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INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

PROGRAM DOCUMENT FOR A

PROPOSED LOAN

IN THE AMOUNT OF US\$750 MILLION TO

THE REPUBLIC OF SOUTH AFRICA

FOR THE

SOUTH AFRICA COVID-19 RESPONSE DEVELOPMENT POLICY LOAN

December 20, 2021

Macroeconomics, Trade And Investment Global Practice
Eastern and Southern Africa Region

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Republic of South Africa

GOVERNMENT FISCAL YEAR*April 1 – March 31***CURRENCY EQUIVALENTS**

(Exchange Rate Effective as of November 30, 2021)

South African Rands

US\$1.00 = 0.71387778

ABBREVIATIONS AND ACRONYMS

AfDB	African Development Bank	MTBPS	Medium-Term Budget Policy Statement
COVID-19	2019 Coronavirus Disease	NDB	New Development Bank
CPF	Country Partnership Framework	NDC	Nationally Determined Contribution
CODI	Corporation of Deposit Insurance	NT	National Treasury
DMRE	Department of Mineral Resources and Energy	PPP	Purchasing power parity
DPE	Department of Public Enterprises	RFI	Rapid Financing Instrument
DPME	Department of Planning, Monitoring and Evaluation	SARB	South African Reserve Bank
DSBD	Department of Small Business Development	SASSA	South African Social Security Agency
DTIC	Department of Trade, Investment and Competition	SCD	Systematic Country Diagnostic
ERRP	Economic Reconstruction and Recovery Plan	SDR	Special Drawing Rights
EVDS	Electronic Vaccination Data System	SME	Small and Medium Enterprise
FDI	Foreign Direct Investment	SOE	State-Owned Enterprise
FY	Financial Year	SRD	Social Relief of Distress
GDP	Gross Domestic Product	SSEG	Small Scale Embedded Generation
ICU	Intensive Care Units	TERS	Temporary Employer-Employee Relief Scheme
IFC	International Finance Corporation	UIF	Unemployment Insurance Fund
IFI	International Financial Institutions	WBG	World Bank Group
IMF	International Monetary Fund	R	South African Rand
MTEF	Medium-Term Expenditure Framework		

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REPUBLIC OF SOUTH AFRICA

SOUTH AFRICA COVID-19 RESPONSE DEVELOPMENT POLICY LOAN

TABLE OF CONTENTS

SUMMARY OF PROPOSED FINANCING AND PROGRAM	3
1. INTRODUCTION AND COUNTRY CONTEXT	5
2. MACROECONOMIC POLICY FRAMEWORK.....	9
2.1. RECENT ECONOMIC DEVELOPMENTS.....	9
2.2. MACROECONOMIC OUTLOOK AND DEBT SUSTAINABILITY	12
2.3. IMF RELATIONS	19
3. GOVERNMENT PROGRAM	19
4. PROPOSED OPERATION	23
4.1. LINK TO GOVERNMENT PROGRAM AND OPERATION DESCRIPTION	23
4.2. PRIOR ACTIONS, RESULTS AND ANALYTICAL UNDERPINNINGS	24
4.3. LINK TO CPF, OTHER BANK OPERATIONS AND THE WBG STRATEGY	35
4.4. CONSULTATIONS AND COLLABORATION WITH DEVELOPMENT PARTNERS	36
4.5. FUTURE LENDING.....	37
5. OTHER DESIGN AND APPRAISAL ISSUES	37
5.1. POVERTY AND SOCIAL IMPACT	37
5.2. ENVIRONMENTAL, FORESTS, AND OTHER NATURAL RESOURCE ASPECTS	39
5.3. PFM, DISBURSEMENT AND AUDITING ASPECTS.....	41
5.4. MONITORING, EVALUATION AND ACCOUNTABILITY	43
6. SUMMARY OF RISKS AND MITIGATION	44
ANNEX 1: POLICY AND RESULTS MATRIX	48
ANNEX 2: FUND RELATIONS ANNEX	51
ANNEX 3: DRAFT LETTER OF DEVELOPMENT POLICY.....	56
ANNEX 4: ENVIRONMENT AND POVERTY/SOCIAL ANALYSIS TABLE	62
ANNEX 5: DPO PRIOR ACTIONS AND ANALYTICAL UNDERPINNINGS	64

The South Africa Covid-19 Response Development Policy Operation (DPO) was prepared by a team led by Wolfgang Fengler (Lead Economist, EECF1) and Edouard Al-Dahdah (Lead Country Economist, EAWDR), together with Claudia Meek, Reshma Sheoraj, Benedicte Baduel, and Jorge Luis Alva-Luperdi. The core team also included Elizabeth Ninan Victoria Monchuk, Wendy Cunningham, Yi-Kyoung Lee, Thulani Matsebula, Ganesh Rasagam, Julian Casal, Marc Schrijver, Franz Gerner, Frederic Verdol, Sarah Moyer, Tandile Gugu Zizile Msiwa, Juanita Whitfield, Lolette Kritzingervan Niekerk, Kobina Egyir Daniel, Amina El Zayat, Uzma Khalil and Khalid Boukantar. The team is grateful for the guidance and support from Marie Françoise Marie-Nelly (Country Director, AFCS1), Asad Alam (Regional Director, EA1DR), Mathew A. Verghis (Practice Manager, EA1M2), Adamou Labara, Humberto Lopez, Asmeen Khan, Vinaya Swaroop, Sajjad Ali Shah, Sheila Braka Musiime, Bekele Debele, Paolo Belli, Francisca Ayodeji Akala, Thomas Buckley, Lisa Kaestner, Ronald Rateiwa, Gabriela Schmidt, Sebastien Dessus, Douglas Pearce, and Casey Torgusson. The team expresses its profound gratitude to the many people involved—in the Bank and on the side of the Government of South Africa—in putting this operation together, going well beyond the call of duty under exceptional operational circumstances and personal hardship.



SUMMARY OF PROPOSED FINANCING AND PROGRAM

BASIC INFORMATION

Project ID

P174246

Programmatic

No

Proposed Development Objective(s)

To protect the poor and vulnerable from the adverse socio-economic impacts of the COVID-19 pandemic, and to pave the way for a resilient sustainable recovery.

Organizations

Borrower: REPUBLIC OF SOUTH AFRICA

Implementing Agency: NATIONAL TREASURY

PROJECT FINANCING DATA (US\$, Millions)

SUMMARY

Total Financing	750.00
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DETAILS

International Bank for Reconstruction and Development (IBRD)	750.00
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INSTITUTIONAL DATA

Climate Change and Disaster Screening

This operation has been screened for short and long-term climate change and disaster risks

Overall Risk Rating

Substantial



Results

Indicator Name	Baseline	Target
Indicator 1: Number of people who receive SRD grants in response to the COVID-19 crisis, in millions	6 million people, in the first phase of the program from March 2020 to March 2021 (March 2021)	An additional 3.4 million people benefit from the second phase of the program, i.e., 9.4 million in total (June 2022)
Indicator 2: Number of workers who received benefits from the UIF-TERS	3.5 million workers (March 2021)	An additional 120,000 workers, i.e., 3.6 million workers in total (June 2022)
Indicator 3: Total value of SRD grants disbursed using digital application and verification procedures, in billion South African Rand.	R 19.5 billion (March 2021)	R 26 billion (June 2022)
Indicator 4: Number of people fully vaccinated and registered on EVDS	0 million (February 2021)	26.5 million (December 2022)
Indicator 5: Eligible deposits insured, in percentage	0 percent of deposits (November 2021)	80 percent of deposits (December 2022)
Indicator 6: Department of Forestry, Fisheries, and Environment (DFFE) presents Sectoral Emissions Targets (SET) for 5 key carbon-intensive sectors: Energy (DMRE), Transport (DoT), Trade and Industry (Dtic), Agriculture (DALRRD); and Water and Sanitation (DWS) to the respective line ministries	0 Key carbon-intense Sectoral Emissions Targets presented by DFFE to the respective line ministries (November 2021)	5 Key carbon-intense Sectoral Emissions Targets presented by DFFE to the respective line ministries (June 2023)
Indicator 7: Avoided CO ₂ emissions as a result of the shutdown of coal-fired power production, in tons	0 tons CO ₂ avoided (October 2021)	900,000 tons CO ₂ avoided (June 2023)
Indicator 8: Embedded Generation Capacity under 100 MW registered under NERSA, in MW	206 – 330 MW (October 2021)	1,500 MW (December 2022)



IBRD PROGRAM DOCUMENT FOR A PROPOSED LOAN TO THE REPUBLIC OF SOUTH AFRICA

1. INTRODUCTION AND COUNTRY CONTEXT

- 2. This proposed Development Policy Operation (DPO) of US\$750 million supports South Africa's response to the 2019 Coronavirus Disease (COVID-19) pandemic.** The program development objectives of this DPO are to protect the poor and vulnerable from the adverse socio-economic impacts of the COVID-19 pandemic, and to pave the way for a resilient sustainable recovery.
- 3. South Africa remains the epicenter of the COVID-19 pandemic in Africa.** As of early December 2021, the country has the highest number of infections on the continent. The number of COVID-19 cases had stabilized around 500 per day until the third week of November 2021 when it suddenly spiked. The Minister of Health subsequently announced the discovery of a new variant, Omicron, on November 25th 2021 which has become the dominant strain. As of November 2021, 88 per cent of confirmed cases were of the Omicron variant, with the Delta variant only comprising 11 per cent. South Africa reported almost 3 million cases of COVID-19 infections and 90,000 deaths, with 2.85 million people recovered from the disease. The number of people with compromised immunity due to the high prevalence of HIV/AIDS (human immunodeficiency virus/ acquired immunodeficiency syndrome) makes South Africa more vulnerable to the COVID-19 pandemic.
- 4. The socio-economic impact of the crisis has been severe.** Even before the pandemic, the unemployment rate was elevated, at 29 percent, with youth unemployment at 56 percent. Despite the Government's COVID-19-related efforts to protect livelihoods, unemployment increased to 34 percent by July 2021, with youth unemployment reaching 64 percent. During the initial months of the pandemic, 2.2 million South Africans lost their jobs and, by the end of 2020, less than 40 percent of these jobs had been recovered. One-quarter of South Africans are currently living in extreme poverty. If the COVID-19 shock had not been mitigated by social protection and government relief grant programs, an additional 2.8 million people would have been at risk of falling into poverty in 2020. However, the Government's strong COVID-19 social protection response package has likely cushioned two-thirds of them against this impact, thereby protecting 1.9 million people from falling into poverty.
- 5. The COVID-19 pandemic hit South Africa after a decade of economic stagnation, resulting in macroeconomic vulnerabilities.** South Africa has been struggling with persistent low growth, which has now been compounded by the COVID-19 crisis. After contracting by 6.4 percent in 2020, South Africa is experiencing a moderate recovery with a projected rebound of 4.6 percent in 2021. Public debt is expected to grow to 71.2 percent of gross domestic product (GDP) in 2021, with a fiscal deficit of 11.5 percent of GDP in 2020. In the context of rising fiscal deficits and higher debt levels, the Government has committed to restoring fiscal sustainability and stabilizing public debt. Most of this debt is in local currency, but a large share is held by foreigners. South Africa also has a deep and liquid financial sector, which remains well-capitalized. The increase in Omicron-driven Covid-19 cases, potentially stricter lockdown measures and foreign tourist cancellations will have a negative effect on the South African economy adding to the downside pressure on GDP potentially reversing progress made during the year. In addition, this adverse effect could spill over into economic activity in the first quarter of 2022, depending on the length and severity of the fourth wave in South Africa.



- 6. The Government has taken bold steps to contain the virus and mitigate its adverse socio-economic impact.** The Government's response to the crisis has been scientific and evidence-based, aiming to protect lives while also supporting livelihoods. At the start of the crisis, the Government put in place a massive economic relief package equivalent to 10 percent of GDP, on top of which it has added complementary measures in 2021. These measures had three main components: protecting lives, protecting the poor and protecting livelihoods. More details about Government's measures are described in Sections 3 and 4.
- 7. The Government has also used the COVID-19 crisis to tackle structural reforms.** An important step was the launch of the Economic Reconstruction and Recovery Plan (ERRP) in 2020, which sets a path for further structural reforms. The ERRP has two aims, namely: (i) to deal with immediate actions toward economic recovery amid the COVID-19 pandemic; and (ii) to rebuild and grow the economy ensuring sustainability, resilience and inclusion.
- 8. Since the ERRP's launch, the Government has made progress in advancing key reforms to support a sustainable recovery.** In 2021, there have been major breakthroughs in three reform areas, which are also supported by this operation. First, the Government adopted new policies in digitizing social protection and health, which creates new efficiencies and better governance in the social sectors. Second, the Government increased the licensing threshold for embedded electricity generation from 1 MW to 100 MW, which will enable firms to generate their own electricity instead of relying solely on Eskom, the state-owned energy utility. This will remove a significant obstacle from investment in embedded generation projects. Third, the National Climate Change Bill was approved by the Cabinet in September 2021, which provides a legal instrument for the implementation of the National Climate Change Response Policy, and a transitional arrangement for South Africa to move toward a lower carbon and climate-resilient economy. The November 2021 Medium-Term Budget Policy Statement further sets out progress made in advancing ERRP including measures to boost household savings by increasing preservations before retirement and to increase flexibility through partial access to retirement funds. To boost tourism and attract skills, the completed e-Visa system will be rolled out to 15 countries by March 2022. In the water sector, legislative drafting and financial modelling have been done to establish a National Water Resources Infrastructure Agency responsible for improving the management of bulk water resources.
- 9. The Climate Change Bill paved the way for a landmark agreement with international partners to help South Africa decarbonize.** On November 2, 2021, at the United Nations Climate Change Conference (commonly referred to as COP26) in Glasgow, the United Kingdom, the United States, Germany, and the European Union committed to mobilize an initial R 131 billion (US\$8.5 billion) over the next three to five years. These partners would support the implementation of South Africa's revised Nationally Determined Contribution (NDC) and ensure access to finance for the decommissioning and repurposing of coal-fired power stations. More details are set out in Sections 3 and 4 of this document.
- 10. The COVID-19 crisis has paved the way for a new relationship between South Africa and the international community.** For the first time in the history of South Africa, the supplementary budget for FY2020 made provisions for US\$7 billion in external financing from international financial institutions (IFIs). The Executive Board of the International Monetary Fund (IMF) approved a US\$4.3 billion loan under its Rapid Financing Instrument (RFI) on July 27, 2020. The Executive Board of the African Development Bank (AfDB) approved a US\$300 million loan in July 2020. The New Development Bank (NDB) has disbursed US\$2 billion in support



of the Government's COVID-19-related responses. In 2020, US\$1 billion was disbursed for health-care programs and in 2021 US\$1 billion disbursed for economic recovery programs. This first World Bank DPO contributes US\$750 million, about one-ninth of the external financing needs and 2 percent of the total financing needs for FY2021. The bulk of the financing for the FY2021 budget, about US\$34 billion out of a total of US\$42 billion, will be raised domestically.

- 11. The proposed budget support is anchored in the World Bank Group Country Partnership Framework FY2022–FY2026.** The World Bank Group's (WBG) Country Partnership Framework (CPF P167262) FY2022–FY2026 which was approved by the WBG Board in July 2021, seeks to help South Africa address its low growth trap by stimulating investment and job creation, and addressing key longstanding structural constraints to sustainable and inclusive economic growth and development. The CPF has been designed with significant flexibility to take into account the uncertainties related to the COVID-19 pandemic, including support through IBRD lending. The Government has now expressed interest in requesting development policy financing, as well as financing for vaccine purchases and the decommissioning of the Komati coal-fired power station. For the WBG, this DPO represents an opportunity to shift from an essentially knowledge-based engagement, with financing coming primarily from the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA), to policy-based IBRD lending to the Government to mitigate the immediate adverse socio-economic impacts of the COVID-19 pandemic and help address longstanding structural constraints.
- 12. This DPO is the first-ever budget support operation the WBG has undertaken in South Africa.** It is only the fifth lending operation since the WBG reengagement with South Africa in 1995 at the onset of democracy. Previous WBG borrowing has so far been to state-owned enterprises (SOEs), which are legally independent entities. The DPO builds on a strong track record in high quality analytical work, including a well-received Systematic Country Diagnostic (SCD), the trust recently gained through an inclusive WBG CPF process, and an investment loan to the SOE, Eskom which closed in June 2021.

Box 1: The COVID-19 pandemic's impact in South Africa

Three large waves of infection of the COVID-19 pandemic have been experienced in South Africa between March 2020, when the index case was detected, and October 2021. During each of these waves, the Government took decisive steps to contain the further spread of the disease, including the declaration of a national state of disaster, and full and partial national lockdowns. The response measures have allowed the country to prepare the health system for early detection, testing and clinical management. While the Government has intensified vaccinations against the COVID-19 virus nationwide, the likely trajectory of the pandemic remains highly uncertain. In all three waves experienced to date, four provinces have had higher infection rates, namely Gauteng, the Western Cape, Kwazulu-Natal and the Eastern Cape. The Government adopted a risk-adjusted approach to reopening the economy with five alert levels of lockdown, with Level 5 being the most restrictive and Level 1 the most relaxed. In mid-October 2021, South Africa eased its lockdown measures to Level 1, allowing for more economic activity and social interactions. However, South Africa is entering the fourth wave, with many provinces having sustained increase in COVID-19 cases since mid-November. The recently discovered Omicron variant has become dominant in South Africa and is likely to lengthen the current wave.



- 13. This first DPO for South Africa sets the stage for a deeper reform engagement with the WBG.** The proposed operation seeks to provide South Africa with relief from its most serious economic crisis in 90 years and assists in restructuring its economy while preparing the country for a resilient recovery. Its design and the selection of prior actions recognize this opportunity by balancing ambition with feasibility. It mirrors the components of the Government's ERRP and the three stages of the World Bank's COVID-19 Crisis Response Approach Paper. The operation consists of two pillars with a total of eight prior actions. The first pillar consists of measures to protect the poor and modernize social welfare. The second pillar focuses on accelerating a resilient and sustainable recovery. More details are set out in Chapter 4.
- 14. This specific operation leverages two main areas of South African strength to mitigate the effects of the COVID-19 crisis.** The first area of strength is social protection. South's Africa system of cash grants is one of the most comprehensive, well-targeted and cost-efficient in the developing world; nearly all poor households receive social assistance support with little leakage to the non-poor population (5 percent compared with 14.4 percent globally). In the face of the COVID-19 pandemic, South Africa can leverage its social protection system quickly and efficiently to provide immediate relief to those who have been hardest hit by lockdowns and the ensuing economic downturn. The second area of strength is the policy buffers that South Africa has built up over time: its domestic financial sector is resilient and its capital markets deep; its floating exchange rate can absorb shocks effectively; inflation is kept under control; and public debt is largely domestic and in the local currency, with long maturities.

Box 2: The role of IFC in South Africa

Private sector investment is essential to reignite growth and tackle South Africa's inequality. In line with the CPF, IFC's focus areas in the country includes sustainable infrastructure, inclusive finance, agribusiness, regional integration, and the education sector. Over the past five years, IFC's portfolio has grown from little more than US\$700 million in FY2016 to US\$2.3 billion in FY2021, when IFC committed a record US\$700 million. However, constraints to private sector investment remain high, and include challenging macroeconomic and business environments, barriers that reduce competition in many sectors, and embattled SOEs, the inefficiencies of which adversely affect the entire economy, thus depressing competitiveness and investments in other sectors. The impact of the COVID-19 outbreak, however, may represent an opportunity to reset parts of the economy and promote more competition.

This DPO is critical to promote reforms, such as those targeted to increase competition and strengthen the resilience of the financial sector and reduce the regulatory burden on businesses, particularly MSMEs. The prior actions in this DPO and some of the initiatives mostly related to MSMEs recently launched by IFC complement each other. They would pave the way toward greater private sector investment and IFC engagement in South Africa—estimated at US\$3.4 billion for a FY20–24 program in a High Reform scenario. Those IFC initiatives include: (i) a SME Study and Survey to help financial institutions understand the challenges faced by SMEs; (ii) a SME Advisory engagement with a second-tier bank to help strengthen the SME proposition; (iii) COVID-19-focused credit lines with some of the largest commercial banks in South Africa; (iv) support the establishment of the first Distressed Asset Recovery Program (DARP) in the country that will help viable SMEs and small corporates facing economic difficulties, mainly due to the prevailing lack of (re)financing capital, and facilitate restructuring of these businesses during their recovery; (v) provision of just-in-time COVID-19 impact analysis for the tourism sector based on a survey of 1,610 respondents; (vi) sharing with the Investment Promotion Agency a "COVID-19 FDI risk assessment" tool to assess the risks and impact on FDI by sector and how to re-focus the investment strategy led by Invest SA; and (vii) support to Ekurhuleni municipality on long-tenor bond issuance to support Infrastructure and related technical assistance.

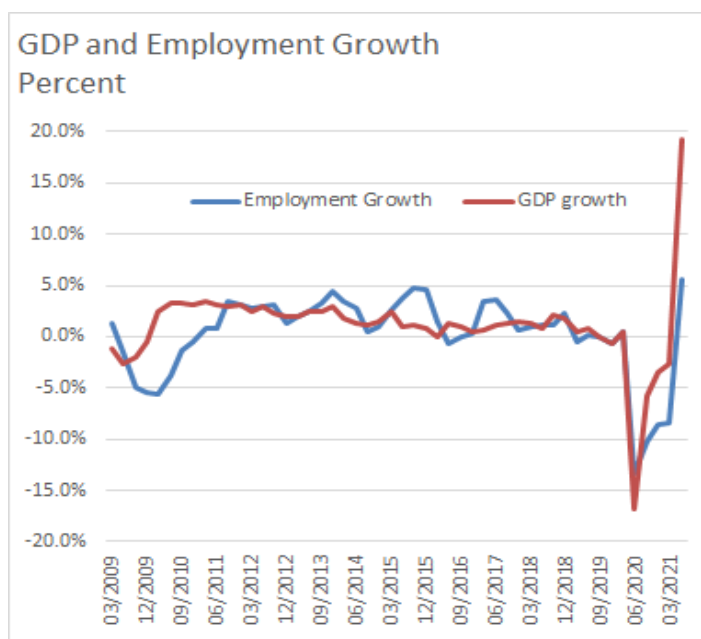


2. MACROECONOMIC POLICY FRAMEWORK

2.1. RECENT ECONOMIC DEVELOPMENTS

- 15. The South African economy has started to recover from the crisis in 2021, supported by a favorable global environment.** Recovering from last year's low base as a result of the strict COVID-19-related lockdown, GDP increased by 7.5 percent in H1 2021 compared with H1 2020, with mining and manufacturing posting the strongest recoveries (25.2 and 17 percent, respectively). On a quarterly basis, real GDP increased by 1 percent in Q1 and by 1.2 percent in Q2. Finance, mining, trade and transport were the main drivers of growth on the production side. On the demand side, household consumption, changes in inventories (lower destocking), and net exports (Q2) drove the increase, while investment continued to lag.
- 16. Nevertheless, the impact of the COVID-19 pandemic is still visible, especially on social outcomes.** In 2020, the economy contracted by 6.4 percent, with broad-based effects across sectors. As a result, the toll on jobs was severe and has been persistent, despite the rebound in activity. In net terms, there were still 1.4 million fewer jobs in June 2021 than in March 2020. This is more than twice the number of jobs losses that South Africa experienced during the 2008 global financial crisis. The unemployment rate has continued to increase, reaching 34.4 percent at end-June 2021 (Figure 1). Even with the relatively strong social assistance system, poverty has increased, reversing years of progress. The poverty rate is estimated to have reached 59.8 percent in 2020 based on the upper middle-income country poverty line (US\$5.50 in 2011 purchasing power parity (PPP)) compared to 57.7 percent in 2019.

Figure 1: The recovery in jobs is lagging despite the dynamic growth rebound



Source: STATSA.



- 17. Civil unrest in July 2021 led to significant economic damage.** Combined with political tensions over the imprisonment of former President Zuma, social hardship translated into civil unrest and looting in July, leading to significant damage (destruction of retail and warehouse facilities, disruption of major road transport corridors, etc.). In the aftermath of these events, President Ramaphosa cited that the economic cost of the unrest, based on property owners' estimates, could amount to R 50 billion (0.9 percent of GDP). This led the Government to reinstate the COVID-19 Social Relief of Distress (SRD) grant until the end of this fiscal year (i.e., end-March 2022).
- 18. The growth rebound in 2021 has translated into improved tax revenues, supporting the reduction of the deficit.** Revenue collection has outperformed budget forecasts so far in 2021, amounting to 43.5 percent of the projected budget outcome for the full year over April–August. This was due to significant increases in corporate income tax (CIT), personal income tax (PIT), and value-added tax (VAT). CIT collection partly reflected provisional payments from mining companies, which have seen an increase in their profits due to higher global commodity prices. This has allowed the Government to announce spending increases for R 38 billion following the July unrest, without affecting the budgeted consolidation path. Last year the overall deficit doubled, reaching 11.5 percent of GDP and public debt increased to 71 percent of GDP. The Government has been financing the deficit mostly through the issuance of domestic debt. However, it has also tapped into multilateral financing for, US\$5.6 billion in FY2020/21, and US\$1 billion so far, this fiscal year.
- 19. Driven by weak imports and favorable export prices, the current account has registered a large surplus since 2020.** Terms of trade have been improving since H2 2020 and are now more than 20 percent above their end-2019 level, driven by favorable commodity export prices. South Africa's trade surplus has surged to record levels so far in 2021. The trade surplus reached 8.6 percent of GDP in H1 2021. Exports increased by 21.1 percent annually over January–August, while imports rose by 27.9 percent over the same period. Precious stones (28.2 percent of the total value of exports), mineral products (24.7 percent), transport equipment/vehicles (9.6 percent) and base metals (8.7 percent) accounted for most exports. The current account surplus was 2.0 percent of GDP in 2020, the first surplus in 18 years.
- 20. South Africa has benefited from favorable global financial market conditions and robust terms-of-trade gains in 2021.** In the context of improving terms of trade, current account surpluses, and robust mining activity, the South African rand and stock market indices have rebounded significantly from their pandemic-induced lows, while market interest rates have reverted to pre-pandemic levels, despite persistent net portfolio outflows. However, the domestic yield curve remains steep amid elevated public debt levels. Globally, increasing certainty that the US Federal Reserve will begin tapering its bond purchase program in the coming months has impacted risk appetite toward emerging markets. Risk sentiment remains sensitive to the extent that the more transmissible delta variant has hurt the pace of the global recovery and there are signs of persistent upward pressure on global inflation. But South Africa has remained broadly resilient.
- 21. In contrast with many emerging peers, the South African Reserve Bank (SARB) has been able to maintain its accommodative monetary policy stance so far in 2021 to support the recovery.** Inflationary pressures have remained contained so far in 2021, with CPI inflation averaging 4.2 percent over January–August. Core inflation in particular has remained broadly stable. Actual inflation and inflation expectations remain well



within the SARB's 3 to 6 percent target range, although market expectations and the SARB's own modeling signal upward pressures in the near future. This has allowed the SARB to maintain its policy stance unchanged and to keep the repo rate at 3.5 percent since July 2020. This contrasts with other emerging market central banks, which had to start hiking policy rates amid inflationary pressures, despite persistently uncertain recoveries (Brazil, Chile, the Czech Republic, Hungary, Mexico, Peru, the Russian Federation, etc.). International reserves have increased since March 2021 and stood at US\$57.1 billion at end-September, partly boosted by the IMF's SDR allocation of US\$4.3 billion in August.

22. The financial sector is well-capitalized and liquid. Banks remain well-capitalized (17.9 percent as of June 2021), despite lower profitability in 2020. The SARB relaxed its guidance on the payment of dividends by banks and proposed returning bank capital adequacy requirements to their pre-COVID-19 level by 2022. The Loan Guarantee Scheme ended in July and the SARB will phase out the treatment of restructured credit agreements for borrowers who have been affected by the COVID-19 pandemic, without the need to hold additional capital against those loans, by April 2022. Nevertheless, loan growth remains stagnant (0.2 percent annually in June 2021) and driven by mortgages.

Table 1. Economic and financial indicators, 2020–23

	2020e	2021p	2022p	2023p
National income and prices	Annual percentage change, unless otherwise indicated			
Real GDP	-6.4	4.6	2.1	1.5
Consumer price inflation	3.3	4.2	4.5	4.5
Fiscals accounts	Percent of GDP, unless otherwise indicated			
Revenues and Grants	25.2	25.9	26.0	26.2
Tax revenues	22.9	23.5	23.6	23.7
Non-tax revenues	2.3	2.4	2.4	2.5
Expenditures	36.7	33.7	32.0	31.3
Interest payments	4.4	4.4	4.6	5.0
Non-interest expenditure	32.4	29.3	27.4	26.3
General Government Balance	-11.5	-7.8	-6.0	-5.1
Total Public debt	71.0	71.2	74.8	77.1
Balance of Payments	Percent of GDP, unless otherwise indicated			
Current Account Balance	2.0	3.7	0.6	-0.5
Trade Balance	4.4	7.2	4.3	2.7
Exports (f.o.b.)	27.4	30.1	28.8	28.3
Imports (f.o.b.)	23.0	22.9	24.5	25.7
Gross Reserves (US\$ million)	55,013	58,813	58,813	58,813
Other memo items				
GDP nominal (US\$ millions)	335,133	422,941	421,218	435,935

Sources: World Bank and IMF staff calculations and estimates based on official data provided by the authorities. Fiscal data reflect the consolidated budget.



2.2. MACROECONOMIC OUTLOOK AND DEBT SUSTAINABILITY

Short-Term Outlook

- 23. GDP growth is projected to rebound to 4.6 percent in 2021, supported by a more favorable global environment.** On the domestic front, the normalization of economic activity (despite a third wave of COVID-19 infections over the winter months July–August) and base effects will mean higher GDP growth. Continued progress in rolling out vaccines (as of end-October 20.8 percent of the population has been fully vaccinated and another 5 percent have received a first dose) will also positively support the recovery, and help limit the health and economic impact of potential future waves of infections. Globally, higher growth in South Africa's trade partners and more favorable global commodity prices will strengthen the contribution of the external sector to growth.
- 24. Fiscal performance in FY2021/22 is expected to be stronger than anticipated in the 2021 budget review, supported by higher revenue collection and GDP.** Despite higher spending than budgeted following the announced package of R 38 billion to address the July unrest, the fiscal deficit is expected to decrease to 7.8 percent of GDP this year, supported by higher-than-expected revenues (projected to be R 100 billion higher). Higher revenue collection has also reduced the Government's borrowing requirement this year. Weekly primary auction sizes (Treasury bonds, Treasury bills and inflation-linked bonds) have totaled R 16.8 billion since May, down from a peak of R 21.6 billion in FY2020/21. Public debt is projected to increase to 71.2 percent of GDP in 2021. More dynamic growth and the rebasing of national accounts, which led to an upward revision of GDP by 10 percent, have also contributed to improved fiscal and debt ratios.

Table 2: Operations of the consolidated government budget, 2020–23

	2020e	2021p	2022p	2023p
		Percent of GDP, unless otherwise specified		
Overall Balance (cash basis)	-11.5	-7.8	-6.0	-5.1
Primary balance	-7.1	-3.4	-1.3	-0.1
Total Revenue and Grants	25.2	25.9	26.0	26.2
Tax revenues	22.9	23.5	23.6	23.7
Non-tax revenues	2.3	2.4	2.4	2.5
Expenditure	36.7	33.8	32.2	31.4
Current expenditure	32.6	29.5	28.5	27.8
Wages and compensation	11.5	10.4	10.1	9.9
Goods and services	4.9	4.4	4.3	4.2
Transfers	11.9	10.3	9.5	8.8
Interest	4.4	4.4	4.6	5.0
Capital expenditures	2.5	2.6	2.8	2.8
Other expenditures	1.6	1.6	0.9	0.7

Sources: World Bank staff calculations/estimates based on official data on the consolidated budget.



25. The current account is set to record another surplus in 2021, driven by the very favorable trade dynamics.

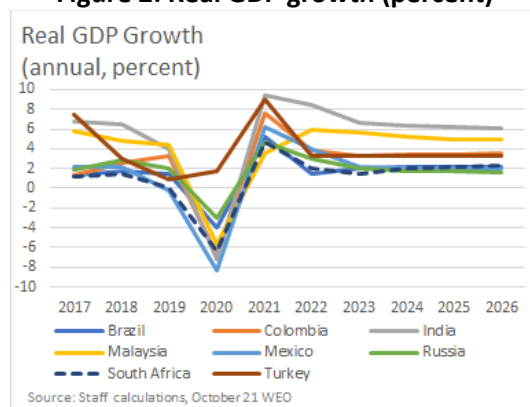
Commodity prices are expected to remain well above their pre-pandemic levels this year, with several reaching all-time highs in international markets. In this context, the current account is projected to reach a surplus of 3.7 percent of GDP this year.

26. The SARB faces fewer policy trade-offs than most emerging peers. Inflation expectations are stable and anchored inside the target band, projected to average 4.2 percent in 2021. The SARB sees inflationary risks from higher domestic import tariffs, rising wage demands and global oil prices. Nonetheless, given structurally weak investment and growth, the impact of accommodative monetary policy in stimulating the economy may be limited. The SARB also has room to mitigate market liquidity stress if global risk aversion rises—among other measures, it can again expand its secondary market purchases of government securities.

Medium-Term Outlook

27. Growth prospects beyond 2021 are still hampered by domestic constraints and uncertainties related to the pandemic. GDP growth is projected at 2.1 percent in 2022 and 1.5 percent in 2023. Despite the growth rebound in 2021, real GDP is not expected to reach its 2019 level before early 2023. Constraints such as weak investment, electricity shortages, and transport and logistical costs and bottlenecks will continue to weigh on economic activity compared with other emerging countries (Figure 2). Private sector investment has remained depressed so far. It is unclear if household consumption will remain robust in a context of weak labor markets and limited fiscal support once savings return to pre-pandemic levels. Finally, the long-term impact of the pandemic on sectors such as tourism, aviation and hospitality could still hamper the growth rebound. In this context, structural reforms are needed to boost private sector competitiveness and productivity, and support higher growth and job creation.

Figure 2: Real GDP growth (percent)



28. Recent progress on structural reforms should gradually support growth over the medium term. Planned reforms, described in the Economic Recovery and Reconstruction Plan and Operation Vulindlela, including those supported by this Development Policy Operation, can contribute to stronger growth over the medium term. GDP growth is projected to reach 2.3 percent annually in 2026. Several steps have been taken in 2021. Amendments to the Electricity Regulation Act were passed in October to increase the licensing



threshold for embedded electricity generation from 1 MW to 100 MW. Long called for by business organization, this reform should ease the constraint on electricity supply and improve business confidence in the short term and raise economic potential in the medium run. Last July, President Ramaphosa also announced the corporatization of the Transnet National Ports Authority (TNRA) and its establishment as an independent subsidiary of the state-owned port operator Transnet. The Government also aims to reorient public expenditure towards investment, notably in infrastructure, and catalyze additional private resources. The 2021 Budget, presented last February, plans to contribute R18 billion over FY2021-FY2023 to the Infrastructure Fund created in 2020. Three projects have started in student housing, digital and water infrastructure. The eVisa system has also been finalized and is expected to be rolled-out by March 2022 to promote tourism. Other announcements, such as the opening of South African Airways (SAA) to private capital, and the opening of ports to private investment are other steps in the right direction. However, additional reforms and further progress on planned reforms (e.g., visas schemes for skilled workers, spectrum auction, etc.) will be needed to increase the economy's potential and improve social outcomes.

29. Based on the Government's plans, fiscal sustainability will be gradually restored over the medium term.

The Government recognizes that the trajectory of fiscal policy and debt had been increasingly unsustainable before the COVID-19 crisis and has worsened during the pandemic. As the COVID-19 shock subsides and the recovery gathers speed, the Government plans to withdraw COVID-19 relief measures, contain expenditure commitments, and improve the impact of fiscal policy on economic and social outcomes (the fiscal multiplier) over the medium term. The Government's strategy rests on improving the composition of public expenditure by rebalancing it towards investment and development. As laid out in the 2021 Medium-Term Budget Policy Statement (MTBPS), this requires reducing fiscal deficits and debt to gradually lower the interest payment bill and reorient resources towards non-interest development spending. According to the 2021 Budget Review, capital spending is budgeted to be the fastest-growing category among non-interest expenditure, increasing by 12.5 percent annually over FY2021/21-FY2023/24 (excluding COVID-19 related spending), after contracting by 6.1 percent per year over FY2015/16-FY2019/20. The consolidation of overall spending is based primarily on expected improvements in social security fund balances once the Temporary Employee/Employer Relief Scheme (TERS) is withdrawn and on restraining the growth of the public sector compensation bill (through adjustments to wage increases and nonwage benefits, along with a reduction in headcounts through attrition). Other categories are also contained, such as social grants, which are budgeted to increase by less than inflation over the Medium-Term Expenditure Framework (MTEF). The budget includes transfers to key SOEs (Eskom, Land Bank, SAA) but no additional commitments have been announced in the MTBPS. However, the Government stressed persistent high risk associated with SOEs' weak financial health and their reliance on continued support from the government and noted that further SOEs support, if needed, would have to be funded through budget reallocations.

30. The World Bank projects that the budget deficit will decrease to 7.8 percent in 2021 and further to 4.4 percent by 2026. The primary balance (the budget balance excluding interest payments) is projected to improve by 3.4 percentage points of GDP in 2021 with the phasing-out of the COVID-19-related measures, and to reach a surplus by 2024. These forecasts assume that the Government's plan is broadly implemented. However, the primary balance improves at a slightly slower pace reflecting more conservative assumptions on the public sector wage bill, and social transfers due to anticipated political economy challenges, as well as a more conservative medium-term growth outlook.



31. Anchored in the Government's fiscal plans, public debt is assessed as being sustainable. Public debt, measured as National Government debt, is estimated to have reached 71 percent of GDP in 2020. Based on the projected fiscal path, public debt is forecast to increase to 71.2 percent of GDP in 2021 and to stabilize at 79.5 percent of GDP in 2026 (Figure 3). In this context, the decrease in the debt-creating flows will be driven by improvements in the primary balance (Figure 4). As noted above, the improvement in the primary balance will be driven, in the short term, by the phasing out of most of the COVID-19-related expenditures as well as booming revenue. In the medium-term, further consolidation – associated with reprioritization to safeguard growth and development spending – and structural reforms will support the primary balance trajectory. However, as Figure 3 highlights, a failure to implement the Government's plan, resulting in the primary deficit following its historical path or remaining constant, would not allow a stabilization of public debt over the forecast horizon.

Figure 3: Public debt trajectories

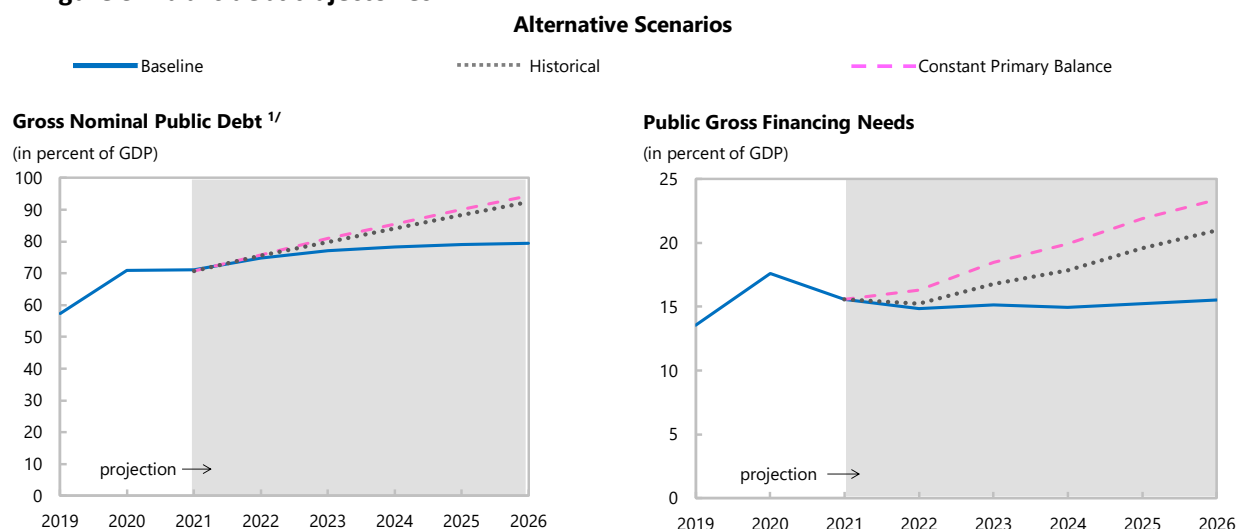
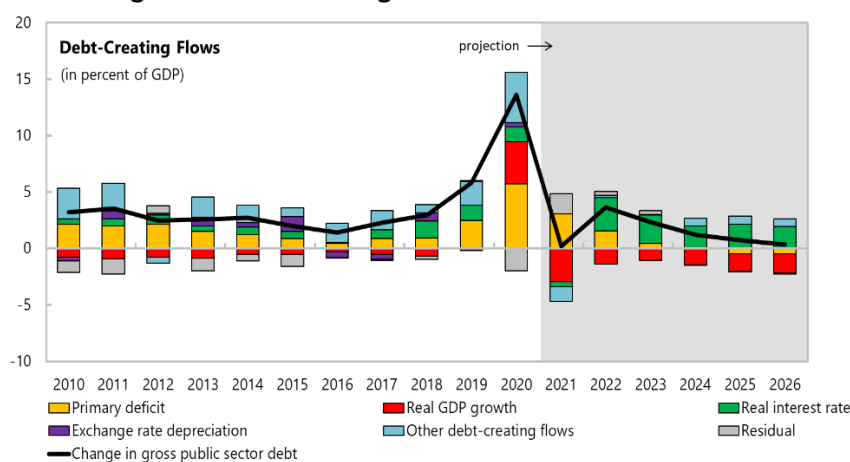


Figure 4. Debt-Creating Flows – Baseline scenario



Source: World Bank Group estimates



32. Public sector financing needs are expected to remain high until 2026. They are projected to decrease from 19.1 percent of GDP in 2020 to 16.1 percent of GDP this year, and further to 14.9 percent by 2023. Fiscal revenues outperformed estimates in FY2020/21, and weekly issuances were left unchanged for most of the fiscal year, resulting in the National Treasury accumulating cash balances of about R 91 billion instead of a projected decrease of R 48 billion. The National Treasury now plans to use these cash balances over the 2021–23 period to reduce the borrowing requirements (by 2 percent of GDP in 2021, and then 0.3 and 0.2 percent of GDP in 2022 and 2023, respectively). The borrowing requirements will continue to be mainly financed domestically with long-term debt instruments. SOEs' financing needs are also projected to average around R 55 billion annually over the next three years.

Table 3: Financing requirements and sources, 2020–23

	2020e	2021p	2022p	2023p
	Percent of GDP			
Financing need	19.1	16.1	14.7	14.9
Main Budget Deficit	9.9	7.3	6.1	5.3
Other consolidated government *	1.6	0.5	-0.1	-0.2
Domestic Short Term Loans Amortizations	6.5	7.4	7.2	7.6
Medium and Long Term Loans Amortization	1.2	1.0	1.6	2.2
Domestic	0.9	0.9	1.4	1.5
Foreign	0.3	0.1	0.2	0.7
Financing sources	19.1	16.1	14.7	14.9
Use of cash balances	-1.6	1.8	0.4	0.4
Reduction in other consolidated government net assets position	1.6	0.5	-0.1	-0.2
Domestic Short Term	8.2	7.5	8.0	8.4
Domestic Medium and Long Term	9.4	5.6	5.8	5.4
External	1.7	0.7	0.7	0.9
o/w World Bank			0.2	
o/w AfDB, IMF, NDB	1.7	0.2		

Source: WB staff estimates

* includes provinces, public entities and social security funds

Economic Risks

33. The evolution of the pandemic globally and domestically presents risks for the growth trajectory. The pace and efficiency of the vaccine rollout worldwide and the impact of vaccines on global growth will affect South Africa through their combined impact on external demand and commodity prices. The rollout and efficiency of vaccines will also determine the potential for recovery of sectors such as tourism and air transport. Supply side bottlenecks and inflation pressures globally will also impact global growth with implications for South Africa's trajectory. Domestically, new waves of COVID-19 infections, if they translate into renewed restrictions on economic activity, could hamper the growth rebound, job creation and, ultimately, South African's income prospects.

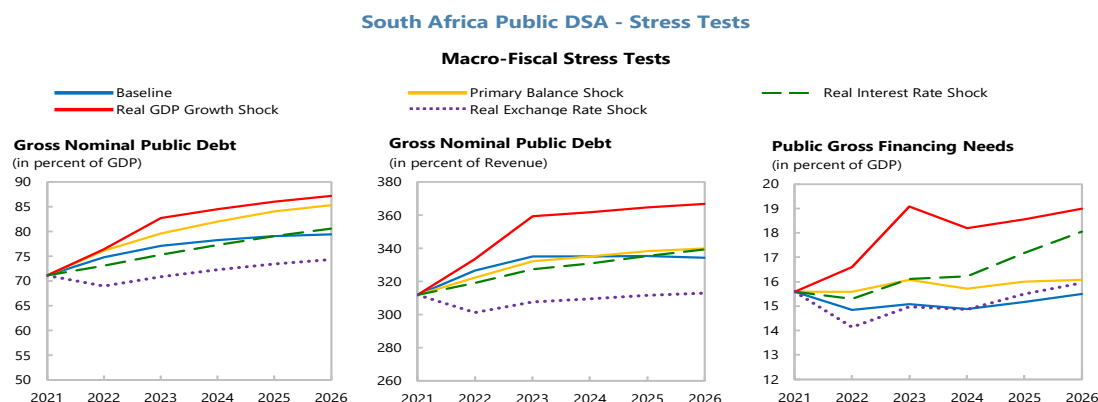


- 34. Significant fiscal slippages would put debt sustainability at risk.** In the short term, a longer-than-expected pandemic and associated economic crisis would increase pressure on health and social expenditures. The 2021 Budget Review identifies a departure from compensation budget ceilings as a major risk to the fiscal and debt trajectories and the MTBPS has allocated R20.5 billion to reflect to wage agreement this year, highlighting that public compensation will remain a risk on the expenditure envelope going forward as no medium-term agreement has been reached yet. Pressures from other stakeholders (e.g., trade unions) or weak SOEs could compromise the Government's ambitious fiscal consolidation plan and put public debt stabilization efforts at risk. Finally, if the transitory revenue overperformance translates into new committed expenditures, it could worsen fiscal sustainability over the medium term. Discussions around strengthening the social safety nets will be reflected in the 2022 Budget. However, the MTBS notes that any new proposal should be consistent with the fiscal sustainability objective. Partly in anticipation of potential risks, the consolidated expenditure framework, as presented in the MTBPS has unallocated and contingency reserves for R20.1 billion in FY2022/23, R33.8 billion in FY2023/24 and R34.3 billion in 2024/25. Difficult tradeoffs and compromises with different stakeholders, as well as unforeseen expenditures from the pandemic or weak SOEs, may occur as was seen in the pre-COVID-19 period. Nonetheless, and despite the persistence of the pandemic, the Government has broadly maintained its policy commitments and it was able to limit growth in the public sector wage bill and transfers to SOEs in the FY2020/21 and FY2021/22 budgets. In this context, the Government's debt stabilization objective appears ambitious, but still attainable.
- 35. Other downside risks to public debt include lower-than-projected GDP growth, higher-than-expected interest rates, and contingent liabilities.** In the decade before the pandemic, GDP growth has systematically underperformed forecasts by the Government and analysts (including the World Bank). Lower-than-projected growth over the forecast horizon would reduce fiscal revenue and the denominator, translating into higher fiscal deficit and public debt ratios. Higher-than-expected interest rates because of changes in global and domestic financial market conditions would increase debt-service costs and make the primary balance adjustment required to stabilize debt larger. Based on the Debt Sustainability Analysis, these shocks¹ would translate into higher public debt (Figure 5). The 2021 Budget Review also identifies the financial position of public entities and local government, and the medium-term debt redemptions of SOEs as important risks to the budget. Contingent liabilities amounted to R1.11 trillion in FY2020/21 to R1.23 and total debt of SOEs to R692.9 billion, of which 60 per cent (R415.5 billion) is guaranteed by government. Nonetheless, these risks are mitigated by the cautious baseline macro-assumptions as well as the Government's commitment to expenditure containment and reforming the SOE sector.
- 36. Macroeconomic risks are also mitigated by the favorable composition of South Africa's public debt.** External debt is low, at less than 10 percent of GDP, but a significant share of domestic debt is held by foreign investors (about 30 percent of the total). South Africa's public debt is also predominantly long-term with an average maturity of more than 12 years, higher than most emerging peers. In this context and depending on global financial conditions, South Africa has some room in terms of debt management to issue shorter maturity tenders while keeping an overall favorable profile. It can also consider raising external borrowing prudently, especially from IFIs.

¹ In the primary balance, this is a minimum shock equivalent to 50 percent of the planned cumulative adjustment or baseline minus half of the 10-year historical standard deviation, whichever is larger. Under the real GDP growth shock, real GDP growth is reduced by 1 standard deviation for 2 consecutive years. In the interest rate shock, nominal interest rates increase by the difference between the maximum real interest rate over history (last 10 years) and the average real interest rate level over the projection, or by 200bp, whichever is larger.



Figure 5. Stress Tests to Public Debt Sustainability



Source: World Bank Group estimates

37. South Africa's fiscal position makes it vulnerable to changes in sentiment in global financial markets.

South Africa issues most of its debt domestically in rand. However, a large share is held by foreigners. Currently, about 30 percent of its public debt is held by non-residents, a share that has declined from a peak of 42.8 percent in early 2018. The country is vulnerable to persistent foreign portfolio investment outflows, which would mean higher yields at a time when debt-servicing costs are already crowding out non-interest budget spending. In case of a shock to global portfolio flows, South Africa's significant domestic savings could substitute for foreign investment. However, this would inevitably crowd out funds for private investment, which would likely translate into weaker economic growth. It would also deepen the sovereign-bank nexus (the link between the health of the banking system and the level of sovereign debt). However, South Africa also has important strengths, including a long-standing flexible exchange rate regime, a relatively strong international investment position, and low external debt that contribute to reduced external sector vulnerability if capital flows were to become more volatile.

38. The financial sector's exposure to sovereign risk has increased during the pandemic. Bank holdings of government debt grew substantially during the pandemic, as non-resident investors reduced their relative exposure to domestic debt and the Government issued more debt. Rising household debt and record-high unemployment also present risks for the banking sector. Household debt as a share of disposable income rose from 64.0 percent at the end of 2019 to 68.3 percent a year later. This risk is mitigated by a lower debt service burden (7.7 percent of disposable income at end-2020, compared with 9.0 percent at end-2019), because of the low-interest-rate environment. Though moderately high foreign currency-denominated corporate debt makes many South African companies vulnerable to exchange rate shocks, they have both financial and natural hedges (e.g., mining companies) to absorb such shocks.

39. There are also upside risks to the outlook. Recent high frequency indicators suggest that the GDP growth rebound is likely to be stronger than currently projected. A continued favorable global environment, especially persistently high commodity prices, could support higher growth in 2022 as well. Increasing South Africa's participation in trade and global and regional value chains could also allow the country to benefit more from global growth. In addition, the signaling effect of the recent structural reforms could boost confidence and support higher private investment, which would contribute to raise the economic potential.



40. The macroeconomic policy framework underlying this operation is assessed as being adequate. Despite South Africa's long-standing challenges to growth and development, the Government's response to the COVID-19 pandemic has been decisive and has been implemented so as to minimize the long-term damage. Growth has been slow for a protracted period, reflecting structural constraints that have been difficult to address. And fiscal discipline has flagged in recent years, resulting in rising fiscal deficits and higher debt levels. Nevertheless, the country also entered this crisis with many policy and institutional strengths, such as an independent central bank committed to price stability, well-developed and deep domestic capital markets, and a well-established record of transparency regarding fiscal and debt management. The authorities are aware that sustained efforts will be needed to address structural impediments to growth, and to control spending while improving its composition and efficiency in order to improve economic prospects. While there are important risks to the fiscal trajectory, they are mitigated by the Government's policy commitments (on fiscal and structural policies) and the strong economic recovery this year. This operation will support these efforts by helping sustain macroeconomic stability and promote inclusive growth.

2.3. IMF RELATIONS

41. The Government of South Africa is on a standard 12-month consultation cycle with the IMF. The 2021 Article IV Consultation mission is scheduled over November 17 to December 3, 2021. The World Bank and the IMF have been collaborating closely on the macroeconomic framework and structural reform agenda in the context of the post-pandemic recovery. Last year, the Executive Board of the IMF approved the authorities' request for emergency support under the Rapid Financing Instrument (RFI) on July 27, 2020. The IMF disbursed SDR 3,051.2 million, equivalent to US\$4.3 billion or 100 percent of South Africa's quota, to be used as budget finance as the pandemic has hit the economy hard in the absence of fiscal space (see Annex 4). IMF support complemented financing from other IFIs, including the AfDB, the NDB and European bilateral and multilateral partners comprising France, Germany, Italy and the European Commission. In August 2021, as part of the IMF's general allocation of Special Drawing Rights, South Africa received SDR 2,924.4 million.

3. GOVERNMENT PROGRAM

42. The Government's response to the COVID-19 crisis focused on providing short-term relief to households and businesses most affected. The Government's socio-economic relief package—the largest and most comprehensive in Africa—consists of three types of measures: (i) measures to protect people's lives and curb the spread of the virus; (ii) measures to protect the poorest and most vulnerable; and (iii) measures to protect jobs and businesses from the short-term economic impacts of the crisis.

- a. Protecting lives.** Investments in the public health system ensured that the Government had the capacity to manage the continued spread of the COVID-19 virus, while vaccinations have also been picking up. After a slow start, South Africa has embarked on an ambitious vaccination program, and has confirmed the purchase of 31 million doses of the single-dose Johnson & Johnson vaccine and 30 million doses of the Pfizer vaccine, and 12 million doses committed through COVID-19 Vaccines Global Access (COVAX). By mid-October 2021, more than 19 million South Africans had received at least one dose of the vaccine and 10.2 million had been fully vaccinated (25 percent of the eligible



population). By end-2021, the Government targets a vaccination rate of at least 40 percent. An important innovation has been the establishment of an electronic vaccination data system (EVDS), which serves a similar purpose to the EU's digital green pass and an important step toward a robust e-health system (see also Prior Action 4, Section IV).

- b. Protecting the poor.** To support the poorest and most vulnerable in 2021, the Government re-introduced the COVID-19 Social Relief of Distress (SRD) program, which provides grants to informal sector workers who are not eligible for unemployment insurance benefits and expanded the SRD program to include caregivers who receive the Child Support Grant on behalf of children. It has also taken steps to improve the transparency, targeting, and efficiency of social grant programs by establishing electronic mechanisms to allow for digital application procedures and eligibility verification (see also Prior Action 1 and 3, Section IV).
- c. Protecting livelihoods.** To mitigate the impact on jobs and businesses, in 2021 the Government took additional measures to support unemployed formal sector workers. To keep people, especially low-wage workers, connected to their jobs and ready to work when firms re-open, the Government announced the expansion of the reach of the COVID-19 Temporary Employer-Employee Relief Scheme (TERS). This scheme allows furloughed workers who have contributed to the Unemployment Insurance Fund (UIF) to receive cash payments directly into their bank accounts in response to the national lockdown during the third wave of the pandemic in July 2021 (see also Prior Action 2, Section IV).

43. The Government's relief package—the largest in Africa—is equivalent to 10 percent of South Africa's GDP. It amounts to R 500 billion (US\$29.41 billion), allocated across the three pillars as follows: (i) R 20 billion (US\$1.17 billion) on health and frontline services, including personal protective equipment, community screening, testing, Intensive care units (ICU), ventilators, medicine and staffing; (ii) R 50 billion (US\$2.94 billion) on social protection of vulnerable households for six months; (iii) R 40 billion (US\$2.35 billion) on job retention schemes; (iv) R 70 billion (US\$4.12 billion) on income support, such as tax deferrals, skills development levy (SDL) holidays, the fast-tracking of value-added tax (VAT) refunds and employment tax incentive (ETI) extensions; (v) R 100 billion (US\$5.88 billion) for support to SMEs and informal businesses; (vi) R 200 billion (US\$11.76 billion) for a credit guarantee scheme, in partnership with the major banks; and (vii) R 20 billion (US\$1.17 billion) for support to municipalities for emergency water supply provision, increased sanitation of public transport and facilities, food provision and shelter for the homeless.

44. A renewed focus on tackling structural reforms to reposition the country. The Government took important steps through the launch of its Economic Reconstruction and Recovery Plan (ERRP), the Second Mid-Term Strategic Framework, the 2020 Mid-Term Budget Policy Statement, the 2021 State of the Nation Address, and the National Budget of 2021 and the 2021 MTBPS announcements to set a clearer path for structural reforms, thereby marking a new growth and development path. These policy frameworks emphasize that the recovery cannot be a return to the path of growth that existed prior to the COVID-19 shock. There is a need for a concerted effort to pursue sources of growth that are not dependent on large-scale public investment and consumption to fully offset its fiscal consolidation strategy.

45. The COVID-19 health and economic shocks have created opportunities for the Government to reflect on how best to rebuild the country. The June 2020 Supplementary Budget announced shifting priorities, the



details of which have been outlined in the ERRP released on October 15, 2020. The ERRP, embedded in the Nation Development Plan, sets out a bold vision and immediate actions to enable an economic rebound, and to build the economy of the future. It has two aims, namely: (i) to deal with immediate actions toward economic recovery amid the COVID-19 pandemic; and (ii) to rebuild and grow the economy ensuring sustainability, resilience and inclusion. The large number of reforms and interventions outlined in the ERRP envisage a growth rate of about 3 percent on average over the next 10 years, which is in line with the WBG CPF optimistic scenario. In the short term, the economic recovery plan will focus on building infrastructure, expanding electricity generation, allocating digital spectrum, and supporting rapid industrialization and employment. At the same time, the Government will roll out structural reforms, such as modernizing network industries, reducing barriers to entry, and increasing regional integration and trade. The Independent Communication Authority of South Africa has temporarily allocated additional radio frequency spectrum to enable the telecommunications industry to manage the surge in data traffic smoothly amid the rapid shift to remote working, learning and online commerce, while also requiring free access to many online sites and platforms hosting important health and educational content.

- 46. The November 2021 MTBPS further sets out progress made in advancing ERRP.** These include measures to boost household savings by increasing preservations before retirement and to increase flexibility through partial access to retirement funds. To boost tourism and attract skills, the completed e-Visa system will be rolled out to 15 countries. In the water sector, legislative drafting and financial modelling have been done to establish a National Water Resources Infrastructure Agency responsible for improving the management of bulk water resources. The Department of Water and Sanitation is fast-tracking its application process to ensure that the 90-day target for issuing single-use water licenses will be implemented by March 2022, as part of improving ease of doing business. The other focus area is about improving the efficiency of South Africa's logistics infrastructure to support export growth. In this regard, government has announced the corporatization of Transnet's National Ports Authority as an independent subsidiary of Transnet and appointed an interim board. This will create incentives for efficiency and competitiveness between port service providers – reducing delays, improving services and introducing cost discipline. Transnet Freight Rail will allow third-party access to the freight rail network by the end of 2022. Allowing private rail operators to use the freight rail network will bolster system volume and capacity.
- 47. Reforming SOEs is a core element of the ERRP.** The mandates of all SOEs are being re-evaluated as part of a rationalization process to ensure that they are responsive to national development needs. The Department of Public Enterprises (DPE) will reprioritize R 40.9 million to operationalize the Presidential State-Owned Enterprises Council, an advisory body that will help the Government to reposition SOEs and develop legislation over the medium term to strengthen governance of these companies. In June 2021, the Government announced a 51 percent strategic equity partner for South African Airways. The objective of the public-private partnership is to ensure a sustainable national airline that will not be dependent on the State budget.
- 48. A greener, secure and reliable energy sector.** One of the key priority interventions in the energy sector is to rapidly expand energy generation capacity. The Government is accelerating the implementation of the Integrated Resource Plan, which was approved by the Cabinet in October 2019, to provide a substantial increase in the contribution of renewable energy sources, battery storage and gas technology. This should



bring 11,800 megawatts (MW) of new generation capacity into the system by 2022. More than half of this energy will be generated from renewable sources. In November 2019, the DPE launched the Eskom Restructuring Paper, which separates entities for generation, transmission and distribution. To achieve this, a long-term solution to Eskom's debt burden will be finalized. In July 2021, the Department of Mineral Resources and Energy published an amendment to Schedule 2 of the Electricity Regulation Act, which exempts generation projects up to 100 MW in size from licensing requirements, whether or not they are connected to the grid. This will enable more firms to generate their own electricity instead of relying solely on Eskom, the state-owned energy utility, thereby removing a significant obstacle to investment in embedded generation projects. Businesses that generate their own electricity will be allowed to sell electricity to the grid (see also Prior Action 8, Section IV). Through these measures, the Government aims to achieve sufficient, secure and reliable energy supply within two years.

- 49. In September 2021, the Cabinet approved the Climate Change Bill for submission to Parliament.** The Bill provides for the effective management of inevitable climate change impacts by enhancing adaptive capacity, strengthening resilience, and reducing vulnerability to climate change, with a view to building social, economic and environmental resilience, and an adequate national adaptation response in the context of the global climate change response. The Bill spells out that all adaptation and mitigation efforts should be based on the best available science, evidence, and information. It gives further effect to South Africa's international commitments and obligations in relation to climate change, and defines the steps to be taken to protect and preserve the planet for the benefit of present and future generations. The tabling of the Climate Change Bill in the National Assembly represents an important step forward in the development of South Africa's architecture to manage and combat climate change (see also Prior Action 7, Section IV).
- 50. In September 2021, South Africa deposited its updated Nationally Determined Contribution (NDC) with the United Nations Framework Convention on Climate Change (UNFCCC).** The NDC represents South Africa's contribution to global efforts to reduce greenhouse gas (GHG) emissions and mitigate climate change. The country's NDC target has been updated from its original range of 398 to 614 Mt CO₂-eq by 2025 and 2030, to a range of 398 to 510 Mt CO₂-eq by 2025 and to a range of 350 to 420 Mt CO₂-eq by 2030. The top of the 2030 range of the revised NDC is consistent with the Paris Climate Agreement's temperature limit of "well below 2°C", and the bottom of the range is consistent with the Paris Climate Agreement's 1.5°C temperature limit. South Africa has also brought forward the year in which emissions are due to decline from 2035 in the initial NDC, to 2025 in the updated NDC. The updated NDC also contains South Africa's first Adaptation Communication, detailing the country's adaptation goals to be implemented via the recently finalized National Climate Change Adaptation Strategy (see also Prior Action 8, Section IV).
- 51. In 2021, the Cabinet approved the tabling of the Financial Sector Laws Amendment Bill (FSLAB) in Parliament.** The Bill forms part of the Twin Peaks regulatory reforms that were introduced in 2011. Since then, the National Treasury and the SARB have undertaken further work to strengthen the framework, particularly in response to moral hazard, where banks might take advantage of the need for the State to bail them out and take increasingly risky decisions in the pursuit of profit. A major component of the framework is the Deposit Insurance Scheme and the bank resolution framework (see also Prior Action 5, Section IV).



52. Prioritizing infrastructure investments. The Government has developed an infrastructure investment project pipeline worth R 340 billion in network industries such as energy, water, transport and telecommunication. Progress is being made on a number of these projects. In total, 62 priority infrastructure projects were gazetted in 2020. An additional 55 new projects from various sectors valued at around R 595 billion, with a funding gap of around R 441 billion, were recently unveiled. Therefore, government will need partnerships with the private sector to fill this funding gap. Government is committed to the Infrastructure Fund, including allocating R100 billion over a decade from 2019/20. Further work is being done to unlock more infrastructure projects for execution. There is strong collaboration with government departments and other institutions such as Infrastructure South Africa and the Development Bank of Southern Africa to prepare 4 projects with an investment value of R84.5 billion in the telecommunications, water and sanitation as well as the transport sectors.

4. PROPOSED OPERATION

4.1. LINK TO GOVERNMENT PROGRAM AND OPERATION DESCRIPTION

53. The Government's three-pronged relief program and its Economic Reconstruction and Recovery Program (ERRP) for structural reforms closely mirror the four thematic pillars of the WBG COVID-19 Crisis Response Approach Paper. The four pillars of the WBG crisis response are: *"(i) a health response aimed at saving lives threatened by the virus; (ii) a social response for protecting poor and vulnerable people from the impact of the economic and social crisis triggered by the pandemic; (iii) an economic response for saving livelihoods, preserving jobs, and ensuring more sustainable business growth and job creation by helping firms and financial institutions survive the initial crisis shock, restructure and recapitalize to build resilience in recovery; and (iv) rebuilding better, by strengthening policies, institutions and investments for a resilient, inclusive and sustainable recovery."*

54. In turn, the proposed operation is closely aligned with all thematic pillars of the WBG Approach Paper. Prior actions under this DPO also fall under the WBG Approach Paper's three stages of Relief, Restructuring and Resilient Recovery. In this operation, the relief stage (in red in the DPO Matrix in Annex 1) involves an *"emergency response to the immediate social, economic and financial impacts of COVID-19"*; the restructuring stage (in blue) focuses on *"restructuring of firms and financial institutions"*, while the resilient recovery stage (in green) entails *"taking advantage of new opportunities to build a more sustainable, inclusive and resilient future in a world transformed by the pandemic"*. This operation also supports the WBG's Green, Resilient, and Inclusive Recovery (GRID) Approach.

55. The program development objectives of this DPO are: (i) protecting the poor affected by the COVID-19 pandemic and modernizing social welfare systems to provide effective support to them; and (ii) accelerating a resilient, sustainable recovery. The elements of the Government's program it supports are: (i) protecting the poor and vulnerable; (ii) protecting jobs and businesses; and (iii) restructuring the economy. Other IFIs, such as the New Development Bank (NDB), are providing budget support to the health response, the first pillar of the government program.



4.2. PRIOR ACTIONS, RESULTS AND ANALYTICAL UNDERPINNINGS

56. The first pillar of the DPO contains measures to mitigate the adverse socio-economic impact of the COVID-19 crisis on vulnerable households, individuals, and workers. The first measure in this pillar channels relief payments to 8.3 million people who are outside of the social grant and unemployment insurance system, through a monthly cash grant of US\$23 per person for up to eight months. The second measure discourages layoffs, hence retaining jobs, by subsidizing wages of temporarily furloughed formal sector workers through cash payments of no more than US\$363 per beneficiary during the third wave of the pandemic in July 2021. The third and fourth measures consider the digitization of public systems and their benefit to government efficiency and the Government's ability to react quickly to respond to crises. These digital advances will be employed even beyond the pandemic. The third measure introduces digital technology to enhance the coverage, transparency, targeting and efficiency of a poverty-targeted COVID-19 response cash-transfer program. The fourth measure supports the health response to the COVID-19 pandemic by leveraging digital platforms to enhance the vaccination effort in South Africa.

Prior Action 1: *To protect vulnerable households from the economic impact of the COVID-19 crisis and to support informal sector workers, the Borrower, through its Department of Social Development, has issued directions through Government Notice No. 681, which: (a) re-introduce the COVID-19 Social Relief of Distress (SRD) Program that provides grants to unemployed and informal sector workers who are not eligible for unemployment insurance benefits; and (b) expand the SRD Program to include unemployed caregivers who receive child support grants on behalf of children.*

57. South Africa has one of the most comprehensive social protection programs in the developing world, though large parts of the population remain uncovered. Thirty percent of the population receives pro-poor social assistance in the form of at least one social grant payment per month, mainly targeted to children, older persons, and people with disabilities. More than half (52.5 percent) of the South African population lives in households receiving cash social assistance, with nearly all of those in the first- and second-income quintiles—the poorest population—receiving some kind of social assistance (99.6 and 97.7 percent, respectively), ranging from 80 percent (children) to 300 percent (older persons, persons with disabilities) of the food poverty line. The primary vulnerable groups that are not covered by the social assistance system are prime-aged workers and informal sector workers who are not eligible for social insurance (e.g., the Unemployment Insurance Fund [UIF]).

58. The Government leveraged the social assistance system to provide emergency relief from the COVID-19-induced economic contraction in March–October 2020. The South African Social Security Agency (SASSA) topped up the monthly payment of social grants to children and their caregivers, older persons, and persons with disabilities, benefiting more than 17 million people. The Child Support Grant (CSG) top-up had two parts. In May 2020, the grant for each eligible child registered in the program was topped up by US\$20 (R 300), from a base of US\$29 (R 440). In the ensuing five months, only the caregiver of children receiving the CSG received a top-up equal to US\$33 (R 500), while the children received the standard base amount.

59. Rather than expand the beneficiary list of social grant programs to others who may have been affected by the pandemic, which would have been difficult to remove once the crisis had passed, the Government created a temporary cash transfer program. The COVID-19 Social Relief of Distress (SRD) grant program provided a monthly sum of R 350 (US\$23) in emergency-relief grants during the period from May 2020 to



April 2021 to over six million affected informal sector workers and unemployed prime-aged individuals who were not eligible for other social grants or the UIF. The SRD grant was intended to supplement household income derived from other labor market or social grant sources. The first phase of the program closed in April 2021. During the first round of the grant, of the ten million applications that were received, 37 percent were from women and 63 percent from men.

60. The third wave of the COVID-19 pandemic and the ensuing lockdown, which hit in July 2021, was accompanied by a change in strategy for COVID-19 relief. First, the Government re-introduced the COVID-19 SRD program for another eight months (until end of March 2022). Second, the Government expanded the SRD program to allow access for caregivers who receive the Child Support Grant on behalf of children, 98 percent of whom are female. The re-introduction of the COVID-19 SRD grant is benefiting more than 3.4 million additional beneficiaries (9.4 million people in total), including informal sector workers and prime-aged workers, who are not eligible for unemployment insurance or any other social benefits. Of the applications received for the reintroduced SRD grant, 46 percent (6.5 million) were from completely new applicants, mostly caregivers, who did not apply in the first round of the grant. Of the new applicants, 78 percent were women. For the 9.4 million approved grants from September 2021, 55 percent were for women and 45 were for men. This restructuring contributes to system efficiency, since temporary, emergency relief programs are now clustered in the COVID-19 SRD program, while the regular social grants programs go back to their core mission of addressing structural poverty among children, older persons, and people with disabilities.
61. The COVID-19 SRD grant, including its extension in August 2021 to March 2022, relies on digital technology to rapidly build a social registry with stringent eligibility criteria, virtual application and registration processes, and electronic cash payments. The program is designed so that all transactions are carried out through mobile phones or computers. As of September 2021, 9.4 million people had already been approved for at least one payment of the second phase of the COVID-19 SRD grant (3.4 million additional beneficiaries compared with the first phase) and 7.5 million people had been paid.
62. **Results:** The re-introduction of the COVID-19 SRD grant is expected to mitigate the socio-economic impact of the pandemic by providing cash grants to more than an additional 3.4 million people (or 9.5 million people in total) affected by the pandemic, equivalent to R 26 billion (US\$1.5 billion). As of September 2021, one-third of applicants of the newest phase of COVID-19 SRD grant were Child Support Grant caregivers and the remaining two-thirds were affected informal sector workers or unemployed who were not eligible for other social grants. The extension of the COVID-19 SRD grant to caregivers who receive the Child Support Grant on behalf of their children will benefit women, who comprise the vast majority (98 percent) of Child Support Grant recipients and were not receiving any other publicly provided income support. At the start of the COVID-19 pandemic, it was expected that an estimated 1.8 million people would escape falling into poverty due to the TERS, the top-up of social grants, and the COVID-19 SRD. Poverty was expected to increase by 1.69 percent compared with an estimated increase of 4.9 percent had the programs not been implemented.

Prior Action 2: *To keep people, especially low-wage workers, connected to their jobs and ready to work when firms re-open, the Borrower, through its Department of Employment and Labor, has issued directions through Government Notice No. 637, which: (a) enhance the targeting of the COVID-19*



Temporary Employer-Employee Relief Scheme (TERS) allowing furloughed workers in hardest hit industries; and (b) allow targeted works to receive cash payments directly to their bank accounts, in response to the national lockdown during the third wave of COVID-19 infections.

63. The COVID-19 lockdown and associated economic downturn has resulted in significant firm closure and a potential loss of 8.4 million jobs. Severing employee-employer ties threatens to slow down the economic recovery. As firms re-open, they will need to engage in costly employee search and training. Support to firms to furlough (rather than lay off) workers during the 2008 global financial crisis in Europe was found to facilitate the recovery period. The South African COVID-19 response strategy is operating under a similar approach of maintaining the employer-employee links through a special fund that pays workers to keep their furloughed staff on their books.
64. In March 2020, the Department of Employment and Labor issued Notice 240/2020, which created the TERS designed to pay between R 3,500 (US\$206) and R 6,732 (US\$393) per employee per month to firms to pay furloughed employees. In April 2020 alone, an estimated 351,000 firms received TERS payments. Since its inception, just over R 63 billion has been disbursed to about 3.5 million workers. The TERS improves on the UIF system in several ways. The program has been implemented under, and financed through, the existing UIF, which had a balance of R 40 billion (US\$2.35 billion) in March 2020. The firms apply for the funds each month through an online portal, receive the grants through direct deposit to bank accounts, and are required to pay out the grant to their employees. Firms that receive the payment are not permitted to dismiss their workers. Workers who are dismissed from their jobs are eligible to receive the standard UIF payment, which pays below the TERS for low-income workers. However, many complaints surfaced from employees who said they had not received payment from their employers.
65. The TERS was designed, piloted and implemented during the COVID-19 crisis to protect workers affected by the various levels of national lockdown from March 2020 to March 2021, and then again in July 2021 when South Africa moved to another Level 4 lockdown, forcing many businesses, especially in the restaurant and hospitality sector, to remain closed or severely restrict their operations. In addition, workers affected by the Level 1, 2 and 3 lockdown restrictions on gatherings since March 2021, especially in the entertainment industry, were also eligible. The original 12 months TERS program instituted protocols to control for duplicate and ineligible applications. It has launched a transparency mechanism—all firm recipients are named through an online website—to provide workers with information to monitor their own receipt of funds and has developed grievance procedures, including independent investigators, to follow up on employee and employer complaints. The original TERS ended in March 2021 but has since become a flexible tool to quickly protect workers affected by temporarily stricter COVID-19 restrictions, such as the Level 4 lockdown in during the third wave of the COVID-19 pandemic in July 2021, where more than 120,000 workers were supported through the temporarily expanded TERS and over R 154 million was paid out. In the expanded TERS used in July 2021, improvements were made so that most workers received their payouts directly into their own bank accounts and not through employers.
66. **Results:** This prior action is expected to mitigate the socio-economic impact of the pandemic. At baseline, job losses were expected to be around 8.4 million. TERS was designed and put in place for 12 months from March 2020 to March 2021 and supported 3.5 million workers who were not dismissed. The expanded TERS program has since become a flexible tool to protect firms and workers affected by temporary lockdown



restrictions. Most payments are also now made directly to workers' bank accounts. It is targeted that more than 120,000 furloughed workers will be supported by June 2022.

Prior Action 3: *To improve the transparency, targeting, and efficiency of social grant programs, the Borrower, through its Department of Social Development, has issued directions through Government Notice No. 681, which introduce the use of electronic means to allow for digital application procedures and automated cross-checking to verify eligibility.*

67. South Africa leveraged the COVID-19 crisis for a major shift in digitizing social protection, which has resulted in major enhancements of its governance. The new directive makes it possible to use digital technologies in the identification of beneficiaries, distribution of cash payments, and monitoring to reduce leakages. Before the pandemic hit South Africa, individual programs in SASSA kept program-specific registry lists that were well curated and carefully targeted through well-defined eligibility criteria. However, with the COVID-19-induced lockdowns, the face-to-face processes quickly pivoted to digital processes. An electronic application, enrolment and payments processing system was built very quickly in April–May 2020 to support the rollout of the initial COVID-19 SRD grant until April 2021. SASSA developed a protocol for a fully digitalized process to deliver the COVID-19 SRD grant and built a new system with the appropriate capacity to import data from other institutions to carry out cross-checks in a fraction of the time that it normally takes to process these data.
68. Over the 18 months since the system was first designed, several improvements took place including broadening the channels through which applications can be submitted, introducing monthly reassessments of eligibility, and expanding options for payments channels for beneficiaries. With the re-introduction of the COVID-19 SRD grant in August 2021, all applicants to the program are required to register through WhatsApp, USSD line, email, the SASSA website, Facebook, or GovChat (an online platform connecting the Government and citizens). Because of the digital enrolment, the application trail was immediately established and gave beneficiaries real-time tracking of their applications at each stage without visiting SASSA offices, using call centers, or dealing with lost reference-number receipts, which provides better customer service and reduces administrative costs. The digital footprint reduces the time and cost of the appeal process as well, allowing for just-in-time cross-checks against live databases that determine eligibility.
69. To support the re-introduction of the COVID-19 SRD grant in August 2021, the Department of Social Development issued a notice to underpin the application for, and enrolment in, the COVID-19 SRD grant by fully electronic means consistent with the improvements made over the past 18 months. The improved system is being used for the re-introduced COVID-19 SRD grant to manage applications, verification and payments more effectively for millions of people, with greater speed and efficiency. Importantly, the eligibility of grant recipients is cross-checked against several linked databases (including SARS, UIF, student bursary fund, home affairs, government employment records, other grant databases, and banking institutions) monthly to ensure recipients are not collecting other social benefits or have had any other status changes affecting their eligibility. Direct deposits to beneficiaries' bank accounts remain the most used payment method, but mobile money and virtual vouchers are also being tested. The enhanced and real-time eligibility verification ensures that 4.6 million ineligible applicants were quickly identified and avoids payments being made to those who do not qualify. The real-time cross-check of eligibility is an



important policy enhancement compared with how other social grants are managed and an efficiency innovation that is expected to generate important fiscal savings through the improved targeting of payments. The savings generated by not paying the 4.6 million ineligible applicants in turn allowed more eligible and poor, unemployed South Africans to benefit from the grant, helping to ensure that as many as possible were able to be protected from the negative economic and social impacts of the COVID-19 crisis.

70. The policy shift in the management of the COVID-19 SRD grant compared with other grants is an investment that can be leveraged going forward also for the management of the other more permanent social grants. SASSA anticipates utilizing the technologies and protocols created for the COVID-19 SRD grant to improve the efficiency of other permanent social grant programs. SASSA is currently in the process of exploring options for how to strengthen the systems for application, verification and eligibility testing, and payments going forward.
71. **Results:** One-hundred percent of COVID-19 SRD applications are digitally managed, and the verification process is fully automated. Within less than two months of the re-introduction of the SRD program in August 2021, 14 million people applied for the grant, 9.4 million beneficiaries were confirmed as eligible, and 7.5 million received their payment in September 2021. The digital protocols that introduced cross-checks across social programs to ensure no double-dipping were re-instituted and improved in 2021 to better monitor eligibility and reduce leakage. The system detected 4.6 million ineligible applicants, of the 14 million original applications in August and September, namely individuals who were already registered with the UIF, received other social grants, were on the Government's payroll system, did not match information in the home affairs database, were duplicate applications, or otherwise did not meet the COVID-19 SRD grant eligibility criteria. As a result, the program avoided paying R 11.2 billion (US\$744 million) to ineligible applications in September 2021. It is expected that R 26 billion will be disbursed through this digital application and verification process from August 2021 to March 2022 when the program has been announced to close.

Prior Action 4: *To improve equitable access to COVID-19 vaccines, the Borrower, through its National Department of Health, has launched the South African COVID-19 Programme Registration, which introduces the use of an Electronic Vaccination Data System (EVDS), compliant with the applicable data protection and privacy legislation, in the rolling-out of the Borrower's COVID-19 vaccination program, setting the stage for future health emergencies, as further evidenced in the COVID-19 Implementation Guide and Toolkit.*

72. South Africa has made significant progress in its health response to the pandemic and began rolling out COVID-19 vaccines in February 2021. The initial rollout of the vaccine targeted 480,000 health workers through the Sisonke clinical trial using the single-dose Johnson & Johnson vaccine. Subsequently, the country has been implementing a nationwide vaccination program, aiming to inoculate 67 percent of its population to achieve herd immunity. As of November 2021, 10.2 million people (17 percent of the population) were fully vaccinated with either one dose of Johnson & Johnson or two doses of Pfizer.
73. The COVID-19 pandemic occurs in a health system that was already suffering from an excess burden of preventable illness and premature death. Though significant improvements have been instigated over the past two decades in maternal and child health, and HIV/AIDS testing and treatment, health indicators



remain poor, and are not on a par with South Africa's level of socio-economic development and health expenditure. Prior to the pandemic, life expectancy was about 62 years, already lower than average for lower middle-income countries. As a result of the pandemic, it has now declined further to just 59 years.

- 74.** The February 2021 shift toward a new electronic vaccine data system (EVDS) has been a critical element in the country's transformation to a digital health system. The EVDS was launched with the purpose of creating a foundation for digital health information systems that inform national policies and interventions. It is premised on the Health Patient Registration platform that is already being rolled out as part of the National Health Insurance (NHI).
- 75. Results:** The system is designed to: (i) capture the relevant metrics of all South African residents who will be vaccinated; (ii) ensure vaccinees are contactable and alerted to optimize adherence to the vaccination regime; and (iii) complete the certification process such that vaccine certificates are easy to obtain for those vaccinated and authorities that may require the certification. The system can provide a response mechanism for any future health emergencies.

PILLAR TWO: ACCELERATING A SUSTAINABLE RECOVERY

- 76. This pillar supports the resilience, competitiveness and sustainability of the South African economy.** It consists of four measures. The first measure establishes a Deposit Insurance Scheme to protect vulnerable depositors in South African banks. The remaining prior actions support the effort to combat climate change for a more sustainable future. The second measure focuses on the National Climate Change Bill, which provides a coordinated and clearly defined architecture for South Africa's response to the impacts of climate change, as well as the country's contribution to GHG emissions. The third measure focuses on the approval of the updated first NDC, which will more closely align South Africa with the Paris Climate Agreement. The fourth and final measure allows for competitive embedded power generation supporting the effort to achieve more reliable, cheaper and cleaner energy.

Prior Action 5: *To increase the resilience of the financial sector, the Borrower, through its National Assembly, has approved the Financial Sector Laws Amendment Bill, which establishes a resolution regime and enables provisions for the Corporation of Deposit Insurance.*

- 77.** The Financial Sector Law Amendment Bill 2020 (FSLAB) was approved by the Cabinet on June 10, 2020 and approved by Parliament (the National Assembly) on September 7, 2021. The FSLAB still requires approval from the National Council of Provinces, after which it will be signed into law by the President. The draft FSLAB, upon enactment, introduces the enabling provisions for establishment of South Africa's first comprehensive explicit Deposit Insurance Scheme to protect depositors in line with international standards. South Africa is currently the only G-20 country that does not have an explicit deposit protection scheme. The Bill also aims to strengthen the resolution framework for all banks, as well as non-bank systemically important financial institutions that may be "too big to fail", by designating the SARB as the resolution authority and expanding the range of tools available to the SARB to fulfill its financial stability mandate. The Bill enables South Africa to meet the basic international standards endorsed by G-20 countries following the 2008 global financial crisis and outlined in the Financial Stability Board's (FSB) Key Attributes of Effective Resolution Regimes for



Financial Institutions. In 2014, a Financial System Stability Assessment (FSSA) indicated strong commitment to adhering to the highest standards for banking supervision and regulation, as well as a high level of compliance with international standards for banking supervision. The FSB conducted a peer review of South Africa in 2020, which found good progress in developing the frameworks for bank resolution and deposit insurance. South Africa is undergoing a Financial Stability Assessment Program (FSAP) update.

- 78.** The non-bank financial institutions that will be covered under the resolution framework include insurance companies and select financial market infrastructures. These institutions are not deposit-taking. The new Deposit Insurance Scheme covers banks, mutual banks and cooperative banks, and these institutions will become mandatory members of the Deposit Insurance Scheme once it is established.² Compared with commercial banks, the overall size of other deposit-taking financial service providers—including mutual banks, cooperative banks and cooperative financial institutions—is small. In addition, there are 6,895 credit providers licensed by the National Credit Regulator that provide credit to consumers and enterprises. However, in terms of asset size, the banking sector accounts for about 95 percent of total assets of depository and non-depository financial institutions.
- 79.** The protection of vulnerable depositors is a key element of the financial safety net in any country, and also contributes to financial stability. Following the enactment of the Bill, the Deposit Insurance Scheme will be established through a newly established Corporation for Deposit Insurance (CODI). The qualifying depositors are individual depositors and non-financial corporates. The maximum coverage level will be R 100,000 (US\$5,882) per qualifying depositor. Commercial banks, mutual banks, local branches of foreign banks and cooperative banks will be members of CODI. The certainty provided by explicit coverage, combined with clear coverage rules, will contribute to depositor confidence and could facilitate further growth in account ownership. This will foster an environment in which emerging banks can grow, thus enhancing competition in the banking sector. The sector is highly concentrated: at the end of March 2021, the combined market share of the five largest banks was 90.1 percent of total bank assets.
- 80. Expected Results:** The prior action will contribute to the establishment and operationalization of the CODI as an independent agency responsible for protecting individuals and non-financial corporates against the loss of insured deposits if a bank fails. CODI would respond through one of two mechanisms. First, as the insurer of a bank's deposits, CODI will pay depositors up to the insured limit. International standards establish that depositors should have access to their insured deposits within a few days of a bank closing. This is achieved by either: (i) providing each depositor with a new account at another insured bank in an amount equal to the insured balance of their account at the failed bank; or (ii) directly paying each depositor for the insured balance of their account at the failed bank. Second, under certain conditions, deposit insurance funds may be used to provide an acquiring bank with cash equaling the difference between the assumed deposits and the market value of the transferred assets, subject to a least-cost test. This contributes to the funding of the resolution of failed banks and is important from a financial stability perspective. The ex-ante funding for CODI is expected to be provided by member financial institutions through: (i) a capital tier built up over time through monthly premiums; (ii) a liquidity tier consisting of contractual deposits placed by members financial institution with CODI; and (iii) an emergency funding facility provided by the SARB only in exceptional cases if there is a shortfall and that will be repaid later through premiums paid by other banks. To perform these

² Cooperative financial institutions (CFIs) are not included in the deposit insurance scheme although the authorities are exploring alternatives for expansion of the financial safety net.



functions, CODI will be established as a subsidiary of the SARB—a separate legal entity with its own CEO and Board. In addition, the prior action will also support increased competition in the banking sector by enhancing depositor confidence in maintaining deposits with commercial banks (besides the four largest banks), mutual banks and cooperative banks.

Prior Action 6: *To enable the development of an effective climate change response and the long-term, just transition to a climate-resilient and lower-carbon society, the Borrower, through its Cabinet, has approved the National Climate Change Bill and its submission to Parliament.*

81. The COVID-19 crisis response creates an opportunity for South Africa to strengthen policies, institutions, and investment for rebuilding better, and making the economy more resilient and sustainable in the long term. Addressing climate change, both the country's contribution to global warming through its GHG emissions, as well as its vulnerability to more frequent and more intense weather events, is central to rebuilding better. In recognition of the challenges posed by climate change to South Africa's development goals, the Cabinet, on September 14, 2021, approved for submission to Parliament of the National Climate Change Bill. On October 11, 2021, the Department of Forestry, Fisheries and Environment (DFFE) formally submitted the Bill in the National Assembly (Gazette No. 45299). The objective of the Bill is to enable the development of an effective climate change response and a long-term just transition to a climate-resilient and low-carbon economy and society. The Bill provides a legal and institutional framework to ensure that climate change policy is implemented within the country's sustainable development and national development goals. It also provides a legislative structure to coordinate and integrate this response and reinforces South Africa's international climate commitments and obligations, including the NDC to the Paris Climate Agreement.
82. The Bill provides specific actions related to coordination and integration, adaptation and resilience, and GHG mitigation. To improve coordination and integration, the Bill defines mechanisms and mandates for harmonization across government and sectors at local, provincial, and national levels. It also provides the legal basis for the establishment of the Presidential Climate Commission (PCC) for organized labor, civil society, and business to advise on South Africa's climate change response, and to serve as a national coordination focal point. To support climate adaptation and resilience, the Bill charges DFFE with the responsibility to define, monitor and mainstream adaptation objectives into national planning instruments, policies and programs, and to develop climate adaptation scenarios that anticipate the likely impacts of climate change in the short, medium and long term. It also calls for the creation of sectoral³ adaptation strategies in line with the National Adaptation Strategy and Plan. Finally, to advance South Africa's GHG mitigation commitment, the Bill provides a legislative foundation for the creation of a national GHG emissions trajectory, the allocation of sectoral emissions targets (SETs), and the allocation of carbon budgets. Together with the carbon tax, which went into effect in June 2019, SETs and carbon budgets form the cornerstone of South Africa's GHG mitigation policy system.

³ National departments and state-owned entities responsible for the following sectors will be required to develop a Sector Adaptation Strategy and Plan: Agriculture; Forestry; Fisheries; Disaster Risk Reduction; Energy; Environment; Health; Human Settlements; Manufacturing; Public Enterprises; Rural Development; Land Reform; Science; Technology; Transport; Water Affairs; and Sanitation.



83. Work to develop approaches for the allocation of SETs and carbon budgets has been underway for several years, and their adoption was approved by the Cabinet in September 2021. Both tools are designed to assist South Africa to meet its absolute GHG reduction targets in terms of its Low Emissions Development Strategy (LEDS).⁴ The World Bank provides technical assistance through the NDC Support Facility (P172748) on the application of SETs to South Africa's economic context. A SET establishes a specific emissions target, which must be aligned with the national GHG emissions trajectory, by sector or subsector. DFFE is responsible for determining which sectors and subsectors are subject to a SET, as well as determining the specific SET.⁵ DFFE is expected to finalize a SET Framework by March 2023. This will be used by DFFE to propose SETs, starting with five priority sectors—energy, transport, agriculture, trade and industry, and water and sanitation – by mid-2023. Together, GHG emissions from these sectors account for about 80 percent of South Africa's emissions profile.
84. A carbon budget, managed by DFFE, is a GHG emissions limit allocated to an entity for a specified time. DFFE is rolling out the carbon budget tool in three phases. A voluntary Phase I ran between 2016 and 2020. It had no prescriptive budget methodology and participating entities were given a 5 percent tax allowance for participation. During Phase II (January 2021–December 2022), a budget allocation methodology will be developed and piloted. January 2023–2027 is expected to be the first phase whereby a mandatory carbon budget allocation is assigned to entities that meet a legislated threshold. Phase III is planned to align with the rollout of the second phase of the carbon tax. This would mean, for example, that liable entities would be taxed at a higher rate for emissions outside their carbon budget.
85. **Expected results:** The Climate Change Bill is expected to provide a coordinated and clearly defined architecture for South Africa's response to the impacts of climate change, as well as the country's contribution to GHG emissions. The full implementation of SETs and carbon budgets will complete the country's mitigation policy system and lead to reduced GHG emissions. The Results Indicator is: Department of Forestry, Fisheries, and Environment (DFFE) presents Sectoral Emissions Targets (SET) for 5 key carbon-intensive sectors: Energy (DMRE), Transport (DoT), Trade and Industry (Dtic), Agriculture (DALRRD); and Water and Sanitation (DWS) to the respective line ministries: 0 Key carbon-intense Sectoral Emissions Targets presented by DFFE to the respective line ministries (November 2021); Target: 5 Key carbon-intense Sectoral Emissions Targets presented by DFFE to the respective line ministries (June 2023).
- Prior Action 7:** *To more closely align South Africa with the Paris Climate Agreement, the Borrower, through its Cabinet, has approved the updated First Nationally Determined Contribution (NDC), which sets more ambitious greenhouse gas (GHG) mitigation targets for 2025 and 2030.*
86. South Africa is a signatory to the United Nations Framework Convention on Climate Change's (UNFCCC) Paris Climate Agreement, which provides a framework to avoid dangerous climate change by limiting global warming to well below 2°C and pursuing efforts to limit it to 1.5°C. The Agreement also aims to support countries in their efforts to strengthen their resilience to the impacts of climate change. Signatories to the

⁴ The LEDS was approved by the Cabinet in September 2020.

⁵ The Draft Climate Change Bill identifies the following sectors and subsectors for potential SETs: Agriculture; Forestry; Fisheries; Cooperative Governance; Traditional Affairs; Economic Development; Energy; Environment; Health; Human Settlements; International Relations; Mineral Resources; National Treasury; Public Enterprises; Public Works; Rural Development; Land Reform; Science; Technology; Trade; Industry; Transport; Water Affairs; and Sanitation.



Paris Climate Agreement register their Nationally Determined Contribution (NDC) with the UNFCCC every five years. The NDC details the specific mitigation and adaptation actions that the country intends to pursue. South Africa published its first NDC in October 2015. The Cabinet approved an update to the NDC on September 14, 2021, and this revised version has been deposited with the UNFCCC.

- 87.** South Africa emits on average 482 MtCO₂e annually.⁶ The country's GHG emissions profile is dominated by emissions from the energy sector and, specifically, from coal-fired power generation, which account for about 44 percent of the total. Because of this out-sized contribution, mitigation in the power sector is critical to achieving the country's mitigation target. The Integrated Resource Plan (IRP) 2019 sets out the decommissioning of about 12 GW of old and inefficient coal-fired power plants by 2030. This is equal to 80 percent of the power plants owned and operated by Eskom and equivalent to 74 percent of South Africa's total electricity capacity. The implementation of the IRP is supported under the recently approved CPF, which includes the decommissioning of 6 GW of coal-fired plant generating capacity as an outcome indicator.
- 88.** South Africa's Updated NDC includes an increase in the level of its proposed GHG mitigation. The 2015 NDC committed to a mitigation range of between 398 and 614 MtCO₂e by 2025 and by 2030. The 2021 NDC commits to an annual mitigation range target of 398–510 MtCO₂e to be achieved between 2021 and 2025, and an annual mitigation range target of 350–420 MtCO₂e to be achieved between 2026 and 2030. By comparison, the upper end of the target range in 2025 has been reduced by 17 percent compared with the 2015 NDC, and the upper end of the target range in 2030 has been reduced by 32 percent, and the lower range by 12 percent. If achieved, these targets set South Africa on track to peak its emissions by 2025. The upper bound of the 2030 target is consistent with South Africa's fair-share contribution to keeping global warming below 2°C. The lower bound 2030 target is consistent with a pathway to limiting warming to 1.5°C. Notably, the NDC underscores that meeting these targets requires the successful implement of the IRP 2019, in addition to the Green Transport Strategy, energy efficiency programs, and the continued implementation of the carbon tax.
- 89.** World Bank engagement on coal-fired plant retirement started in April 2020 with the endorsement of the Energy Petroleum Agency for South Africa (PASA), which includes a strategic focus on a Just Energy Transition (JET), and Eskom's commitment to retire coal-fired plants speedily and sustainably in line with the IRP 2019. As of October 2021, the World Bank has raised US\$5 million in Energy Sector Management Assistance Program (ESMAP) grants to support Eskom in the preparation of detailed analytics for the decommissioning and/or repurposing of four coal-fired power plants (Camden, Komati, Hendrina, and Grootvlei) totaling 6 GW. The Komati coal-fired power plant has been selected as a pilot project by the Department of Public Enterprises (DPE) to demonstrate to the South African public that coal-fired plants can be retired in a sustainable manner. Following a request from the National Treasury from June 23, 2021, the Bank is currently preparing the Just Energy Transition Project (JETP) with Eskom to decommission and repurpose the Komati power plant. Shutting down coal-fired operations at Komati will result in the avoidance of 2,622,550 tons of CO₂ per year. This is equal to 0.5 percent of South Africa's total annual GHG emissions. While this amount is relatively small, this effort is meant to pave the way to further and much larger emissions avoidance as a result of reduced coal-fired power generation. Komati is expected to be

⁶ DFFE's most recent GHG inventory includes emissions data up to 2017. Total annual emissions in 2017 reached 482 MtCO₂e; this figure includes emissions from forestry and other land uses.



shut down by October 2022.

- 90. Results:** The updated NDC provides more ambitious national GHG mitigation goals for 2025 and 2030. Discontinuing the use of coal-fired power generation is critical to achieving the target in both years. The Results Indicator is: Avoided CO₂ emissions as a result of the shutdown of coal-fired power production – Baseline: 0 carbon emissions avoided (October 2021) – Target: 900,000 tons CO₂ avoided (June 2023).

Prior Action 8: *To increase competition and power generation capacity in the energy sector, the Borrower, through its Department of Mineral Resources and Energy, has amended Schedule 2 to the Electricity Regulation Act through Government Notice No. 737, which exempts from licensing embedded generation with a nominal installed capacity below 100 megawatts as per Schedule 2 to the Electricity Regulation Act.*

- 91.** Eskom, the state-owned vertically integrated power utility, dominates the South African electricity market value chain, with limited competition and private sector participation in generation. South Africa has experienced periods of load shedding since 2007. The most severe was in first semester of 2021, with national power cuts for up to 15 percent of the time in the whole semester. This was mainly due to inadequate maintenance over the years of the aging generation fleet (average coal-fired plant age is over 40 years) leading to frequent plant breakdowns. Eskom's inability to provide reliable power for South Africa's economy hampers the SOE's ability to initiate the shutdown of its oldest coal-fired plants. The rapid deployment of additional generation capacity has, therefore, become a government priority.
- 92.** To increase competition and security of electricity supply, private sector participation and acceleration of renewables deployment to decarbonize the energy sector, the 1 MW limit for license exemption for new embedded generation (EG) was raised to 100 MW, fitting within the power consumption profile of the vast majority of industrial facilities. Increased EG will improve security of supply by lowering the electricity demand on the grid and gradually replacing thermal backup power that was massively deployed in 2008/2009 at the aftermath of the country's 2007 power crisis. The vast majority of EG installations are expected to be renewables, as it was proven to be the least-cost power generation option in South Africa since 2019. The mining industry is a typical and core beneficiary sector of this policy and has already indicated its commitment to installing up to 2,000 MW of solar PV at the mining sites over the next two years to meet some of its electricity demand and secure its production. Several mining companies have already started the registration process with NERSA to finance, build, and operate solar PV plants up to 100 MW. The amendment will not undo or dilute existing environmental regulations in South Africa as the installation and operation of these facilities are not exempt from having to comply with the requirements as set out in the National Environmental Management Act. The EG is still required to obtain an environmental authorization and any other applicable licenses in terms of the environmental legal requirements as may be necessary, for instance an Air Emissions License. The South African legislative framework, together with the application of the guidelines, ensure that impacts such as GHG emissions and air pollution associated with the installation of fossil-fuel energy generation are mitigated and monitored to prevent adverse impacts on the environment, forests, and natural resources.
- 93.** The recently approved IRP for 2019–30 bolstered the EG concept by making provisions for the licensing of up to 500 MW per year of new generation capacity from embedded generation by 2030. Moreover, the 2019–30 IRP has highlighted wind and solar as least-cost generation technologies, implying that new EG will mainly



use renewable sources of energy. This additional EG capacity could help narrow the gap in the supply of electricity in the country, adding the needed flexibility to replace the centralized thermal generation. It would also give consumers the option of seeking an alternative source of electricity supply, thereby opening the market to competition with private sector participation in power generation.

94. The Government had earlier included EG as a key component of the post-COVID-19 economic recovery, by selecting the Embedded Generation Investment Programme (EGIP) into its Strategic Infrastructure Projects (Government Gazette No. 43547, July 24, 2020). By ‘gazetting’ the EGIP—a 400 MW EG investment funded by the DBSA and the Green Climate Fund—the Government gave a strong signal on its commitment to fast track the needed policy for EG scale-up.
95. **Results:** This Prior Action is expected to help accelerate investment and meet the EG target planned in the IRP (i.e., add up to 500 MW annually since 2020, or 1,500 MW by end-2022), with mostly private sector-financed generation capacity using renewables technologies. This measure also cost-effectively promotes clean energy, because most EGs are expected to be solar photovoltaic systems, and technologies related to wind and biogas. This policy action will contribute to solve South Africa’s larger power generation gap that Eskom is facing and will hence have positive effects on the power system operation, reducing pressure on Eskom to meet power demand and associated load shedding.

ANALYTICAL UNDERPINNINGS:

96. A rich body of analytical work by the Government, academia, think tanks and the World Bank underpins the prior actions of this DPO (see Annex 5).

4.3. LINK TO CPF, OTHER BANK OPERATIONS AND THE WBG STRATEGY

97. **The new CPF aligns both with the Government’s short-term socio-economic response to the COVID-19 crisis and its medium-term ERRP in key sectors.** This DPO, similar to the overall CPF, supports the Government’s short-term socio-economic relief package, while sowing the seeds of long-term economic transformation, in line with the three stages of the World Bank COVID-19 Crisis Response Approach Paper: relief, restructuring and resilience recovery.
98. **The new CPF spans the fiscal years 2022 to 2026, and builds flexibility to respond to the Government’s financing needs and emerging priorities.** The three CPF strategic focus areas are: (i) promoting increased competition and improved business environment for sustainable growth; (ii) strengthening MSME performance and skills development to support job creation; and (iii) improving the infrastructure investment framework and the efficiency of infrastructure services in selected SOEs. Governance, gender and the digital economy are cross-cutting themes. In doing so, the CPF responds to the binding constraints to poverty and inequality reduction as identified in the Systematic Country Diagnostic and Country Private Sector Diagnostic.
99. **The World Bank is preparing a Country Climate and Development Report (CCDR).** The new core diagnostic tool designed to identify and prioritize high-impact climate action that will inform future World Bank engagements and investments. The CCDR analysis comes at a time when South Africa is working to manifest a green recovery following the COVID-19 pandemic. The report will therefore focus on identifying



opportunities to align South Africa's decarbonization plans with economic recovery and job creation. It will also focus on how the country's transition to a low-carbon economy will be sustainable and just for all.

100. **The COVID-19 pandemic has given a renewed sense of urgency to the Government's reform agenda.** The Government has requested financing for vaccine purchase under the vaccine facility and for the decommissioning of the first coal-fired plant, Komati, as well as development policy financing to support the COVID-19 response under the ERRP.

4. CONSULTATIONS AND COLLABORATION WITH DEVELOPMENT PARTNERS

101. **This budget support operation is following budget support operations by other development partners including with the African Development Bank (AfDB), the New Development Bank (NDB) and the International Monetary Fund (IMF).** When the Government of South Africa requested budget support from the WBG, it also requested US\$4.2 billion, US\$2 billion and US\$300 million from the IMF, the NDB, and the AfDB, respectively. The European Union and the Governments of Germany, Italy and France also put forward €750 million (US\$880 million) in budget support loans and €50 million (US\$57 million) in grants. The Executive Boards of the NDB and the AfDB have already approved their respective operations. The IMF Executive Board also approved South Africa's request for an RFI on July 27, 2020.
102. **The National Treasury consulted with all key stakeholders** including the National Economic Development and Labour Council which consists of Government, labour, business and community organisations on its borrowing requirements from IFI's as well as the recently approved CPF. In addition, the Assets and Liabilities team of the National Treasury held extensive consultations with the Economic Policy, Budget Office, Public Finance divisions of the National Treasury responsible for oversight of line Ministries affected by the prior policy actions.
103. **The WBG and the AfDB held joint discussions with the National Treasury and other technical counterparts, and developed a common policy matrix in 2020.** The World Bank is continuing these government-led discussions in 2021. These consultations have informed the program design, including environmental and social aspects of this budget support operation. The WBG has consulted the Department of Social Development (DSD) on the COVID-19 response prior actions relating to the extension and digitization of the COVID-19 Social Relief of Distress Grant. The Unemployment Insurance Fund (UIF) was consulted on the COVID-TERS and its impact. The Department of Health has been consulted on the establishment of the EVDS. The CoDI has received ongoing technical assistance from the World Bank on establishing a bank resolution framework and deposit insurance scheme in relation to the FSLAB Bill. The Department of Forestry, Fisheries, and Environment has been consulted on the NDC and Climate Change Bill.
104. **The WBG has carried out intensive consultations since December 2019 on its overall engagement in South Africa.** These consultations involved government entities at the national and subnational levels, academia, civil society stakeholders, youth groups, and organized business. The consultations confirmed the full alignment between the WBG and the Government's diagnostics and priorities. CPF focus areas, objectives and work program also complement those of other development partners.



4.5. FUTURE LENDING

- 105. The new World Bank Group CPF (FY2022–FY2026) paves the way for supporting South Africa with all World Bank lending instruments.** The World Bank has the space to engage with South Africa in future IBRD lending operations that could build on this DPO. The CPF has intentionally maintained flexibility to be able to adapt to country demand and unforeseen or changing priorities. However, the World Bank remains ready to deepen the engagement with South Africa and to deploy its global expertise with transition economies, including through policy-based lending.
- 106. In terms of investment lending, the World Bank has extended a potential retroactive financing facility to finance COVID-19 vaccines in South Africa.** The Government has requested financing to access the African Vaccine Acquisition Trust (AVAT) for up to US\$800 million to retroactively finance existing contracts already as part of South Africa's COVID-19 Vaccination Strategy to achieve 67 percent herd immunity. The Government has also requested a US\$250 million investment operation to support the decommissioning of the Komati coal-fired power plant as pilot operation as it moves toward its Just Energy Transition.
- 107. South Africa has embarked on a number of major transformations that could pave the way for future policy-based engagements.** This includes the Government's push to remove obstacles to create jobs, attract investment and further modernize the already robust social protection system. Another area of increased attention is green growth, which is closely linked to South Africa's energy transition, and already a cornerstone of this operation.

5. OTHER DESIGN AND APPRAISAL ISSUES

5.1. POVERTY AND SOCIAL IMPACT

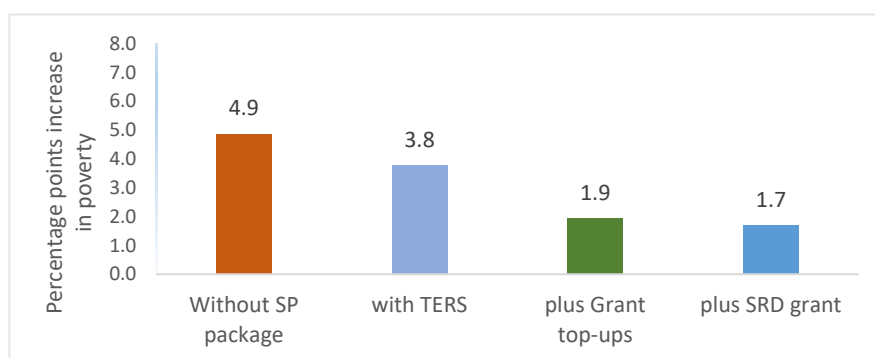
- 108. The Poverty and Social Impact Analysis shows that the prior actions supported by this operation play a significant role in containing the negative poverty impacts of the COVID-19 crisis.** The targeted SRD grants and the TERS for furloughed workers in industries severely affected by the COVID-19 crisis provide crucial income support to low-income households. The SRD scheme fills in a gap in the safety net by reaching those that were neither covered by the UIF COVID-TERS nor accessing other social grants. These latter grants were also topped up to respond to the unprecedented shock, providing an overall decisive response by the social protection system to the crisis. These actions have mitigated the negative effects of the crisis by providing households with counter-cyclical cash transfers to compensate for the drop in labor income caused by the pandemic.
- 109. Estimates show that, without this decisive social protection response, poverty would have been more than 3 percentage points higher.** The job losses and negative income shocks brought about by the pandemic exert pressure on poverty and inequality, which were extremely high even before the COVID-19 crisis. Poverty increased from 53.2 percent in 2011 to 55.5 percent in 2015, due partly to a decline in economic activity and fall in household consumption associated with labor market challenges and slow job creation. At 0.63, the consumption-based Gini index is the highest in the world and has increased since 1994. Microsimulations show that the COVID-19 pandemic would have led to a poverty increase of almost 5 percentage points if households had not received any income support. With the benefit package implemented through the national social protection system, the poverty increase has been contained to



1.7 percentage points. The significant negative poverty impacts of the pandemic have been largely averted because public transfers were able to compensate many households for the income drop caused by employment losses during the crisis.

Figure 4: Poverty impact of the COVID-19 pandemic with and without support package

Percentage point increase using official upper bound poverty line



Source: World Bank. Simulated impact of the COVID-19 shock and the benefit package using data from NIDS-CRAM and national upper-bound poverty line of R 1,138 per person per month.

- 110. The extension of TERS to furloughed workers has prevented more than 600,000 people from falling into poverty (Prior Action 2).** Payments from the UIF considerably offset the significant negative poverty impacts of the pandemic. TERS reduces the poverty impact to just 3.8 percentage points, instead of 4.9 percentage points. Accordingly, the TERS scheme of the UIF supported in this DPO prevents some 660,000 people from falling into poverty.
- 111. Top-ups to the three largest existing social grants have protected an additional 1.9 percent of the population from falling into poverty (Figure 4).** The temporary top-ups of the main existing social assistance programs provide important support to weather the COVID-19 shock. Although these grants are smaller than the TERS payments of the UIF, they cover a larger proportion of the low-income population due to their targeted design. With TERS and the top-ups to the disability grants, old-age pensions and child support grants, poverty increased by 1.9 instead of 4.9 percentage points, protecting 1.8 million people from falling into poverty.
- 112. The COVID-19 Social Relief of Distress (SRD) grants have prevented an additional 120,000 people from falling into poverty (Prior Action 1).** The SRD grants provide benefits to those who lost their jobs and are not receiving any other form of assistance. This program covers about 43 percent of those who experienced job losses as a result of the COVID-19 pandemic, including people ineligible for TERS benefits because they work in informal employment. Because the SRD recipients include people not receiving the more progressive grant top-ups, benefits are concentrated among those who bear the brunt of the crisis in the upper middle of the income distribution.



- 113. The digitalization of social protection systems (Prior Action 3) is also expected to have significant positive distributional impacts.** Making use of electronic means to allow for digital application procedures and eligibility verification to social transfer programs, and for suitable payment methods for social grants, will enable the system to be more transparent, better targeted and more efficient, resulting in overall benefits to the poor and vulnerable. Finally, the rest of the prior actions in this DPO are expected to have a neutral effect on distributional issues, or at least no clear negative impacts on poverty and inequality.

5.2. ENVIRONMENTAL, FORESTS, AND OTHER NATURAL RESOURCE ASPECTS

- 114. South Africa's environmental laws, regulations and policies are generally sound.** Over the past 20 years, the Government has made significant strides in developing its framework for environmental management and mainstreaming environmental sustainability into decision-making processes, starting with the National Environmental Management Act (Act No. 107 of 1998) (NEMA) and GN R. 982 (December 4, 2014), and its subsequent amendments pertaining to environmental impact assessments (EIAs). Public participation is mandatory, even for projects that require only basic assessments. According to the Promotion of Access to Information Act, 2000, information disclosure is also required. The Department of Fisheries, Forestry and Environment (DFFE) is the responsible authority for EIAs and decision-making at the national level. At a provincial level, the EIA and the decision-making process are dealt with by dedicated provincial governmental environmental departments under the DFFE. The capacity and track record of the DFFE in managing environmental risks associated with development initiatives and ensuring environmental compliance are well-established.
- 115. Prior Action 3 and 4 are likely to generate small quantities of e-waste but will have a positive impact by significantly reducing paper usage and waste by moving to a digital platform for social grant application and tracking of the country's COVID-19 vaccination health program.** The importance of a digital system has been further highlighted by the pandemic. Generation of e-waste is anticipated to be insignificant at this stage since the Department of Social Development and Department of Health are adequately equipped with the necessary electronic facilities, but e-waste generation is likely to occur throughout the implementation lifecycle of digital platforms. South Africa has a well-established legislative framework to manage waste. At the beginning of 2021, the DFFE published the updated National Waste Management Strategy in terms of Section 6 of the National Environmental Management: Waste Act 59 of 2008, which was promulgated in 2008 and amended in 2014. DFFE has identified strengthening of policies and legislation and implementation of management plans and measures to reduce priority waste streams, such as e-waste, by 30 percent in its strategic plan for FY2019/20 to FY2023/24. The new waste strategy and the DFFE's strategic plan both focus on the development of a circular economy to reduce waste and support collaboration with the private sector to implement an Industrial Waste Management Plan to address, among others, electronic waste management in the country.
- 116. Prior Actions 6 and 7 will have a significantly positive impact on South Africa's environment, forests and natural resources** According to the NDC, average temperatures in South Africa are increasing at a rate of more than twice that of the global average, which is resulting in more frequent droughts and extreme weather events. The country's economy and energy production are among the most coal-dependent in the world. The Climate Change Bill was recently tabled in Parliament for consideration. The new Climate Change Bill provides for a holistic response to climate change and makes an impact by enhancing adaptive



capacity, strengthening resilience, and reducing vulnerability, and calls for a just transition to a lower carbon economy. In response to this commitment, the country's largest state-owned power producer, Eskom, is currently undertaking studies to determine the feasibility of repurposing selected coal-intensive power generation units within its portfolio to low-carbon renewable alternatives. The transition that the Bill brings to move from a coal-dependent to a low-carbon economy will have a significantly positive impact on improving air quality, reducing GHG emissions, and also reducing impacts on natural resources.

- 117. Priority Action 7 supports Priority Action 6 in transitioning to a low-carbon economy by re-iterating South Africa's commitment to meeting GHG mitigation consistent with the Paris Climate Agreement clarifying the country's climate adaptation needs and priorities.** The National Environmental Management Act (Act No. 107 of 1998) and the National Environmental Management Air Quality Act (Act No. 38 of 2004) broadly imply that climate change should be considered during an environmental impact assessment. However, there is no explicit requirements to do so, and hence the majority of EIAs have failed to adequately assess the climate change risks of new developments. In June 2021, the DFFE published, for public review, its guidelines for consideration of climate change implications in environmental authorizations that will embed the requirements for a climate change impact assessment in law. To fully achieve the outcomes of PA 6 and PA 7, the adoption of the draft guidelines and institutional capacity strengthening to ensure compliance will be prudent. The adoption of the guidelines and strengthening of institutional capacity; to enforce the guidelines; will have a significantly positive impact by ensuring climate resilience are considered, carbon budgets and allocations are implemented and adverse negative impacts on natural resources are avoided or reduced.
- 118. Priority Action 8 is likely to have a significantly positive impact as preference is given to the installation of renewable energy generation rather than conventional fossil-fuel energy generation.** While the exemption for embedded generation up to 100 MW does, in principle, allow for all types of generation technologies, most investments will be in renewables, especially solar PV installations. Hence, this PA will be instrumental in the transition to cleaner energy. In particular, the PA will contribute to scaling up renewable generation that will reduce the electricity demand from the Eskom grid and allow for the decommissioning of conventional coal-fired power plants (and repurposing them with cleaner and renewable energy generation capacity). The exemption for generation licenses for private renewable energy projects is anticipated to accelerate investments by independent power producers (IPPs) in renewable generation capacity, which is likely to have an impact on land use due to land requirements for installation. The decommissioning and repurposing of redundant coal-fired power plants will provide an opportunity for the remediation and utilization of these facilities. It will also allow for the installation of new renewable energy generation and, in so doing, is likely to remediate existing pollution while preventing the acquisition of new or additional land. Installation of cleaner and renewable energy options to supplement the energy grid would support the NDC objective to reduce GHG emissions by decreasing dependence on coal-fired energy generation. This would also contribute to a reduction in pollution and could contribute to a reduction in environmental degradation exploitation of natural resources and have a positive impact through improved air quality.
- 119. Considering the stringent legislative requirements now imposed on fossil-fuel energy generation, it is unlikely that IPPs will opt for investments in the installation of fossil-fuel generation over renewable energy generation.** These legislative requirements include the Minimal Emissions Standards set out in the



NEM: Air Quality Act (Act No. 38 of 2004), the Carbon Tax Act (Act No. 15 of 2019) promulgated in 2019, and the recent launch of BID windows by the Government specifically for renewable energy generation projects. It is anticipated that the installation of fossil-fuel energy generation by IPPs will be insignificant and unlikely to exacerbate current GHG emissions, while still contributing to reduced emissions, due to the improved technology and stringent legislative minimal emission standards requirements for new installations compared with conventional “dirty” coal-fired power generation. Even though exempted from a generation license, IPPs will still be required to undertake an EIA to identify and mitigate any potential adverse environmental impacts related to either the installation of the selected renewable energy generation technology or fossil-fuel energy generation, and to obtain an environmental authorization in line with the National Environmental Management Act (Act No. 107 of 1998). Under the new proposed guidelines for consideration of climate change implications in environmental authorizations, published by the DFFE for public review in June 2022, fossil-fuel energy generation installations will be required to assess and determine their contribution to GHG emissions as part of their EIA and air emissions license application. The South African legislative framework, together with the application of the guidelines once adopted, will help to ensure that impacts such as GHG emissions and air pollution associated with the installation of new fossil-fuel energy generation are mitigated and monitored to prevent adverse impacts on the environment, forests and natural resources.

5.3. PFM, DISBURSEMENT AND AUDITING ASPECTS

- 120. The recipient is the Republic of South Africa.** The loan is for US\$750 million. The closing date for the loan is June 30, 2023.
- 121. South Africa has a satisfactory financial management system.** The country’s fiduciary framework is adequate to support the proceeds of the credit as evidenced by the conclusions of the 2014 Public Expenditure and Financial Accountability (PEFA) and ongoing Public Financial Management (PFM) reforms. The 2014 PEFA indicates that South Africa continues to maintain its impressive record of fiscal discipline. The PFM systems, as guided by the PFM Act, provide a sound basis for resource allocation according to priorities. The PFM Act outlines the duties of national, provincial, municipal government and public entities in relation to the level of service provision required under each unit of government. The PFM Act establishes the two main government funds: (i) the National Revenue Fund (NRF), where all government revenue, both domestic and foreign, are deposited; and (ii) the Reconstruction and Development Programmes (RDP) Fund, where all development assistance funds are deposited. Appropriation out of the NRF is only by parliamentary approval, while the RDP Fund is based on financing agreements with each development partner and national priorities.
- 122. South Africa has a strong PFM framework.** The Government applies a MTEF, which is premised upon a three-year rolling macro-fiscal framework, is program prioritized, and has an efficient re-programming of resources and program implementation controls. Furthermore, it serves as a firm budget allocation guideline for the management of departmental revenue collection and expenditure. The chart of accounts is fully aligned with the budget structure. Both the recurrent and capital budget preparations are integrated into a single budget process managed by the National Treasury. The budget documentation is reviewed by a number of committees in Parliament pre- and post-approval (implementation phase), and are available for public access. The budget is annually published on the Government’s website. During budget



implementation, the National Treasury within 30 days after the close of the preceding month compiles and publishes in the government gazette, a statement of revenue, expenditure and actual borrowings of the National Revenue Fund. The financial reports provide information on the current period and the period to date, as the case may be, comparing budgets to actuals and variations thereon. Over the years, South Africa has consistently entrenched its reputation as a global leader in budget transparency. In fact, the country ranked first out of 117 countries in the 2019 Open Budget Index conducted by the International Budget Project.

- 123. The Accountant General is responsible for the preparation of consolidated financial statements and on improving the timeliness, accuracy and efficiency of financial reporting.** Each department prepares its own financial statements within two months, i.e., by May 31, and submits them to the Auditor General. They are audited by June 30 and sent to the Accountant General for consolidation. The draft Consolidated Financial Statements are submitted to the Auditor General by mid-August. These timelines are always met. In addition, the consolidated audited financial statements are published for public access within the stipulated timelines.
- 124. The Government continues to implement reforms to further strengthen PFM systems.** The reforms address weaknesses identified in 2014 PEFA and other reports such as the annual Auditor General (AG) reports. The AG has consistently reported weaknesses in supply chain management resulting from irregular expenditure, unauthorized spending, and wasteful and fruitless expenditures, non-compliance with legislation, and a number of auditees producing poor quality financial statements. A number of development partners are supporting the Government to implement these reforms, the major ones being the European Union, GIZ, DFID, USAID, and the Governments of France, Ireland and Belgium.
- 125. External auditors have reported no concerns with the audited financial statements of the South Africa Reserve Bank (SARB).** The independent external auditors issued an unqualified audit report for the period to March 31, 2021. The audited financial statements of the SARB are published on its website. The IMF has not undertaken a safeguard assessment on the SARB.
- 126. The proposed operation would consist of a single tranche of US\$750 million disbursed upon satisfactory implementation of the development policy program.** The operation would follow the IBRD's disbursement procedures for DPOs and would not be linked to specific expenditures. Once the Financing Agreement becomes effective and a withdrawal application has been received, the IBRD will deposit the loan proceeds into an account designated by the Government at the SARB—provided the IBRD is satisfied with the program being carried out by the Government and with the appropriateness of the country's macroeconomic policy framework. The deposit will be part of the country's foreign exchange reserves. The Government will credit the local-currency equivalent in the budget management system using the prevailing exchange rate. As a due diligence measure, the Government will provide the IBRD with confirmation that the amount of the loan proceeds has been accounted for in the country's budget management system, with an indication of the exchange rate applied and the date of transfer, and that the account used to deposit loan proceeds is part of the country's foreign exchange reserves. The confirmation will be expected within 30 days of disbursement. If the proceeds of the loan are used for excluded expenditures as defined in the Financing Agreement, the IBRD will require a direct refund of an amount equal to payment, promptly upon notice from the IBRD. Amounts refunded to the World Bank



upon such request will be canceled. No dedicated account is required since the control environment is assessed to be adequate.

- 127. Auditing requirements.** The budgeted public expenditures to be financed by the loan's South African rand equivalent will be subject to external audit by the auditor-general under the normal auditing arrangements applicable to the Government. The IBRD will have access to these audit reports.

5.4. MONITORING, EVALUATION AND ACCOUNTABILITY

- 128. The WBG and the DPME at the Presidency of the Republic of South Africa have agreed to jointly monitor the result indicators of this operation, as an integral part of the monitoring of the Government's implementation of its response to the COVID-19 pandemic.** The World Bank, in partnership with the Open Government Partnership, will help the DPME build a dashboard to monitor select indicators of the Government's response and support a platform for government to work with citizens, civil society and business, to track spending on the COVID-19 response, so that the resources achieve their intended goals. In doing so, the World Bank builds on years of sharing international good practice in performance monitoring and evaluation.
- 129.** According to the 2018–2019 Auditor Generals' Public Finance Management Act Report, the disappointing audit outcomes in 2018–19, the slow progress over the past five years in implementing audit recommendations, and the insights gained from the first year of implementing the material irregularity process, all show that the system of accountability within public sector had reached a point where accounting officers and authorities need to invest in preventative controls. Notable was that only 36 percent of auditees complied with supply chain management legislation, and that the award of contracts to employees and families of public servants, and cases of conflict of interest, had all increased. With an already weak control environment, the national state of disaster caused by the COVID-19 pandemic has provided an environment for possible abuse of emergency procedures and relief funds, by both the public sector and the private sector.
- 130. In support of transparency, the Government has established the e-tenders portal.** This provides a free single point of access to information on all tenders (invitations, corrigendum and award notices) made by all public sector organizations at all spheres of government. This includes tenders of, among others, all national and provincial departments, metros, district municipalities, local municipalities, municipal entities, all public entities, SOEs, constitutional bodies, etc. While the site lists the procurement opportunities, the actual full procurement notice and the tender documents are only available from the procuring entity themselves. Information on awarded contracts is provided on the site but is not current, and in some cases is incomplete. These inadequacies hinder the transparency objective. Using the Promotion of Access to Information Act (2000) and the Promotion of Administrative Justice Act (2000), the public and civil society can gain access to pertinent information or cause the Public Protector of South Africa to investigate allegations.
- 131. According to the Statement on the virtual Cabinet Meeting of Wednesday, August 5, 2020, allegations of corruption concerning COVID-19 procurements and funds have surfaced.** The allegations being investigated include the fraudulent distribution of food parcels, social relief grants, procurement of PPEs and other medical supplies, and the looting of the UIF's COVID-19 Temporary Employee/Employer Relief Scheme. Measures to deal with the allegations include establishing a special coordination center to strengthen the



collective efforts among law-enforcement agencies to prevent, detect, investigate, and prosecute COVID-19-related corruption. In addition, President Ramaphosa recently signed a proclamation authorizing the Special Investigations Unit (SIU) to investigate any unlawful or improper conduct in the procurement of any goods, works and services during or related to the national state of disaster in any state institution. The Cabinet also approved the setting-up of a team of five ministers to, among others, look into all COVID-19-related procurements made during the lockdown period and strengthen current procurement systems. All government departments will be expected to submit all procurement contracts awarded during this period to this ministerial team to be published and made accessible to the public. Additional short-term measures could also include: (i) timely consequence management; (ii) enhancing the functionality of the e-tenders portal as noted above to improve the transparency on all public contract awards; and (iii) third-party monitoring and risk-based specialized independent audits. Long-term measures could include concerted efforts to professionalize the procurement cadre, and the rolling-out of a fully-fledged electronic government procurement system. With procurement and contract data becoming available in electronic format, the use of analytical tools will improve the quality of reporting on public spend information, identifying red flags, and making evidence-based decisions and policies.

- 132. Grievance Redress.** Communities and individuals who believe that they are adversely affected by specific country policies supported as prior actions or tranche release conditions under a World Bank Development Policy Operation may submit complaints to the responsible country authorities, appropriate local/national grievance redress mechanisms, or the WB's Grievance Redress Service (GRS). The GRS ensures that complaints received are promptly reviewed in order to address pertinent concerns. Affected communities and individuals may submit their complaint to the WB's independent Inspection Panel, which determines whether harm occurred, or could occur, as a result of WB non-compliance with its policies and procedures. Complaints may be submitted at any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the World Bank's corporate Grievance Redress Service (GRS), please visit <http://www.worldbank.org/GRS>. For information on how to submit complaints to the World Bank Inspection Panel, please visit www.inspectionpanel.org.

6. SUMMARY OF RISKS AND MITIGATION

- 133. The overall risk rating for this DPO is substantial.** This assessment reflects several interrelated risks that may jeopardize the achievement of the program development objectives. These risks include: (i) political and governance risks; (ii) macroeconomic risks; (iii) social and environmental risks; (iv) stakeholder risks; and (vi) the cross-cutting risks associated with the COVID-19 pandemic. Table 6 summarizes the risks. This assessment is consistent with that of CPF. Moderate risks include sector strategies and policies risks, implementation risks and fiduciary risks. Substantial risks are discussed in further detail.
- 134. Political and governance risks are rated as substantial.** The majority ruling African National Congress (ANC) party governs by consensus. It encompasses diverging and often opposing interests from trade unions, organized business, community leaders, and the party base about the timing, opportunity, formulation and implementation of reforms. The South African local elections were held on 1 November 2021. Although the ANC remains dominant, there was no absolute winner in 66 of the 230 contested municipalities



including in five of eight major cities. These municipalities will be governed by coalition and the ruling alliances will need to lead through compromise. This risk could impact program implementation in the event that the Government's ability to implement elements of the reform agenda could be delayed or even stalled due to a lack of political consensus.

- 135. Macroeconomic risks are substantial.** They also play out through multiple channels. Some of these risks stem from concerns about the sustainability of the trajectory of the debt, the reduction in revenues, the expanding deficit as a result of the socio-economic response to the COVID-19 pandemic, and the financial viability of large SOEs such as Eskom and Transnet. These substantial risks could impact the implementation of the program. These risks, already described in the downside scenario featured in Section 2 of this document, could increase further in the case of a resurgence of the COVID-19 pandemic. The adoption and implementation of fiscal and structural measures announced in the Medium-Term Budget Policy Statement in November 2021 will help mitigate these downside risks.
- 136. Social and environmental risks are substantial.** They are respectively appraised in detail in Sections 5.1 and 5.2 of this program document. The poverty and social risks posed by the onset of the COVID-19 pandemic in South Africa are significant. The poverty impacts are partially averted because public transfers are able to compensate many households for the income drop caused by employment losses during the crisis. Future waves of the COVID-19 pandemic could impact the implementation of this program, although prior actions 1, 2, 3 and 4 will help to mitigate these social risks. Environmentally, South Africa is reliant on fossil-fuel energy generation, and coal-fired plants in particular. The national power provider, Eskom, struggles to provide reliable power for South Africa's economy. Over the past 20 years, the Government has made significant strides in developing its framework for environmental management and mainstreaming environmental sustainability into decision-making processes. The capacity and track record of the DFFE in managing environmental risks associated with development initiatives and ensuring environmental compliance are well-established and will serve to mitigate some of the environmental risk. The prior actions 6, 7, and 8 in this program document will help to mitigate these climate and power risks. However, the implementation of this program could be at risk if the South African Government were to fall behind schedule on the decommissioning of already announced coal-fired power plants.
- 137. Stakeholder risks are substantial and related to political risks.** The ruling ANC, trade unions and other stakeholders within the governing party's alliance have historically been cautious about borrowing from IFIs, out of concerns about the surrender of policy autonomy, which could present an implementation risk for this program. The severity of the COVID-19 crisis has made it necessary for the Government to access IFI development financing to sustain its reform efforts and maintain the capacity of the state to implement its development goals. Continued government ownership of the actions this DPO supports will help mitigate stakeholder risks.
- 138. The risk from the COVID-19 pandemic stems from cross-cutting concerns on the economy and the general welfare of the population and is assessed as substantial.** South Africa has recorded the highest number of confirmed cases of COVID-19 infections on the African continent. As of early November 2021, a total of three million positive cases and around 90,000 deaths had been reported. Its stringent lockdown, including the extended closure of businesses, schools and borders, and the enforcement of social distancing measures have enabled it to rein in the number of daily new infections. If there was another wave of the COVID-19 pandemic, this could present a risk to the implementation of the program. The Government's wide-ranging set of measures to support lives, livelihoods and business recovery has helped mitigate some



of the immediate impacts. Many of these measures are highlighted in this program document, including prior actions 1, 2, 3 and 4. As of mid-December 2021, ~27 million vaccine doses have been administered. The vaccine effort will contribute greatly to mitigating the risk of severe illness, hospitalizations and death. The EVDS provides an efficient, digitally enabled platform to register vaccines and is discussed in detail in prior action 4. Table 6 rates this risk under “Other Risks”.



Table 6: Summary Risk Ratings

Risk Categories	Rating
1. Political and Governance	● Substantial
2. Macroeconomic	● Substantial
3. Sector Strategies and Policies	● Moderate
4. Technical Design of Project or Program	● Moderate
5. Institutional Capacity for Implementation and Sustainability	● Moderate
6. Fiduciary	● Moderate
7. Environment and Social	● Substantial
8. Stakeholders	● Substantial
9. Other	● Substantial
Overall	● Substantial



ANNEX 1: POLICY AND RESULTS MATRIX

Alignment with WB COVID-19 Crisis Response Approach Paper: in red, relief; in blue, restructuring; in green resilient recovery

Prior actions	Results			
Prior Actions under DPF	Indicator Name	Baseline	Target	Source
Pillar One --- Protecting the poor and modernizing social welfare				
PA 1: COVID-19 Grants: To protect vulnerable households from the economic impact of the COVID-19 crisis and to support informal sector workers, the Borrower, through its Department of Social Development, has issued directions through Government Notice No. 681, which: (a) re-introduce the COVID-19 Social Relief of Distress (SRD) Program that provides grants to unemployed and informal sector workers who are not eligible for unemployment insurance benefits; and (b) expand the SRD Program to include unemployed caregivers who receive child support grants on behalf of children.	Indicator 1: Number of people who receive SRD grants in response to the COVID-19 crisis, in millions	6 million people, in the first phase of the program from March 2020 to March 2021 (March 2021)	An additional 3.4 million people benefit from the second phase of the program, i.e., 9.4 million in total (June 2022)	Department of Social Development, SRD report
PA 2: Protecting jobs: To keep people, especially low-wage workers, connected to their jobs and ready to work when firms re-open, the Borrower, through its Department of Employment and Labor, has issued directions through Government Notice No. 637, which: (a) enhance the targeting of the COVID-19 Temporary Employer-Employee Relief Scheme (TERS) allowing furloughed workers in hardest hit industries; and (b) allow targeted works to receive cash payments directly to their bank accounts, in response to the national lockdown during the third wave of COVID-19 infections.	Indicator 2: Number of workers who received benefits from the UIF-TERS	3.5 million workers (March 2021)	120,000 additional workers, i.e., 3.6 million workers in total (June 2022)	Unemployment Insurance Fund, TERS Report



<p>PA 3: Digital social protection: To improve the transparency, targeting, and efficiency of social grant programs, the Borrower, through its Department of Social Development, has issued directions through Government Notice No. 681, which introduce the use of electronic means to allow for digital application procedures and automated cross-checking to verify eligibility.</p>	<p>Indicator 3: Total value of SRD grants disbursed using digital application and verification procedures, in billion South African Rand.</p>	<p>R 19.5 billion (March 2021)</p>	<p>R 26 billion (June 2022)</p>	<p>Department of Social Development</p>
<p>PA 4: Digital health: To improve equitable access to COVID-19 vaccines, the Borrower, through its National Department of Health, has launched the South African Covid-19 Programme Registration , which introduces the use of an Electronic Vaccination Data System (EVDS), compliant with the applicable data protection and privacy legislation, in the rolling-out of the Borrower's COVID-19 vaccination program, setting the stage for future health emergencies, as further evidenced in the COVID-19 Implementation Guide and Toolkit.</p>	<p>Indicator 4: Number of people fully vaccinated and registered on EVDS, in million</p>	<p>0 million (February 2021)</p>	<p>26.5 million (December 2022)</p>	<p>Department of Health</p>
<p>Pillar Two --- Accelerating a resilient and sustainable recovery</p>				
<p>PA 5: Financial resilience: To increase the resilience of the financial sector, the Borrower, through its National Assembly, has approved the Financial Sector Law Amendment Bill, which establishes a resolution regime and enables provisions for the Corporation of Deposit Insurance.</p>	<p>Indicator 5: Eligible deposits insured, in percentage</p>	<p>0 percent of deposits (November 2021)</p>	<p>80 percent of deposits (December 2022)</p>	<p>Corporation for Deposit Insurance</p>
<p>PA 6: Climate change response: To enable the development of an effective climate change response and the long-term, just transition to a climate-resilient and lower-carbon society, the Borrower, through its Cabinet, has approved the National Climate Change Bill and its submission to Parliament.</p>	<p>Indicator 6: Department of Forestry, Fisheries, and Environment (DFFE) presents Sectoral Emissions Targets (SET) for 5 key carbon-intensive</p>	<p>0 Key carbon-intensive Sectoral Emissions Targets presented by DFFE to the respective line ministries</p>	<p>5 Key carbon-intensive Sectoral Emissions Targets presented by DFFE to the respective line ministries (June</p>	<p>Department of Forestry, Fisheries, and Environment (DFFE)</p>



	sectors: Energy (DMRE), Transport (DoT), Trade and Industry (Dtic), Agriculture (DALRRD); and Water and Sanitation (DWS) to the respective line ministries	(November 2021)	2023)	
PA 7: Greenhouse gas mitigation: To more closely align South Africa with the Paris Climate Agreement, the Borrower, through its Cabinet, has approved the updated First Nationally Determined Contribution (NDC), which sets more ambitious greenhouse gas (GHG) mitigation targets for 2025 and 2030.	Indicator 7: Avoided CO ₂ emissions as a result of the shut-down of coal-fired power production, in tons	0 tons CO ₂ avoided (October 2021)	900,000 tons CO ₂ avoided (June 2023)	Eskom
PA 8: Energy expansion. To increase competition and power generation capacity in the energy sector, the Borrower, through its Department of Mineral Resources and Energy, has amended Schedule 2 to the Electricity Regulation Act through Government Notice No. 737, which exempts from licensing embedded generation with a nominal installed capacity below 100 megawatts as per Schedule 2 to the Electricity Regulation Act.	Indicator 8: Embedded Generation Capacity under 100 MW registered under NERSA, in MW	206 – 330 MW (October 2021)	1,500 MW (December 2022)	NERSA registration records



ANNEX 2: FUND RELATIONS ANNEX

**FOR
INFORMATION**

FO/DIS/21/152
November 9, 2021

To: Members of the Executive Board
From: The Secretary
Subject: **South Africa—Assessment Letter for the World Bank**
Board Action:
Executive Directors' **information**
Publication:
Not yet decided*
Questions: Ms. Coronel, AFR (ext. 38119)
Mr. Miyajima, AFR (ext. 39395)

South Africa—Assessment Letter for the World Bank

November 9, 2021

This assessment letter, requested in relation to a World Bank's Development Policy Financing Operation, provides an update on economic developments and the outlook in South Africa since the Rapid Financing Instrument (RFI) staff report was issued in July 2020. The assessment is based on preliminary data and information available to the team ahead of the Medium-Term Budget Policy Statement (MTBPS) and the Article IV consultation mission scheduled for later in November 2021.

Recent Economic Developments

1. South Africa entered the COVID-19 pandemic facing subdued growth and

deteriorating macroeconomic conditions. Per-capita output growth stagnated in the decade preceding the pandemic as private investment lost dynamism, productivity deteriorated, and business confidence faltered, in a context of widespread corruption, state capture, and difficulties to muster political support to implement much-needed structural reforms. As subdued growth and delayed adjustment and reform eroded fiscal and external strength, the sovereign's credit ratings were lowered to below investment grade. Amid significant structural rigidities, unemployment worsened, a large share of the population fell deeper into poverty, and South Africa remains one of the most unequal societies in the world despite its formidable growth potential. Well-targeted social grants support large segments of the population and arguably limit social discontent, albeit at a high fiscal cost.

2. The COVID-19 crisis has exacerbated South Africa's vulnerabilities. Three waves have hit the country (2.9 million cases), leaving considerable loss of life and social and economic challenges. Although the rate of infection has significantly fallen, the vaccination rollout has suffered setbacks



(about 20 percent of the population out of a targeted 67 percent has been fully vaccinated). As the pandemic worsened, the nation witnessed a sharp contraction in output, large capital outflows, and significant asset price and exchange rate depreciation. The government reacted swiftly by announcing a large fiscal package to assist affected households and businesses. The SARB supported lending and liquidity conditions to safeguard price and financial sector stability. The government's COVID-19-related interventions have worsened the fiscal and debt positions, which were already under strain from large fiscal transfers to SOEs and a high wage bill. Monetary accommodation was supportive albeit somewhat constrained by potential inflationary pressures, notably from public wages, capital outflows, and attendant currency depreciation amid the uncertain global environment. Employment and private investment remain subdued with large adverse social implications.

3. Some key policy buffers mitigated the COVID-19 impact. A flexible exchange rate regime absorbed some of the negative impact of the shock; well-anchored inflation expectations, underpinned by a sound inflation targeting framework and strong central bank credibility, allowed for monetary accommodation; and deep domestic financial markets and strong bank balance sheets absorbed government financing, mainly in local currency and with relatively long maturities.

4. The rapid economic recovery surprised on the upside but may not be durable. Growth recovered faster than anticipated in the first half of 2021 (7½ percent year on year) despite the impact of multiple COVID-19 waves and frequent power outages due to public utility company Eskom's weaknesses. The recovery, however, was not accompanied by a rebound in private investment or a pickup in job creation, signaling its fragility—unemployment continued to worsen to 34 percent overall and a staggering 64 percent for the youth while bank lending remained weak. Benign global market conditions supported asset price recovery, but the term premium remained elevated, reflecting high fiscal risks. Bank soundness indicators were solid, but the potential delayed impact of protracted weak growth and a deepening bank-sovereign nexus warrants close monitoring. On the positive side, the external current account balance temporarily improved to a record-high surplus from historical deficits as favorable commodity prices boosted exports and the pandemic reduced import volumes.

Outlook and Risks

5. On current policies, the near-term growth recovery is set to be followed by a lackluster medium-term outlook that would further increase macroeconomic vulnerabilities. IMF staff estimates output growth at 5 percent in 2021 but projects it to ease to 2.2 percent in 2022 and average 1.3 percent in the medium term, weighed down by structural constraints and less favorable terms of trade. The fiscal deficit is expected to narrow in 2022 to around 7 percent of GDP supported by favorable commodity prices, the phasing out of COVID-19-related measures, and some moderation in transfers to SOEs. However, the medium-term budget deficit is projected to remain high, at above 6 percent of GDP. On current policies, the growing interest bill would increasingly weigh heavily on fiscal expenditures. Financing of the deficit is expected to originate mainly from domestic sources as nonresident appetite is likely to remain dampened by high fiscal



risks and uncertain global market conditions. The debt ratio—close to 70 percent of GDP in 2020—is expected to slightly decline in 2021, but resume rising thereafter to reach about 80 percent of GDP by 2025. Inflation would remain around the center of the 3 to 6 percent official target range, and the external current account would return to a deficit in 2022 that would gradually widen to around 2½ percent of GDP in the medium term.

6. Main risks to baseline projections relate to the pace of adjustment and reform and to evolving global market conditions. Domestically, slower-than-expected progress or reversals in structural and governance reforms, adoption of populist measures, and/or lingering uncertainty about additional COVID-19 outbreaks amid vaccination delays, would weigh on investor sentiment and growth. In particular, Eskom raises macro-critical challenges, and a worsening of its operational and debt problems would have considerable adverse macro-fiscal consequences. Additional transfers to the troubled SOEs, wage bill overruns, and other current expenditure pressures could also lead to higher-than-expected budget deficits and debt, increasing the country's risk premium. Social unrest and greater policy uncertainty could damage confidence and halt growth. Externally, nonresident investor appetite for South African assets may be sapped by adverse developments, including de-anchoring of inflation expectations in advanced economies, increases in core yields, and widening of risk premia across emerging economies. By contrast, potential reform acceleration and lasting favorable terms of trade can sustain a fast pace of output growth and boost employment.

Macroeconomic Policies

7. Recent economic policies have been unsuccessful in addressing South Africa's structurally subdued growth and macroeconomic vulnerabilities. Increased fiscal expenditure has pushed government debt higher, but growth has remained unresponsive, hampered by sluggish productivity improvements, human capital weaknesses, and subdued private investment. The COVID-19 crisis has highlighted these vulnerabilities, particularly the limited resilience of the labor market, evidenced by rising unemployment. While the government has stressed the importance of good governance and structural reforms both in its development plan and in the Operation Vulindlela initiative, progress in implementing reform and encouraging private investment has been insufficient, weighing on the economic recovery. The weak and deteriorating performance of SOEs, particularly Eskom, is a considerable obstacle to economic efficiency and sound fiscal policy.

8. Policies must focus on turning the cyclical rebound into a lasting and inclusive recovery, while preserving macro-fiscal stability. Overcoming the COVID-19 pandemic by accelerating the pace of vaccination, preventing further infections, and continuing to support the most vulnerable remains a key near-term priority. At the same time, decisive fiscal consolidation and steadfast implementation of structural reforms are needed in the near term to make room for COVID-19-related spending considering the lack of fiscal space and the need to restore public debt sustainability. Bold and credible action in three critical areas is needed to achieve a sustainable growth revival:



- **Achieving a decisive fiscal consolidation to address debt sustainability concerns.** The February 2022 budget (for the fiscal year ending in March 2023) is an opportunity to put in place a credible growth-friendly consolidation package to stabilize debt and then set it on a declining path. This would require reining in pressures to deviate from a medium-term adjustment plan, including containing wage inflation—currently undermined by a compromising agreement with unions—and streamlining government transfers to inefficient SOEs. The consolidation effort will need to be based largely on expenditure to address the current distortions while protecting social spending and productive public investment. Revenue measures could complement the adjustment, particularly if aimed at reducing tax expenditures, addressing tax evasion, and taxing carbon. Ongoing reforms to improve planning and execution of public investment should be integrated in the budget process to avoid undue fragmentation. Introducing a well-designed and credible debt anchor to complement the existing expenditure ceiling would support these efforts.
- **Keeping inflation low and stable and preserving financial sector soundness.** The SARB is encouraged to maintain an accommodative monetary policy stance to support the economy while keeping inflation under control. However, inflation risks should be monitored vigilantly, particularly those coming from the fiscal stance and administered prices. The authorities' plans to gradually liberalize exchange controls, which should facilitate adherence to the OECD Codes of Liberalization, are welcome. With fiscal risks high and rising, the Prudential Authority should continue to closely monitor the financial sector-sovereign nexus. More broadly, measures to bolster the strength of the large and diverse domestic financial system amid a weak macroeconomic outlook should be implemented.
- **Implementing announced and pending structural reforms.** A streamlined and transparent business and regulatory environment that encourages competition and entrepreneurship is essential to attracting private investment in all sectors of the economy—a sine qua non condition to reignite growth. Deepening regional integration and resisting protectionism are necessary to reverse the declining productivity growth. Stepped-up efforts to streamline SOE operations to make them efficient and competitive and reduce their burden on the budget are crucial. Priority should be given to reforms in network industries considering their critical impact on the entire economy and the fiscus. A bold labor market reform strategy to make it more flexible will help the economy to benefit from a growing labor force. Sustained reform efforts would help secure an inclusive recovery and facilitate the transition toward a green economy in the digital age. Further efforts to improve governance and fight corruption would also provide a boost to productivity and economic growth.

Relations with the IMF

9. IMF Staff has continuously provided policy and technical advice to the authorities, including during the COVID-19 pandemic. The Article IV consultation mission is scheduled for November 17–December 6, 2021 and the Board discussion for early-February 2022. The IMF-World Bank Joint FSAP final mission took place in June 2021 and the findings will be presented to the IMF



Board at the time of the Article IV consultation discussion. Recent technical cooperation includes assistance on public wage bill management (end-2020) and on capital flow management (ongoing).

10. An RFI for 100 percent of quota (\$4.3 billion) was approved by the IMF Board on July 27, 2020. The RFI supported the authorities' efforts to address the challenging health situation and severe economic impact of COVID-19. Some progress has been made in meeting the governance and transparency commitments accompanying the RFI request, but there have been delays in completing the procurement (contracts and allocation) database of the National Treasury, and the publication of the COVID-19-related spending report on a regular basis is yet to start. South Africa is undergoing a Post-Financing Assessment (PFA) as its total GRA credit outstanding of SDR3.1 billion is above the threshold of SDR1.5 billion. South Africa's capacity to repay the Fund under the RFI is deemed adequate and will be reassessed during the forthcoming Article IV Consultation.

11. South Africa received an SDR allocation for 100 percent of quota (\$4.2 billion) in August 2021. The disbursement took place in the context of the 2021 General SDR Allocation to all members to help build FX reserves and confidence, and cope with the impact of the COVID-19 crisis.

Table 1. South Africa: Selected Economic Indicators, 2018–26

	2018	2019	2020	2021	2022	2023	2024	2025	2026
				Est.			Proj.		
National income and prices (annual percentage change)									
Real GDP	1.5	0.1	-6.4	5.0	2.2	1.4	1.3	1.3	1.3
CPI (annual average)	4.6	4.1	3.3	4.4	4.5	4.5	4.5	4.5	4.5
Output gap (percent of potential real GDP)	-0.9	-2.0	-9.5	-5.1	-3.2	-2.3	-1.6	-1.0	-0.7
Labor market (annual percentage change)									
Unemployment rate (percent of labor force, annual average)	27.1	28.7	29.2	33.1	34.0	35.8	37.0	37.6	38.3
Savings and Investment (percent of GDP)									
Gross national saving	13.3	13.3	14.7	16.4	14.1	13.8	13.7	13.7	13.6
Public (incl. public enterprises)	1.3	1.0	-3.5	-2.0	-0.2	0.4	0.4	0.2	-0.1
Private	12.0	12.3	18.2	18.4	14.3	13.4	13.3	13.5	13.7
Investment (including inventories)	16.5	16.0	12.7	13.5	15.0	15.2	15.4	15.7	16.0
Public (incl. public enterprises)	4.8	4.3	3.9	3.5	3.6	3.6	3.5	3.5	3.5
Private	11.0	11.1	9.8	9.7	10.1	10.3	10.6	10.9	11.2
Fiscal position (percent of GDP) 1/									
Revenue, including grants	26.4	26.9	25.2	25.1	26.1	26.2	26.3	26.3	26.4
Expenditure and net lending	30.2	31.7	36.0	33.6	33.1	32.5	32.5	32.8	33.2
Overall balance	-3.7	-4.8	-10.8	-8.4	-7.0	-6.4	-6.2	-6.5	-6.8
Primary balance	-0.3	-1.1	-6.6	-4.1	-2.2	-1.2	-0.7	-0.5	-0.2
Gross government debt 2/	51.6	56.3	69.4	68.8	72.3	74.9	77.4	80.2	83.0
Balance of payments (percent of GDP unless otherwise indicated)									
Exports of Goods and Services (volume, annual percentage change)	2.8	-3.4	-12.0	12.2	1.8	3.1	3.1	2.9	2.9
Imports of Goods and Services (volume, annual percentage change)	3.2	0.5	-17.4	15.1	11.3	4.4	4.0	3.6	3.6
Current account balance (billions of U.S. dollars)	-13.1	-10.6	6.6	11.9	-3.8	-6.3	-7.9	-9.7	-12.8
percent of GDP	-3.2	-2.7	2.0	2.9	-0.9	-1.4	-1.7	-2.0	-2.4
Overall balance	0.2	0.5	-1.0	1.1	-0.1	-0.2	-0.2	-0.2	-0.2
Gross reserves (billions of U.S. dollars)	51.6	55.1	55.5	60.0	59.8	58.7	57.6	56.5	55.4
percent of short-term debt (residual maturity)	89.2	98.4	76.7	88.2	86.2	84.3	77.3	75.4	75.5
Total external debt	42.6	47.6	56.4	45.1	44.2	43.5	43.5	44.7	44.6

Sources: Haver, South African National Treasury, World Bank, and Fund staff estimates and projections.

1/ Consolidated government unless otherwise indicated.

2/ National government.



ANNEX 3: DRAFT LETTER OF DEVELOPMENT POLICY



MINISTRY: FINANCE
REPUBLIC OF SOUTH AFRICA

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Ref: M3/4/2/2(463/2021)

Mr. David Malpass
President
World Bank Group
WASHINGTON D.C
USA

Dear Mr. David Malpass,

LETTER OF DEVELOPMENT POLICY

On behalf of the Government of South Africa, I am writing to request the support of the World Bank Group (WBG) for a Development Policy Operation (DPO) loan of \$750 million to assist in the country's fight against the COVID-19 pandemic. This request comes at a time when the Government of South Africa is seeking to strengthen its long-term partnership with the WBG through a Country Partnership Framework (CPF) that sets out joint priorities over the next years. My letter outlines the impact of COVID-19 on South Africa and the measures the Government of South Africa has taken to protect people's lives and livelihoods and support the country's economic recovery.

i. Health, Social and Economic Impact of COVID19 on South Africa

The health impact

The COVID-19 pandemic has already exacted a tremendous toll on the lives and livelihoods of South Africans. South Africa currently ranks seventieth worldwide in terms of the total number of confirmed COVID-19 cases. It has recently emerged from a third large wave of infection. As at November 2nd, 2021, the total number of confirmed COVID-19 cases in the country stood at 2.9 million, the number of recoveries was 2.4 million recoveries and the number of deaths 89 197. South Africa has a large number of people living with HIV, which may make them more vulnerable to COVID-19. To date 15.3 million South African have been vaccinated for COVID-19.

The Government of South Africa declared a national state of disaster on March 15th, 2020, ten days after the first COVID-19 infection was detected. It imposed a five-week nation-wide lockdown as of March 27, 2020. The swift response of the Government of South Africa slowed the transmission of the virus and bought more time to prepare the healthcare sector for a surge in cases, but infection rates and deaths continued to increase after the lockdown was progressively lifted starting from June 1, 2020. Since then, restrictions have been reintroduced and lifted in response to the second and third waves. Investments in the public health system aim to ensure that the Government has sufficient capacity to manage the continued spread of the virus. An amount of R21.5 billion was made available to the healthcare response in the 2020/21 special



adjustments budget and R19.3 billion has been allocated in 2021/22, of which R10.3 billion is to the vaccination programme. As of 2 November 2021, 15.3 million people have been vaccinated, of which 12.5 million are fully vaccinated.

The economic impact

The normalisation of economic activity from 2020 continued in the first half of 2021, when South Africa's GDP rose by 7.5 per cent compared with the first half of 2020. The rapid recovery was supported by global growth, export commodity prices and the easing of Covid-19 lockdown restrictions. However, significant domestic factors weigh on the momentum in the second half of 2021. Sectors such as manufacturing, wholesale and retail, restaurants, hospitality, and recreation, were particularly hard hit by the combination of the third wave of COVID-19 infections, public violence and disruptions to Transnet as a result of fire and cyber-attacks. Despite this; the IMF (October WEO) expects the economy to grow by 5.0 per cent in 2021, stabilizing at 2.2 per cent in 2022. In addition, the benchmarking and rebasing exercise conducted by Statistics South Africa and the Reserve Bank in August 2021 has resulted in GDP being 11 per cent larger than previously estimated.

Risks to growth are high both in the global and domestic environments and present downside risks to economic growth in South Africa. The evolution of the Covid-19 pandemic, possible future waves of infection, and subsequent government responses are central to broader economic recovery and normalization. In addition, higher-than-anticipated, and more persistent, global inflation is expected to drive monetary policy tightening in advanced economies, led by asset purchase tapering first and then followed by increased interest (policy) rates. This is expected to reduce excess liquidity in global financial markets, placing downward pressure on equities and upward pressure on bond yields. The latter will feed into more expensive government borrowing and lower fiscal space and ability to respond to any further Covid-19 (or other) related disasters. Domestically, policy uncertainty and the slow implementation of structural reforms, particularly around electricity supply constraints, continue to weigh on business confidence and investment, while any further deterioration in the public finances could trigger further credit rating downgrades, resulting in increasing borrowing costs that crowd out public spending on service delivery and infrastructure.

A prolonged weakness of the South African economy sharply increases the risk of negative spillovers to the Sub-Saharan African region in general and its southern half in particular. South Africa's estimated nominal GDP in 2019 accounted for about one fifth of Sub-Saharan Africa's total, and around half the GDP of the 16 countries members of the Southern African Development Community (SADC). Spillover channels are likely to manifest themselves in falling trade, reduction in cross border investment, contraction in remittance flows and lower fiscal transfers to the four neighbouring countries that are part of the Southern African Customs Union (SACU).

The social impact

The economic restrictions imposed to slow the spread of COVID-19 have led to severe distress for households that lack income and savings, as shown by the long queues for food parcels. Between three and five million informal-sector workers and their families are particularly vulnerable. Nearly 3.5 million South Africans risk falling into poverty. With a Gini coefficient of 0.63, South Africa remains the most unequal countries in the world. This makes overcoming these challenges very complex, in an environment of low growth and insufficient job creation. Accordingly, the Government of South Africa has expanded the reach of its social protection system by providing temporary Social Relief of Distress grants to over three million vulnerable people not receiving other forms of social assistance. It has done so by using electronic means



that only eligible applicants receive this assistance, without duplication. Equally significantly, it has temporarily increased social grants to 17.5 million existing recipients of old age pension, child support grants, disability grants and other smaller grants.

ii. Bold fiscal relief measures

In 2020/21, the government of South Africa announced one of the largest fiscal support packages among emerging and G20 countries in response to the social and economic effect of the COVID-19 pandemic. The announced package amounted to R500 billion (around \$26 billion) in relief measures in 2020/21 which consisted of R200 billion in credit guarantee scheme for medium and small businesses, R70 billion in tax deferrals and payment holidays to ease liquidity constraints that businesses were facing, R40 billion in wage protection measures through the Temporary Employee Relief Scheme (TERS) and R190 billion expenditure measures (of which R145 billion of the expenditure measures were adopted in 2020/21).. The expenditure measures include:

- **Spending on healthcare** to manage the spread of the virus, undertake mass testing and contact tracing, procure Personal Protective Equipment (PPE) and support the treatment of those affected by the diseases (R20 billion).
- **Support for vulnerable, low-income households** to meet their basic food security needs, provide time bound top-up of existing social grants and introduce new COVID19 tailored grants (R50 billion). Through our local government, we are also providing additional support for cleaning, sanitizing and provision of clean water to poor and rural communities (R20 billion).

In June 2021, the President announced a fiscal support package for 2021/22 to respond to the recent developments in the Covid-19 pandemic and unrest, mainly in KwaZulu-Natal and Gauteng. The package includes R5 billion in revenue foregone measures, specifically an expansion of the Employment Tax Incentive (ETI) for four months from 1 August 2021 and spending measures amounting R33.9 billion. These spending measures include:

- A temporary re-introduction of the R350 Social Relief of Distress (SRD) grant until the end of the financial year, at a cost of R26.7 billion. The SRD grant will include support to child caregivers on an application basis.
- Financial backing of SASRIA of R3.9 billion, pending a regular assessment of the insurance payouts.
- Support to small businesses that are not covered by SASRIA amounting to R2.3 billion. These amounts are composed of reprioritisation of R1 billion and additions of R1.3 billion to the baselines of the Department of Trade, Industry and Competition and the Department of Small Business Development.
- R950 million of additional funds will be allocated to the Police (R250 million) and the South African National Defence Force (SANDF) (R700 million).

In addition to the above, the Unemployment Insurance Fund (UIF) set aside R5.3 billion for the extension of the Covid-TERS coverage. The fiscal support package is also underpinned by an acceleration of the vaccination programme. Fiscal indicators show that government is sufficiently ahead of its revenue estimate to accommodate the fiscal relief measures.



iii. Monetary policy support to the financial sector and real economy

The SARB has undertaken extraordinary measures to support the economy within the confines of its mandate, by lowering the policy rate and providing market liquidity. It cut its policy rate by 2.75% since February 2020, taking the rate to its lowest level on record. In addition, the SARB released capital buffers for banks to keep credit flowing to the real economy. To ensure orderly market functioning, the SARB purchased government bonds on the secondary market. The SARB remains committed to managing inflation within its target range and to ensuring soundness of the financial system.

iv. Fiscal consolidation

The 2021 Budget is framed by two policy objectives: promoting economic recovery and returning the public finances to a sustainable position. Returning the public finances to a sustainable position will require ongoing restraint in expenditure growth and implementation of structural reforms to support economic growth. In this context, the fiscal stance aims to narrow the deficit and stabilise the debt-to-GDP ratio, primarily by controlling non-interest expenditure growth; provide continued support to the economy and public health services in the short term, without adding to long-term spending pressures; and improve the composition of spending, by reducing growth in compensation while protecting capital investment. Net reductions to main budget non-interest spending from the 2020 Budget to the 2021 Budget amount to R264.9 billion over the 2021 medium-term expenditure framework (MTEF) period. The 2021 Budget confirmed that government remains on track to achieve a primary fiscal surplus by 2024/25 and stabilise debt in the following year.

v. Reforms for long-term growth and recovery

South Africa faces structural problems that are well identified in its National Development Plan. These constraints include high levels of inequality, spatial disparities, low levels of education and uneven quality of public services. Policy uncertainty has weighed on business confidence, compounded by electricity supply shocks. Inefficient and ineffective investment spending by state-owned corporations (SOCs), such as the electricity utility Eskom, has slowed productivity growth. The Government of South Africa has pledged to boost the economy's potential growth by addressing the most binding microeconomic constraints, including;

- **Easing doing business** by supporting the development of Micro, Small and Medium Enterprises (MSME) through measures that address lack of competition, high levels of concentration in the economy, distorted ownership patterns, and red tape. The reforms are in line with the target to place South Africa within the top 50 global performers in the World Bank Doing Business index. Although the index has been discontinued, work to simplify the regulatory environment and simplify business processes critical to economic growth and development is ongoing through Invest SA.
- **Modernizing our network industries** such as road, rail and telecommunications to lower costs, increase efficiency and improve business competitiveness. Our network industries are dominated by state owned corporations (SOC), with low levels of competition and efficiency. The Investment and Infrastructure Office located in the President's Office is coordinating initiatives across government to crowd in private sector investment in these network industries as well as to improve the quality and efficiency of implementation. A new project pipeline was announced at the Sustainable Infrastructure Development Symposium SA (SIDSSA) containing 55 projects to the value of R595 billion. Approximately one third of the projects



announced for the 2020 pipeline, valued at R119 billion, are currently under construction or have been completed.

- **Increasing electricity supply**, which remains a key constraint to economic growth. Cabinet is committed to implementing energy sector reforms, such as the unbundling of Eskom into self-standing business units for generation, transmission and distribution. In line with our long-term energy plan, the Integrated Resource Plan 2019, the Government of South Africa is supporting the decommissioning of coal fired power stations and private-sector participation in electricity production. The Department of Mineral Resources and Energy is planning to acquire power from private players under a new bid window of our Renewable IPPs Program and will allow municipalities to procure power directly from the private sector. Importantly, to encourage private sector-led job-creation and investment into renewable energy, the Department of Mineral Resources and Energy raised the capacity limit for electricity self-generation exempt for licensing from 1 megawatt to 100 megawatts which should alleviate pressure on the grid over the medium term.
- **Investing in a green economy** through a Just Transition present an opportunity for the South African economy to decarbonize the economy in a way that leads to inclusive economic development. Setting ambitious climate goals through the NDCs and prioritizing this Just Transition in energy in particular has positioned South Africa for partnerships and significant climate finance. This includes commitments coming from COP 26 where key partners in the EU, USA and UK have committed \$8.5 billion to fast tracking South Africa's decarbonisation. In the long run the green trajectory of the economy should result in significant structural reform and jobs created in key green sectors.
- **Developing the digital economy** as a catalyst for growth. Our Information and Communication Technology (ICT) regulator plans to conclude the process of permanent licensing of the high-demand spectrum (HDS) in the short term and finalise migration from analogue to digital signals. This long-awaited measure will unblock the growth of the telecommunications sector and promote innovation, job creation. It will also bring new services, including adapting distance education for learners at all levels, a critical measure in the socially distanced environment of COVID-19. The rest of Southern Africa depends on South Africa's digital infrastructure, technology know-how, financial services sector, higher education system and talent, meaning that these positive developments in South Africa will benefit the whole region.
- **Fighting corruption.** Last but not least, the Government of South Africa is determined to reinforce transparency and accountability in the use of public monies. In a demonstration of its commitment to transparency and accountability and to confront allegations of corruption, the Office of the Chief Procurement Officer (OCPO) has published all transactions on Covid-19 as reported by government institutions for the supply of goods and services relating to the COVID-19 pandemic on the National Treasury website. Cabinet established a ministerial team to compile and collate a comprehensive report of the details of all transactions by national departments, provincial governments and more than seventy other public entities as part of the response to the coronavirus pandemic. To date 95% of provincial and national departments and state entities have submitted all information regarding COVID-19 procurement to the Ministerial team. On 25 August the OCPO issued instruction to all government institutions on reporting guidelines for covid-19 related expenditure and as from end September 2020 the NT will publish monthly reports on this expenditure. In addition, the Department of Monitoring and Evaluation has developed a framework to monitor the implementation of the socio-economic measures to respond to the COVID-19 pandemic, and the Auditor General will be of course auditing the use of COVID-19 resources.



vi. A coalition to support South Africa

South Africa's financing needs have risen sharply as the Government of South Africa responds to this unprecedented emergency. The Government will be largely relying on its own resources and drawing on the deep domestic financial markets. However, it has also drawn on its development partners including the IMF, AfDB, NDB, EU and is now drawing on the World Bank and other bilateral partners. The IMF, AfDB and NDB Boards have already approved their loans. Timely financial support from the World Bank will allow the Government of South Africa to weather the crisis and set the stage for a recovery path and long-term development for the country.

vii. Value that the World Bank support will bring to South Africa

As an upper middle-income country, South Africa has endeavoured to maintain a prudent macro fiscal policy environment, meeting its financing needs through access to deep liquid domestic and international capital markets over the last two decades. This is the first time in South Africa's history as a shareholder of the World Bank Group that we reach out to request budget support. The proposed loan will assist the Government of South Africa to address the immediate challenge of financing critical health and social safety net programmes whilst also continuing to develop our structural reform agenda to build back better.

The proposed WBG budget support operation aligns with the three components of the socio-economic program of the Government of South Africa: (a) protecting the poor and vulnerable; (b) ensuring sustainable growth and job creation; and (c) strengthening policies, institutions and investments for rebuilding better, including first steps to addressing the country's structural challenges. It seeks to strike a delicate balance between short-term response and long-term economic transformation. Its design and choice of prior actions build on Governments' strong commitment and its desire to lead the change. South Africa is also actively working to strengthen its long-term partnership with the WBG through the recently approved Country Partnership Framework (CPF). There is broad agreement with stakeholders on the three CPF focus areas; namely: (i) promote increased competition and improved business environment for sustainable growth; (ii) strengthen the performance and skills development of MSMEs to support job creation; and (iii) improve the infrastructure investment framework and selected infrastructure services.

viii. Conclusion

The WBG support to South Africa, and the African continent more generally, is most critical during this distressing time. The proposed DPO will go a long way in supporting efforts to save lives and livelihoods and sustain the Government of South Africa's structural reform program to ensure the long-term prosperity of South Africans. We value working with the World Bank as a trusted partner to the people of South Africa and look forward to deepening our engagement through this DPO and the upcoming CPF.

Yours sincerely,

ENOCH GODONGWANA
MINISTER OF FINANCE

Date: 03/12/2021



ANNEX 4: ENVIRONMENT AND POVERTY/SOCIAL ANALYSIS TABLE

Prior Actions	Significant positive or negative environment effects	Significant poverty, social or distributional effects positive or negative
<i>Pillar One --- Protecting the poor and modernizing social welfare</i>		
PA 1: COVID-19 grants: To protect vulnerable households from the economic impact of the COVID-19 crisis and to support informal sector workers, the Borrower, through its Department of Social Development, has issued directions through Government Notice No. 681, which: (a) re-introduce the COVID-19 Social Relief of Distress (SRD) Program that provides grants to unemployed and informal sector workers who are not eligible for unemployment insurance benefits; and (b) expand the SRD Program to include unemployed caregivers who receive child support grants on behalf of children.	Neutral	Positive – direct impact of poor and vulnerable households
PA 2: Protecting jobs: To keep people, especially low-wage workers, connected to their jobs and ready to work when firms re-open, the Borrower, through its Department of Employment and Labor, has issued directions through Government Notice No. 637, which: (a) enhance the targeting of the COVID-19 Temporary Employer-Employee Relief Scheme (TERS) allowing furloughed workers in hardest hit industries; and (b) allow targeted works to receive cash payments directly to their bank accounts, in response to the national lockdown during the third wave of COVID-19 infections.	Neutral	Positive – it will protect jobs of vulnerable workers.
PA 3: Digital social protection: To improve the transparency, targeting, and efficiency of social grant programs, the Borrower, through its Department of Social Development, has issued directions through Government Notice No. 681, which introduce the use of electronic means to allow for digital application procedures and automated cross-checking to verify eligibility.	Neutral	Positive as better SP targeting will support the poor and translate to further poverty reduction
PA 4: Digital health: To improve equitable access to COVID-19 vaccines, the Borrower, through its National Department of Health, has launched the South	Positive as it will reduce generation of paper waste and utilization of natural	Neutral – better vaccine service delivery to have economy wide



African Covid-19 Programme Registration, which introduces the use of an Electronic Vaccination Data System (EVDS), compliant with the applicable data protection and privacy legislation, in the rolling-out of the Borrower's COVID-19 vaccination program, setting the stage for future health emergencies, as further evidenced in the COVID-19 Implementation Guide and Toolkit.	resources to produce paper.	benefits.
<i>Pillar Two--- Accelerating a resilient and sustainable recovery</i>		
PA 5: Financial resilience: To increase the resilience of the financial sector, the Borrower, through its National Assembly, has approved the Financial Sector Law Amendment Bill, which establishes a resolution regime and enables provisions for the Corporation of Deposit Insurance	Neutral	Neutral
PA 6: Climate change response: To enable the development of an effective climate change response and the long-term, just transition to a climate-resilient and lower-carbon society, the Borrower, through its Cabinet, has approved the National Climate Change Bill and its submission to Parliament.	Positive as it will incentivize emitters to move to cleaner technologies and contribute to reduce South Africa's GHG emissions in line with the emission trajectory stipulated in the NDC, increase climate resilience and protect the environment.	Neutral
PA 7: Greenhouse gas mitigation: To more closely align South Africa with the Paris Climate Agreement, the Borrower, through its Cabinet, has approved the updated First Nationally Determined Contribution (NDC), which sets more ambitious greenhouse gas (GHG) mitigation targets for 2025 and 2030.	Positive as it will lead to a significant reduction in GHG emissions by aligning the country's targets with those of the Paris Climate Agreement and promoting a transition to a greener and low carbon economy and in doing so increase climate resilience and protection of ecosystems.	Neutral
PA 8: Energy expansion. To increase competition and power generation capacity in the energy sector, the Borrower, through its Department of Mineral Resources and Energy, has amended Schedule 2 to the Electricity Regulation Act through Government Notice No. 737, which exempts from licensing embedded generation with a nominal installed capacity below 100 megawatts as per Schedule 2 to the Electricity Regulation Act.	Positive as it will favor installation of renewable energy and thus reducing dependance on current coal-based energy production.	Neutral



ANNEX 5: DPO PRIOR ACTIONS AND ANALYTICAL UNDERPINNINGS

Prior Actions	Analytical Underpinnings
Protecting the poor and modernizing social welfare	
<p>PA 1: COVID-19 Grants: To protect vulnerable households from the economic impact of the COVID-19 crisis and to support informal sector workers, the Borrower, through its Department of Social Development, has issued directions through Government Notice No. 681, which: (a) re-introduce the COVID-19 Social Relief of Distress (SRD) Program that provides grants to unemployed and informal sector workers who are not eligible for unemployment insurance benefits; and (b) expand the SRD Program to include unemployed caregivers who receive child support grants on behalf of children.</p>	<p>Analytical Work:</p> <ul style="list-style-type: none"> - Philip K, Manias M, Parikh A. 2020. Mitigation and Relief measures for COVID 19: A proposal for special COVID-19 grant. The Presidency of South Africa - World Bank (forthcoming). "Social Protection Systems Assessment for South Africa: Social Assistance," draft. - Sydney Johnson, Sydney, Remy Reya and Julia Ilhardt. 2020. "Adapting South Africa's Social Protection System for COVID-19." CSSR Working Paper No. 451. Centre for Social Science Research. - Bassier, I., Budlender, J., Zizzamia, R., Leibbrandt, M., Ranchhod, V. (2020). Locked down and locked out: Repurposing social assistance as emergency relief to informal workers. Version 2. Cape Town: SALDRU, UCT. (SALDRU Working Paper Number 261). - World Bank (2021). "Social Assistance Programmes and Systems Review: South Africa". - <p>Findings: Analytical work findings underscore the robustness of the targeting and the cost effectiveness of the South African social protection system.</p>
<p>PA 2: Protecting jobs: To keep people, especially low-wage workers, connected to their jobs and ready to work when firms re-open, the Borrower, through its Department of Employment and Labor, has issued directions through Government Notice No. 637, which: (a) enhance the targeting of the COVID-19 Temporary Employer-Employee Relief Scheme (TERS) allowing furloughed workers in hardest hit industries; and (b) allow targeted works to receive cash payments directly to their bank accounts, in response to the national lockdown during the third</p>	<p>Analytical Work:</p> <ul style="list-style-type: none"> - Department of Employment and Labor. 2020. "UIF COVID-19 Disaster Relief Plan: Progress Report as at 08 June 2020." - Gentili, Ugo. 2020. "How Can Cash Transfers Support Informal-Sector Workers in the COVID-19 (Coronavirus) Crisis?" World Bank. - Díez F, Duval R, Maggi C, Ji Y, Shibata M, and Tavares M, 2020. Options to Support the Incomes of Informal Workers During COVID-19 <p>Findings: Analytical work findings underscore the robustness of the targeting and the cost effectiveness of the South African social protection system.</p>



<p>wave of COVID-19 infections.</p>	
<p>PA 3: Digital social protection: To improve the transparency, targeting, and efficiency of social grant programs, the Borrower, through its Department of Social Development, has issued directions through Government Notice No. 681, which introduce the use of electronic means to allow for digital application procedures and automated cross-checking to verify eligibility.</p>	<p>Analytical Work:</p> <ul style="list-style-type: none"> - World Bank (2021). "Social Assistance Programmes and Systems Review: South Africa". <p>Findings: Analytical work findings underscore the robustness of the targeting and the cost effectiveness of the South African social protection system.</p>
<p>PA 4: Digital health: To improve equitable access to COVID-19 vaccines, the Borrower, through its National Department of Health, has launched the South African Covid-19 Programme Registration, which introduces the use of an Electronic Vaccination Data System (EVDS), compliant with the applicable data protection and privacy legislation, in the rolling-out of the Borrower's COVID-19 vaccination program, setting the stage for future health emergencies, as further evidenced in the COVID-19 Implementation Guide and Toolkit.</p>	<p>Analytical Work:</p> <ul style="list-style-type: none"> - Department of Health (2019). National Digital Health Strategy for South Africa 2019 – 2024, Department of Health, Pretoria - Tsegaye, T. and Flowerday, S. (2021). <u>A system architecture for ensuring interoperability in a South African national electronic health record system</u>. South African Computer Journal 33(1), 79–110. https://doi.org/10.18489/sacj.v33i1.838 - Harselman M, Both A, Hannes T et al (2016). A Digital Health Innovation Ecosystem for South Africa. IST-Africa 2016 Conference Proceedings. http://www.ist-africa.org/Conference2016 <p>Findings: The EVDS allows for the recording of patient information nationally, whereas hitherto, South Africa's health system had not been conducive for ensuring interoperability between the disparate provincial ICT systems.</p>



Pillar 2: Accelerating a resilient and sustainable recovery	
<p>PA 5: Financial resilience: To increase the resilience of the financial sector, the Borrower, through its National Assembly, has approved the Financial Sector Laws Amendment Bill, which establishes a resolution regime and enables provisions for the Corporation of Deposit Insurance.</p>	<p>Analytical Work:</p> <ul style="list-style-type: none"> - World Bank South Africa Financial Sector Development and Reform (FSDRP) Program. - National Treasury and SARB joint discussion paper “Strengthening South Africa’s resolution framework for financial institutions”(August 2015). - SARB discussion paper “Designing a deposit insurance scheme for South Africa” (May 2017). - SARB discussion paper “Ending too big to fail: South Africa’s intended approach to bank resolution” (2019). - SARB discussion paper “Coverage and reporting rules for deposit insurance in South Africa” (April 2020). - SARB discussion paper “The deposit insurance funding model and the implications for banks” (August 2020). <p>Findings: The associated key findings of above World Bank supported ASA and National Treasury and SARB analytical work include: (i) Setting out policy proposals to strengthen South Africa’s resolution framework in line with the FSB’s Key Attributes. The designation of the SARB as resolution authority was one of the policy proposals. The proposals were incorporated into the draft FSLAB; (ii) Providing high-level proposals for the establishment of an explicit deposit insurance scheme for South Africa. Areas covered included deposit insurance coverage, definition of qualifying deposits, funding, governance and payout that informed the enabling provisions in draft FSLAB: (iii) the SARB has initiated a strategic project to prepare for the establishment of CODI and is at an advanced stage of recruiting a CEO to support implementation. The preparations involve a range of policy, legal, operational and institutional aspects. The discussion paper on ‘Coverage rules and reporting for deposit insurance in South Africa’ provides details on the proposed coverage rules, that is, the treatment of specific depositors, accounts and products for deposit insurance coverage. The discussion paper on the deposit insurance funding model and the implications for banks provides details of the key design features of the deposit insurance scheme for South Africa, and some initial options for the funding it through contributions from the banking sector. These papers along with other forthcoming papers will inform the establishment of CODI which is the expected result of the prior action.</p>
<p>PA 6: Climate change response: To enable the</p>	<p>Analytical Work:</p>



<p>development of an effective climate change response and the long-term, just transition to a climate-resilient and lower-carbon society, the Borrower, through its Cabinet, has approved the National Climate Change Bill and its submission to Parliament.</p>	<ul style="list-style-type: none"> - Department of Forestry Fisheries and Environment. 2021. Sectoral Emissions Target Framework. - World Bank. 2009 Tax Policy to Reduce Carbon Emission in South Africa Policy Research Working Paper concludes that a carbon tax would carry the least marginal abatement cost among alternative energy tax options to achieve climate change mitigation in South Africa. - National Treasury. 2010. Reducing Greenhouse Gas Emissions: The Carbon Tax Option. Discussion Paper for Public Comments; and National Treasury. 2013. Carbon Tax Policy Paper provide the rationale and assessment of carbon tax and design options. - Department of Forestry, Fisheries and Environment. 2011. National Climate Change Response White Paper. - South Africa: Supporting the Implementation of Nationally Determined Contribution (P172748) supports the implementation of the carbon tax through (i) review of emission intensity benchmark, (ii) analysis of trade exposure allowance methodology, (iii) interaction between the carbon tax and the carbon budgets, (iv) design of sectoral emission targets and carbon budgets; and (v) updating job and socio-economic impacts of transition pathways.
<p>PA 7: Greenhouse gas mitigation: To more closely align South Africa with the Paris Climate Agreement, the Borrower, through its Cabinet, has approved the updated First Nationally Determined Contribution (NDC), which sets more ambitious greenhouse gas (GHG) mitigation targets for 2025 and 2030.</p>	<p>Analytical Work:</p> <ul style="list-style-type: none"> - Department of Forestry, Fisheries and Environment. 2017. National GHG Inventory Report South Africa, 2017. - Department of Forestry, Fisheries and Environment. 2015. First Nationally Determined Contribution. - Department of Mineral Resources and Energy. 2019. Integrated Resource Plan. - Department of Forestry, Fisheries and Environment. 2021. Update to the First Nationally Determined Contribution.
<p>PA 8: Energy expansion. To increase competition and power generation capacity in the energy sector, the Borrower, through its Department of Mineral Resources and Energy, has amended Schedule 2 to the Electricity Regulation Act through Government Notice No. 737, which exempts from licensing embedded generation with a nominal installed capacity below 100 megawatts as per Schedule 2 to the Electricity Regulation Act.</p>	<p>Analytical work:</p> <ul style="list-style-type: none"> - IFC Benchmark report, Regulatory and Tariff Review for Distributed Generation in the Commercial and Industrial Sectors in Southern Africa (2020). - NERSA Guidelines report, Registration Procedure in Terms of Schedule 2 of the Electricity Regulation Act (Act No.4, 2006), version 2 (October 2020). - NERSA, List of Registered Embedded Generation Facilities in 2021 (September 2021). - WWF Briefing paper, Understanding and Managing Residential Solar Rooftop PV in South Africa (August 2020). - SAPVIA-CSIR, Solar PV Industry Jobs Report (April 2021). - DMRE Strategic Plan 2020-2025 (September 2020). - DMRE, Address of DMRE Minister to the parliament, Budget Vote 34 (May 2021).



- Meridian Economics briefing note, Survey Results, Scoping Interest in the South Africa Distributed Energy Generation Sector (January 2021).

Findings: overall the studies highlighted that license exemption on EG would have a direct and immediate impact on private investment acceleration for EG infrastructure. The Centre for Scientific and Industrial Research also estimated that SSEG could create up to 57,000 jobs by 2030 and install a cumulative capacity of 4,900 MW.

