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The mini budget, the South African Reserve Bank (SARB) and the public protector: a mystery solved.

We are a mysterious lot. Ours is a country of conspiracies and subversive forces and unanswered questions. Oh, and rumours, we are strong on rumours. There are many rumours and questions.

For example, why did our ignoramus of a public protector recently propose to change the mandate of the SARB? Where is the smiling suit (the honourable minister of finance) going to get the money to pay SAA or fill the huge tax hole in the budget? How does state capture fit in with all of this?

Let's see if we can unpack some of these questions.

Here are some facts:

- Our newish minister of finance will deliver his first (and hopefully last) mini budget tomorrow.
- This is not really a budget but more of a report-back on how the economy and state finances performed the past six months and how the minister sees things pan out over the remainder of the year.
- This is also not typically the forum to announce changes to taxes or significant changes to spending plans, but it is possible.
- What we know, is that state revenue is running well behind budget and that the budgeted shortfall can be as much as R 60 billion (our view is for a shortfall of approximately R 45 billion).
- We also know that there is tremendous pressure on the spending side of the budget. For example, we know that the minister must somehow allocate the money already spent on feeding SAA and the other paracitals. The R 5 billion already spend this year on SAA may have been illegally paid.
- We know that the public protector recently made some, let's just say weird, suggestions on what the mandate of the SARB should be.
- We know that in future the presidency will be responsible for the budgetary process.
- Could there be a link between these developments? I think so!

First, some background. During 2004-2006, the South African (SA) economy was cooking. State revenue was exceeding the budgeted estimates and the then minister of finance, Trevor Manuel, had a nice problem — he had too much money, for one of the major beneficiaries of a growing economy is the state because economic growth equals more taxes.

The problem is, however, that once the other ministers discover that tax collections exceed estimates, they will discover all sorts of reasons why this money must be spent. At the same time, the SARB also had a nice problem. SA was a darling investment destination and massive amounts of money were flowing into the country. This is good but capital inflows equal more liquidity and too much liquidity will eventually unleash too much inflation.

So, finance had too much money which was too much of a temptation for politicians, while the SARB had to deal with too much liquidity in the market. The answer was easy, Treasury would simply transfer these "extra" tax receipts from the state's bank accounts to the SARB and announce that this money would be used to acquire Forex reserves. In the process, market liquidity would be reduced while Manuel would "get rid" of his extra cash.

Fortunately, Treasury and the SARB entered into an agreement that these monies will in future not be available for normal state spending. This amount currently stands at approximately R 70 billion. It is reported as part of state deposits, which it is, but the fact that it is not available for normal spending is not normally mentioned.

That is not all. There is an additional, approximately R 100 billion in Forex that belongs to the state which is held by the SARB. This is typically Forex receipts by the state, for example, Forex loans, and can also only be used for Forex spending. For instance, the state will borrow US$ which will form part of the SARB's official reserves and the state can only use these dollars to repay foreign loans or other Forex expenses. Point is, this money is not available for normal rand expenses, although it is also reported as part of state deposits.

There is even more. The SARB is the custodian of the country's reserves. These reserves consist mostly of gold and other Forex reserves. The "owner" of these reserves is the country and the "state" (which I suppose is represented by the minister of finance) represents the "country".

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Whenever the rand weakens, the rand value of gold (and other Forex) increases but when the rand strengthens, the rand value falls.

In recent years, the rand mostly fell in value with the result that the official reserves held by the SARB increased in rand value. To revalue the assets in their custody, the SARB periodically readjust the value of these assets (mostly gold and Forex). The total accumulated revaluation currently stands at a cool R 240 billion! But remember, this is all just book profits and still unrealised!

Let's summarise: the SARB holds R 70 billion worth of Treasury deposits that was initially used to drain excess liquidity and which is not (re agreement) available for state spending. The SARB also holds approximately R 100 billion in Forex that belongs to Treasury but which is also (re agreement) only available for spending on Forex and not for rand spending. Lastly, the SARB has accumulated an amount of R 240 billion in unrealised Forex profits which, technically, also belongs to "the state".

That means that roughly R 410 billion is potentially available for state spending if the SARB can somehow be "captured".

Now, just imagine if the public protector was successful in her attack on the SARB. The SARB's mandate would have changed to some "public interest" mandate, instead of an inflation mandate. Obviously, the current governors at the SARB would have been a hindrance and would have had to be replaced by a more agreeable team. The agreements between SARB and Treasury would have been renegotiated and Gigaba would have had instant access to at least R 170 billion, or maybe even the full R 410 billion, to spend on SAA and the other parasites!

The result would have been a massive increase in liquidity which the SARB, assuming they were still interested in protecting the value of the rand, would have had to drain by issuing SARB debentures at a high cost — eventually for the account of the taxpayer. Or if the SARB decided not to drain liquidity, massive inflation would have been the consequence.

Maybe this theory makes sense. Capturing the SARB would have things much easier for Gigaba and the rest of the Zuma patronage. SAA et al would have been funded quite easily. The price would have been a bankrupt SARB or massive inflation, which can always be blamed on hoarders, capitalists and other unsavoury characters.

Or maybe this is the reason why Zuma took over the budgetary process. This will allow him to determine the priorities of the budget, like a nuclear deal, perhaps without following the normal parliamentary processes. But still, the money must come from somewhere…

Perhaps this explains the attack on the SARB and the link with the budget. Fortunately, it was unsuccessful and Gigaba still needs to somehow explain how he is going to square this circle. Unless he somehow succeeds in convincing the SARB to relax the conditions of Treasury's deposits at the SARB, I only see one realistic option available to Gigaba to plug the gap — by simply borrowing even more. Which will result in a further downgrade…

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