DEVELOPMENT POLICY LOAN
PROGRAMME LOAN – WORLD BANK

national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

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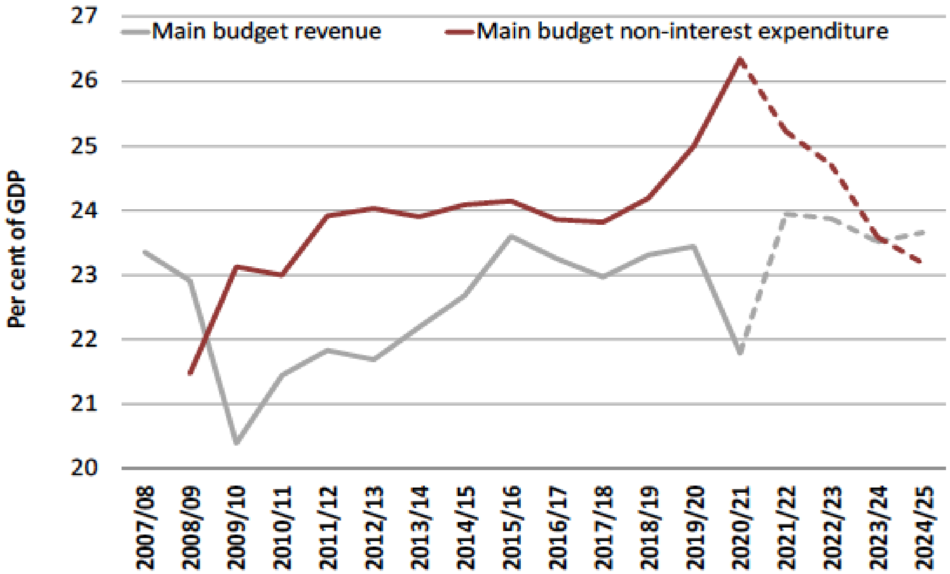
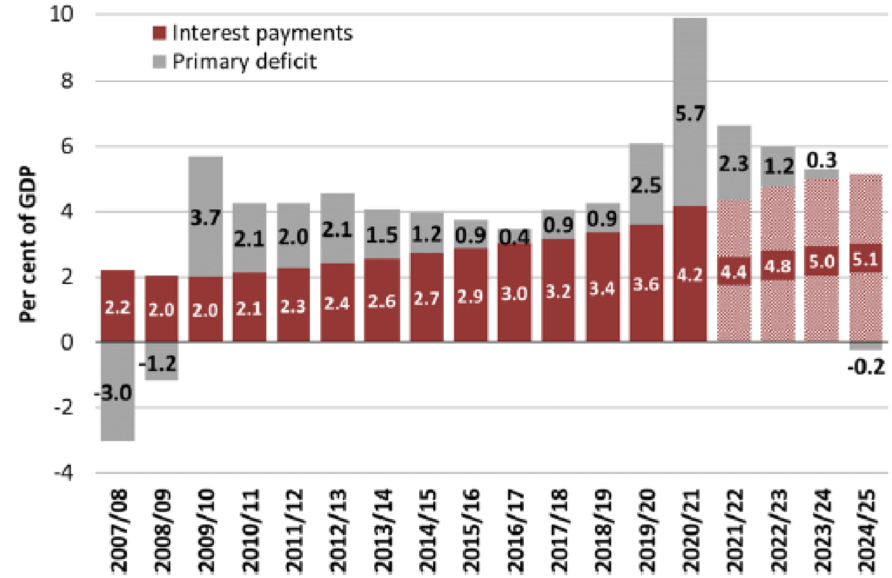
GOVERNMENT HAS TO FINANCE ITS DEFICIT, MATURING DEBT AND DEBT SERVICE COSTS





Excludes Eskom financial support and transactions in financial assets and liabilities

- South Africa's fiscal position was already weak prior to the economic crisis in 2022
- The COVID-19 pandemic lead to a historic economic contraction, an unprecedented widening of the budget deficit and a spike in debt stock.
- Interest payments now absorb a growing share of national resources, averaging nearly 5 per cent of GDP over the next two years.
- Reducing our funding costs, through concessional funding, can assist with narrowing the budget deficit, which is key to stabilizing the debt-to-GDP ratio

GROSS BORROWING REQUIREMENT AND FINANCING

Table 3.9 National government gross borrowing requirement and financing

R billion	2020/21 Outcome	2021/22 Revised	2022/23	2023/24	2024/25
			Medium-term estimates		
Gross borrowing					
Main budget balance	-550.6	-409.9	-380.4	-355.4	-349.7
Redemptions	-67.6	-65.2	-113.0	-154.7	-155.8
Domestic long-term loans	-53.2	-61.3	-97.3	-113.1	-120.4
Foreign loans	-14.4	-3.9	-15.7	-41.6	-35.5
Total	-618.3	-475.1	-493.3	-510.0	-505.5
Financing					
Domestic short-term loans (net)	95.3	–	54.0	53.0	52.0
Domestic long-term loans	523.4	285.3	381.8	373.0	369.4
Foreign loans	91.9	77.6	47.0	64.7	66.2
Change in cash and other balances	-92.4	112.2	10.5	19.3	17.9
Total	618.3	475.1	493.3	510.0	505.5

Source: National Treasury

- US$5.3 billion (R77.6 billion) will be raised from international finance institutions and capital markets to finance foreign currency commitments in 2021/22.
- The US$750 million loan is part of this amount – and since it is highly concessional, it helps to reduce the overall cost of our dollar denominated debt.

CONCESSIONAL FINANCING IS CHEAPER THAN NON-CONCESSIONAL FINANCE

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Non-concessional	Concessional
• Involves raising of debt in the capital markets. • The price is set by the market and cannot be negotiated. • Certain elements such as the countries credit rating is used to determine the risk premium to be charged on the debt. • A poor credit rating reflects a higher risk premium, and this prompts an increase in the interest. • A rising interest rate environment and market volatility have the potential to negatively impact raising of debt.	• Financing that is extended on terms substantially cheaper than market loans. • Concessional finance is provided by major financial institutions, such as development banks and multilateral funds. • The concessionality is achieved either through interest rates below those available on the market or by grace periods, or a combination of these. • Concessional loans typically have long grace periods (a period after the disbursement where no capital repayments are required).

SUMMARY OF THE WORLD BANK DEVELOPMENT POLICY LOAN

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- In July of 2020, the government of South Africa requested a budget support loan from the World Bank (WB) through their development policy financing program.
- The purpose of the financing was for government to respond to the sharp revenue losses and resultant budget deficit in the wake of the Covid-19 pandemic in early 2020 and to execute the plans put in place to mitigate the impacts of the COVID-19 pandemic on the economy and livelihoods of ordinary citizens.
- The program is a non-earmarked budget financing that supports policy and institutional reforms in developing countries to help achieve sustainable growth and poverty reduction.
- The program supports the countries own policy reform agenda, these would be policies or reforms that were publicly pronounced either through the budget or by the presidency as reforms government wants to institute.
- Due to its AAA rating, the WB can borrow at very low rates on international capital markets. The World Bank uses this leverage to offer their member countries lower interest rates than they would receive on the market.
- There are no conditions attached to the loan. It is a budget support loan to assist the government in dealing with the impact of Covid 19.
- The DPL is a low interest loan of US$750 million with a 13-year repayment period including a grace period of 3 years.
- The loan complements the Government's debt strategy to reduce its debt service cost and make use of cheaper sources of funding.

WHAT IS A DEVELOPMENT POLICY LOAN AND UNDER WHICH CONDITIONS ARE THEY DISBURSED?

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- DPLs are used by the World Bank (WB) to provide budget support to a member country's programme of policy and institutional reforms that promote inclusive growth and sustainable poverty reduction.
- They provide rapidly disbursing financing to help the borrowing country address actual or anticipated development financing requirements.
- In the case of South Africa, the US$750 million Development Policy Loan (DPL) supports South Africa's response to the COVID-19 pandemic.
- The World Bank was able to disburse the concessional funding because:
  - The South African Government's crisis response has been sound.
  - The Government took bold steps to contain the virus and mitigate its adverse socio-economic impact with the aim to protect lives, the poor and livelihoods.
  - The Government also used the COVID-19 crisis to tackle structural reforms including the launch of the Economic Reconstruction and Recovery Plan (ERRP) in 2020, which aims to deal with immediate actions toward economic recovery in the short term; and to rebuild and grow the economy ensuring sustainability, resilience and inclusion.

HOW WILL THIS DPL BE IMPLEMENTED AND WHAT CONDITIONS ARE ATTACHED?

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- In terms of implementation mechanism, DPLs follow the country policy process and are not ear-marked for specific projects but provide general budget support.
- This DPL will contribute towards addressing the financing gap stemming from additional spending in South Africa response to the COVID-19 crisis.
- It reflects priorities to modernize the country's social protection and health services and to improve delivery systems which will apply even beyond the pandemic.
- It also enhances financial sector stability, specifically the establishment of a deposit insurance scheme. It further supports South Africa's commitment to climate change.
- <u>There are no conditions attached to the loan</u>. It is a budget support loan to assist the government in dealing with the impact of Covid 19.
- However, before a country can receive a DPL, the WB must confirm that the country's macroeconomic policy framework is adequate.
- This assessment focuses primarily on the current and prospective macroeconomic policy framework rather than looking solely at recent economic outcomes.
- This can be therefore be viewed as a vote of confidence in South Africa's macroeconomic framework.

HOW DOES THIS LOAN FEATURE IN THE BROADER SCHEME OF SA'S BORROWING REQUIREMENT?

- The US$750 million loan contributes about one-ninth of the external financing needs and 2 percent of the total financing needs for 2021/22.
- The bulk of the financing for 2021/22 will be raised domestically.
- This is a small amount in the bigger scheme of SA's gross borrowing requirement, but it is an important step to reducing our funding costs.
- Other loans concluded with DFIs include:

Institutions	Terms (years)	Grace period[1] (years)	Amount billions
New Development Bank	30	5	US$1.0
International Monetary Fund	5	3	US$4.3
African Development Bank	20	5	R5.04
New Development Bank	30	5	US$1.0
New Development Bank	25	4.5	US$1.0

1. A period after the disbursement where no capital repayments are required

Source: National Treasury

END