COUNTRY FOCUS REPORT 2026

SOUTH AFRICA

Mobilizing South Africa's Development Financing at Scale in a Fragmented World



AFRICAN DEVELOPMENT BANK GROUP

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ACRONYMS AND ABBREVIATIONS

AfCFTA	African Continental Free Trade Area
AfDB	African Development Bank
AEO	African Economic Outlook
AML	Anti-Money Laundering
AU	African Union
CFR	Country Focus Report
CIPC	Companies and Intellectual Property Commission
CRGE	Climate Resilient Green Economy
DFIs	Development Financial Institutions
DSA	Debt Sustainability Assessment
ECCE	Country Economics Department
EESE	Equity Express Securities Exchange
ESG	Environmental, Social, and Governance Investments
EU	European Union
FATF	Financial Action Task Force
FDI	Foreign Direct Investment
FICA	Financial Intelligence Centre Act
FSCA	Financial Sector Conduct Authority
FSR	Financial Sector Regulation
G20	Group of 20 Industrialized Countries
GDP	Gross Domestic Product
ICT	Information and Communication Technology
IFIs	International Financial Institutions
IMF	International Monetary Fund
IPP	Independent Power Producer
JSE	Johannesburg Stock Exchange
MDBs	Multilateral Development Banks
MW	Megawatts
NCA	Natural Capital Accounting
NDC	Nationally Determined Contributions
NDP	National Development Plan
NBFIs	Non-Bank Financial Institutions
ODA	Overseas Development Assistance
OECD	Organization for Economic Co-operation and Development
PEM	Payments Ecosystem Modernisation
PFMA	Public Finance Management Act
PPPs	Public-Private Partnerships
REIPPPP	Renewable Energy Independent Power Producer Procurement Programme
RDGS	Regional Development and Governance Structure
SACU	Southern Africa Customs Union
SADC	Southern African Development Community
SARS	South African Revenue Service
SDGs	Sustainable Development Goals
SDRs	Special Drawing Rights
SEEA	System of Environmental-Economic Accounting
SEZs	Special Economic Zones
SIPs	Strategic Integrated Projects
SMEs	Small and Medium Enterprises
SOEs	State-Owned Enterprises
VAT	Value-Added Tax
WTO	World Trade Organization

EXECUTIVE SUMMARY

Real Gross Domestic Product (GDP) growth in South Africa improved modestly to 1.1% in 2025, up from 0.5% in 2024, thanks to recovery in agriculture and horticulture, expansion in finance, real estate and business services, trade, catering, and accommodation. GDP growth is projected to remain subdued at 1.2% in 2026 due to increased global risks and supply the impact of shock on energy and food prices because of the Middle East conflict. Domestic risks include persistent infrastructure deficits, ongoing electricity and water supply problems, inefficiencies in freight rail and port operations, local government governance failures, and fiscal vulnerabilities stemming from state-owned enterprise (SOE) bailouts. Adding uncertainty are global risks, such as the Middle East conflict, China's economic slowdown, trade tensions and the effects of U.S. tariffs. Along with these, the escalating climate crisis, volatile commodity prices and continued tightening of global financial conditions, triggered by high global energy and food prices threaten growth.

South Africa faces large financing needs to bridge infrastructure and socio-economic gaps, including in roads, energy, health care, and education. The 2025 CFR estimated that the country needs US$254-US$329 billion (about 8.7% – 11.2% of GDP) for investments in basic education, technical and vocational education and training, transport, water and sanitation between 2022-2030. Gross borrowing for 2026/27 is projected to decrease to US$22.4 million down from US$33.2 million , in part due to the phase out of payments for debt relief at the State-owned electiricity utility Eskom.

Governance and institutional reforms in South Africa should emphasize building a capable and ethical state to accelerate the transition from a bureaucratic legacy to an efficient, accountable, and transparent public service. Key actions comprise implementing the 2030 National Development Plan, strengthening accountability to tackle corruption, restructuring local governments, and improving intergovernmental cooperation. Furthermore, it is critical to bolster financial systems, reduce leakages, improve risk management, and enhance financial agency. This requires enhancing institutional reforms, with emphasis on strengthening regulatory frameworks at sub-national government levels, digitizing public sector governance systems to bolster transparency and accountability, harnessing the country's natural, human, financial, and business capital, and deepening regional integration and economic cooperation.

GENERAL INTRODUCTION

South Africa is a middle-income country with per capita income estimated at US$6,267 in 2025 and a population of about 63.1 million. Located at the edge of Southern Africa, it has a coastline of almost 3,000 km, stretching along the Atlantic and Indian Oceans and land surface covering 1.2 million square km. Of this area, 79% is classified as agricultural land, mostly grazing, with only 11% suitable for crop production. Under the theme "Mobilizing Development Financing at Scale in a Fragmented World", the Country Focus Report (CFR) supplements the analysis contained in the African Development Bank's 2026 African Economic Outlook. The CFR was prepared through a consultative process. In-country data gathering was undertaken during 1st March– 31st April 2026 and complemented with data provided by the Bank's Statistics Department, desk review and data from other international sources.

The 2026 CFR for South Africa examines the country's recent growth trends, and examines options for mobilizing capital at scale to accelerate inclusive economic growth, diversification and structural transformation. It assesses the decline in global development financing and the rising risks for South Africa, including higher borrowing costs, volatile capital flows, increased debt, and exposure to external shocks, as well as the structural vulnerabilities within domestic financial systems. The report has three chapters.

Chapter one focuses on the recent key macroeconomic trends and outlook over the medium-term. It considers fiscal policies, inflation, public debt, and financial flows, as well the main downside risks and upside triggers and analyzes social development.

Chapter two discusses options for mobilizing capital at scale for accelerated and resilient growth. It examines how South Africa can mobilize substantial development financing by strengthening domestic resource mobilization, enhancing public financial management, expanding financial inclusion, formalizing the informal sector, leveraging public–private partnerships and regional capital markets, and utilizing the country's demographic and natural resource assets. Chapter three looks at the need to strengthen and modernize South Africa's financial systems and agency in a changing global environment characterized by tightening financial conditions.

1 MACROECONOMIC PERFORMANCE AND OUTLOOK

Key Messages

- Though South Africa is a middle-income country, it continues to struggle with the problems of a 'dual economy' characterized by high levels of poverty, unemployment, income inequality, and spatial disparities.
- South Africa's economy has underperformed in the last four years (2022-2025), averaging at 1.1% a year, hindered by persistent electricity shortages, logistical challenges, local government failures, a severe drought, declining capital investment, and structural issues like insufficient skills and skewed asset ownership.
- Real GDP growth increased to 1.1% in 2025 from 0.5% in 2024, reflecting recovery in agriculture and horticulture, expansion in finance, real estate and business services, and trade, catering and accommodation.
- The fiscal deficit including grants remained unchanged at 4.5% of GDP in 2025 as tax revenue collection improved. The current account deficit rose to an estimated 0.9% of GDP in 2025 from 0.6% in 2024, reflecting slower export growth.
- Real GDP growth is projected to rise to 1.2% in 2026 and 1.6% in 2027, underpinned by improved energy supply, better industrial activity, and ongoing structural reforms under Operation Vulindlela, a joint initiative of the Presidency and National Treasury, focusing on, logistics, water, regulatory and governance improvements, among others. Risks to the economic outlook include global geopolitics, infrastructure gaps, logistical bottlenecks, the escalating climate crisis and fiscal vulnerabilities arising from bailouts of SOEs.

1.1 Introduction

This chapter analyzes South Africa's economic performance for 2025 and growth projections over the period 2026-2027. It assesses trends in, among others, key macroeconomic indicators, fiscal and monetary policies, and changes in domestic and international financial flows like remittances, Foreign Direct Investment (FDI), and Official Development Assistance (ODA), investment, and public debt. The chapter discusses the main downside and upside risks to the outlook and provides policy options to foster macroeconomic stability and resilient economic transformation Progress in achieving socioeconomic outcomes is also examined.

1.2 Growth Performance

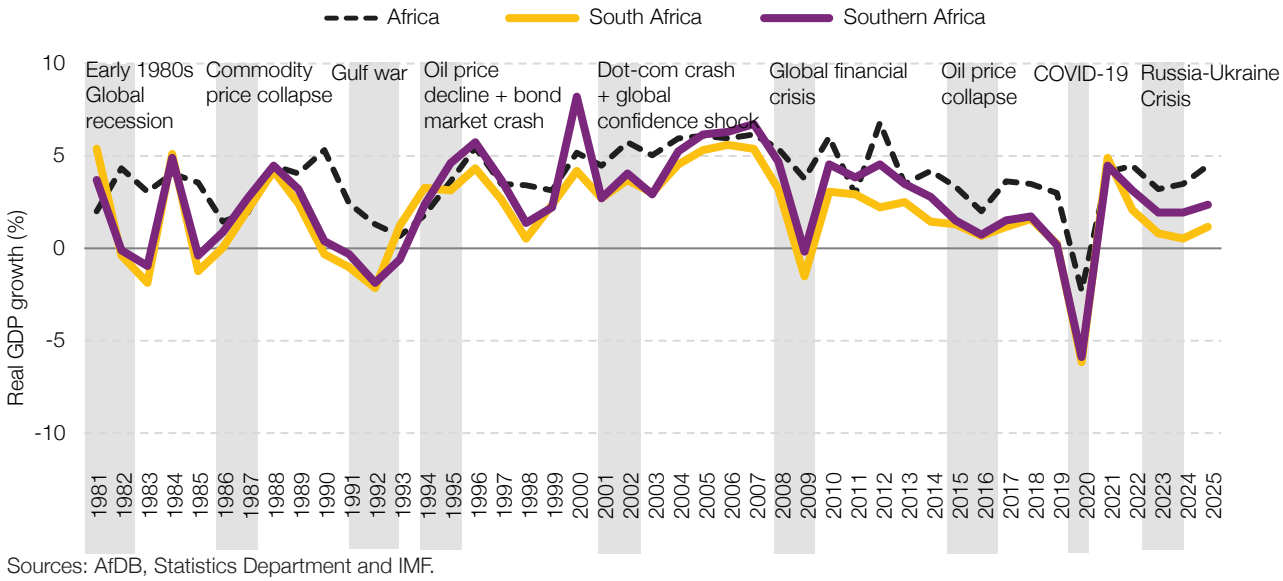
Real GDP growth in South Africa improved modestly to 1.1% in 2025 from 0.5% in 2024, supported on the supply side by recovery in agriculture and horticulture, as well as stronger activity in finance, real estate and business services, and trade, catering and accommodation. However, growth remained constrained by contractions in manufacturing, electricity, gas and water, and construction activities.

Output in the primary and tertiary sectors remained positive, while the secondary sector contracted and stayed below pre-pandemic levels. The primary sector grew by 6.4%, driven by a rebound in agriculture, while the tertiary sector increased by 1.3%, supported by stronger activity in financial services, trade, transport, and related services. In contrast, construction contracted by 4.4%, marking its ninth consecutive annual decline due to weak public and private investment. Electricity, gas and water output declined by 4.3% due to reduced electricity generation at Eskom, while manufacturing contracted by 1.2% amid weak demand and persistent logistics bottlenecks, notably rail and ports.

On the demand side, growth was driven mainly by household consumption, which contributed 2.1 percentage points to GDP growth in 2025, supported by easing inflation and stronger consumer spending. Government consumption also supported growth, while weak investment and lower exports weighed on overall growth performance. Household consumption expenditure grew by 3.6%, while gross fixed capital formation declined by 2.2% and exports by 2.5%.

South Africa's growth performance since 1980 is characterized by three distinct phases (Figure 1): a period of stagnation and isolation in the 1980s, a democratization boom in the mid-2000s, and a decade of decline and slow growth post-2009. The period 1981-1993 was defined by capital flight, international financial sanctions, and domestic political instability. During this period 1981-1993, economic growth averaged 1.0% annually, below the 1.7% average growth rate for global emerging markets. Following the 1994 elections, South Africa reintegrated into the global economy. Thus, the period of 1994-2008 experienced rising foreign investment and structural reforms, with annual real GDP growth averaging 3.6%, driven by the commodity super-cycle and rising domestic consumer spending. The 2008/09 global financial crisis triggered a downturn, whose effects on the economy were aggravated by domestic structural bottlenecks, including electricity supply constraints (load-shedding), inefficiencies in transport and logistics, and receding investor confidence. As a result, annual real GDP growth averaged 1.4% during 2009-2019. Major disruptions like the COVID-19 pandemic and escalation of structural constraints, notably energy shortages, further reduced annual real GDP growth to 0.5% during 2020-2025.

Figure 1: Historical Growth Performance (1980–2025)



Sources: AfDB, Statistics Department and IMF.

1.3 Other Recent Macroeconomic and Social Developments

1.3.1 Monetary Policy, Inflation, Exchange Rate

Price pressures continued to ease in South Africa during 2024–2025, allowing the South African Reserve Bank (SARB) to gradually adopt a more accommodative monetary policy stance. Average inflation decreased to 3.2% in 2025 from 4.4% in 2024, marking the lowest annual inflation rate since 2004 (1.4%), largely reflecting stable food prices. Inflation eased further to 3.0% in February 2026 from 3.5% in January 2025, remaining within the SARB's target range of 3%–6%. Lower inflation was mainly driven by housing and utilities, food and non-alcoholic beverages, insurance, and financial services. The moderation in inflation since May 2024 prompted six consecutive 25-basis-point reductions in the SARB's policy benchmark rate, from 8.25% in September 2024 to 6.75% in December 2025. Consequently, the prime lending rate dropped from 11.75% to 10.25% over the same period. The rand appreciated by 13% against the U.S. dollar in 2025, supported by a weaker dollar and improved investor sentiment.

1.3.2 Financial sector

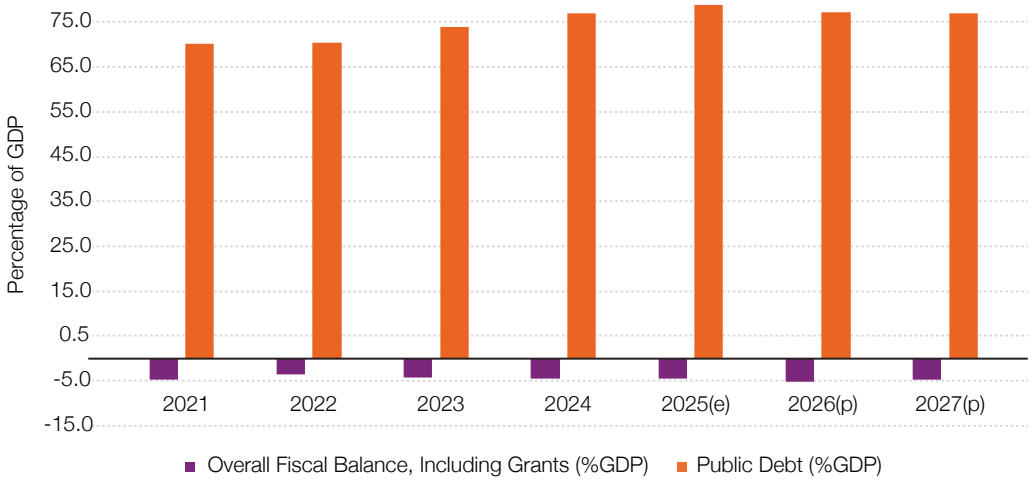
South Africa has a sophisticated and large financial sector with an asset to GDP ratio exceeding 200% to 300% of GDP%, well above that of most emerging markets. The financial system is well-developed with strong banking institutions, pension funds and a dynamic stock exchange. It has one of the largest and most developed capital markets in Africa. The Johannesburg Stock Exchange is among the most sophisticated markets globally with a market capitalization of 277.1% of GDP over the period 2020-2024. Non-performing loans decreased to 4.5% of total gross loans in 2025, from 5.7% in 2024 and the capital adequacy ratio increased to 17.8% in 2025, compared with 17.2% in 2024. Household financial distress from rising interest rates since late 2021 has led to mortgage defaults but easing borrowing costs are expected to support the sector.

1.3.3 Fiscal Policy and Public Debt

Despite ongoing fiscal consolidation measures, particularly revenue-mobilization initiatives, the fiscal deficit remains high at an estimated 4.5% of GDP in 2025, unchanged from the 4.5% recorded in 2024-Figure 2, with increased non-interest expenditure offsetting the improvements in revenue collection. Total revenues increased to an estimated 28.8% of GDP in 2025/26 from 27.8% and 27.4% in 2024/25 and 2023/24, respectively, reflecting stronger than expected collections from net value-added tax (VAT), corporate income and dividends taxes, and improved economic growth performance. Total expenditure increased slightly to an estimated 33.2% of GDP in 2025/26, compared to 32.3% and 31.7% in 2024/25 and 2023/24, respectively, reflecting growth in non-interest spending.

Debt-service costs have risen from 12.0% of revenue in 2015/26 to 21.3% in 2025/26, crowding out other social spending. Debt-service costs are projected to rise from about from US$24.8 million in 2025/26 to US$27.6 billion in 2028/29, but as a percentage of revenue to reduce to 21.6% in 2028/29. The government has relied on both external and domestic credit sources, including concessional loans from international financial institutions, to finance the fiscal deficit. The gross borrowing requirement, comprising the budget deficit, maturing government debt, and the Eskom debt-relief arrangement, was estimated at US$34.1 million in 2025/2026, including US$4.7 million for Eskom debt relief. Public debt-to-GDP ratio increased to an estimated 78.9% of GDP in 2025/26 from 77.0% in 2024/25, thereby elevating debt pressures with a shift from concessional multilateral debt to short-term domestic debt (Figures 3 and 4). The debt build up is due to sluggish economic growth, persistent budget deficits, bailouts for struggling SOEs, and debt service costs. Public debt is projected to stabilize at about 76.5% of GDP in 2028/29.

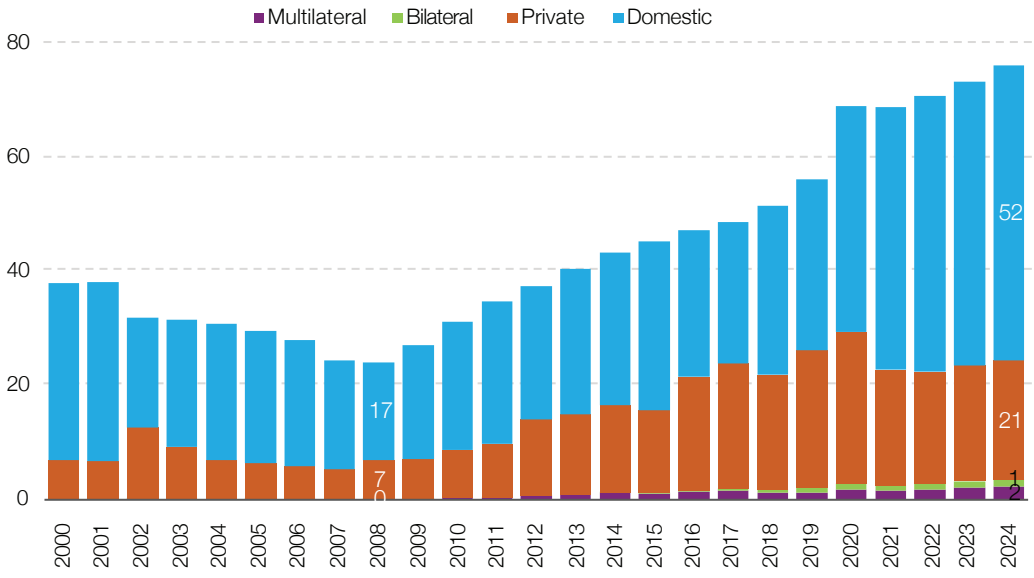
Figure 2: Trends in Fiscal Balance and Public Debt in South Africa (Percent of GDP)



Source: AfDB statistics, 2026

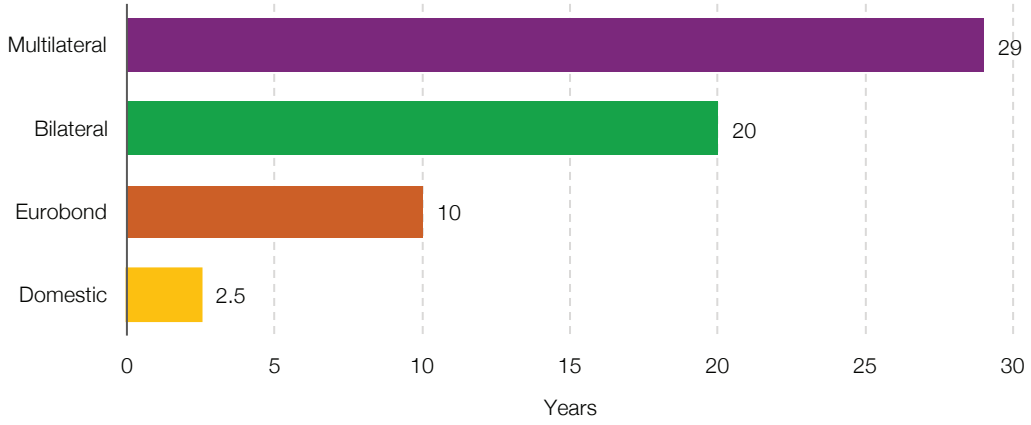
The development financing landscape in South Africa as illustrated in Figure 3, reflects reliance on domestic and private funding, which has increased debt service costs. Domestic debt has increased since 2008 and represented more than half (52%) of South Africa's public debt. Commercial debt from private creditors increased from 7% of public debt in 2008 to 21% in 2024, reflecting South Africa's better market access and high financing needs. The AEO 2026 reports that commercial creditors are playing an increasingly important role in frontier market economies, but low-income countries still rely on concessional lending including from the African Development Fund (ADF) and the International Development Association (IDA) as well as the bilateral creditors.

Figure 3: South Africa's Debt Vulnerabilities Remain Amid Evolving Development Financing Landscape



Sources: Staff calculations based on data from IMF World Economic Outlook database and International Debt Statistics database
Note: Domestic debt is calculated as the difference between gross public debt (IMF WEO) and external public and publicly guaranteed (PPG) debt. External PPG debt is defined as the sum of bilateral, multilateral, and private external debt.

Figure 4: Distribution of Debt Maturity by Instrument (Domestic, Eurobond, Bilateral, Multilateral) in Africa 2015-2024

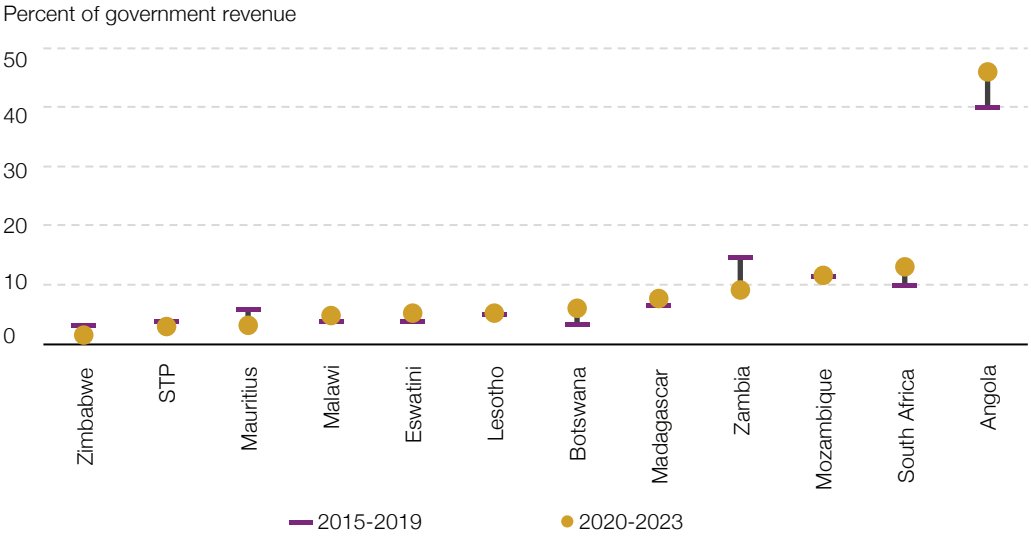


Source: Sy and Laws, 2026
https://www.imf.org/en/publications/fandd/issues/2026/03/the-new-face-of-african-debt-amadou-sy

Overall, higher costs and shorter maturities of commercial debt and domestic debt in Africa (Figure 4) aggravate debt refinancing risks in countries, with the concentration of external debt in US dollar exacerbating currency risks.

In South Africa, the external public debt service averaged approximately 13% of government revenue between 2020-2023 (Figures 5 and 6), slightly below the Government's 15% risk benchmark.

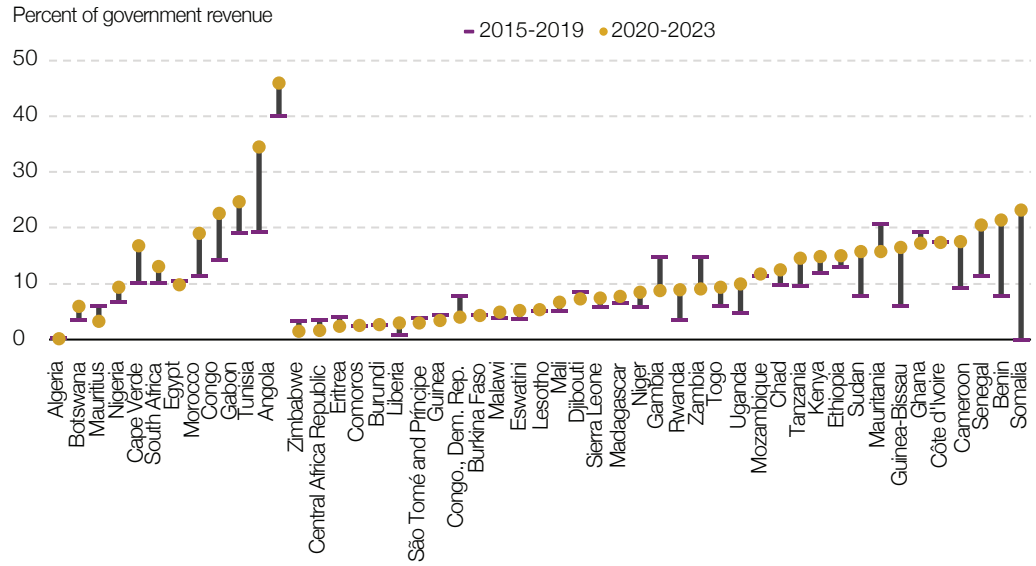
Figure 5: External public debt service (principal and interest) as percent of government revenue, period average (Southern Africa)



Source: Staff calculations using data from World Bank International Debt Statistics

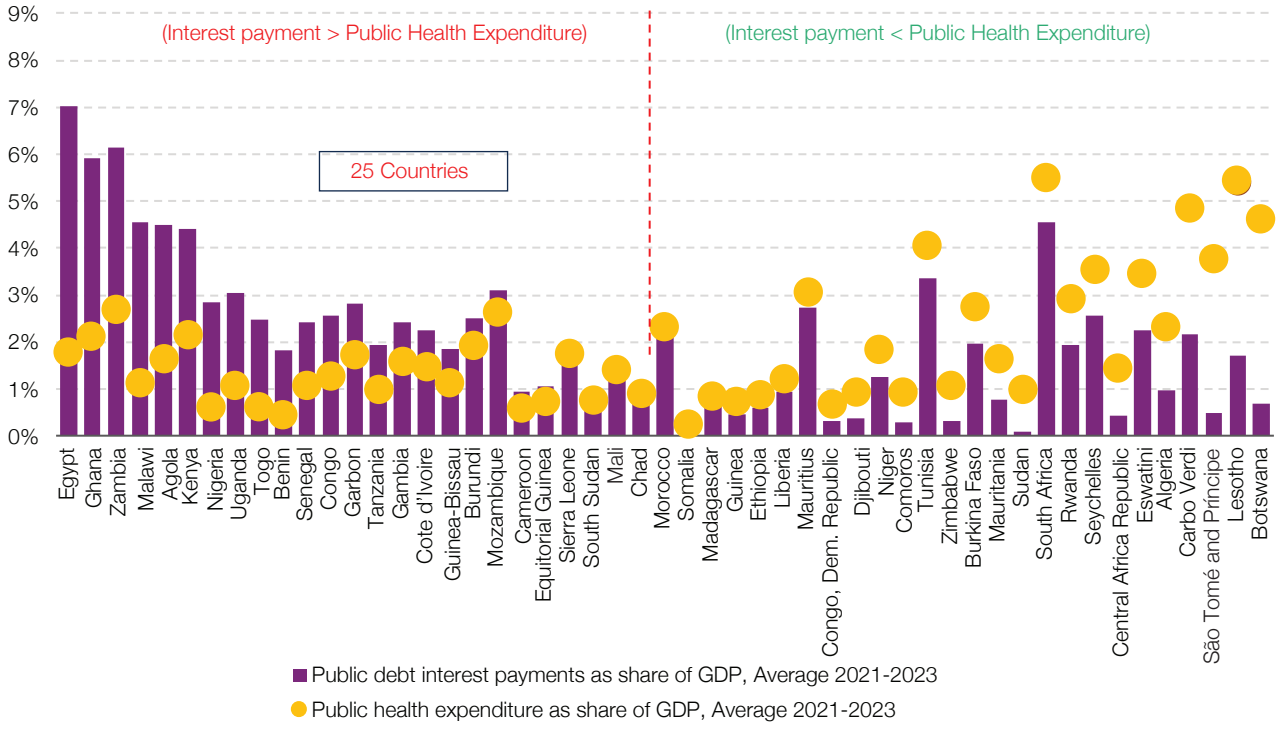
South Africa allocated 10.1% of its total government revenue during 2025-2019 toward external public debt service (principal and interest) as shown in Figure 5 and 6. Despite the increase in external public debt service as a share of government revenue over the period 2015-2023 (Figures 5 and 6), South Africa's external public debt interest payments remain below the share of the budget allocated to public health (Figure 7).

Figure 6: External Public Debt Service (Principal and Interest) as a Percent of Government Revenue Period Average (Africa)



Source: Staff calculations using data from World Bank International Debt Statistics

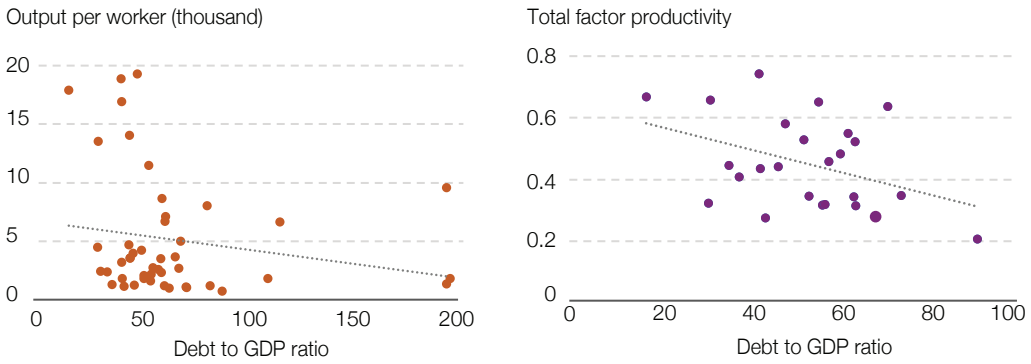
Figure 7: External public debt interest payment vs public health expenditure, as percent of GDP, average 2021-2023



Source: UNCTAD, A World of Debt Database (2025).

Cross-country evidence reveals that countries with higher public debt levels tend to exhibit lower productivity outcomes, although the direction of causality could vary across country and regional contexts (Figure 8).

Figure 8: Relationship between public debt and productivity



Source: African Development Bank Group (2026) African Economic Outlook 2026

1.3.4 External Position – External Financial Flows

The current account deficit weakened to an estimated 0.9% of GDP in 2025 from 0.6% in 2024, reflecting slower export growth and increased imports for investments in renewable energy. For 2025, the trade surplus narrowed slightly to US$12.5 million (2.8% of GDP) from US$12.6 million (2.9% of GDP) in 2024. Increased imports from China plus lower vehicle exports to the U.S. offset the expanded value of merchandise and net gold exports. Higher imports are expected to push the current account deficit up to 1.3% of GDP in 2026 and 1.4% in 2027. Gross reserves increased to $75.89 billion (6.1 months of imports) in December 2025 compared to US$65.46 billion (5.6 months of imports) in December 2024. Increases in the gross reserves and international liquidity position were mainly due to the uptick in the US dollar gold price and valuation adjustments. FDI inflows eased from US$3.5 billion (0.9% of GDP) in 2023 to US$2.5 billion (0.6% of GDP) in 2024.

1.3.5 Social developments

Due to historical inequality and low economic growth, the official unemployment rate remained high at 31.4% in Q4 2025. According to Statistics South Africa data, the share of people below the Upper Bound Poverty Line (UBPL) decreased from 78.7% in 2006 to 66.7% (about R2,846 or USD170 per person per month) in 2023 representing a 12 percentage points decline, although the number of people below the UBPL increased from 37.3 million in 2006 to 40.8 million in 2023. Poverty is driven by low economic growth, skills gaps, high unemployment, infrastructure deficits, and economic shocks. Income inequality, measured by the Gini coefficient, dropped from 0.72 in 2006 to 0.64 in 2023, but South Africa remains a highly unequal country.

Table 1: Key Macroeconomic and Social Indicators

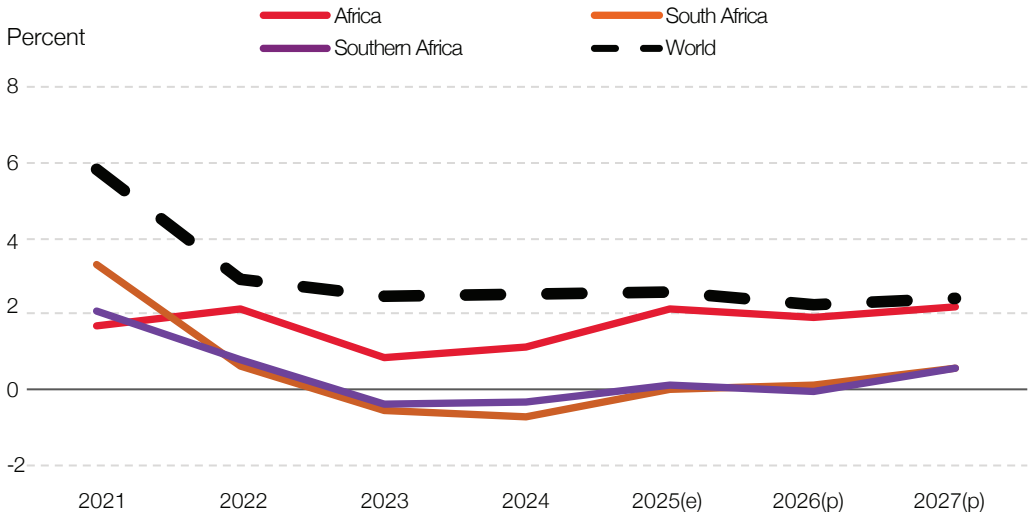
Indicators	2021	2022	2023	2024	2025(e)	2026(p)	2027(p)
Real GDP Growth (%)	4.9	2.1	0.8	0.5	1.1	1.2	1.6
Real GDP Growth per capita (%)	3.3	0.6	-0.5	-0.7	0.0	0.1	0.5
Inflation	4.5	6.9	5.9	4.4	3.2	3.9	3.6
Overall Fiscal Balance, Including Grants (% of GDP)	-4.6	-3.6	-4.3	-4.5	-4.5	-5.1	-4.7
Current Account (% of GDP)	3.7	-0.3	-1.1	-0.6	-0.9	-1.4	-1.6
Population	60.6	61.4	62.2	63.0	63.1	63.2	63.3
Life expectancy	62.7	63.9	66.3	66.5	66.9	67.0	67.2

Source: Data from domestic authorities; estimates (e) and prediction (p) based on authors' calculations. AfDB Statistics Department, March 29, 2026, Note: *Data in fiscal year 1 April (n-1)/ 31 March (n)

The number of unemployed persons stood at 7.8 million in Q4 2025. Unemployment is highest among women at 34.6% and youth (15-34) at 43.8%. These dynamics underscore the country's 'dual economy,' which poses risks to social cohesion and human development. Life expectancy at birth for 2025 is estimated at 66.9 years (64.0 years for males and 69.6 years for females).

South Africa's real GDP per capita annual growth rate lags the continental and global growth rates (Figure 9) on account of structural economic challenges notably energy, transport and logistics infrastructure constraints, high poverty unemployment and income inequality.

Figure 9: Real GDP per Capita Growth (2021–2027)



Sources: African Development Bank statistics, World Economic Outlook, October 2025, and United Nations Population Division estimates.

1.4 Macroeconomic Outlook and Risks

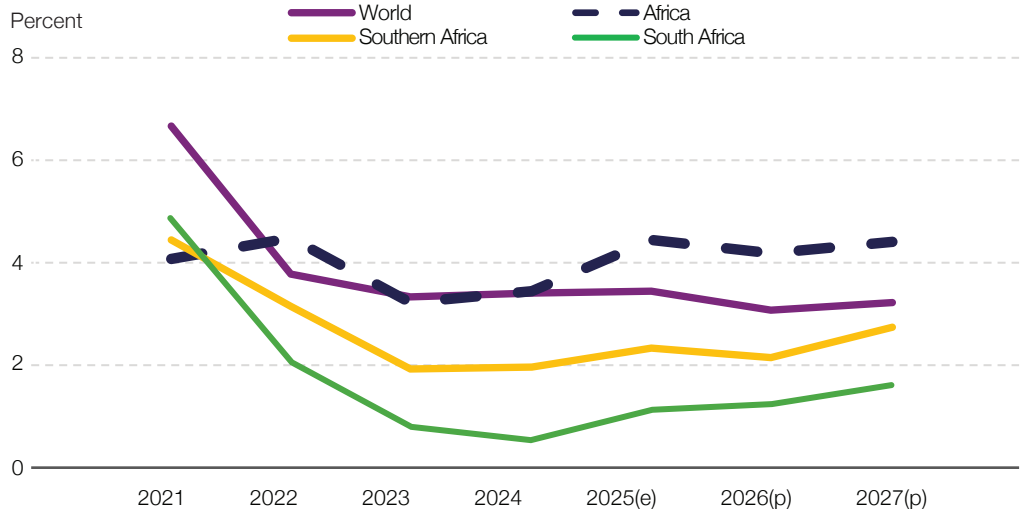
1.4.1 Outlook (Economic growth – Inflation - Fiscal and External position)

Real GDP growth in South Africa is projected to rise to 1.2% in 2026 and 1.6% in 2027 (Figure 10), underpinned by improved energy supply, strong mining activity, and ongoing structural reforms in energy, logistics, water, and regulation and governance. Real GDP per capita growth is projected to recover to 0.1% in 2026 and 0.5% in 2027. Inflation is projected at 3.9% and 3.6% in 2026 and 2027 respectively. The overall fiscal deficit including grants is expected to increase to 5.1% of GDP in 2026 before stabilizing at 4.7% in 2027, due to fiscal consolidation. Higher imports are expected to increase the current account deficit to 1.4% of GDP in 2026 and 1.6% in 2027. African economies continue to demonstrate remarkable resilience despite recurrent global shocks and increased fragmentation (Figure 10). The continent's real GDP growth is projected to moderate to 4.2% in 2026 on account of the Middle East conflict, and recover to 4.4% in 2027 if the conflict is not protracted.

1.4.2 Risks

Domestic risks include persistent infrastructure deficits, notably in electricity and water supply, inefficiencies in freight rail and port operations, local government governance weaknesses, and fiscal vulnerabilities arising from SOE bailouts. External risks comprise geopolitical tensions, the effects of U.S. tariffs, and climate shocks. Surging oil prices triggered by the Middle East conflict could stoke inflationary pressures, requiring the central bank to raise its policy rate. In the medium term, inflation is expected to rise, driven by elevated fuel and food prices, electricity and water price rises, as well as higher insurance premiums.

Figure 10: Real GDP growth: Africa and other regions, 2021 - 2027



Sources: African Development Bank statistics and Word Economic Outlook April 2026

Box 1: Implications of the Middle East Conflict

South Africa has medium exposure to the Middle East crisis, mainly because it is a net importer of crude oil and refined petroleum products. Brent crude has traded above US$100 per barrel since mid-March 2026, from below US$68 in February 2026. The rand (ZAR) has depreciated towards R16.90 to the U.S. dollar, from R15.72 in January 2026, as investors reduced exposure to emerging market assets. Sources of crude oil imports are diversified, mainly from Nigeria at 48% (4.5 billion litres) and Saudi Arabia at 18% (1.7 billion litres) in 2024, followed by Angola (15% or 1.5 billion litres), the United States (8% or 718 million litres), and Ghana (6% or 584 million litres). This diversification is expected to reduce vulnerability to direct disruptions in the Middle East. However, some vulnerability remains through refined fuel imports and indirect transmission channels, including higher fuel and shipping costs, supply chain and trade disruptions, exchange rate pressures, and financial market volatility. Coal, oil, and natural gas are the primary sources of energy in South Africa, and limited domestic oil and gas reserves increased exposure to global energy shocks.

Supply chains are also expected to be negatively affected, particularly the US$1.3-billion fruit export market, where 90% of shipments to the Middle East are reported to be delayed or stranded due to disruptions at key transit points in the region, an important market for South African citrus, apples, and grapes. Rising fuel, insurance, and shipping costs are expected to increase transport, logistics, and manufacturing costs, contributing to higher domestic inflationary pressures. These constitute the main first-round effects of the conflict through the energy and trade transmission channels. As a result, the South African Reserve Bank (SARB) has adopted a more cautious monetary policy stance, tightening monetary conditions to anchor inflation expectations.

Second-round effects may emerge through sustained inflationary pressures, exchange rate depreciation, weaker household purchasing power, tighter financial conditions, and slower real GDP growth. Persistently high global oil prices could also intensify fiscal pressures through rising subsidy and social spending requirements, while lower growth could constrain fiscal space for essential public investment and service delivery.

In response to the conflict, the government announced temporary measures to cushion domestic fuel price pressures, including a temporary reduction in the general fuel levy effective from 1 April 2026 as a short-term relief measure. South Africa also maintains strategic fuel reserves and an estimated three-month fuel supply buffer to mitigate immediate supply disruptions. In addition, the Department of Mineral and Petroleum Resources (DMPR) has initiated a review of domestic fuel price mechanisms and formulas to improve efficiency in fuel price regulation.

The government is also reviewing social protection measures, including redesigning the Social Relief of Distress grant into a potential "job seeker's grant" under the proposed Basic Income Support framework. However, prolonged fiscal pressures arising from higher fuel costs, weaker growth, and rising financing needs could increase demand for budget support operations and constrain public investment spending.

Sources: National Treasury, Department of Mineral and Petroleum Resources, and AfDB Staff Estimate

1.5 Policy options to accelerate South Africa's economic development

This section outlines l actions to sustain growth, support structural transformation, and strengthen resilience to macroeconomic and external shocks.

1.5.1 Short-term policy recommendations

Accelerating South Africa's economic development requires faster implementation and execution of ongoing structural reforms under **Operation Vulindlela and the Economic Reconstruction and Recovery Plan (ERRP)** to address persistent constraints in energy, logistics, infrastructure, and regulation, and support a sustained growth path above 3%. These reforms aim to crowd in private investment, improve infrastructure efficiency, reduce regulatory bottlenecks, and restore investor confidence. In the short term, **policy actions should focus on lowering business costs, improving service delivery, and accelerating implementation of reforms already initiated by government.**

Key short-term priorities include **improving governance and operational efficiency at Eskom, Transnet, and municipalities to reduce electricity disruptions, logistics bottlenecks, and costs of doing business**. Fiscal consolidation should continue **through expenditure rationalisation, strengthening public procurement systems, reducing wasteful expenditure, and improving revenue** administration while protecting priority social spending. Supporting small, medium, and micro enterprises (SMMEs) through easier access to finance, streamlined licensing processes, and reduced regulatory compliance costs are also important to stimulate private sector activity and employment creation. Operation Vulindlela remains the primary reform mechanism for removing structural bottlenecks through regulatory reform and greater private sector participation in strategic sectors. Ongoing priority interventions include:

- **Energy Security:** Accelerating private sector investment in electricity generation through reforms to energy market regulations, expanding transmission infrastructure, and unbundling Eskom into separate generation, transmission, and distribution entities to improve competition and energy reliability.

- **Logistics and Transport:** Expanding private sector participation in freight rail and port operations through concession agreements and operational partnerships to improve efficiency, reduce export delays, and lower logistics costs at strategic hubs such as the Port of Durban.

- **Digital Infrastructure:** Expanding broadband access and lowering data costs through spectrum auctioning, investment in digital infrastructure, and improved competition in telecommunications markets to strengthen digital inclusion and productivity.

- **Water Sector Reforms:** Establishing the National Water Resources Infrastructure Agency to coordinate financing, implementation, and maintenance of large-scale water infrastructure projects and improve long-term water security.

1.5.2 Medium-to-long-term policy recommendations

Over the medium to long term, South Africa should **deepen industrialisation and local economic development** by leveraging **Special Economic Zones (SEZs)**, support mining exploration, and promote labour-intensive manufacturing sectors linked to the green economy. Expanding manufacturing capacity, beneficiation, and export diversification will be critical to raise productivity, increase employment, and boost economic resilience.

Additional reforms should focus **on improving local government capacity**, enhancing public-private partnerships, and reducing regulatory barriers that constrain private investment and SMME growth. Labour market reforms aimed at furthering competitiveness, skills development, and labour absorption are also needed to reduce persistently high unemployment, particularly among the youth.

Maintaining **macroeconomic stability through prudent fiscal management, ensuring debt sustainability, and improved public sector efficiency** is remain essential to support investor confidence and create fiscal space for infrastructure and social spending. Strengthened social protection systems, alongside improvements in education, digital governance, and spatial inclusion, will also be important to ensure that growth is inclusive, resilient, and poverty reducing.

2 MOBILIZING CAPITAL AT SCALE FOR ACCELERATED AND RESILIENT GROWTH IN SOUTH AFRICA

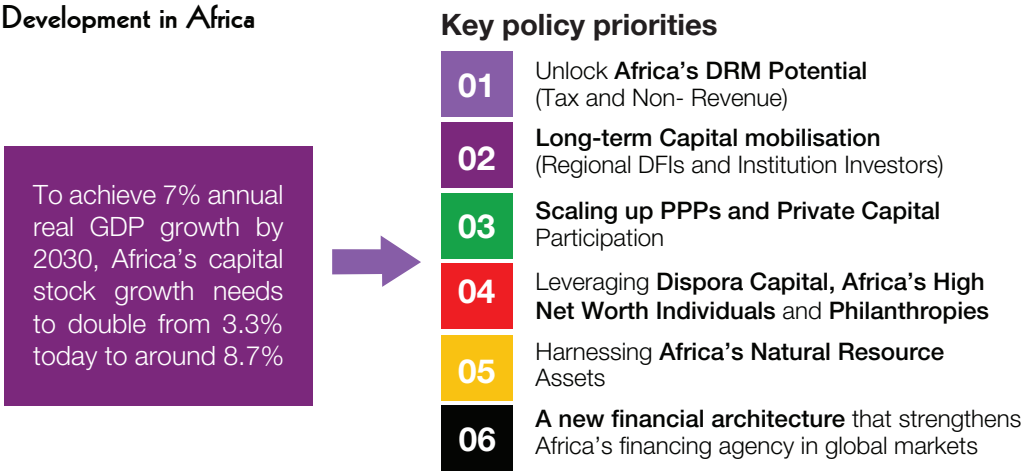
Key Messages

- South Africa has one of the most sophisticated capital markets in Africa, with total market turnover estimated at 29% in 2025. More than 800 instruments, including equities, exchange-traded funds, and bonds, are traded across over 400 listed entities.
- South Africa finances approximately 90% of its national budget from domestic resources, while foreign financing contributes around 10%, reflecting relatively strong domestic resource mobilisation.
- Despite a relatively advanced financial system, development financing needs remain high due to infrastructure gaps, energy and water shortages, and persistent inequality.
- Scaling up blended finance, public-private partnerships, and bankable infrastructure pipelines will be critical to mobilising private investment and finance for infrastructure development and the just energy transition.

2.1 Introduction

South Africa can mobilize substantial development financing by strengthening domestic resource mobilization, enhancing public financial management, expanding financial inclusion, formalizing the informal sector, leveraging public–private partnerships and regional capital markets, and utilizing its demographic and natural resource assets. Key strategies include deepening financial inclusion with digital banking and fintech, while transitioning the large informal sector into the formal economy through tailored, simplified tax regimes and incentive-based support, and utilizing its demographic and natural resource assets. South Africa's natural capital is diverse, comprising human capital – a population of 63.1 million in 2025, minerals (gold, platinum, diamonds, iron ore, manganese, and coal), agricultural land and forests as well as renewable resources. However, like many African nations, South Africa's financing gaps hinder achieving sustainable development. To accelerate Africa's growth toward the 7% annual rate needed to drive sustainable and inclusive development, the growth of the continent's capital stock needs to more than double from the current 3.3% per year to around 8.7% (Figure 11). This will require accelerated capital mobilization anchored on unlocking long-term capital, scaling up PPPs, leveraging diaspora capital, natural resource, and a new financial architecture. Successful implementation of these reforms will enable Africa to increase its annual real GDP growth to 7% by 2030.

Figure 11: Accelerating Capital Mobilisation for Inclusive Growth and Sustainable Development in Africa

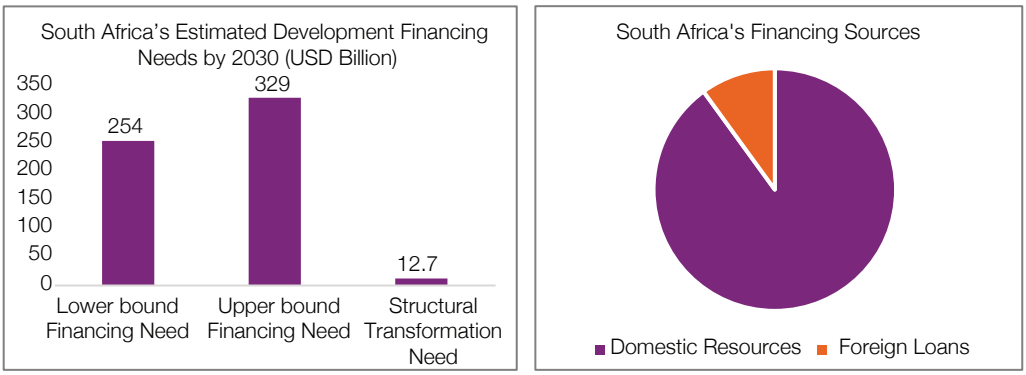


Source: African Development Bank Group (2026) African Economic Outlook 2026.

2.2 Quantifying South Africa's development financing needs

Substantial financing is needed to bridge persistent infrastructure and socio-economic gaps, particularly in transport, energy, healthcare, education, and water and sanitation. According to the 2025 CFR, financing needs by 2030 are estimated at between US$254 billion and US$329 billion (about 8.7–11.2% of GDP), including for basic education, technical and vocational education and training, transport, and water infrastructure. In addition, financing required to accelerate structural transformation is estimated at US$12.7 billion annually by 2030-Figure 12. Government's 2026 medium-term expenditure framework prioritises infrastructure development, protection of social services, and improved delivery of basic services. These large spending pressures contributed to the fiscal deficit widening from 3.6% of GDP in 2022 to 4.5% in 2025. Despite these challenges, around 90% of the national budget is financed through domestic resources, while foreign loans account for about 10%.

Figure 12: South Africa's Financing Needs, Financing Flows, and Gaps



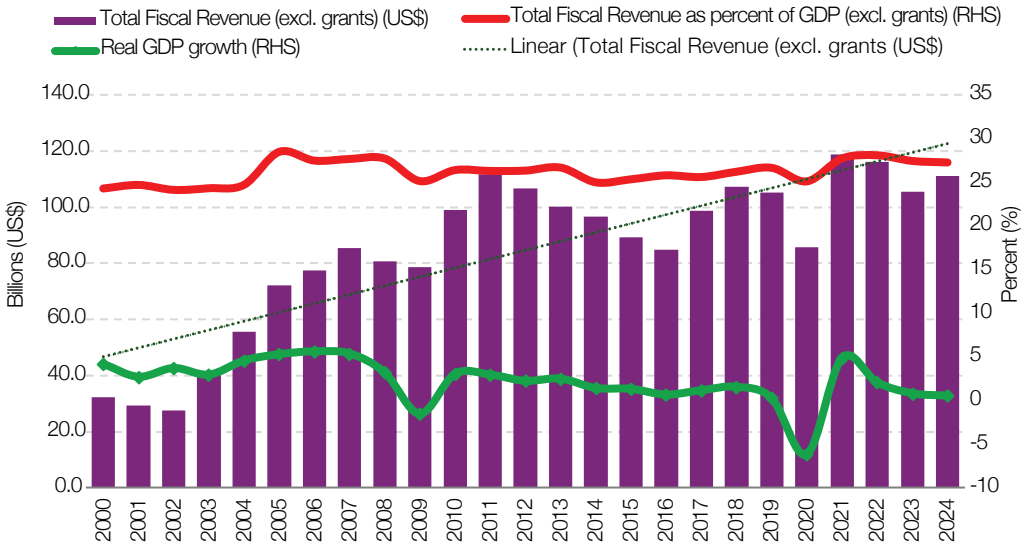
Sources: Country Focus Report 2024, AfDB Staff Estimates

2.3. Mobilizing fiscal resources at scale

2.3.1 South Africa's Domestic Revenue

Gross tax revenue in 2025/26 reached US$117 billion (R2.01 trillion) and was US$1.4 billion higher than planned, supported by higher-than-expected net VAT collections, corporate income tax, and dividend tax collections, amid improved growth. Considering the strong tax revenue performance, government withdrew the R20 billion (US$1.2 billion) in tax increases provisionally included in the May 2025 Budget. Furthermore, personal income tax brackets and medical tax credits will be fully adjusted for inflation, after two years of no inflationary relief. Despite challenging economic conditions, South Africa's tax-to-GDP ratio increased from 24.5% in 2023/24 to 25.9% in 2025/26. Fiscal revenues (tax and non-tax revenues, excluding grants) increased from 25.1% of GDP in 2000 to 27.3% in 2024, reflecting improvements in collection efficiency (Figure 13).

Figure 13: Trends in South Africa's Fiscal Revenue (excluding grants), 2000-2024



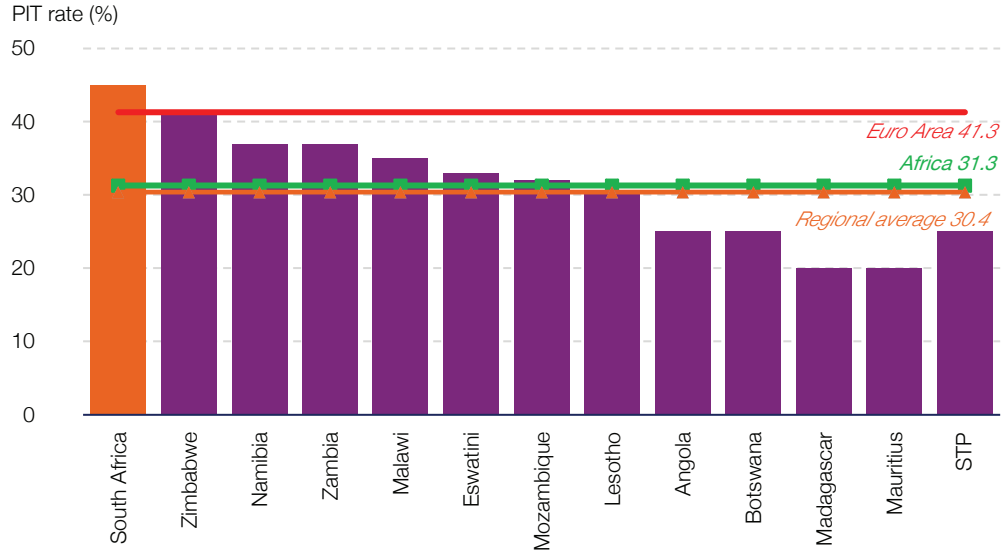
Source: African Development Statistics

2.3.2 South Africa's Tax Structure and Revenue Administration: Patterns, Gaps, and Challenges

South Africa's tax structure is characterized by a high reliance on a narrow base of personal income tax (PIT), Corporate Income Tax (CIT), and value-added tax (VAT), accounting for about 81.3% of total tax revenue in 2024/25. The fuel levy, together with specific excise and customs duties, accounted for 12.5%, whereas other taxes made up the remaining 6.2%.

Despite weak growth and power outages, South African Revenue Service (SARS) has achieved record collections, at US$117 billion in the 2025/26 financial year. SARS is focusing intensely on broadening the tax base to include the informal sector and social influencers and enhancing compliance through digitalization. Organized crime, particularly in tobacco, fuel, and gambling, remains a significant source of revenue leakage, with estimates suggesting losses between US$ 3-5

Figure 14: Statutory Personal Income Tax (PIT) Rates in Southern African countries (Percent), 2010-2023

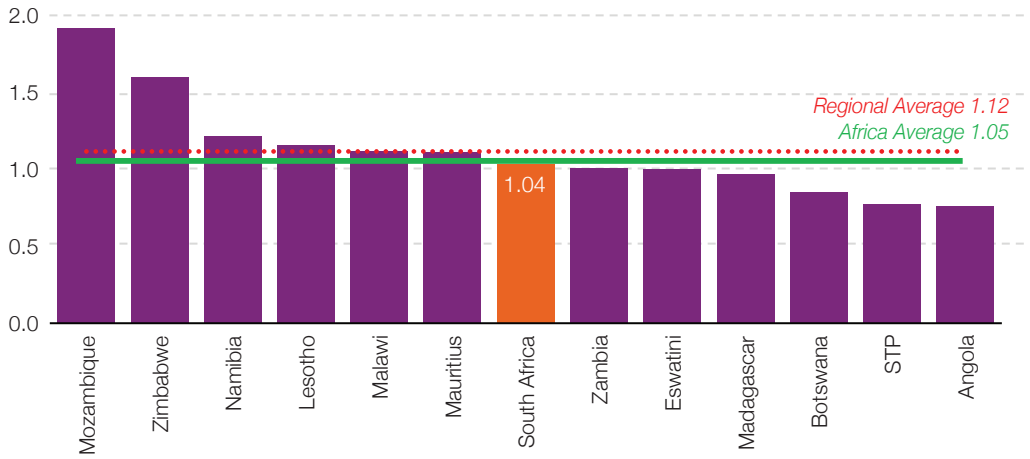


Sources: AEO 2026; and PricewaterhouseCoopers (PwC)

2.3.3 Tax Efficiency, Buoyancy, and Structural Revenue Gaps in South Africa

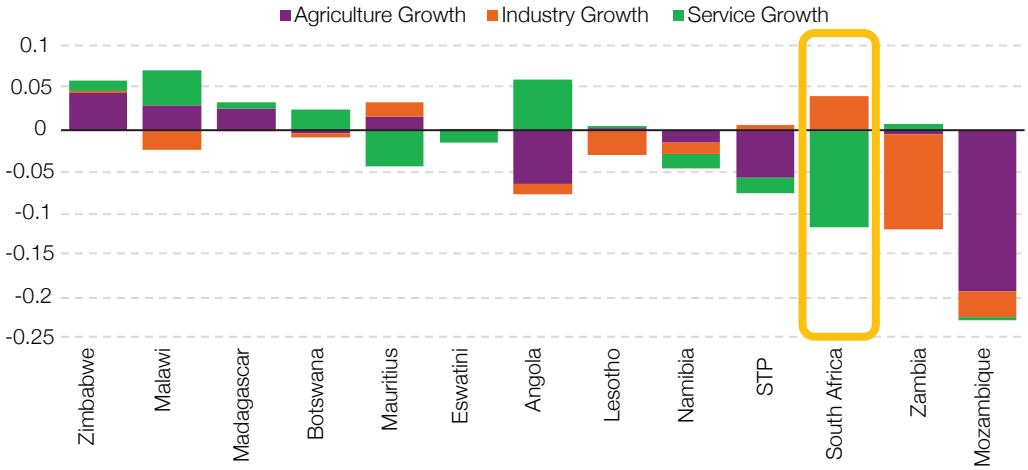
SARS collection milestone in 2025/26 of more than R2 trillion (US$117 billion) in net revenue was supported by its data-driven and automated compliance strategy. Revenue collections have grown at a compound annual rate of 6.8% over the past seven years, with the tax-to-GDP ratio estimated at 25.9% in 2025. Tax revenues reflect a high responsiveness to economic growth in South Africa, with tax-buoyancy of between 1.03 and 1.7 (Figure15). Revenue losses from smuggling, customs fraud, and illicit trade continue to undermine fiscal performance and revenue efficiency. A sectoral decomposition (Figure 16) reveals that tax buoyancy is driven primarily by non-sectoral factors such as changes in tax policy and improvements in tax administration, while sectoral factors contribute marginally (industry) or exert a negative effect (services).

Figure 15: Tax Revenue Buoyancy in Southern African countries



Sources: AEO 2026; and Staff estimation using data from the African Development Statistics

Figure 16: Sectoral Tax Revenue Buoyancy in Southern African Countries



Sources: AEO 2026; and Staff estimation using data from the African Development Statistics

2.3.4 Operationalizing South Africa's Untapped Revenue Potential

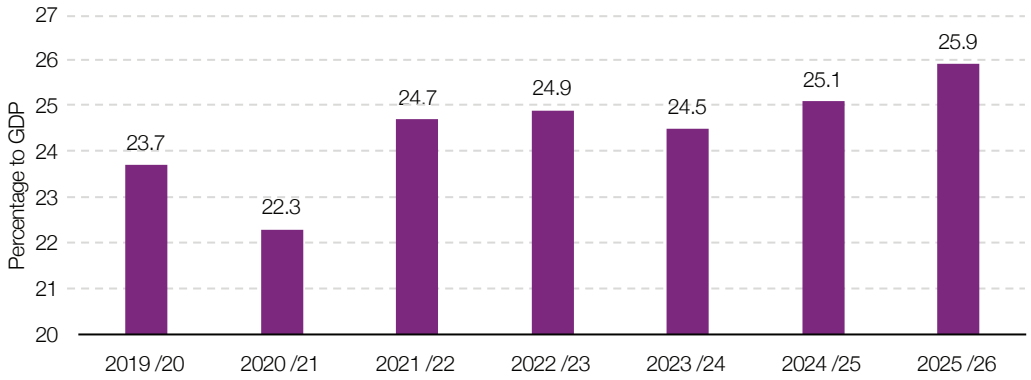
Practical measures to unlock South Africa's unrealized revenue capacity, summarized in Table 2, centre on three priority areas, aimed at strengthening domestic tax mobilization and sustaining the upward trajectory in the tax-to-GDP ratio (see Figure 17), while protecting vulnerable households. Beyond enhancements in tax policy and administration, a multi-faceted approach focuseing on minerals beneficiation, tourism expansion, green energy, and formalizing the informal economy, with an overall aim to move beyond traditional commodity exports and foster inclusive growth will be critical. Structural reforms must be accelerated in logistics, energy, water and municipalities to increase economic growth and leverage the mineral wealth while expanding the digital economy, thereby expanding the tax base.

Table 2: Policy instruments for effective revenue mobilization

Pillar 1: Tax Instruments	Pillar 2: Non-Tax Instruments
- Broadening the tax base by integrating informal economic activity. - Potentially expanding coverage by reducing tax expenditures, optimizing property taxes, and leveraging digital technologies for compliance. - Modernizing tax and customs administration through integrated digilization.	- Strengthening tax administration through data analytics. Update taxpayer registers, using unique identification numbers linked to biometric data. - Enhancing tax compliance and enforcing compliance, particularly in the digital economy. - Natural resource revenues.
Cross-cutting:	
A progressive tax system to protect vulnerable households and support economic development.	

Source: National Treasury

Figure 17: South Africa's Tax-to-GDP Ratio, 2019-2025 (Percent)



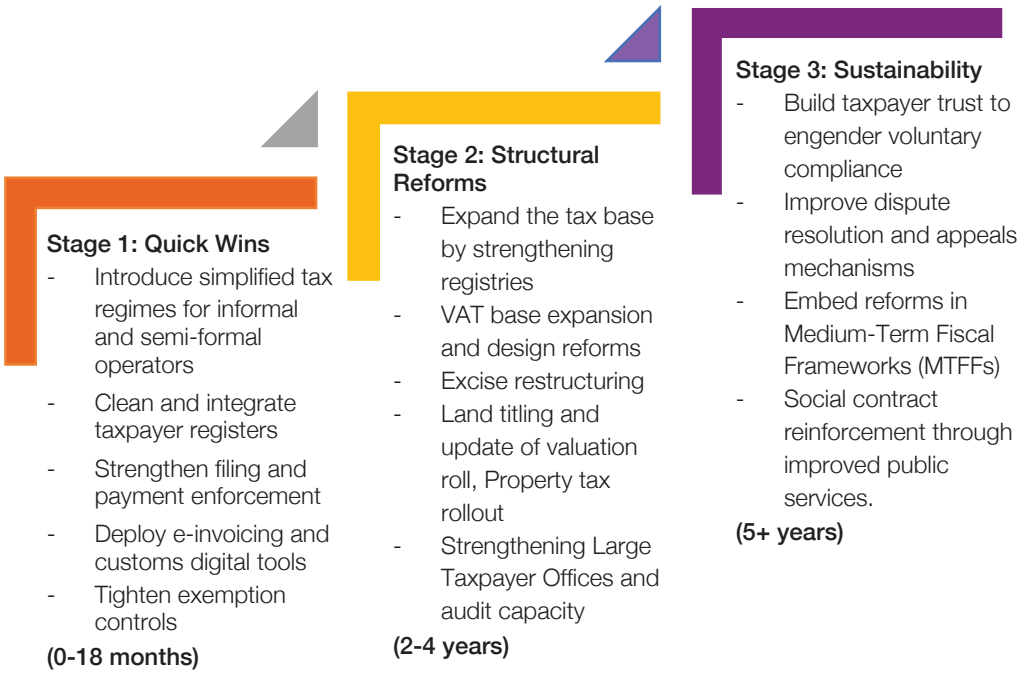
Source: National Treasury

2.3.5 Revenue Reforms and Sequencing

A phased strategy as illustrated in Figure 18, is essential for revenue reforms. In the short term, priority should be to introduce simplified tax regimes for informal and semi-formal operators. SARS is implementing A.I. and data science to automate risk detection, preventing billions in illegal refund outflows.

Reforms can also include integrating taxpayer registers, strengthening filing and payment enforcement, improving the administration of tax exemptions and waivers, and deploying digital tools for VAT and customs administration. Structural reforms include tax base broadening, notably tightening compliance for trusts and religious institutions, as well as tackling the illicit economy,Successful implementation of these reforms is expected to support further growth if the tax-to-GDP ratio.

Figure 18: Reform sequencing timeline: from quick wins to sustainable fiscal capacity



Source: AfDB Staff elaboration, 2026

2.3.6 Institutional Enablers and Digitalization of Revenue Collection Systems

The digitization (e-filling) of revenue collection in South Africa has transitioned SARS from an organization relying on traditional paper-based methods for compliance to a "smart, modern" agency using artificial intelligence, big data, and machine learning. As of 2026, SARS has fully integrated A.I. into its "Smart Modernization" strategy, allowing for automated, real-time risk assessments and pre-population of tax returns. Digital technology allows for faster clearing and inspection of goods at border posts, improving both trade facilitation and revenue collection. As a results, revenue climbed to US$18.7 billion in 2024/25, up from US$7.6 billion six years previously. Furthermore, digital audit trails and real-time reporting are expected to reduce corruption and build citizen trust and transparency.

Box 2: Key Actions and Reforms Aimed at Modernizing Revenue Collection in South Africa

SARS is undergoing a major modernization process (Modernisation 3.0) focused on transforming the tax administration into an intelligent, data-driven entity. The aim is to make tax compliance seamless. Through real-time data matching third-party data (banking, payroll, asset registries) is automatically tallied against declarations before assessments are finalized. SARS is expanding auto-assessments for individuals, with over 4 million taxpayers in 2026 receiving automatic assessments based on third-party data. Effective 1 March 2026, crypto-asset service providers were required to report transactions to SARS, closing a significant transparency gap. SARS is intensifying its focus on high-revenue sectors – tobacco, alcohol, and fuel – to combat smuggling, counterfeit goods, and black-market transactions. Using A.I. to identify impermissible VAT and personal income tax refund claims before payment, SARS prevented more than US$4.5 billion (R75 billion) in potential leaks in 2025/26. SARS has reformed the small business tax system by increasing the turnover tax threshold to US$140 000 (R2.3 million) from 1 April 2026, encouraging formalization. Supported by new technology, SARS registered 1.3 million new taxpayers across various tax categories in 2025/26, contributing net revenue of (US$0.3 million (R4.9 billion).

Sources: SARS; National Treasury; and CFRA 2025

2.3.7 Role of International Cooperation and Development Partners

International cooperation and development partners are critical to SARS in modernizing its administration, combating illicit financial flows, and securing the tax base. Through strategic partnerships, SARS enhances its technological capabilities, exchanges information, and builds capacity to meet global tax standards. Collaborating with the Organisation for Economic Co-operation and Development (OECD) to implement the Global Minimum Tax on SARS eFiling from March 2026, SARS protects the domestic tax base in line with Global Anti-Base Erosion rules. Regional integration and customs capacity is augmented by partnering with the Southern African Customs Union (SACU), AfDB, and the African Continental Free Trade Area (AfCFTA) to improve customs processes, facilitate trade and collect more revenue.

2.3.8 Other relevant Issues on South Africa's revenue

South Africa's revenue landscape is characterized by the historic, yet fragile, achievement of crossing the US$117 billion (R2 trillion) net revenue mark. While SARS has shown strong compliance-driven growth, structural and economic issues continue to threaten long-term fiscal stability. A significant portion of revenue is generated through, compliance efforts rather than organic economic growth. SARS reported US$17.9 billion in compliance revenue for 2024/25, a 15.8% increase, driven by A.I.-enabled auditing and A.I.-powered debt management. The "Two-Pot" retirement system generated roughly US$0.65 billion in PAYE (Pay-As-You-Earn) tax

revenue, higher than initial projections, boosting the 2025/26 revenue collections.

2.4 Improving Public Financial Management Systems

2.4.1 Progress with Persistent Institutional Gaps

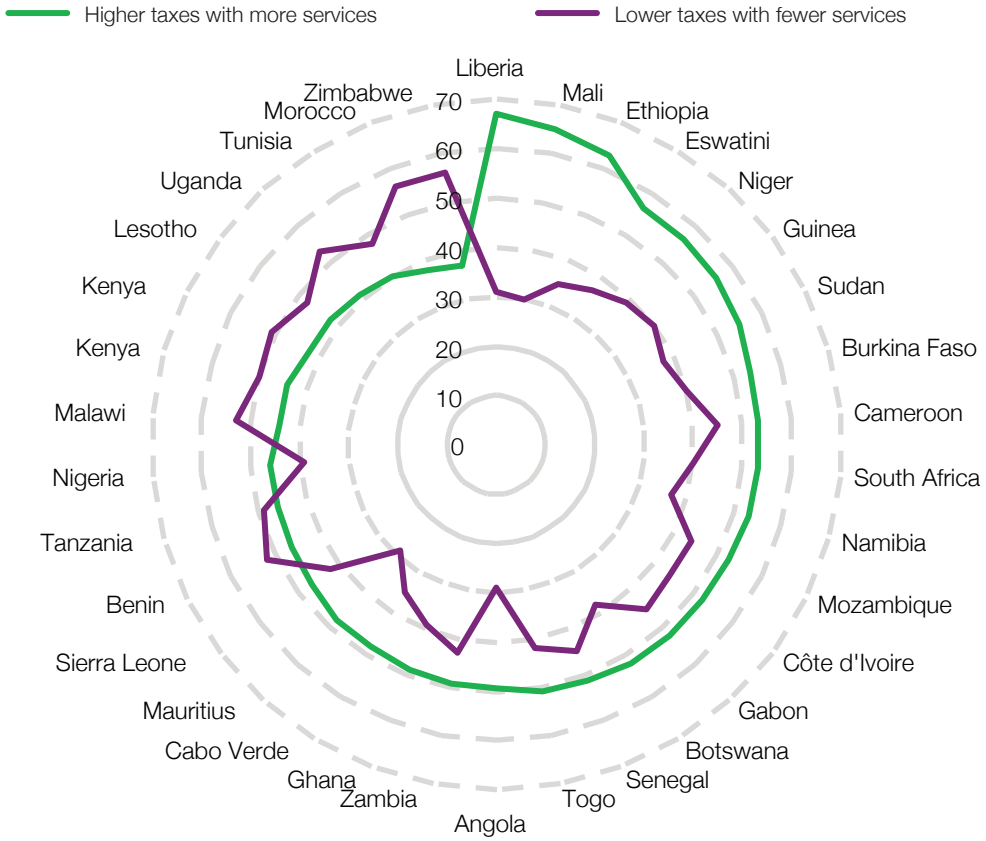
South Africa's fiscal system is reaching a turning point, moving towards stabilisation after years of rising debt and persistent fiscal deficits. Although high debt-service costs and structural constraints continue to weigh on public finances, stronger revenue collection and expenditure discipline are improving fiscal sustainability. According to the 2026 Budget Review, government aims to stabilise debt while maintaining a primary surplus without introducing new tax increases. Gross public debt is projected to peak at 78.9% of GDP in 2025/26 before gradually declining to 76.5% by 2028/29. Fiscal performance has also improved, with the primary surplus projected to increase from 0.9% of GDP in 2025/26 to 1.3% and 1.8% in 2026 and 2027, respectively, reflecting stronger revenue mobilisation and spending control.

2.4.2 Improvements in transparency and fiscal accountability

Improving public financial management systems in South Africa is a central pillar of the 7th administration's (2024-2029) strategy to restore fiscal sustainability and rebuild public trust. While the country has one of the world's most transparent budget frameworks, recent reports from the office of the Auditor-General of South Africa (AGSA) and National Treasury indicate that systemic implementation challenges remain. Improving public financial management in South Africa focuses on strengthening accountability, enforcing the Public Finance Management Act (PFMA), and enhancing skills to curb corruption and irregular expenditure. Key strategies include professionalizing financial roles, modernizing integrated financial management information systems, and fostering a culture of consequence management across all government spheres.

A central element of sustaining revenue performance and fiscal sustainability is strengthening the fiscal social contract between governments and citizens through improved delivery of public services. In this context, taxpayers' willingness to meet their tax obligation depends on expectations regarding the quality-of-service delivery. When taxpayers cannot explicitly link public revenue reforms to better service delivery, tax morale weakens, voluntary compliance declines, and the effective tax base remains limited. Cross country evidence indicates that an important share of citizens is willing to pay taxes when they can clearly associate taxation with better public service delivery (Figure 19).

Figure 19: Strengthening Fiscal and Social Contract between Government and Citizens Improves and Sustains Revenue Performance



Source: AEO 2026; and Staff Calculations using data from the 2022 Afrobarometer surveys

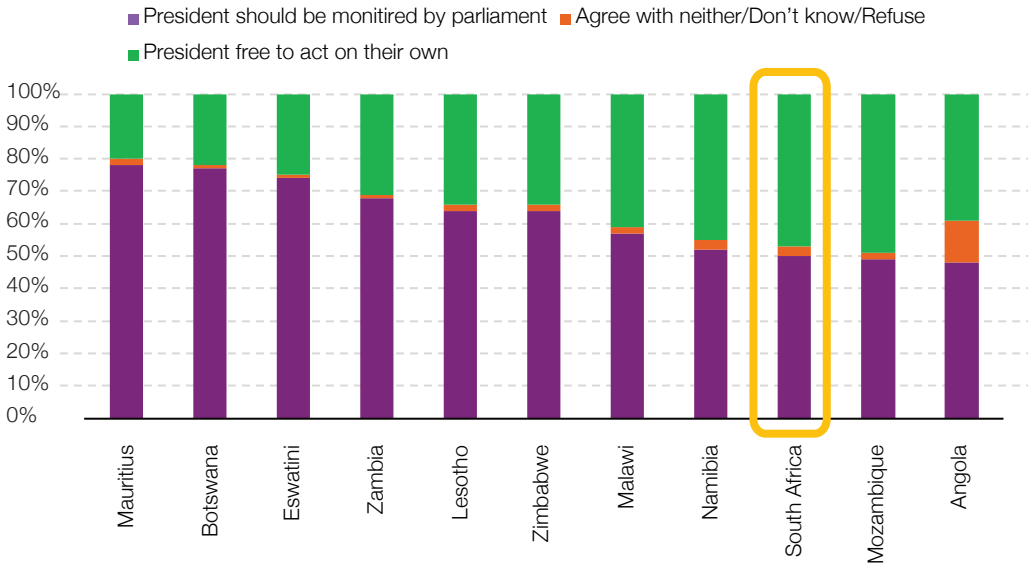
2.4.3 Has Budget transparency translated into credibility

South Africa combines high budget transparency with persistent fiscal credibility challenges. The country ranked among the top performers globally on the 2023 Open Budget Index, scoring 83/100, reflecting strong budget disclosure and public access through platforms such as Vulekamali. However, fiscal credibility has been weakened by poor accountability, SOE liabilities, and procurement inefficiencies. Structural reforms under Operation Vulindlela are supporting fiscal stability and investor confidence. Improved fiscal discipline also contributed to South Africa's sovereign credit rating upgrade by S&P Global in 2025 and removal from the FATF grey list.

2.4.4 Strengthening Oversight, Audit, and Public Accountability

In South Africa, public demand for legislative oversight is a constitutionally mandated, multi-layered process (Figure 20). The Auditor-General audits spending for compliance, while Parliament uses oversight committees to scrutinize budget implementation. Anti-corruption agencies such as the Special Investigating Unit investigate fraud, and civil society organisations monitor accountability and promote transparency in public spending. As the supreme audit institution, the Auditor General holds the executive accountable by auditing government departments, public entities, and municipalities. It flags irregular, and wasteful expenditure, focusing on financial compliance and reporting. Parliament uses portfolio committees and the Standing Committee on Public Accounts (SCOPA) to scrutinize departmental reports and the Auditor General's findings. Key weaknesses in oversight include delayed action on audit findings, political interference in oversight committees, capacity constraints in law enforcement, and slow criminal prosecutions.

Figure 20: Public Demand for Legislative Oversight in South Africa



Sources: AEO 2026

2.4.5 Digital Transformation of Public Financial Management Systems

South Africa is modernizing its public financial management (PFM) systems by shifting toward Digital Public Infrastructure (DPI) to enhance efficiency, transparency, and service delivery. This transformation, driven by National Treasury, aims to replace outdated systems with integrated digital solutions, such as e-procurement and AI-driven budgeting, to reduce manual errors and combat corruption. Systems and data are fragmented, and better inter-departmental coordination is needed. The roadmap aims for a whole-of-government, citizen-centric digital approach. South Africa has suffered a surge in cyberattacks, with thousands occurring weekly, particularly targeting finance, government, and infrastructure, often featuring ransomware and data theft. Successful digital transformation depends equally on adopting advanced technology and building institutional readiness, which includes developing human capital, leadership, and infrastructure.

2.4.6 Economic Dividends and Fiscal Gains from Closing the Efficiency Gap

The efficiency gap in South Africa's revenue and spending represents a major fiscal challenge. Public investments do not fully translate into productive capital, which hampers economic growth and revenue mobilization. According to the 2026 Budget Review, debt service costs are a major drain, set to consume 22 cents of every rand collected in revenue, widening the gap between revenue and expenditure. Efficiency reforms, like Operation Vulindlela, are unlocking economic dividends through higher growth, private sector investment, and job creation. This is expected to improve economic competitiveness, strengthen fiscal discipline, and increase primary surpluses, thereby expanding the fiscal space without raising taxes.

2.5 Formalizing the Informal Sector

2.5.1 Economic Costs of Informality and the Returns to Formalization

South Africa's informal sector contributes an estimated 27.6% of GDP (Figure 21), and remains an important source of employment. This is consistent with most Sub-Saharan African countries, where informality accounts for 50% to 85% of employment. Entering the formal sector in South Africa remains difficult due to complex regulations, high compliance costs, and administrative burdens. These hurdles disproportionately affect SMMEs, which often lack the capacity to comply with labour, tax, licensing, and municipal regulatory requirements,

constraining productivity and business growth.

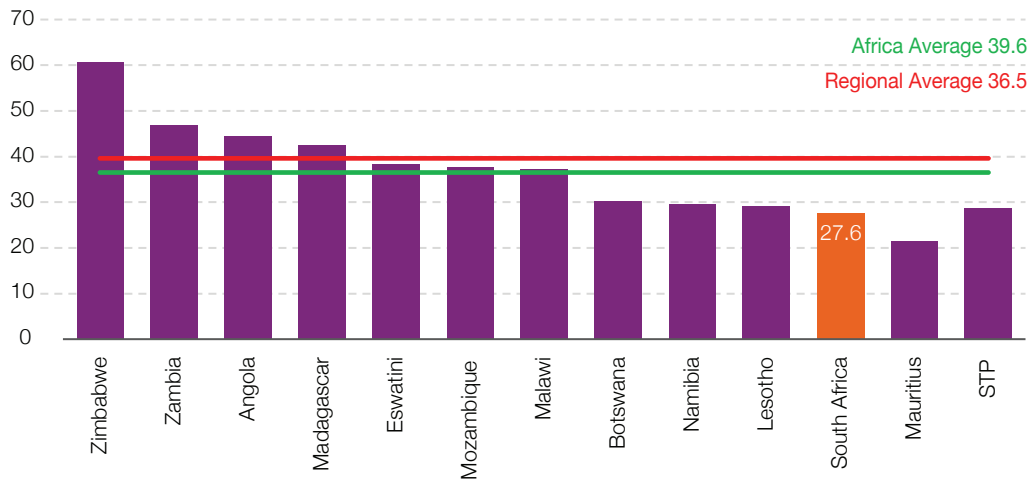
Formalization in South Africa acts as a gateway for SMMEs to move beyond survivalist operations into scalable businesses. While it introduces immediate costs, the long-term returns centre on legitimizing the firm to unlock capital and market opportunities. Formalized businesses in South Africa have significantly better access to improved credit access and financial services. While tax registration with SARS is a key aspect of formalization, it is often viewed as a major deterrent due to the complexity of the tax system and compliance costs. To promote compliance, the government offers tax incentives, and rebates. Introduction of SARS eFiling has improved compliance and firm growth.

2.5.2 Digitalization as a Catalyst for Formalization

Digitalization is emerging as a key catalyst for formalizing South Africa's informal economy by linking informal, cash-based enterprises to the formal financial system. By adopting digital tools, informal businesses, can improve productivity, reduce operational risks, and gain access to credit and financial services. SARS is increasingly deploying digital tools, as well as artificial intelligence and third-party data integration to support a smart and modern tax administration system. The aim is to simplify compliance for formal businesses while bringing informal actors, including spaza shops, freelancers, and sole proprietors, into the formal economy.

The SARS MobiApp allows informal actors to register for tax, submit income tax returns (ITR12), and pay penalties or outstanding debt directly from a smartphone. SARS uses third-party data from banks and employers to pre-populate tax returns, having auto-assessed over 4 million taxpayers by 2024–25, reducing manual filing burdens. The use of linked administrative data (e.g., linking tax or employment records) allows for the automatic payment of social benefits, reducing application burdens on beneficiaries. The Two-Pot Retirement System allows taxpayers to access a "savings component" of their retirement funds while having a "vested component" protected. The 2026 amendments allow withdrawal of the full balance of one's savings component, even if below R2,000 (about US$120). SARS is implementing complementary revenue reforms focused on digital modernization, simplifying tax for small businesses, and linking tax administration to social protection to enhance compliance and reduce inequality.

Figure 21: Contribution of the Informal Sector to GDP in Southern African Countries (2015–2020)



Sources: AEO 2026; and Staff calculations using data from Elgin et al. (2021)

2.6 Scaling-Up Public-Private Partnerships (PPPs)

2.6.1 Building Credible PPP Enabling Frameworks and Project Preparation Ecosystems

Scaling up (PPPs) in South Africa to tackle systemic constraints requires urgent regulatory reforms and increased state capacity. Key bottlenecks include political instability, inadequate skills, and high corruption risk. Effective, large-scale implementation of PPPs relies on transparent procurement, project prioritization, and shifting toward long-term, sustainable partnerships that ensure value for money.

South African PPP frameworks are undergoing significant reforms to transition to a more efficient, investment-friendly model. National Treasury is implementing these reforms, with 2026 being a "year of real opportunity" for PPPs, particularly for projects aligned with the Built Environment and infrastructure reforms, as noted in the 2026 Budget Review. Project preparation, appraisal, and PPP functions have been consolidated in the Infrastructure Finance and Implementation Support Agency (IFISA). National Treasury, through the Government Technical Advisory Centre (GTAC), remains the primary regulator, overseeing feasibility and procurement.

South Africa’s infrastructure pipeline shows high potential but suffers from slow implementation, with often only 10% of projects reaching financial close due to weak preparation. While energy projects Renewable Energy Independent Power Producer Procurement Programme (REIPPPP) have been successful, key bottlenecks include slow regulatory approvals, poor project structuring, and limited capacity at local levels. The 2026 National Budget committed over US$59 billion to public sector infrastructure spending over the medium term. The Infrastructure Fund recently approved 12 blended finance projects worth US$2.2 billion across water, transport, student housing, and health.

2.6.2 Making Marginal Projects Bankable and Connecting them to Capital Markets

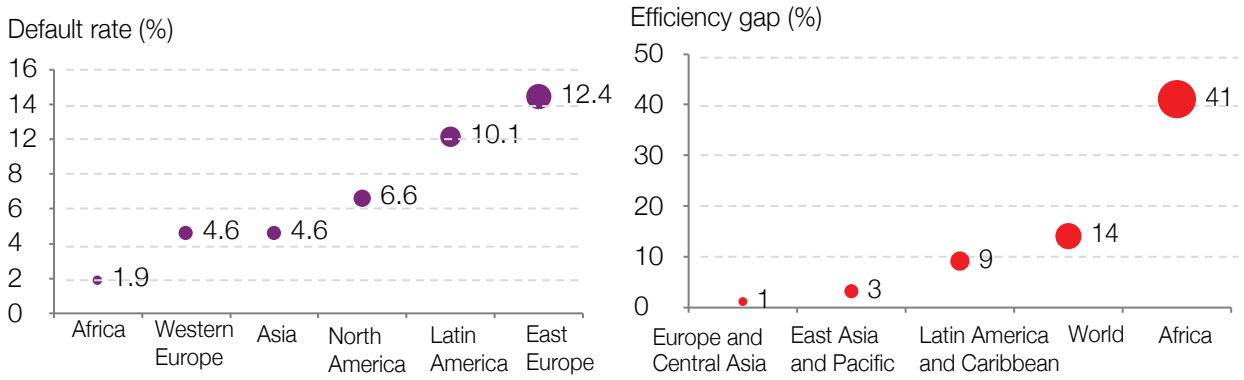
Making marginal projects bankable in South Africa, involves transforming high-risk or low-margin initiatives into attractive investments through rigorous preparation, blended finance, and de-risking mechanisms, aligning with the country's US$59 billion-plus infrastructure-led growth strategy. South Africa's removal from the FATF grey list in 2025 significantly bolstered investor confidence and lowered international transaction costs.
South Africa is strengthening sovereign, municipal, and corporate bond markets through regulatory reforms, infrastructure modernization, and increased use of sustainable finance instruments. In November 2025, National Treasury launched its first Infrastructure and Development Finance Bond, raising US$690 million to support priority infrastructure projects, while green, social, and sustainability bonds are increasingly being used to finance municipal water, electricity, and transport infrastructure. The country is also scaling blended finance and deepening financial markets to bridge large infrastructure funding gaps. This effort is supported by the launch of the IFISA Programme Office, aimed at mobilising private finance and technical expertise to accelerate infrastructure delivery.

The new programme office consolidates key infrastructure financing functions into a single high-impact structure to strengthen project implementation and blended finance mobilisation. Complementing these reforms are efforts to deepen capital markets and attract long-term institutional investment through improved market frameworks and revisions to Regulation 28 of the Pension Funds Act, enabling greater infrastructure investment by pension funds, insurers, and asset managers.

Africa consistently records one of the lowest default rates on infrastructure and related project finance loans globally, with empirical data showing rates as

low as 1.9% —well below the rates observed in the Asia, Latin America, and Western Europe (Figure 22). Despite this strong performance track record, investors often apply inflated risk premiums. This mismatch creates an environment where African governments and developers pay unnecessarily high borrowing costs, even though their payment records show strong financial security. This finding supports the argument that African infrastructure projects are often perceived as riskier than they are.

Figure 22: Africa Has the Lowest Default Rates on Infrastructure and Related Projects



Sources: (a) Moody's Analytics, 2020; (b) African Development Bank staff calculations

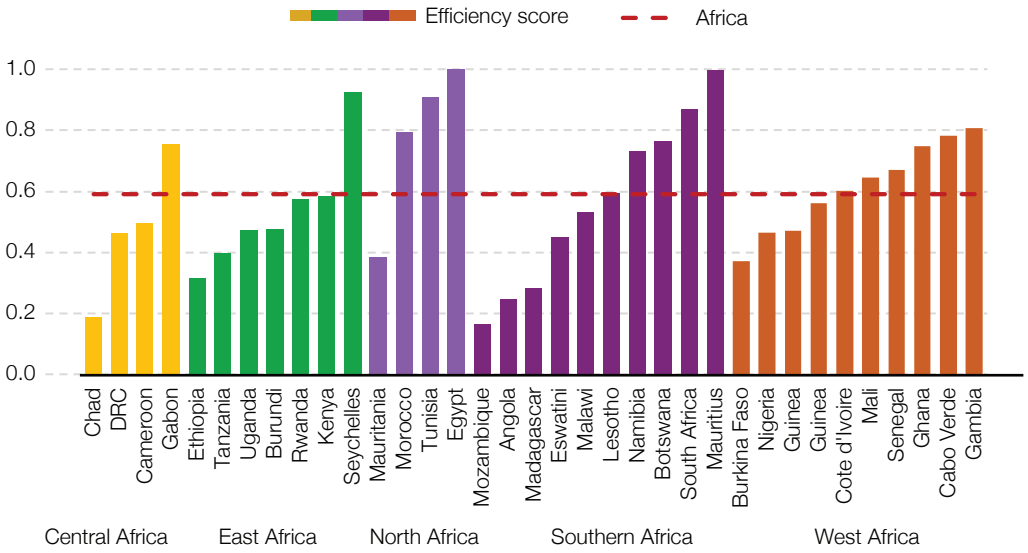
2.6.3 Managing Fiscal Risks and Safeguarding Value-for-Money

The South African government manages fiscal risks and ensures efficiency in PPPs through a rigorous regulatory framework overseen by the National Treasury, aimed at ensuring "value for money," affordability, and appropriate risk transfer. As of 2026, these measures are being strengthened through new guidelines, standardized contracts, and the establishment of IFISA to streamline project preparation. PPPs are governed by the Public Finance Management Act (PFMA) and Treasury Regulation 16, which mandate a structured, phased approach (inception, feasibility, procurement, and management). National Treasury uses the PPP Fiscal Risk Assessment Model to quantify fiscal impacts, identify contingent liabilities(like guarantees), and perform sensitivity analyses.

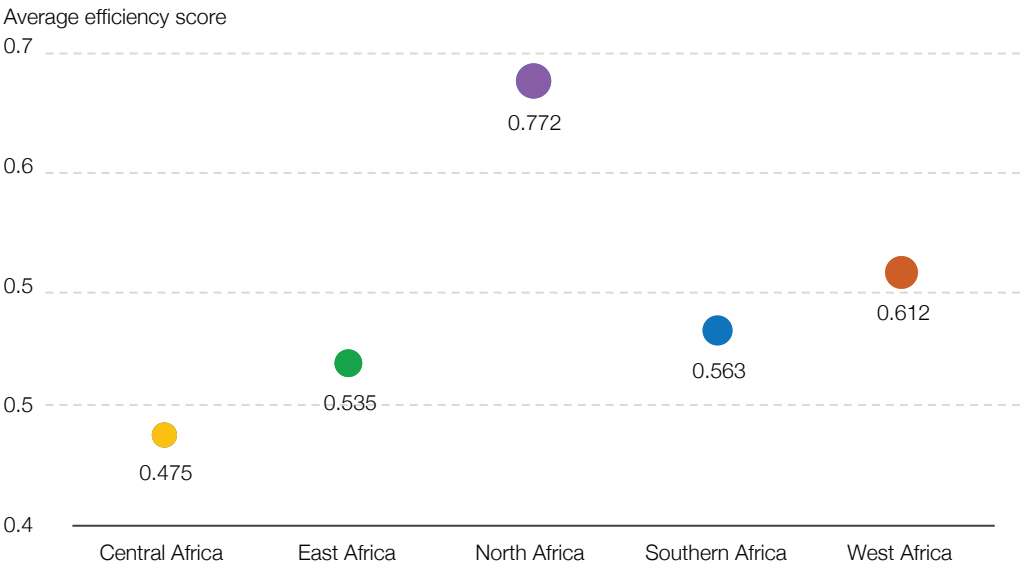
Renegotiations in South African PPPs are frequent due to the long-term, complex nature of contracts, often creating risks where benefits are skewed toward the private sector. Inefficient, premature, or weak feasibility studies often result in risks being improperly allocated (e.g., passing too much risk to government), which increases the likelihood of project failure, particularly those involving public sector funding obligations.

Africa's average efficiency score is estimated at about 59%, implying that roughly 41 cents of every dollar spent on public investment does not translate into productive capital. South Africa's average public investment efficiency score stands at 86.9% (Figure 23), above the Southern Africa regional average of 56.3%. Nonetheless, South Africa's efficiency gap of 13.1% means that of US$100 spent on public investment, US$13.1 does not translate into productive capital. South Africa can improve its efficiency score by converging towards international best practices in public investment management, notably investment planning, project selection, and execution.

Figure 23: Public Investment Efficiency Gaps by Region



Sources: (a) Moody's Analytics, 2020; (b) African Development Bank staff calculations; Efficiency gap = 1 - efficiency score.



Sources; AfDB, AEO, 2026

2.7 Mobilizing Long-Term Capital from Regional and Institutional Investors

2.7.1 Pension Funds as Patient Capital: What the Data Implies for Reform

South Africa's pension industry is highly developed, with assets managed by life insurers alone exceeding US$297 billion at the end of 2025, and total retirement assets reaching US$298 billion by the end of 2023. However, this sector faces challenges from frequent withdrawals under the two-pot retirement system implemented in 2024, raising concerns about long-term sustainability.

The Government Employees Pension Fund is the largest single entity, holding US$118 billion as of March 2025, following a strong 13.1% annual growth in its investment portfolio. Asset managers maintain a high stake in equities, which account for roughly 54.6% of total investments. Debt instruments make up about 27.3%. Following regulatory changes, funds can invest up to 45% (plus an additional 10% in Africa) in

foreign assets. As a result, many funds have increased their foreign holdings to diversify their portfolios. Cash allocations hover around 7%–10%. Interest in private equity and private debt to enhance returns and diversify away from listed equities is growing, although these remain small compared to traditional asset classes.

2.7.2 Sovereign Wealth Funds: Shifting from Outward Bias to Strategic Investment Windows

In South Africa, the mandate and governance of retirement funds are regulated by the Pension Funds Act, with Regulation 28 serving as the primary tool for managing asset allocation risk. Governance is led by a Board of Trustees, which must comprise at least 50% member-elected representatives. Trustees have a fiduciary duty to act in the best interests of the fund's members, overseen by the Financial Sector Conduct Authority (FSCA). The primary mandate is to protect long-term retirement savings from excessive risk and concentration, ensuring funds are diversified across asset classes.

South African investors are increasingly utilizing the full 45% offshore (including Africa) allowance to access global sectors (like technology) not available on the Johannesburg Stock Exchange (JSE) and to hedge against rand volatility. The 55% minimum domestic requirement forces significant exposure to a shrinking number of JSE-listed companies, though many of these firms earn over 50% of their revenue globally, providing a partial indirect offshore hedge. A new centrally governed framework is being established to manage over US$5.3 billion in unclaimed retirement benefits to reduce fees and improve payouts. While offshore limits have increased, many managers remain wary of blindly externalising funds due to currency timing risks. Some asset managers argue local assets currently offer better value compared to expensive global counterparts.

2.7.3 Other relevant Issues: Mobilizing Climate Funds and Resilience-Focused Financing

South Africa is mobilising climate finance through initiatives such as the US$8.5 billion Just Energy Transition Partnership (JETP) and the Green Climate Fund, with financing largely directed toward renewable energy and coal transition projects. Climate finance flows average about US$10.8 billion annually, although significant financing gaps remain, particularly for adaptation in water, agriculture, and forestry, which receive less than 10% of total climate finance. To bridge these gaps, government is scaling blended finance, private sector participation, and dedicated adaptation mechanisms such as the proposed Climate Change Response Fund. South Africa also has one of Africa's most active green bond markets, supported by Johannesburg Stock Exchange sustainability frameworks. Complementary reforms include expanding TVET programmes, social protection, and economic diversification to support a just and inclusive low-carbon transition.

2.8 Leveraging Diaspora Capital

2.8.1 State of Financial Resources from the African Diaspora

The financial contribution from the African diaspora to South Africa remains modest compared to other countries like Egypt and Nigeria. While South Africa has a large economy (estimated at $410.34 billion in 2025), its diaspora remittance inflows are less than 1% of GDP. A large portion of financial flows into South Africa (and outflows from SADC neighbours like Zimbabwe) occurs through informal channels, estimated at roughly 17% of the formal market size, making actual diaspora contributions likely higher than official data suggests.

South Africa is a major source of remittances for the rest of the continent, hosting nearly 4 million SADC migrants who send money back to countries like Zimbabwe and Malawi. South Africa has a complex, dual remittance market where formal channels (banks, MTOs) compete with significant informal mechanisms, often driven by high costs and documentation needs. While informal channels are popular for being faster and cheaper by at least 5% of remittances, formal methods are growing, yet remain expensive, often costing over 8% for Sub-Saharan Africa.
A study by the SARB concluded that

transaction costs are not only determinants of cross-border payments but also migration stock, financial access, macroeconomic instability particularly exchange rate volatility, income level (GDP per capita) and mobile money penetration (SARB, 2025). Cross-border payments are crucial to foster financial inclusion, trade, and economic integration in Sub-Saharan Africa.

2.9 Harnessing Africa's Natural Resources Assets

2.9.1 Moving Beyond the Extractive Model

According to the South Africa 2025 CFR, South Africa's natural capital is diverse, consists of human capital (a population of 63 million in 2024), minerals (gold, platinum, diamonds, iron ore, manganese, and coal), agricultural land and forests as well as renewable resources. The bulk of national wealth comprises human capital, with an estimated value of US$2.1 trillion in 2018, followed by produced capital (US$1.2 trillion), renewable capital (US$213.8 billion) and non-renewable capital (US$186.1 billion). The value of net foreign assets was estimated at US$38.6 billion. South Africa's natural capital, including the diverse ecosystems, mineral resources, agricultural land, and biodiversity, plays a critical role in economic growth, revenue generation and employment. Taxes on mining, royalties and exploration licenses contribute 3% of domestic tax revenue. Oceans and beaches contribute about 35% of GDP, ecosystem services 7% and mining 6%. Forests cover about 14% of the total land area and contribute 10.4% of agriculture and 4.5% of manufacturing GDP.

South Africa can leverage its abundant natural resources, including minerals (platinum, gold, coal, manganese), oceans, and land to drive economic growth by increasing beneficiation, promoting sustainable mining, and investing in renewable energy. Effective management, technological innovation, and strong governance are essential to turn this wealth into inclusive development. Despite improvements, aging infrastructure and logistical bottlenecks in rail and ports remain critical risks to the export potential of minerals and agricultural goods and to economic growth.

2.9.2 Natural Capital, Economic Performance, and Macroeconomic Sustainability

South Africa's natural capital comprising vast mineral deposits, water, and biodiversity is the foundation of its economic performance. However, traditional macroeconomic metrics like GDP often overlook ecosystem degradation. Achieving macroeconomic sustainability requires integrating Natural Capital Accounting to protect resources while driving inclusive, resilient growth. South Africa utilizes the United Nations System of Environmental-Economic Accounting (SEEA) to formally integrate ecological thresholds into traditional financial metrics like GDP.

2.9.3 Natural Capital as a Source of Financing

Natural capital is rapidly evolving from an ignored externality into a core investable asset class. As of 2026, the country is leveraging Natural Capital Accounting (NCA) and innovative financial instruments to bridge the biodiversity funding gap. By using the System of Environmental-Economic Accounting (SEEA), South Africa tracks natural assets to inform policy and unlock funding, including biodiversity credits, green bonds, and debt-for-nature swaps. The government and municipalities use green bonds to raise capital for climate and environmental projects. As of 2024, South Africa's sustainable bond market had grown to over R20 billion, with proceeds funding renewable energy, water management, and low-carbon infrastructure. The government has introduced fiscal measures such as Section 37D of the Income Tax Act, which allows a 4% annual tax deduction for landowners who declare their land as a National Park or Nature Reserve. Additionally, South Africa recently increased permit and license fees for Threatened or Protected Species to bolster conservation revenue.

2.9.4 Governance, Institutions and Macroeconomic Stability

Oversight mechanisms for good governance and resource management are primarily rooted in the Constitution of the Republic of South Africa, 1996, which mandates the separation of powers and establishes various watchdog bodies. These mechanisms operate across national, provincial, and local spheres to monitor executive action and ensure public funds are used effectively. South Africa is maintaining macroeconomic stability, characterized by low inflation a resilient financial system, and improved energy supply. However, growth remained slow at 1.1% in 2025 and structural constraints persist. Fiscal policy aims sustainability challenges from high debt-servicing costs. The banking sector remains well-capitalized with a capital adequacy ratio of 17.2%, and nonperforming loans (4.5%) in 2025. Improvements in energy supply and logistics, along with private sector participation, are key to stabilizing public sector entities and supporting growth.

2.10 Crowding in Global Private Capital in a Fragmented World

2.10.1 Foreign Direct Investment signals both South Africa's Potential and its Fragility

Foreign direct investment (FDI) fluctuated in 2025, recording a strong Q1 inflow (US 661 million) and a significant recovery in Q4 (US$2.2 billion) after substantial Q3 outflows, driven by investments in logistics and media. Total annual direct investment liabilities, however, saw a net outflow of US$2.3 billion for 2025. FDI supports social development through skills transfer, workforce training programs, and improved infrastructure development. Key sectors driving this growth include mining, manufacturing, and renewable energy. FDI in South Africa has historically been concentrated in mining and natural resources, which needs diversification to ensure broader economic benefits. FDI in South Africa is coupled with inclusive development mandates. The government increasingly ties foreign investments to local-content quotas, employment preservation, and technology transfer requirements, among others. The state emphasizes leveraging blended finance through institutions like the Industrial Development Corporation (IDC) to de-risk investments and crowd-in private capital specifically for women- and youth-led enterprises.

2.10.2 De-risking and Blended Finance: Building Bankable Pipelines

Blended finance in South Africa combines public/concessional funds with private capital to de-risk sustainable infrastructure and development projects. In South Africa, Development Finance Institutions (DFIs) such as the Development Bank of Southern Africa (DBSA) and IDC employ mechanisms like guarantees, subordinated debt, and technical assistance, thereby lowering investment barriers to attract private investors to critical sectors such as renewable energy and transport, particularly supporting the US$58.4 billion infrastructure drive. They mitigate political and economic risks, conduct due diligence, and provide technical assistance to make infrastructure and SME projects bankable. PPPs are undergoing a significant overhaul to address historical declines in project volume. As of March 2026, the government has implemented several reforms to streamline these structures across infrastructure, energy, and digital sectors. In key sectors like energy, blended finance supports climate adaptation, including renewable energy and infrastructure upgrades. To reverse the decline in PPP transactions over the past 15 years, the National Treasury and Operation Vulindlela have:

- **Simplified Approval Processes:** As of June 2025, PPP project approval processes for projects valued at US$ 0.12 million or less were streamlined.
- **Allowed Unsolicited Proposals:** The regulations now allow for unsolicited proposals, promoting private sector initiative.
- **Use Hybrid Models:** Projects now regularly utilize a mix of DFI loans, grants, and private equity.

2.10.3 External Portfolio Inflows

South Africa is actively restructuring its approach to external capital inflows, shifting from antiquated exchange controls toward a modernised, positive capital flow management framework designed to attract investment in sectors such as renewable energy, manufacturing, and digital infrastructure. South Africa's portfolio inflows were volatile in 2025, in Q4 2025 shifting between marginal inflows of US$167 million (R2.8 billion) and much stronger quarterly inflows of US$2.4 billion (R40.8 billion) in Q3 2025, heavily influenced by non-resident debt security acquisitions and international corporate restructuring rather than hefty investments in domestic equities. Foreign investors bought debt worth over US$761 million in the fourth quarter of 2025, alongside ongoing divestments or marginal allocations in local equity markets. Net portfolio investments have undergone dramatic cyclical shifts; while previously seeing outflows, inbound investment figures have been temporarily boosted by corporate restructuring such as share distributions by multinational entities like Anglo American to non-resident shareholders.

2.10.4 Leveraging Fragmentation to Build Strategic Platforms

South Africa is advancing a structural reform agenda under Operation Vulindlela to improve investment readiness, with emphasis on decarbonisation, digitisation, and economic diversification. The World Bank's Business Ready (B READY) 2024 report showed relatively strong performance in labour regulations and business entry frameworks, although operational efficiency and implementation gaps remain. Mobilising finance remains constrained by high public debt, illicit financial flows, regulatory bottlenecks, and infrastructure risks, contributing to significant financing gaps and limiting SMME growth. External financing is also affected by sovereign risk and weak investor confidence.

Taking on these challenges, government is implementing institutional and regulatory reforms aimed at improving policy certainty, reducing contract disputes, and strengthening the investment climate. The joint Operation Vulindlela initiative between the Presidency and National Treasury continues to support reforms in energy, logistics, and water sectors. Regulatory institutions are digitising systems, improving case management, and expanding alternative dispute resolution mechanisms to accelerate approvals and reduce business costs. Fiscal consolidation efforts, including targeting a primary budget surplus in 2026, are also aimed at stabilising debt and reducing sovereign risk.

2.10.5 Strengthening Partnerships to Mobilize Capital, Investment, and Trade

Multilateral Development Banks (MDBs) and the AfDB strengthen South Africa's financial system by providing large-scale infrastructure financing, technical assistance for policy reform, and catalysing private investment. They focus on promoting sustainable development, enhancing governance in financial institutions, managing climate risk, and fostering regional integration through non-concessional and concessional funding. The SARB remains the primary authority for ensuring financial stability, while the MDBs provide crucial external support and capital to complement its efforts. MDBs use innovative instruments like hybrid capital, risk-transfer mechanisms, and portfolio guarantees to lower investment risks and attract private investors to emerging markets.

South Africa is deeply integrated through the SADC and SACU, facilitating trade via regional protocols, with a strong push towards the AfCFTA to boost preferential trade. The focus is on harmonizing financial regulations and liberalizing tariffs, though, as of 2024, trading with SADC continues largely under SACU/SADC treaties rather than AfCFTA. The South Africa-EU Clean Trade and Investment Partnership (CTIP) signed in November 2025, aims to facilitate investment in renewable energy, green hydrogen, and transport, while tackling regulatory bottlenecks to increase trade.

2.11 Conclusion and Policy Recommendations

2.11.1 Short-term policy actions

To mobilize additional development financing, South Africa needs to scale up public-private partnerships, blended finance, and bankable infrastructure projects to attract private sector investment, particularly for the Just Energy Transition. Priority actions include strengthening project preparation facilities, expanding guarantees and risk-sharing instruments, and improving the pipeline of investment-ready infrastructure projects.

Strengthening the capacity of institutions such as the Financial Sector Conduct Authority and the South African Reserve Bank to monitor cross-border financial flows and support sustainable financial instruments will also be important. Policy efforts should better connect domestic institutional capital, including pension funds and insurers, with priority investment sectors through de-risking mechanisms and blended finance structures.

Expanding access to finance for Micro, Small, and Medium Enterprises (MSMEs) should remain a key priority, given that only about 5% of formal MSMEs have access to credit. Operationalising the Small Enterprise Development Finance Agency as a streamlined "one-stop shop," expanding digital financing channels and credit guarantees, and simplifying licensing and permitting processes would help reduce investment barriers, support entrepreneurship, and promote inclusive private sector development.

2.11.2 Medium to long-term policy actions

South Africa's long-term development potential lies in leveraging its mature financial sector through strategic partnerships and international capital to bridge large financing gaps while navigating increasingly fragmented global markets. Over the medium to long term, policy implementation should focus on deepening capital market reforms, strengthening regional financial integration, and expanding the use of sustainable finance instruments such as green bonds, infrastructure bonds, and blended finance facilities. Greater use of DFIs to de-risk projects, improvements in public financial management, gradual relaxation of restrictive exchange controls, and stronger market competition to reduce transaction costs will support investment mobilisation. Strengthening institutional capacity at national and municipal levels to prepare, implement, and monitor large-scale infrastructure projects will also be critical for improving investor confidence and sustaining long-term financing mobilisation.

3 STRENGTHENING AND CONSOLIDATING SOUTH AFRICA'S FINANCIAL SYSTEMS AND AGENCY IN THE CHANGING WORLD

Key Messages

- South Africa boasts the most developed capital market on the continent, anchored by the Johannesburg Stock Exchange (JSE). The financial sector features robust regulatory frameworks, deep liquidity, and broad access to diverse financial instruments. The JSE ranks among the top 20 stock exchanges globally and features a market capitalization exceeding US$1.22 trillion.
- The country finances about 90% of its national budget through domestic resources, while foreign loans account for roughly 10%, reflecting relatively strong domestic resource mobilization capacity.
- Despite its advanced financial system, South Africa continues to face large development financing gaps linked to inequality, electricity and water infrastructure constraints, and aging rail networks.
- Strengthening and consolidating South Africa's financial systems requires structural, regulatory, and policy reforms. These should be designed to ensure macroeconomic stability, boost financial inclusion, and enhance the sector's resilience against global shocks.
- Closing financing gaps will require greater mobilization of private capital, blended finance, improved project preparation, and leveraging DFIs to de-risk investment.

3.1 Introduction

South Africa's financial architecture and agency need to be strengthened and modernized in a weakening global environment marked by tightening financial conditions. The decline in global development financing is a problem, as are rising risks for South Africa, including higher borrowing costs, volatile capital flows, increased debt, and exposure to external shocks, as well as the structural vulnerabilities within domestic financial systems. Following the establishment of a Government of National Unity (GNU) in 2024, South Africa is focusing on fiscal discipline, infrastructure investment, and modernizing regulatory systems to boost investor confidence and ensure long-term stability. The SARB is spearheading the Payments Ecosystem Modernisation (PEM) programme, with a major overhaul expected to be implemented over the next three years. South Africa exited the Financial Action Task Force (FATF) grey list in October

2025, following a 32-month period of intensive reforms to strengthen anti-money laundering and counter-terrorism financing systems.

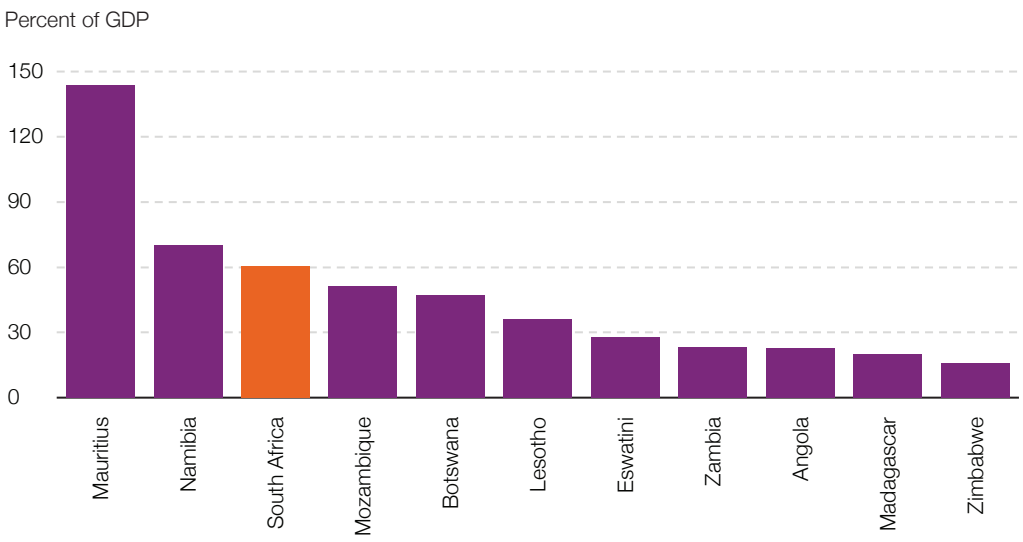
3.2 Strengthening South Africa's financial system: addressing bottlenecks and expanding reach and impact

3.2.1 State of South Africa's Financial Systems

South Africa's financial system is highly developed, supported by a strong regulatory framework and technologically advanced markets, and is widely regarded as the most sophisticated in Africa and among the leading systems in the developing world. The country has deep capital markets, with the JSE ranked among the world's top 20 by market capitalization, while regulation aligns with international standards, including Basel III compliance. The banking sector is highly concentrated, dominated by six major banks, Standard Bank, FirstRand, Absa, Nedbank, Investec, and Capitec, which account for about 93% of industry assets. Banks remain well-capitalized and supervised by the SARB and FSCA. Bank deposits and credit to the private sector stood at 60.4% of GDP in 2021 (Figure 24), reflecting a relatively developed, bank-based financial system. DFIs focus on economic development, infrastructure, and job creation. Key institutions include the Industrial Development Corporation (IDC), Development Bank of Southern Africa (DBSA), Land Bank, and National Empowerment Fund (NEF). Their role is to fill the funding gap for infrastructure, for MSMEs and startups that fail to secure commercial bank funding. As shown on Figure 26, the depth of the insurance market is highest in South Africa (60.1% of GDP), followed by Namibia and Mauritius.

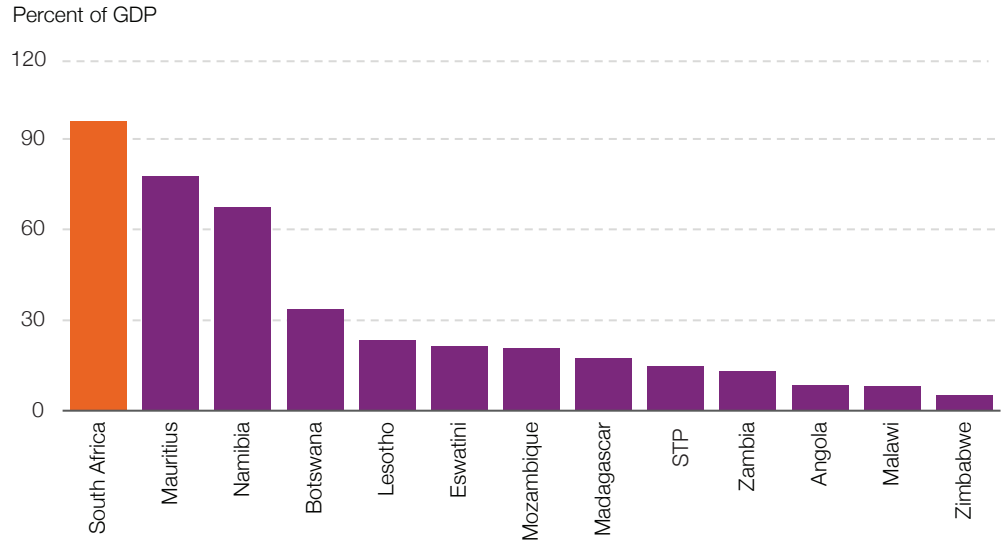
South Africa's financial architecture remains structurally misaligned, with high savings levels failing to translate into productive investment, contributing to low fixed capital formation and persistent inequality. The 2025 National Planning Commission report noted that, although the financial system is resilient, it remains biased toward short-term returns rather than long-term investment needed for economic transformation. Key challenges include high borrowing costs, financial exclusion, racial disparities in access to finance, and low investment levels. The economy also remains vulnerable to external shocks, including capital flow reversals and commodity price volatility, which heighten macroeconomic instability. Additional constraints include reliance on foreign-dominated capital markets and limited influence in global financial governance.

Figure 24: Bank Deposits to GDP (%), 2021



Source: World Bank Global Financial Development Database

Figure 25: Domestic Credit to the Private Sector in Southern African Countries, % of GDP, 2015-2024



Sources: AEO 2026; and African Development Bank staff computations based on World Bank (WDI), 2025

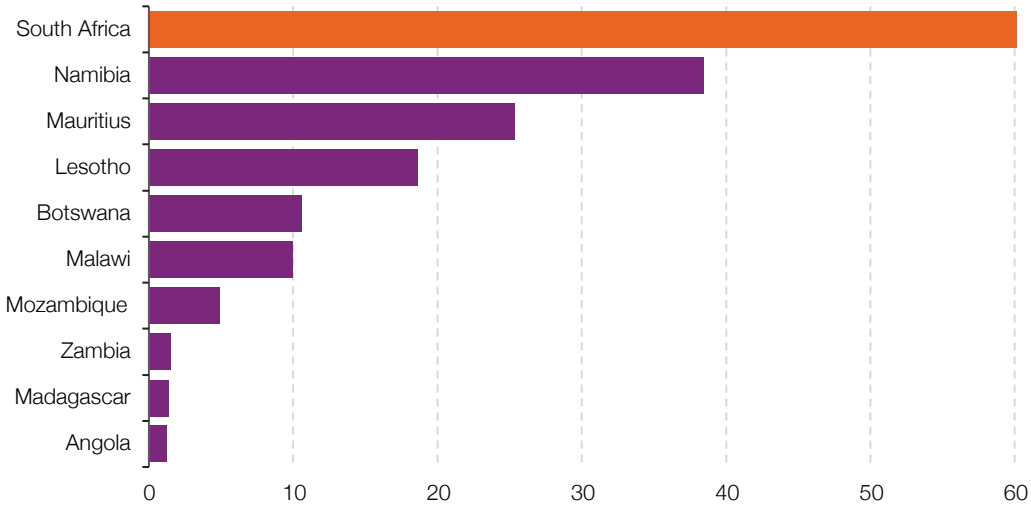
3.2.2 Broadening the catchment area: Expanding the financial sector's reach and impact

Expanding the financial sector's reach and impact in South Africa is a priority, with initiatives in 2026 focusing on modernizing payment systems, increasing digital financial inclusion, and strengthening regulatory frameworks to drive economic growth and stability. The sector is transitioning towards greater digital banking, with new competitors like TymeBank, Discovery Bank, and Bank Zero enhancing competition and reducing fees. National Development Banks (NDBs) in South Africa, such as the DBSA, can significantly enhance access to affordable financing by providing long-term loans, offering blended finance and de-risking investments to attract private capital. They bridge funding gaps in key sectors like infrastructure, renewable energy, and MSME development. This includes supporting projects with high social returns but lower financial returns.

In South Africa, financial regulators, led by the SARB under the Twin Peaks framework established through the Financial Sector Regulation (FSR) Act of 2017, play a central role in maintaining macro-financial stability and supervising systemic risks. The Prudential Authority and FSCA complement this role through risk-based regulatory frameworks that support financial inclusion, innovation, and market development.

Mobilization of long-term development finance and deepening of financial markets are increasingly being supported by reforms in the pension fund and insurance sectors. A key reform has been the evolution of Regulation 28 of the Pension Funds Act, which introduced a specific definition for infrastructure investment. This allows retirement funds to allocate up to 45% of assets to domestic infrastructure and an additional 10% across the rest of Africa. The private equity investment limit was also increased to 15% to support greater financing for long-term development projects.

Figure 26: Insurance market landscape in Southern Africa - Insurance company assets, percent of GDP



Sources: AEO 2026; and Swiss Re Institute (2026)

3.3 Consolidating South Africa's financial system: the case for a cohesive and integrated financial architecture

3.3.1 South Africa's Financial System Integration

Building a well-integrated financial system in South Africa involves buttressing regulatory frameworks (e.g., Basel III), modernizing payment systems (Vision 2025), and enhancing financial inclusion through digital adoption. Key strategies include reforming the National Payment System, fostering competition, aligning Regulation 28 to boost infrastructure investment, and ensuring robust oversight by the SARB.

Coordination among local banks, DFIs, regional institutions, and development partners in South Africa is structured around PPPs, blended finance mechanisms, and strategic mandates to accelerate infrastructure development and industrialization. The DBSA and IDC act as primary integrators, linking public and private actors, while the National Treasury regulates these interactions.

Pan-African integration involves aligning local financial architecture with continental frameworks, such as the AfCFTA and the Pan-African Payment and Settlement System (PAPSS). This strategy aims to leverage South Africa's advanced financial services sector to drive regional value chains, enhance trade, and foster sustainable growth by channelling capital into productive, long-term African investments. The national financial system in South Africa is undergoing significant modernization and reform to enhance stability, financial inclusion, and competition, driven by the SARB and the National Treasury through the PEM Programme.

Key improvements include transitioning from a cash-reliant economy to a digital-first approach, strengthening regulatory frameworks against financial crime, and enhancing infrastructure to support digital payment adoption. Increasing Africa's representation and voice in MDBs and IFIs is essential to ensure that the continent's growing economic and demographic significance is reflected in global financial decision-making processes. These reforms could pave the way for a more equitable and sustainable global financial system that supports Africa's aspirations for development and integration.

Building a Resilient Economy through Effective Risk Mitigation and Diversified Financing

Building a resilient South African economy requires a shift from state-led financ-

ing toward more diversified, private sector-led funding supported by stronger risk-mitigation measures. Current reforms focus on stabilizing public debt, scaling-up infrastructure and energy transition investment through blended finance, and expanding innovative instruments such as climate adaptation bonds and debt-for-adaptation swaps. Efforts to strengthen domestic resource mobilization include modernizing tax administration, deepening capital markets, and improving financial inclusion. Amendments to Regulation 28 of the Pension Funds Act now allows retirement funds to allocate up to 45% of assets to domestic infrastructure, helping mobilize institutional capital for development financing. At the same time, the SARB continues to strengthen macro-financial stability through enhanced macroprudential regulation, stress testing, and to reduce sovereign and financial sector risks.

Institutional and Governance Reforms to Strengthen Financial Systems in South Africa

South Africa is strengthening its financial system through institutional and regulatory reforms to improve financial stability, oversight, and market efficiency. Reforms are gradually shifting the sector toward a more principles-based regulatory framework. A major milestone was South Africa's exit from the FATF grey list in October 2025 after addressing anti-money laundering and terrorism financing deficiencies. Other reforms include consolidating prudential oversight under the Prudential Authority, operationalizing the Corporation for Deposit Insurance, strengthening bank resolution powers under the SARB, and establishing a National Payments Utility to modernize payment systems and support fintech participation. Broader reforms also seek to bolster public financial management, improve regulatory compliance, enhance regional payment integration under SADC and AfCFTA frameworks, and expand blended finance mechanisms to crowd in private investment for infrastructure and climate-related projects.

3.3.2 Policy Pathways to Consolidate South Africa's Financial System

South Africa's financial system remains resilient, supported by profitable and well-capitalized banks, but underlying economic vulnerabilities continue to pose risks to stability. Key challenges include high sovereign-bank interconnectedness, volatile capital flows, weak economic growth, and persistent infrastructure constraints. Gross public debt remained elevated at 78.9% of GDP in 2025, with debt-servicing costs absorbing about 18% of government revenue, limiting fiscal space to respond to shocks. Public debt is largely domestically financed, with domestic borrowing accounting for around 52% of total debt in 2024. High unemployment and elevated borrowing costs have also placed pressure on households and small businesses. However, banking sector indicators remain robust, with non-performing loans and the capital adequacy ratio remaining within statutory thresholds.

Domestic financial institutions remain heavily exposed to government debt. Any sharp repricing of South African Government bonds remains a primary trigger for systemic fragility. As foreign investor interest in domestic bonds remained muted due to higher risk aversion (roughly 25% in 2025), local banks and financial institutions increased their share of government debt holdings.

While regulators maintain high standards, risks, alongside the heavy bank exposure to government debt, vulnerability to global shocks, and weak economic growth hinder stability. Proposed solutions involve fortifying regulatory policy, accelerating structural reforms, and improving compliance. Improved coordination between fiscal policy and financial stability authorities (SARB) to balance growth and stability. While exposure to government debt is high, the financial sector is considered well-capitalized, with high non-systemic bank holdings of government debt (compared to emerging market peers) mitigated by the overall resilience of the largest banks.

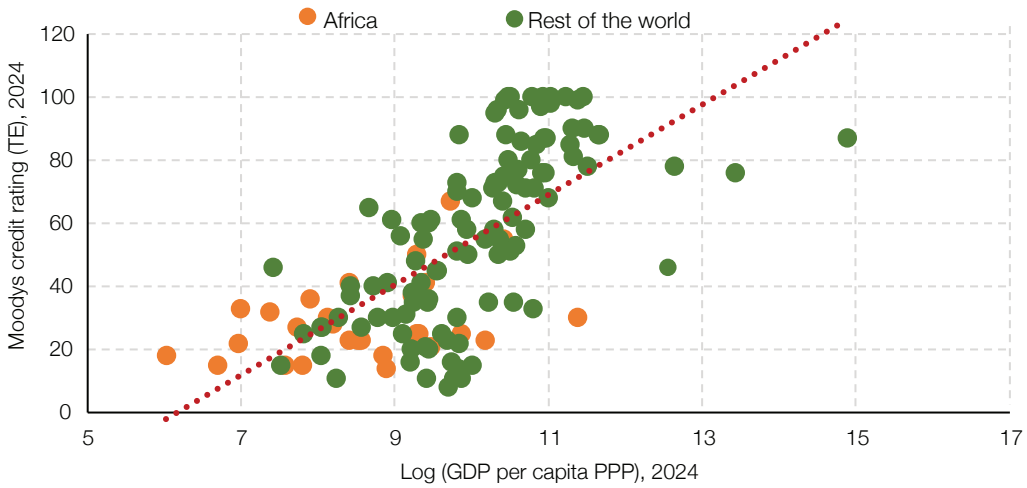
3.4 Towards financial agency and sovereignty

3.4.1 Imperatives of South Africa's financial Agency

South Africa is bolstering its financial system to mobilize domestic institutional capital, including pension funds, insurers, and banks, while enhancing regional financial integration under SADC and the AfCFTA framework. Reforms focus on modernizing exchange controls, integrating regional payment systems, and strengthening regulatory oversight. The National Treasury is reviewing exchange control regulations to better manage digital and cross-border financial flows, including crypto assets, while higher transaction limits for international payments aim to support digital trade and investment. South Africa's removal from the FATF grey list in October 2025 improved investor confidence and is expected to support lower borrowing costs and increased capital inflows. Additional anti-money laundering and counter-terrorism financing reforms are also being introduced to boost financial system integrity.

Cross country evidence reveals higher GDP per capita could improve credit risk rating outcomes (Figure 27). Major agencies like S&P, Fitch, and Moody's use GDP per capita of around $6,300 as a fundamental consideration to assess economic strength. Persistent stagnation in per capita income has often prevented sovereign upgrades out of speculative/junk territory. Overall, progress with reform implementation as is the case with South Africa's successes with the ongoing energy, transport, and logistics reforms, and fiscal discipline can improve credit ratings. In May 2026, Moody's Ratings changed South Africa's outlook to positive from stable and affirmed the government's domestic and foreign-currency long-term issuer and senior unsecured ratings at Ba2.

Figure 27: GDP Per Capita is Highly Correlated with Credit Risk Ratings



Source: Staff calculations using data from World Bank International Debt Statistics

3.4.2 Institutional Structures for a Resurgent and Impactful Financial Sector

A resurgent and impactful financial sector in South Africa is anchored by the "Twin Peaks" regulatory model, which clearly separates market conduct from prudential oversight to ensure both stability and fairness. Key institutional structures and reforms driving this impact include the Prudential Authority housed within the SARB, which ensures the safety and soundness of financial institutions, including banks and insurers. By March 2026, it also assumed prudential supervision of retirement funds and collective investment

schemes. The Financial Sector Conduct Authority (FSCA) is an independent entity that monitors market conduct to ensure customers are treated fairly. Its Regulatory Strategy 2025–2028 focuses on proactive enforcement and leveraging supervisory technology for real-time oversight. The National Financial Ombud launched on 1 March 2024, as a single "umbrella" body, amalgamated four previous schemes (Banking, Credit, and Insurance) to provide a simpler, more accessible dispute resolution service for consumers.

Box 3: National examples of successful or current reforms for strengthening financial architecture and governance

South Africa strengthened its financial architecture by setting up a National Financial Ombud Scheme (March 2024) to streamline consumer protection, and implementing the Twin Peaks model via the Conduct of Financial Institutions (COFI) Bill. Key reforms include digitizing municipal financial management and enhancing Prudential Authority supervision for financial stability.

The "Twin Peaks" Regulatory Model established by the FSR Act of 2017, separates oversight into two specialized pillars to ensure both stability and fair treatment. A major governance success was South Africa's exit from the FATF Grey list on 24 October 2025. This was a reform action where government implemented 22 specific action items, including strengthening anti-money laundering (AML) and the combating financing of terrorism (CFT) frameworks. Following the FATF exit, South Africa was also removed from the European Union's "High-Risk Third Country" list in early 2026. The Public Audit Amendment Act grants the Auditor General of South Africa stronger powers to enforce consequence management for financial mismanagement in municipalities and state departments.

Modernisation and Future Architecture: Payments Ecosystem Modernisation: The SARB is implementing a three-year programme to transform the national payment system, introducing an activity-based regulatory model by late 2026 to allow non-bank fintechs to offer services like e-money. Conduct of Financial Institutions (COFI) Bill: A pending "Phase 2" reform will create a single, holistic legal framework for market conduct, replacing multiple fragmented laws. Subnational Fiscal Architecture: The 2026 Budget introduced structural interventions at the municipal level, shifting from mere oversight to active governance and technology-driven accountability.

Source: SARB and National Treasury.

3.5 Conclusion and Policy Recommendations

Tackling South Africa's financial system challenges entails a sequenced reform agenda focused on strengthening macroeconomic stability, improving financial intermediation, modernizing infrastructure, and enhancing institutional credibility. While South Africa maintains one of the most sophisticated financial systems in Africa, structural constraints, including weak logistics networks, electricity shortages, low investment, and high sovereign debt exposure continue to limit the financial sector's ability to support inclusive and sustained growth.

3.5.1 Short-term policy actions

- **Restore fiscal credibility and stabilize debt dynamics** by maintaining primary budget surpluses through improved expenditure efficiency, stricter control of non-priority spending, enhanced tax compliance, and reduced leakages in public procurement and SOEs. This should be supported by strengthened coordination between National Treasury and SOEs to limit contingent liabilities and reduce fiscal risks.
- **Anchor inflation expectations around the new 3%** target through clear forward guidance by the SARB, enhanced monetary policy communication, and maintaining policy credibility to reduce inflation persistence and lower long-term borrowing costs.

- **Strengthen financial integrity and regulatory credibility** ahead of the 2026/27 FATF mutual evaluation by fully implementing outstanding anti-money laundering and counter-terrorism financing reforms, improving beneficial ownership transparency, and strengthening enforcement capacity within supervisory institutions and law enforcement agencies.

- I**mprove the regulatory environment for fintech and digital finance by publishing a joint SARB–FSCA policy paper** clarifying the treatment of artificial intelligence, digital assets, cybersecurity, consumer protection, and data governance in financial services. This would reduce regulatory uncertainty facing fintech firms and digital payment providers.

- **Accelerate infrastructure project preparation and execution** by expanding the role of the DBSA and Infrastructure South Africa in preparing bankable infrastructure projects, standardizing PPP frameworks, and fast-tracking approvals for strategic energy, water, and transport investments.

3.5.2 Medium to long-term policy actions

- **Place public debt on a sustainable downward trajectory** through sustained fiscal consolidation, improved economic growth, stronger expenditure controls, and reforms that expand the revenue base while reducing reliance on debt-financed spending.

- **Introduce a credible fiscal anchor framework into legislation** requiring future administrations to maintain transparent medium-term fiscal plans, debt sustainability targets, and expenditure rules to strengthen fiscal credibility and investor confidence.

- **Modernize and deepen the financial sector regulatory** framework by implementing the Conduct of Financial Institutions (COFI) Bill, strengthening macroprudential oversight, and enhancing coordination between the SARB, Prudential Authority, FSCA, and National Treasury to improve financial stability and consumer protection.

- **Complete the Payments Ecosystem Modernisation (PEM) Programme and deepen financial inclusion** by allowing broader participation of fintechs and non-bank entities in the national payment system, expanding digital financial services, reducing transaction costs, and improving access to affordable finance for underserved households and MSMEs.

- **Strengthen domestic capital mobilization and long-term investment financing** by operationalizing Regulation 28 reforms, expanding blended finance instruments, and using DFIs and guarantee mechanisms to crowd in pension, insurance, and private sector capital toward infrastructure, climate finance, and industrial development projects.

- **Enhance climate and financial resilience** by integrating climate risk into financial sector supervision, developing a regulated domestic carbon market, scaling-up green and transition finance instruments, and strengthening transition planning to attract long-term sustainable investment.

- **Expand regional and continental financial integration and strengthen South Africa's financial agency** by aligning domestic payment systems and regulations with SADC and AfCFTA frameworks, deepening participation in PAPSS, reforming exchange control frameworks, and positioning South Africa's financial institutions and capital markets as a regional hub for mobilizing African infrastructure and development finance.

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