Parliamentary Budget Office

PARLIAMENT
OF THE REPUBLIC OF SOUTH AFRICA

Quarterly Economic Brief

March 2023
No. 36

The Parliamentary Budget Office (PBO) has been established in terms of the Money Bills Amendment Procedure and Related Matters Act (Act no. 9 of 2009). The PBO provides independent, objective and professional advice and analysis to Parliament on matters related to the budget and other money bills. The PBO supports the implementation of the Act by undertaking research and analysis for the finance and appropriations committees.
The PBO provides a quarterly analysis of economic developments for Members of Parliament following the release of quarterly economic data by Stats SA, the South African Reserve Bank and the National Treasury.

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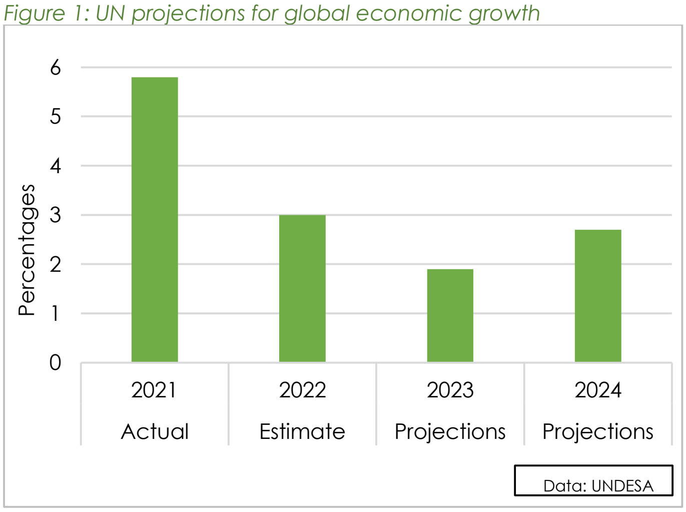
This report incorporates data available up to 9 March 2023 and was released on the 23 March 2023.

Introduction

This Quarterly Economic Bulletin (QEB), compiled by the Parliamentary Budget Office (PBO) provides an update on the performance of the South African economy for the fourth quarter of 2022. The QEB provides economic updates, particularly on macroeconomic performance, based on the most recent quarterly and monthly data releases from organisations such as Statistics South Africa (Stats SA), the South African Reserve Bank (SARB) and the United Nations Department of Economic and Social Affairs (UNDESA).

Global economic outlook

Figure 1: UN projections for global economic growth



The United Nations Department of Economic and Social Affairs (UNDESA) estimates that global economic growth for 2022 was 3 per cent and they forecast global growth below 2 per cent in 2023 and below 3 per cent in 2024. The relatively large global growth rate in 2021 was due to a rebound from the Covid-19 pandemic, which induced a 3.3 per cent decline in 2020.

The largest impediment to global economic growth during 2022 was the war in Ukraine. The global impact of the war led to rising prices due to shortages in food and energy markets. This inflation came on top of the rise in prices caused by decreased production and disruption to global value chains due to the pandemic. The food and energy price increases impeded the post-pandemic recovery. Efforts within countries and by multilateral institutions have helped to ease the shortage of food and fuel, particularly in developed countries.

The lockdown due to the pandemic in China during 2022 also negatively affected global growth. The easing of lockdown creates the possibility that Chinese production and problems in global value chains may ease. However, there is much uncertainty about global growth in 2023 and 2024 because of the possibility that large increases in Covid-19 infections could reoccur there. There is also uncertainty with regard to how long the war in Ukraine will last and the damages caused in the region and globally. One concern is that the continuation of the war creates a possibility that shortages of food and energy could return over the next year or two and that inflation will rise again. There is also a possibility that drought, floods, fires and other global climate change related events will affect global food markets and contribute to the disruption in global value chains.

Global growth in 2022 was also constrained because many countries had ended fiscal support introduced to counter the impact of the pandemic and raised interest rates in an attempt to curb inflation. The outlook for 2023 and 2024 is negatively affected by the possibility that central bankers around the world will continue to increase interest rates in the hope that decreasing economic growth and increasing unemployment will slow down inflation. In early March 2023, Jerome Powell, Chairperson of the US Fed announced that the US Fed would increase interest rates over a longer period. The response in US bond markets to Powell's announcement was increased trade in bonds, which resulted in the yield on US Treasury Bonds increasing to over 5 per cent - the highest it has been since 2007. When bond yields rise the price of bonds fall. The reason for the rise in bond yields is because bond traders expect continued raising of interest rates to trigger a recession in the US economy.

The US Fed seemed to have failed to take into account the impact of their interest rate increases on the levels of risk in the US banking system. The rise in interest rates caused the poor investment choices by Silicon Valley Bank (SVB), the sixteenth largest bank in the US (based on assets on 31 Dec. 2022), to culminate in a run on the bank that forced it to close. It was the second largest bank failure in the history of the USA and the largest since the global financial crisis of 2008. The reason for the run on the bank was that almost 90 per cent of depositors in the bank had deposits larger than the US$250 000 limit covered by the Federal Deposit Insurance Agency.

SVB was seen as a safe bank until the rise in interest rates. It had a large increase in deposits during 2021 and chose to invest those deposits in long-term US treasury bonds. The increase in interest rates by the US Fed caused the market value of the assets of Silicon Valley Bank to fall below that of its deposits. Some depositors that were not covered by depositors' insurance aggressively rushed to get their money out of the bank. In order to pay these depositors, the bank had to sell its assets below their market value, which meant that there would not be enough assets to cover all depositors. The run on the bank occurred because other uninsured depositors feared they would not be able to get their money out of the bank.

On Friday, 10 March 2023, SVB was placed under the receivership of the Federal Deposit Insurance Corporation (FDIC). That same day depositors withdrew a large amount from Signature Bank, which caused the third largest bank failure in US history. The next day, Saturday 11 March, US regulators took over Signature Bank.

The failure of SVB and Signature has spooked uninsured depositors in the US and caused sell offs and share price declines of banks in the USA. Finance sector commentators say that a large number of US banks could be in a similar situation to SVB because of the rise in interest rates. Systemic risks within the US financial system and globally have increased. In order to avert further runs on banks and bank failures, the US government promised to cover all depositors in SVB. However, the situation in the US financial system remains uncertain.

Until, the failure of SVB, most financial commentators predicted that the US Fed would continue to increase interest rates over the next year. There is uncertainty over whether the US Fed will continue to raise interest rates. However, the impact of several previous interest rate increases in the US caused other countries to increase their interest rates as well, in part to limit the flight of capital to the higher interest rates on US financial assets. Poorer performance of the US economy combined with higher interest rates and the additional uncertainty caused by the bank failures and rise in systemic financial risks could lead to much poorer global growth rates in 2023 and 2024 than currently predicted.

There is heightened global concern about the interrelatedness and cumulative impact of several serious risks, including the cumulative impact of the pandemic, global climate change disasters, geopolitical risks, including the Ukraine war and the cost of living crisis. Further raising of interest rates and the possibility of bank failures and financial crises together with heightened risk of recessions in developed countries will add to the severity of the existing crises.

Developing countries, including South Africa, still have unemployment levels below the pre-Covid levels. They are still struggling to recover from the Covid-19 crisis and face an uphill road to recovery. In January 2023, the UN Secretary General advocated for developing country governments to embark on "bold, targeted and timely" fiscal expansion and support from developed countries to support their recovery and stimulus.

South African economic situation:

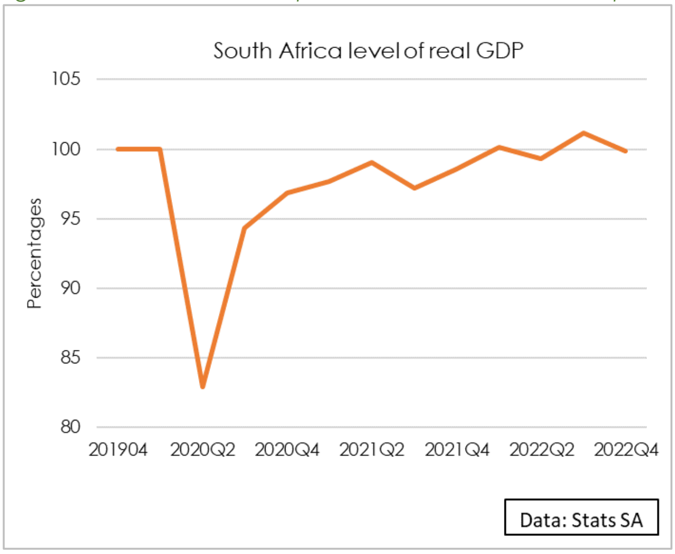
Gross domestic product[1]

South Africa's gross domestic product (GDP) decreased by 1.3 per cent on a quarter-on-quarter seasonally adjusted (qqsa) basis in the fourth quarter of 2022, following a 1.8 per cent expansion in the previous quarter. It was the sharpest contraction since the third quarter of 2021, mostly due to severe load shedding and logistical bottlenecks exacerbated by the Transnet strike in October 2022.

Economic growth for the 2022 calendar year was 2 per cent compared to the rebound growth of 4.9 per cent achieved in 2021. Following the GDP decline in the fourth quarter of 2022, the level of real GDP dipped back to below the pre-COVID level (fourth quarter of 2019). Put differently, the level of real GDP at the end of 2022 was lower than three years ago.

[1] All expenditure/growth data is seasonally adjusted and annualised unless otherwise stated

Figure 2: Real GDP fell below pre-COVID levels in the fourth quarter



Transport, construction and personal services sectors recorded positive growth, but the other seven of the ten industries of the South African economy contracted in the fourth quarter.

Table 1: Quarterly economic performance by sector

% change q/q	Agriculture	Mining	Manufacturing	Utilities*	Construction	Trade	Logistics**	Business services***	Government	Personal services	GDP
2022Q4	-3.3	-3.2	-0.9	-1.9	0.5	-2.1	0.7	-2.3	-0.7	0.2	**-1.3**
2022Q3	30.5	1.6	1.6	-2.7	3.9	1.0	3.6	1.6	0.3	-1.3	**1.8**
2022Q2	-12.8	-3.0	-5.5	-1.3	-2.9	-1.0	2.5	2.4	-1.6	0.1	**-0.8**
2022Q1	-1.8	-2.4	4.6	2.3	-0.5	3.0	1.6	1.9	1.1	0.5	**1.6**
2021Q4	16.4	-3.2	2.4	-3.1	2.6	3.9	2.9	-0.7	-0.3	2.5	**1.4**
2021Q3	-24.7	-1.1	-4.3	0.3	1.1	-4.4	-1.6	1.2	0.3	0.3	**1.8**
2021Q2	11.3	2.0	-1.8	0.6	-1.6	3.2	6.7	-0.5	0.5	2.7	**1.4**
2021Q1	6.1	4.1	0.4	-0.6	0.2	0.9	-2.8	0.9	0.2	1.0	**0.8**
2020Q4	7.1	-1.3	5.5	0.5	2.3	1.5	4.6	2.8	0.2	1.6	**2.7**
2020Q3	0.5	45.1	36.1	12.7	14.7	26.2	13.2	6.5	0.3	4.6	**13.8**
2020Q2	-3.8	-31.0	-31.5	-12.2	-27.4	-27.0	-22.8	-10.6	-0.3	-6.7	**-17.1**

Source:StatsSA
*Utilities includes electricity. gas and water
**Logistics includes transport .storage and communication
***Business services includes finance. real estate and business services

Value added by the primary sector decreased by 3.2 per cent in the fourth quarter of 2022, due to declines in the agricultural and mining sectors. According to Stats SA, reduced production of field crops and horticulture weighed on the agricultural sector's performance. While the decline in the value added by the mining sector was due to decreased output for diamonds, iron ore and platinum group metals. Value added by the secondary sector decreased by 0.8 per cent in the fourth quarter, largely dragged down by the manufacturing and utilities industries. In contrast, the construction sector contributed positively to GDP growth, due to increased activities in residential and non-residential buildings as well as construction works.

With the exception of the transport and personal services sectors, all tertiary sectors reported negative growth rates in value added during the fourth quarter of 2022. Value added in the sector contracted by 1.2 per cent qqsa, with the finance sector recording the largest contraction. According to Stats SA, the negative growth in the financial sector was driven by decreased activity in the banking sector, auxiliary services as well as in insurance and pension funding.

Expenditure on GDP

South Africa's expenditure on GDP decreased by 1.3 per cent in the fourth quarter of 2022 after a 1.7 per cent expansion in the previous quarter. The largest negative contribution to quarterly real GDP was due to a decline in exports. Imports increased in the fourth quarter, which meant that net trade made a negative contribution to GDP in the final quarter of 2022. The weak export performance was due to the more than 10-day strike by Transnet workers in October, which worsened logistical bottlenecks in the bulk export sector. Stats SA reported that in terms of export commodities, base metals, mineral products (coal) and paper performed the worst in the fourth quarter.

Table 2: Quarterly sector performance of expenditure components of GDP

% change q/q	Household consumption	Government consumption	Investment*	Exports	Imports	GDP
2022Q4	0.9	-0.7	1.3	-4.8	-0.8	**-1.3**
2022Q3	-0.3	0.6	0.3	3.8	0.1	**1.7**
2022Q2	0.4	-1.0	0.3	-0.1	5.4	**-0.8**
2022Q1	1.0	1.1	3.5	3.7	5.2	**1.7**
2021Q4	3.0	0.2	1.6	8.3	8.4	**1.5**
2021Q3	2.8	0.5	-1.1	-6.9	-3.4	**-1.8**
2021Q2	1.6	0.4	-0.3	3.0	0.2	**1.4**
2021Q1	0.5	-0.6	-3.1	1.7	6.7	**0.6**
2020Q4	3.1	0.7	5.3	6.1	10.9	**2.8**

Source:StatsSA
*Investment refers to gross fixed capital formation

In contrast, household consumption spending which makes up 67 per cent of GDP made the biggest positive GDP contribution (0.6 percentage points). However, the performance was not broad-based across the major consumer spending components. Spending on non-durable goods (mainly food and beverages) declined by 0.2 per cent qqsa. Whilst the largest boost to consumer spending in the fourth quarter came from the services sector (mainly restaurants and hotels). Despite this moderate quarterly rise in household spending, consumers remain financially distressed, struggling with higher cost of living and interest rates. Moreover, unemployment remains critically high, especially among the youth.

Employment

The official unemployment rate declined to 32.7 per cent in the fourth quarter of 2022 from 32.9 in the third quarter of 2022. According to Stats SA, a large number of persons moved from the "not economically active" to the "employed" category between the two quarters, which resulted in a decline of 0.2 percent in the employment rate. The number of employed persons increased by 169 000 to 15.9 million between the two quarters. Despite these increases, total employment remains stuck below its pre-COVID level.

The expanded unemployment rate (which includes individuals who desire employment regardless of whether they actively seek work) increased by 0.3 per cent to 39.4 per cent in the fourth quarter of 2022 compared to the third quarter.

Table 3: Key labour statistics – Quarterly Labour Force Survey (QLFS)

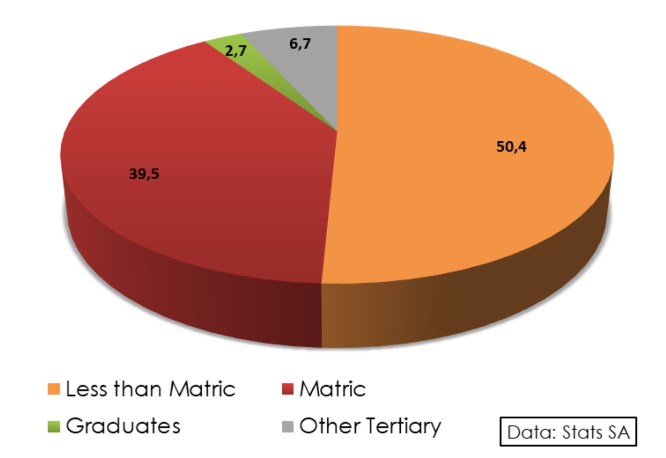
	4Q 2022	3Q 2022	4Q 2022
Labour force ('000s)	**22 466**	**23 491**	**23 688**
Employed	**14 544**	**15 765**	**15 936**
Unemployed - official	**7 921**	**7 725**	**7 753**
Unemployed - broad*	**12 492**	**11 931**	**11 849**
Not economically active ('000s)	**17 423**	**16 831**	**16 774**
Discouraged job-seekers	3 806	3 514	3 363
Other (not economically active)	13 617	13 317	13 412
Unemployment rates			
Official unemployment rate (narrow)	35,3%	32,9%	32,7%
Broad unemployment rate*	36,5%	39,1%	39,4%
Labour Force Participation Rate	56,3%	58,3%	58,5%
* The broad unemployment rate includes discouraged job seekers			
**Data Source: Quarterly Labour Force Survey, Stats SA			

At a provincial level, the largest employment increases were recorded in the Western Cape (167 000) and North West (23 000), while the biggest employment losses were recorded in Limpopo (20 000) and Gauteng (18 000).

Gender disparities persist in South Africa's labour market, with the proportion of men in employment higher than that of women and the unemployment rate among men lower than amongst women. According to the official definition of unemployment, the unemployment rate for women in the fourth quarter of 2022 was 46.6 per cent, compared to 39. 2 per cent for men.

The youth in South Africa continue to be disadvantaged in the labour market with an unemployment rate higher than the national average. According to the Quarterly Labour Force Survey (QLFS), South African youth aged 15-24 years and 25-34 years recorded the highest unemployment rates of 61 per cent and 39.9 percent respectively, while the current official national rate stands at 34.5 percent. In the fourth quarter of 2022, up to 50.4 percent of the 7.8 million unemployed had education levels below matric, followed by those with matric at 39.5 per cent.

Figure 3: Proportion of the unemployed by education level – fourth quarter of 2022 (%)



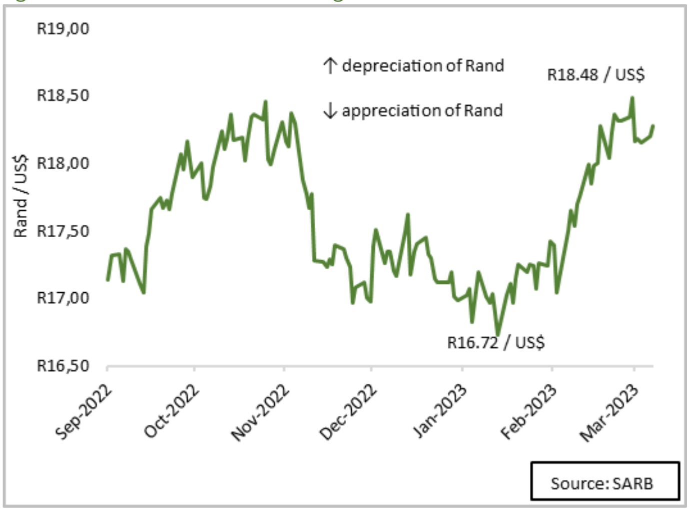
According to Stats SA, six of the eight industries surveyed in the formal sector (non-agriculture) reported a rise in employment. The rise in formal sector job gains was mainly driven by finance at 103 000 followed by trade and transport at 52 000 and 43 000 respectively. In contrast, community and social services shed 122 000 jobs over the same period.

Exchange rate

The South African rand depreciated by 10.2 per cent against the US dollar over the first two months of 2023 reaching R18.48 in February, its lowest since October 2022. The weakness in the rand largely reflected a general tightening of global financial conditions amid market speculation that the US Fed will continue to hike up interest rates in response to sustained higher inflation. Domestically, the recent grey listing of South Africa by the Financial Action Task Force (FATF), severe load shedding and a notable deterioration in the current account deficit also placed downward pressure on the rand.

The IMF projects a slowdown in global economic growth in 2023, driven by higher interest rates, environmental risks as well as the continuous war in Ukraine. A sharper-than-expected downturn in the global economy could result in assets perceived to be riskier, including emerging market currencies, coming under renewed pressure.

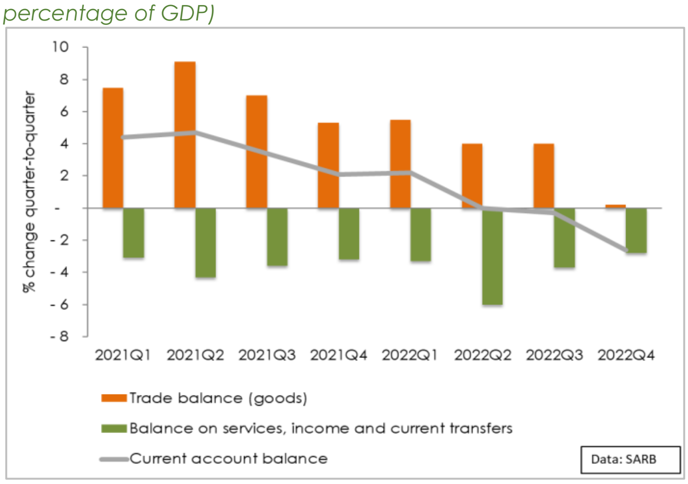
Figure 4: The rand-dollar exchange rate weakens in 2023



Current account

South Africa's current account remained at a deficit during the fourth quarter of 2022. The deficit on the current account narrowed to R174 billion (2.6% of GDP) in the fourth quarter from a revised surplus of R3.1 billion in the third quarter of 2022. This was the largest current account gap since the third quarter of 2019, driven mainly by the shortfall in the services income and current account transfers (financial outflows) which narrowed for a second consecutive quarter from R228 billion in the third quarter to R186 billion in the fourth quarter of 2022. Meanwhile, the goods surplus narrowed further to R12.2 billion in the fourth quarter from R249 billion in the previous quarter. The value of merchandise imports grew while that of exported goods declined.

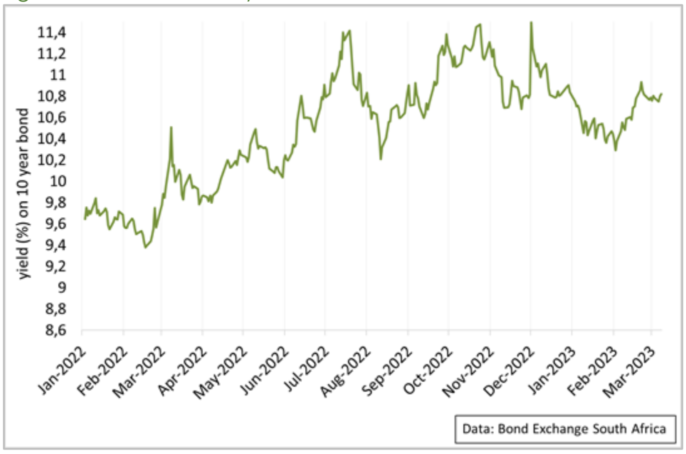
Figure 5: Change in the balance of the current account (as a percentage of GDP)



Sovereign risk and debt outlook

The yield on the country's 10-year bond increased throughout much of 2022 reflecting the impact of the war in Ukraine, which contributed to heightened global inflationary pressures that led to monetary policy tightening by most central banks in advanced economies. Higher interest rates in advanced economies often trigger capital outflows from emerging market economies such as South Africa. The increase in domestic bond yields during most of 2022 also reflected the depreciation in the exchange value of the rand and higher inflation.

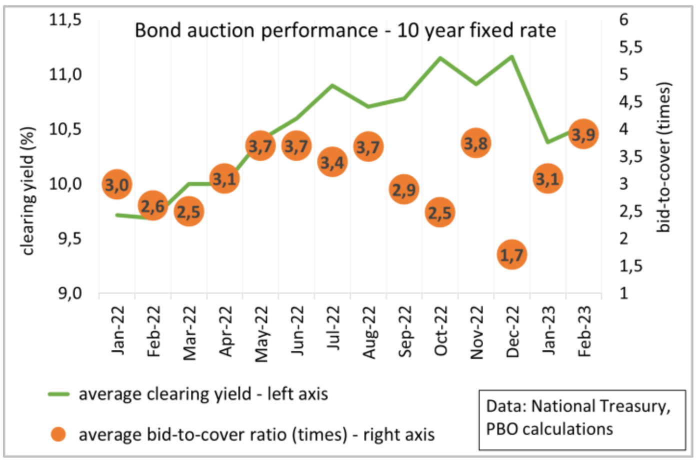
Figure 6: Yield on SA 10-year bond



Since the end of November 2022, South Africa's bond performance improved somewhat along with the appreciation in the exchange value of the rand over this period. In the first two months of 2023, the average clearing yields (the interest government has to pay to finance the budget deficit and refinance maturing debt) declined whilst the demand for domestic bonds increased at government's weekly bond auctions.

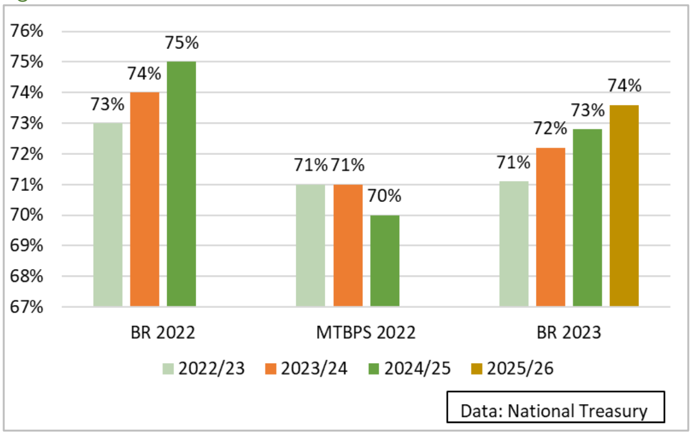
According to the SARB, primary dealers placed R16.8 billion worth of orders in February, more than four times the R3.9 billion of bonds that were on offer. That was the strongest demand since June 2021, and is comparable to an average bid-to-cover ratio of 3.8 times recorded at the end of November.

Figure 7: Increasing cost of issuing government debt



The 2023 Budget expects debt to stabilise at a higher level of 73.6 per cent of GDP in 2025/26 compared with the 71.4 per cent estimated in the 2022 MTBPS. The rise in debt is mainly due to the government's partial take-over of Eskom's debt stock. About a quarter of the total R254 billion assistance to Eskom will be financed through previous baseline budget provisions, with the rest having to be borrowed. As a result, the government's gross borrowing requirement will be substantially higher than previously expected, which would likely require a larger issuance of long-term government bonds. Interest payments are also set to increase from 15.3 per cent of overall main budget expenditure in 2022/23 to 17.5 per cent during 2025/26. However, even with the assistance to Eskom, the debt trajectory remains less onerous than outlined in the 2022 Budget.

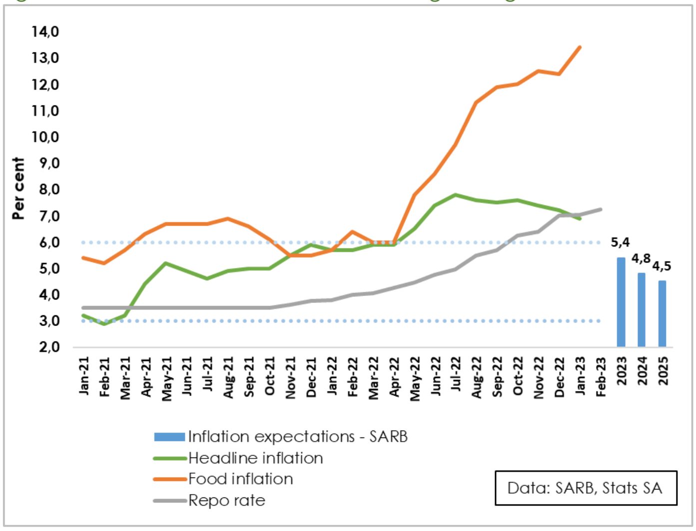
Figure 8: Gross loan debt as a share of GDP



Inflation and monetary policy

Headline consumer inflation (CPI) increased by a more-than-decade high of 6.9 per cent in 2022. The largest contributors to the acceleration of inflation were transport and food prices due to the ongoing geopolitical conflict between Russia and Ukraine, which resulted in supply chain disruptions and higher crude oil prices. Part of the inflationary pressures can also be attributed to companies potentially passing on load-shedding-related input cost pressures to consumers. After 350 basis points worth of policy interest rate increases since November 2021, the SARB's Monetary Policy Committee (MPC) decided to again increase the repurchase rate by 25 basis points to 7.25 per cent in their January 2023 meeting. Several economists predict that the SARB is approaching the end of its hiking cycle given that inflation is projected to moderate to below the Bank's preferred 4.5 per cent mark in the fourth quarter of 2023. However, the domestic and global risks to the medium term inflation outlook remain elevated.

Figure 9: Inflation breached the SARB's target range



Domestic fiscal and economic outlook

The government expects to achieve a primary fiscal surplus in the current fiscal year and over the MTEF as a result of higher-than-expected corporate and personal income tax collections as well as continued fiscal consolidation. However, the PBO argues that austerity hurts the real economy, erodes the state's capacity to deliver services and risks higher debt. Austerity is disastrous for developing a capable state that adequately addresses historical inequalities and meets the country's developmental objectives.

In terms of economic performance, the outlook for GDP growth over the medium term remains relatively poor. The National Treasury lowered its growth forecast for 2023 to 0.9 per cent, down from the 1.4 per cent forecast in the 2022 MTBPS. Several constraints have added additional downward pressure to the domestic GDP growth outlook. Intensified load shedding, continued fiscal consolidation, higher interest rates, bottlenecks at Transnet's ports as well as a weakening growth outlook in some of the country's major export markets will likely curb economic growth.

An important strategy to kick start growth in the face of these problems is to build household resilience through fiscal expansion to support social services and grants and improving and investing in services infrastructure. This spending on households will serve to boost aggregate demand in the economy.

Table 4: Revised SA growth outlook

GDP growth outlook - calender year*	2023	2024	2025
National Treasury - MTBPS 2022	1,4%	1,7%	1,8%
National Treasury - Budget 2023	0,9%	1,5%	1,8%
South African Reserve Bank - November 2022	1,1%	1,4%	1,5%
South African Reserve Bank - January 2023	0,3%	0,7%	1,0%
IMF - World Economic Outlook - October 2022	1,5%	1,8%	-
IMF - World Economic Outlook - January 2023	1,1%	1,3%	1,4%
*Growth projections correspond to publication date and not forecast date			
Data: National Treasury, South African Reserve Bank, International Monetary Fund			

Box 1: South Africa's Greylisting by the Financial Action Task Force (FATF)

On 24 February 2023, South Africa was greylisted by the Financial Action Task Force (FATF) - a global money laundering and terrorist financing watchdog. The FATF is an intergovernmental organisation that was established in 1989 as a G7 initiative to develop a global money laundering strategy. The FATF identifies jurisdictions with weak measures to combat money laundering and terrorist financing (AML/CFT). South Africa is one of 23 countries that are currently on the greylist. Being on the greylist means that South Africa is "under increased monitoring" as it actively works with the FATF to address its strategic deficiencies in its regime. In 2019, South Africa underwent an assessment of the effectiveness of its measures to combat money laundering and terrorist financing. The International Monetary Fund (IMF) provided the country with recommendations. The report was adopted in 2021. By 2023 it had become clear that South Africa had not implemented the measures outlined and thus the decision to put South Africa on the greylist was not a surprise.

What does the rating mean for the country?

The extent to which the greylisting will impact South Africa is unknown. The mainstream analysis suggests that the greylisting will have significant and negative implications for the country. The SARB and National Treasury anticipated that the greylisting will lead to reputational damage, lead to capital outflows, as well as impact cross-border transactions with possible "action taken by foreign banks that provide correspondent banking services".

A 2021 IMF paper estimates that, on average, countries experienced capital outflows of 7.6 per cent of GDP after greylisting. For a country like South Africa, this would have potentially serious outcomes given the already stagnant growth and low levels of investment. Large negative impacts on economic growth in the medium to long term would exacerbate the high unemployment, poverty and inequality. However, the FAFT decision to greylist South Africa was anticipated by the markets, which means that markets may have already adjusted risk assessments of South Africa prior to the rating. If this is the case, immediate impacts to the economy will be subdued. Going forward it will also be important that South Africa's macroeconomic performance is not wholly attributed to the greylisting. As noted in the brief, South Africa faces a myriad of historic and current issues which threaten the economy and households.

Criticisms of FAFT

There have been widespread criticisms of the FAFT. In February 2021, the FATF published a report called Mitigating the Unintended Consequences of the FATF Standards which sought to assess the unintended consequences of the Standards' misapplication. The project focuses on four undesirable effects:

- De risking, or the loss or limitation of access to financial services. The practice has notably affected nonprofit organisations (NPOs) and correspondent banking relationships;
- Financial exclusion, a phenomenon whereby individuals are denied access to basic financial services;
- Suppression of NPOs or the NPO sector (through failure to properly apply a risk based approach);
- Threats to fundamental human rights stemming from the misuse of the Standards or anti money laundering and counter-terrorist financing (AML/CFT) assessment processes to support laws that may violate rights such as due process or the right to a fair trial.

The FATF concluded that states should respect human rights and undertake a risk-based assessment. Some critics have raised issues with how the watchdog could be used to undermine democracy. In 2021, a Reuters investigation found that the FATF recommendations had been misused by some governments to launch crackdowns against rights activists and opponents. These are all concerns that must be taken seriously by the government when measures are being implemented. In addition, there is also a substantial body of work that criticizes the way that international organisations have developed into important indirect sources of power in global politics and how these organisations aim to alter the world through comparative measures. The political economy of international agency influence on domestic policy must also be reckoned with.

An opportunity for reform

The calls for financial sector reform are not new in South Africa. For years, organisations such as the Alternative Information and Development Centre, and others, have called for the government to prioritise the tackling of illicit financial flows (IFFs). It should not have taken an external international agency to tackle these issues. This raises questions about the extent to which public input is taken seriously by government. Since the risk of greylisting, Parliament passed two laws to FAFT recommendations. The SARB has indicated that it plans to monitor its financial jurisdiction with a more risk-based approach. The government has actively engaged in measures to curb money laundering and other illicit transactions.

Despite these efforts, Minister Enoch Godongwana has acknowledged that South Africa was greylisted because of a failure to adequately investigate and prosecute money laundering and terrorist financing. As the President noted, "the greylisting is an opportunity for us to tighten our controls and improve our response to organised crime". The PBO welcomes a renewed will to tackle these issues. Greylisting is also an opportunity for South Africa to increase its regulation of the financial sector, more broadly.