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Global Aging 2010: South Africa

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- South Africa's population is expected to grow to 57 million by 2050, with the proportion of elderly people increasing to 10.1% from 4.6% today.
- Age-related spending is projected to increase to 8% of GDP in 2050 from 4.5% at present, while net general government debt would increase to 93% of GDP in our base-case scenario.
- Alternative scenarios -– incorporating a balanced budget assumption for 2016 and the assumption of no additional age-related spending -– led to significantly lower net general government debt levels.

Standard & Poor's Ratings Services' analysis of South Africa is part of a global study conducted to analyze the cost of aging. We presented our findings in "Global Aging 2010: An Irreversible Truth", published Oct. 7, 2010, on RatingsDirect. The underlying data projections are from the U.N., the Organization for Economic Cooperation and Development and the International Monetary Fund. Our study explores various scenarios--including a no-policy-change scenario--and the implications that we currently believe these scenarios could have on sovereign ratings over the next 40 years. We included an additional 17 sovereigns in this year's report, which expanded the scope of the study's coverage to more than two-thirds of the world's population. For the 32 sovereigns that we included in the first edition of our global aging special report in 2006, our findings this year provide an update of our analyses--including information on long-term demographic, macroeconomic, and budgetary trends, all in the context of the countries' current fiscal positions. We have published the methodology of our study, which details the simulation model, assumptions, and data sources used (see "Global Aging 2010: An Irreversible Truth--Methodological And Data Supplement", published Oct. 7, 2010).

Results For South Africa

The data suggests that in South Africa, the old-age dependency ratio will rise to 15% in 2050 from 7% in 2010 (see table). (The old-age dependency ratio is the number of people aged 65 and older divided by the number of those aged 15-64.) Overall, it is expected that the population will increase over the entire projection period, to about 57 million in 2050. The proportion of the working age population is projected to grow to 68% by 2050 from the current 65%.

In our view, an aging population can place pressure on economic growth and public finances. Demand for publicly provided health care and long-term care services and state pensions could increase. Without further government reforms (which is our base-case scenario), total age-related public expenditures in South Africa are projected to rise to 8% of GDP in 2050 from 4.5% today. This increase of 3.5% of GDP is less than the expected 7.8-percentage-point increase for the median of our 49-sovereign sample. The bulk of South Africa's age-related spending is health care related, followed by pension spending outlays. In our view, however, the increase in age-related spending in South Africa will be moderate throughout the projection period.

The projected moderate increase of age-related spending suggests a modest fiscal impact over the medium term. Nevertheless, if unmanaged, the weight of government spending could rise to close to 36% of GDP by 2050, from an estimated 33.5% at present. Our analysis suggests that without fiscal or structural policy reforms, age-related spending could contribute to a rise in South Africa's net debt to 93% of GDP by 2050; this would still be significantly lower, however, than the sample median at 245% of GDP.

Our Base-Case Scenario's Expected Impact On The Ratings

On the basis of the fiscal projections of our study, we derived hypothetical sovereign credit ratings for South Africa. In practice, Standard & Poor's takes a large number of factors into consideration when determining sovereign credit ratings (see "Sovereign Credit Ratings: A Primer", published May 29, 2008). In the very long term, however, prolonged fiscal imbalances and wealth (as measured by GDP per capita) tend to become the dominant factors. The simulated macroeconomic and fiscal dynamics imply that South Africa's long-term foreign currency rating would remain in the 'BBB' category, although the level of economic prosperity -- measured by GDP per capita -- would come increasingly into line with those on sovereigns currently rated in the 'A' category. In our view, however, the projected improvement in GDP per capita would be unable to fully offset the potential structural fiscal deterioration.

Alternative Scenarios Could Result In Different Economic And Fiscal Prospects

In addition to our base-case, we have considered several other long-term scenarios. One of these scenarios envisages significant structural reforms. In this scenario, the government would freeze all age-related spending (as a percentage of GDP) at current levels and balance the budget by 2016. Other scenarios assume higher economic growth, persistently lower real interest rates, or creditors demanding risk spreads as a function of South Africa's government debt ratio.

Fiscal consolidation could help reduce the government's debt burden considerably

Factors that could affect a country's sustainability gap are useful in our analysis to better understand the fiscal burden. The sustainability gap is the difference between the current structural primary balance and the one that guarantees the sustainability of public finances. In our base-case scenario, the sustainability gap is 3.4% of GDP for South Africa, which is below the median for the sample. Under our simulation, this sustainability gap is entirely driven by age-related spending. Nevertheless, as our upside scenario--a balanced budget in 2016--indicates, fiscal consolidation could significantly contribute to a reduction of South Africa's future debt burden.

The Effects Of Age-Related Spending On Sovereigns' Future Creditworthiness

The base-case scenario is not a prediction. Rather, it is a simulation that highlights the importance of age-related spending trends as a factor in the evolution of sovereign creditworthiness. In our view, it is unlikely that governments would, as a general matter, allow debt and deficit burdens to spiral out of control or that creditors would be willing to subscribe to such high levels of debt. Historically, once governments are confronted with unsustainably rising debt burdens, they usually react by tightening their fiscal stances or reforming their expenditure programs.

South Africa (Republic of) -- Aging Population Data And Scenario Outputs

	2010	2015	2020	2025	2030	2035	2040	2045	2050
Demographic and economic assumptions									
Population (mil.)	50.5	51.7	52.7	53.8	54.8	55.5	56	56.5	56.8
Working-age population (% of total)	65.1	65.1	65.2	65.4	65.9	66.5	67.1	67.6	67.6
Elderly population (aged over 65; % of total)	4.6	5.2	6.5	7.2	7.9	8	8.7	8.8	10.1
Old-age dependency ratio (%)	7	8	10	11	12	12	13	13	15

South Africa (Republic of) -- Aging Population Data And Scenario Outputs (cont.)									
Real GDP (% change)	2.3	3.1	4	3.8	3.6	3.5	3.3	3.3	3.1
Age-related government expenditure (% of GDP)									
Pensions	1.3	1.4	1.6	1.8	1.9	2	2.1	2.2	2.3
Health care	3.2	3.5	3.7	4	4.3	4.7	5	5.4	5.7
Long-term care	0	0	0	0	0	0	0	0	0
Unemployment benefits	0	0	0	0	0	0	0	0	0
Total	4.5	4.9	5.3	5.8	6.2	6.7	7.1	7.6	8
.									
Scenario 1: Base-case (% of GDP)									
Net general government debt	28	37	38	41	47	55	65	78	93
General government balance	(6.2)	(3.2)	(2.5)	(3.1)	(3.8)	(4.6)	(5.5)	(6.5)	(7.7)
General government expenditure	33.5	31.2	30.5	31.1	31.8	32.6	33.5	34.5	35.7
Interest payments	3	3.4	2	2.1	2.3	2.6	3.1	3.6	4.3
Hypothetical long-term sovereign rating	BBB	BBB	BBB	A	A	BBB	BBB	A	A
Sustainability indicators									
Initial budgetary position	0								
Long-term change in budgetary position	3.5								
Sustainability gap	3.4								
.									
Scenario 2: Balanced budget in 2016 (% of GDP)									
Net general government debt	28	37	23	12	3	(3.0)	(7.0)	(8.0)	(8.0)
General government balance	(6.2)	(1.0)	1	1	0.9	0.7	0.4	0	(0.5)
Hypothetical long-term sovereign rating	BBB	BBB	A	A	A	A	A	AA	AA
Sustainability indicators									
Initial budgetary position	(2.8)								
Long-term change in budgetary position	3.1								
Sustainability gap	0.3								
.									
Scenario 3: No additional age-related spending (% of GDP)									
Net general government debt	28	36	36	35	34	33	33	32	32
General government balance	(6.2)	(3.0)	(1.8)	(1.7)	(1.7)	(1.6)	(1.6)	(1.6)	(1.6)
Hypothetical long-term sovereign rating	BBB	BBB	A	A	A	A	A	AA	AA
.									
Scenario 4: Lower interest rate (% of GDP)									
Net general government debt	28	34	32	34	38	44	53	63	75
General government balance	(6.2)	(3.1)	(2.1)	(2.6)	(3.2)	(3.8)	(4.6)	(5.4)	(6.3)
Hypothetical long-term sovereign rating	BBB	BBB	BBB	A	A	A	BBB	A	A
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Scenario 5: Discriminating investors (% of GDP)									
Net general government debt	28	34	33	37	42	50	60	73	89
General government balance	(6.2)	(3.2)	(2.4)	(3.0)	(3.7)	(4.5)	(5.5)	(6.6)	(8.0)
Hypothetical long-term sovereign rating	BBB	BBB	BBB	A	A	BBB	BBB	A	A

South Africa (Republic of) -- Aging Population Data And Scenario Outputs (cont.)									
Scenario 6: Higher growth (% GDP)									
Net general government debt	28	36	36	38	41	47	56	66	77
General government balance	(6.2)	(3.2)	(2.4)	(2.9)	(3.5)	(4.2)	(5.0)	(5.9)	(6.9)
Hypothetical long-term sovereign rating	BBB	BBB	BBB	A	A	A	A	A	A

Related Criteria And Research

Global Aging 2010: An Irreversible Truth, Oct. 7, 2010

Global Aging 2010: An Irreversible Truth--Methodological And Data Supplement, Oct. 7, 2010

South Africa (Republic of), Jan. 19, 2010

Criteria For Determining Transfer And Convertibility Assessments, May 18, 2009

Sovereign Credit Ratings: A Primer, May 29, 2008

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