infrastructure
- R1,7 billion for water, sanitation and other municipal infrastructure investment
- R6,9 billion for improving teachers' salaries
- R5 billion to allow for pay progression in police salaries and an increase in police numbers
- R3 billion for public transport investments and roads, including for the 2010 Soccer World Cup
- R3,7 billion for the delivery of municipal services
- R776 million for the National Student Financial Aid Scheme
- R1 billion to revitalise Further Education and Training colleges
- R1,4 billion for South Africa's African development agenda, including peacekeeping operations, the African Union and the Pan-African Parliament
- a new micro-agricultural finance scheme, with funding of R1 billion.

Auditor-General

The Constitution guarantees the independence of the

Auditor-General. The office audits national, provincial and local government. The Auditor-General has the power to audit the activities of public entities without the approval of the CEO or directors.

South African Reserve Bank

The bank, which is independent, formulates and implements monetary policy and regulates the supply of money by influencing its cost.

An important responsibility of the bank is to ensure that the banking system as a whole is sound and meets the requirements of the community.

The bank acts as a banker to other banking institutions. It is also the custodian of the statutory cash reserves and provides facilities for the clearing and settlement of inter-bank obligations.

Monetary policy

The main objective of monetary policy is to secure a stable financial environment. Policy is therefore not applied to address short-term cyclical events.

Growth in broad monetary aggregated M3 exceeded 11% throughout 2004, registering the highest value for the year of 14,9% in October.

South African Revenue Service's 'volumetrics' as at May 2005:
- 14 600 employees
- 14 million returns processed
- 1,4 million corporate taxpayers
- 4,3 million individual taxpayers
- 573 876 value-added tax vendors
- 300 268 pay-as-you-earn employers
- 14 million passengers moving through customs
- 68 775 consignments stopped
- 1,4 million Southern African Customs Union movements
- 1 851 total seizures
- 998 221 export transactions and 1,7 million import transactions
- R21 billion collections over budget.

Source: Finance Ministry, Budget Vote, 2005

The banking industry

At the end of December 2004, 35 banks, including 15 branches of foreign banks and two mutual banks, were registered with the Office of the Registrar of Banks. Furthermore, 45 foreign banks had authorised representative offices in South Africa. By the end of December 2004, the banking institutions collectively employed 116 940 workers.

Four major groups dominated the South African banking sector, holding 82% of its assets:

- Amalgamated Banks of South Africa (Absa) Group Limited
- Standard Bank Investment Corporation Limited
- FirstRand Holdings Limited
- Nedcor Limited.

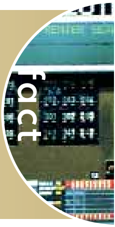
Industry-wide net income after tax declined to 0,4% of total assets in 2002. As a percentage of equity, industry-wide net income after tax decreased from 9,2% in 2001 to 5,4% in 2002.

In July 2005, Barclays, the third-largest British bank, paid R30 billion for a 53,9% stake in Absa. At the time, it was the biggest foreign direct investment yet in post-apartheid South Africa.

Insurance companies

As at 31 March 2004, 78 long-term insurers were registered. The total net premiums received and outstanding for 2003 (unaudited figures) amounted to R156,8 billion, while total assets amounted to R822,1 billion.

Online banking accounts reached the one million mark in South Africa for the first time at the end of 2003. According to the World Wide Worx research report, *Online Banking in South Africa 2004*, the number of online bank accounts in South African grew by 28% in 2003. The number of online bank accounts reached 1,04 million and was expected to increase by more than 30% during 2004.



Banknotes with improved security features went into circulation from 1 February 2005.

The upgraded banknotes retain the Big Five animal motif on the front and the economic sector themes on the back. There are, however, some design changes. Celebrating South Africa's democracy, the upgraded banknotes were the first to show the South African Coat of Arms and to use all 11 languages across the denominations.

The improved security features make it easier for the public to distinguish between good banknotes and counterfeit ones and further give the upgraded banknotes a distinct look. Examples are the shimmering gold band, visible on the back of the banknote when it is tilted, as well as the colour-changing ink on the number value on the front bottom right of the R50, R100 and R200 banknotes.

Development Bank of Southern Africa (DBSA)

The primary purpose of the bank is to promote economic development and growth, human resource development and institutional capacity-building. The bank's mandate is focused on infrastructure.

The DBSA estimates the scale of the impact of its funding operations using economic modelling techniques. According to these, the level of DBSA loan approvals in South Africa and the Southern African Development Community is projected to grow to R6 billion per year by 2013/14. This in turn should have an impact of creating a 127 000 jobs in South Africa, connecting 2,4 million households to one or more basic services and contributing R22,2 billion to the local economy. Toward this end, it plans to invest R45,6 billion (loans and equity finance) in infrastructure development and well over R1 billion in technical assistance, capacity-building grants and knowledge development/networking.