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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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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 third 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) and the South African Reserve Bank (SARB).

Global economic outlook

The International Monetary Fund's (IMF's) October World Economic Outlook forecasts global economic growth at 3.2 per cent for 2022. While their forecast for global growth for 2022 is unchanged from their July 2022 forecast, they have revised their forecast for global economic growth in 2023. Their July 2022 forecast was 2.9 per cent and the revised October 2022 forecast is 2.7 per cent. The level of uncertainty in global economic outlook is evident in the IMF's October 2022 warning that there is a 25 per cent probability that global economic growth could drop to below 2 per cent in 2023.

The United Nations Conference on Trade and Development, in its October 2022 Trade and Development Report, issued an even firmer warning that tighter monetary and fiscal policy choices in advanced economies increase the risk of a global recession and prolonged stagnation. They warn that these actions may inflict worse damage than the financial crisis in 2008 and the COVID-19 shock in 2020.

Figure 1 Annual real GDP growth for South Africa, Advanced economies, Emerging Market Economies and the World

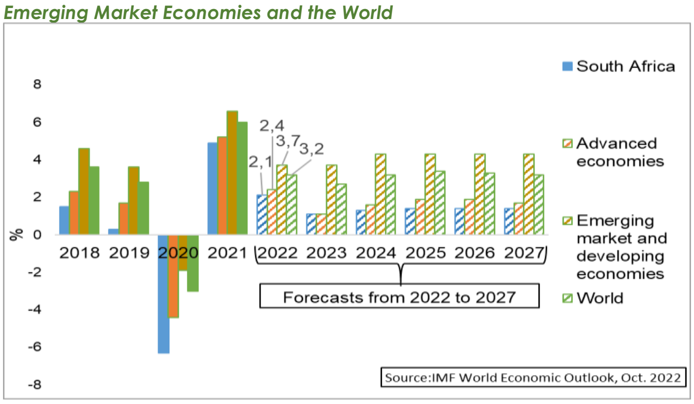


Figure 1 plots the actual levels of economic growth and the IMF's October 2022 forecasts from 2022 to 2027. It shows global recovery to pre-Covid-19 levels. It is worth remembering that global economic growth levels had begun to decline before the pandemic and that the forecasted recovery is muted and extremely uncertain. It is also notable that South Africa's economic growth forecasts are much below that of the world average over the period and even below that of the advanced economies. South Africa's expected performance below these global benchmarks points to problems beyond electricity supply and will require future economic plans to transcend structural reforms. It requires state driven social policies to directly address unemployment, poverty and inequality in conjunction with policies to transform the structure of the South African economy.

There is a difference of opinion in international agencies about the use of and effectiveness of increasing interest rates to attempt to control inflation. The International Monetary Fund is in support of countries raising interest rates to tame inflation while the United Nations agencies are against it. There is a strong argument against increasing interest rates because the current inflation is not caused by macroeconomic policy, including more monetary liquidity and fiscal policy. The increase in global inflationary pressures was largely due to enduring supply chain disruptions due to the Covid-19 pandemic that affected production around the world.

The use of monetary policy, which is to increase interest rates to deal with inflation is an extremely blunt instrument that, as the UN warns, will very likely constrain economic activity and growth. The problem with raising interest rates is that it hurts household consumption and production, employment and investment. It often causes increased unemployment. When the cause of inflation is not due to excess demand but global supply disruptions then increasing interest rates causes unnecessary socio-economic harm in economies that have already suffered due to the ongoing impact of the 2008 global financial crisis and the ongoing Covid-19 economic disruptions. Further, a number of governments increased debt to respond to the negative health and economic impacts of the pandemic. Raising interest rates now when there are higher public debt service costs and higher risks of debt default across Africa and the developing world seems likely to worsen economic instability.

Over the past few years, the PBO has warned about many interconnected serious global and domestic risks. The term 'polycrisis' has now entered into the global discourse, including recent articles in the influential Financial Times newspaper. There is interrelatedness between non-economic crises such as geopolitical conflicts, political instability within countries, climate change related factors and economic factors, including increased debt, financial fragility, growing inequality, and inflation due to supply chain disruptions.

The current inflation is clearly due to increased fuel and food prices related to the Russian war in Ukraine. The geopolitical conflicts have exacerbated the supply chain disruptions that emerged during the Covid-19 pandemic. The problem is that further geopolitical conflicts, including tensions over Taiwan, may lead to longer-term problems in global supply chains. There seems to be a conscious choice to shift oil and gas sourcing by European countries and the Biden Administration is rallying European allies to shift production away from reliance on Chinese produced products. There may be restructuring of global supply chains and even possibly the reversal of global chains and the regionalisation of some value chains.

South African economic situation:

Gross domestic product[1]

South Africa's gross domestic product (GDP) increased by 1.6 per cent on a quarter-on-quarter seasonally adjusted (qqsa) basis in the third quarter of 2022, following a 0.7 per cent contraction in the previous quarter. Base effects were partly responsible for the quarterly rise in the GDP growth rate, following a poor second quarter performance which was caused by the severe flooding in Kwa-Zulu Natal. The floods disrupted operations at the key export port in Durban. In nominal terms, GDP grew by 7 per cent year-on-year during the first three quarters of 2022, outpacing National Treasury's expectation in the October medium-term budget policy statement (MTBPS) of 6.1 per cent for the entire 2022. The better-than-expected figure bodes well for the near-term government revenue outlook.

Table 1 Quarterly economic performance by sector

% change q/q	Agriculture	Mining	Manufacturing	Utilities*	Construction	Trade	Logistics**	Business services***	Government	Personal services	GDP
2022Q3	19.2	2.1	1.5	-2.1	3.1	1.3	3.7	1.9	0.3	-1.2	1.6
2022Q2	-11.1	-3.5	-5.7	-1.2	-2.0	-1.0	2.4	2.5	-1.5	0.1	-0.7
2022Q1	-2.4	-2.1	5	2.0	-0.8	3.1	1.8	1.8	1.4	0.8	1.7
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 eight of the ten industry sector categories made a positive contribution to GDP in the third quarter of 2022. Relatively strong growth in value added was recorded for the agriculture sector, which made the biggest contribution to growth. Whereas, value added by the utilities and personal services sectors declined during the quarter.

Value added by the primary sector increased by 8.2 per cent in the third quarter of 2022, mainly due to a 19.2 per cent rise in agricultural production. The expansion in agricultural output was driven by bumper crops, particularly of field crops and horticultural products. The mining sector also contributed positively to GDP growth.

The secondary sector performance was slightly better in the third quarter. Value added in the sector rose by 1.2 per cent qqsa, following a 4.8 per cent decline in the previous quarter. Improved production in the manufacturing and construction sectors made up for the decline in the utilities industry. Following five consecutive quarters of decline, the construction sector registered a 3.1 per cent qqsa growth rate, mainly attributable to increased activities in residential and non-residential buildings as well as construction works.

With the exception of the personal services sector, all tertiary sectors reported positive growth rates in value added during the third quarter of 2022. The transport sector recorded the highest growth rate in value added of all the tertiary sectors (3.7%), mainly attributable to increased activity in land transport, transport support services and communication services.

Expenditure on GDP

South Africa's expenditure on GDP increased by 1.6 per cent in the third quarter of 2022, following a 0.7 per cent contraction in the previous quarter. Exports pushed expenditure on GDP higher in the third quarter. The quarterly rise in exports was mainly due to mineral product exports, likely reflecting higher coal exports despite rail and port infrastructure challenges.

Table 2 Quarterly sector performance of expenditure components of GDP

% change q/q	Household consumption	Government Consumption	Invesment*	Exports	Imports	Exp on GDP
2022Q3	0.3	0.5	0.3	4.2	0.6	1.6
2022Q2	0.6	-0.7	0.5	0.3	5.6	0.7
2022Q1	1.4	1.0	3.6	3.9	4.9	1.9
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
2020Q3	17.8	0.3	14.1	28.5	-0.6	14.0
2020Q2	-20.5	-0.5	-22.1	-29.9	-18.2	-17.0

Source:Stats SA
*Investment refers to gross fixed capital formation

In contrast, household consumption expenditure, which makes up 67 per cent of GDP, fell by 0.3 per cent. This decline was driven by weaker spending on non-durable goods, the category most impacted by high food and fuel prices.

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

Gross fixed capital formation increased by a marginal 0.3 per cent in the third quarter, following a 0.5 per cent rise recorded in the previous quarter. After three consecutive quarters of growth, private sector capital expenditure declined on a quarterly basis. The impact of this decline on overall fixed investment was mitigated by increases in public corporations' and general government capital expenditure.

Employment

The official unemployment rate declined to 32.9 per cent in the third quarter from 33.9 per cent in the second quarter of 2022. According to Stats SA, a large number of people moved from the "unemployed" to the "employed" and "not economically active" categories between the two quarters, which resulted in a decline of 1.0 per cent in the unemployment rate. While the number of unemployed people declined by 269 000 to 7.7 million between the two quarters, employment increased by 204 000 in the third quarter of 2022.

The expanded unemployment rate (which includes individuals who desire employment regardless of whether they are actively seeking work) decreased by 1.0 per cent in the third quarter compared to the second quarter of 2022.

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

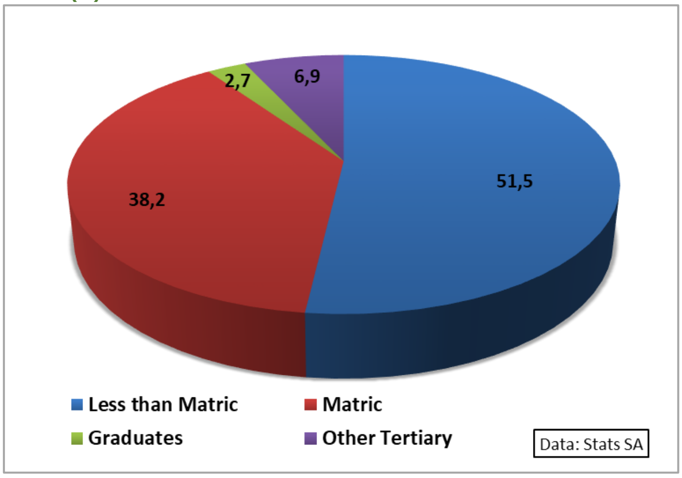
	3Q 2021	2Q 2022	3Q 2022
Labour force ('000s)	**21 925**	**23 556**	**23 491**
Employed	**14 285**	**15 562**	**15 765**
Unemployed - official	**7 643**	**7 994**	**7 725**
Unemployed - broad*	**12 484**	**12 282**	**11 931**
Not economically active ('000s)	**17 820**	**16 621**	**16 831**
Discouraged job-seekers	3 862	3 568	3 514
Other (not economically active)	13 958	13 053	13 317
Unemployment rates			
Official unemployment rate (narrow)	34,9%	33,9%	32,9%
Broad unemployment rate*	46,1%	44.1%	43,1%

* The broad unemployment rate includes discouraged job seekers
**Data Source: Quarterly Labour Force Survey, Stats SA

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. In the third quarter of 2022, the unemployment rate for women was 35.1 per cent, compared to 32.4 percent for males, according to the official definition of unemployment.

The youth in South Africa also continue to be disadvantaged in the labour market with an unemployment rate higher than the national average. The Quarterly Labour Force Survey (QLFS) indicates that South African youth aged 15 to 24 and 25 to 34 had the highest rates of unemployment, at 59.6 and 40.6 per cent, respectively, whereas the current official national rate stands at 34.5 per cent. Up to 51.5 per cent of the 7.7 million unemployed people in the third quarter of 2022 had education levels below matric, followed by those with matric at 38.2 per cent.

Figure 2 Proportion of the unemployed by education level – second quarter of 2022 (%)

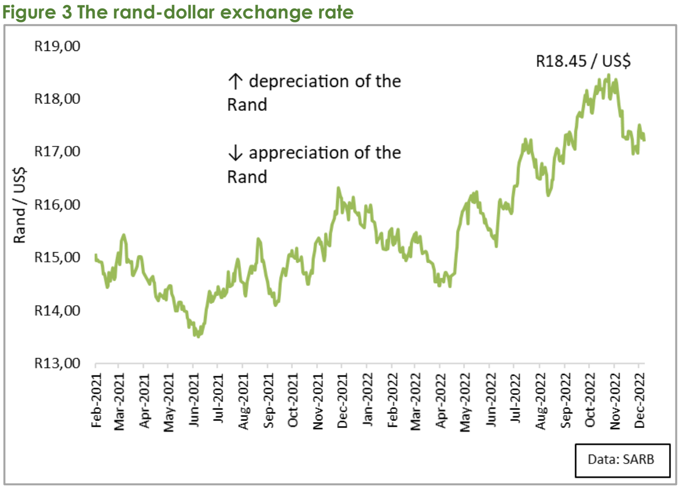


Stats SA indicated that six of the eight industries surveyed within the formal sector (non-agriculture) reported a rise in employment. The manufacturing sector recorded the largest number of job gains over the quarter at 123 000, followed by the trade and construction sectors at 80 000 and 46 000 respectively.

Exchange rate

The South African rand and other emerging markets currencies experienced significant volatility in 2022. Year-to-date, the rand has weakened by 8 per cent against the US dollar reaching R17.50 to a US dollar at the beginning of December 2022. The weakness in the rand largely reflected a strengthened US dollar. The US dollar strengthened against global currencies when the US Federal Reserve Bank rapidly hiked policy rates in response to increasing inflation. The rand's volatility also reflected uncertainty regarding global economic growth prospects in response to China's reimplementation of strict COVID-19 lockdown measures and the ongoing war in Ukraine. Domestically, severe bouts of electricity load-shedding as well as heightened political uncertainty following the release of the Section 89 independent panel report negatively impacted on the rand's performance at the beginning of December 2022.

Figure 3 The rand-dollar exchange rate

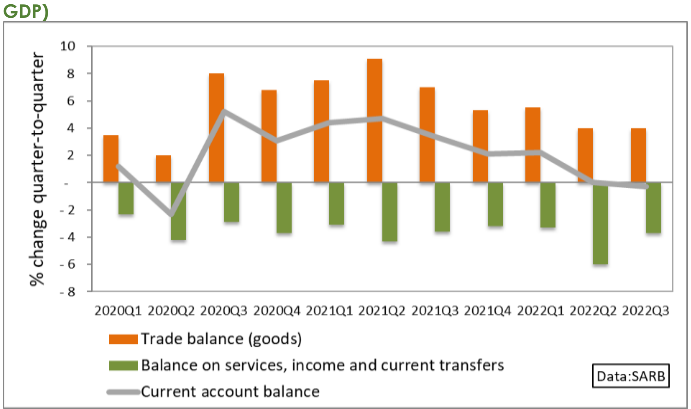


Current account

The current account remained in deficit during the third quarter of 2022. Despite the larger exports of goods than imports, a deficit on the current account remained due to financial outflows. Compared to the previous quarter, the deficit on the current account of the balance of payments narrowed to R18.1 billion (0.3% of GDP) in the third quarter of 2022, from R107 billion (1.6% of GDP) in the second quarter. While the deficit on the services account grew, the third quarter deficit was lower due to noticeably smaller deficits on the primary income account and the secondary income account.

The shortfall on the services, income and current transfer account (financial outflows on the current account) narrowed noticeably to R251 billion (-3.7%) in the third quarter of 2022, from an all-time high of R358 billion (-5.4%) in the second quarter. South Africa's trade surplus, which remained positive, declined between the two quarters to R233 billion from R252 billion. The value of merchandise imports increased more than that of goods exported.

Figure 4 Change in the balance of the current account (as a percentage of GDP)



Sovereign risk and debt outlook

The yield on South Africa's 10-year benchmark bond has trended upwards (worsened) throughout much of 2022. The yield on this bond is often treated as an indicator of market sentiment with regard to the riskiness of South African government bonds but domestic bond yields were largely impacted by global events over this period, notably rising global inflationary pressures caused by the Russia-Ukraine war as well as the subsequent tightening of monetary policy by most advanced-economy central banks. This upward trend in bond yields occurred across many emerging market economies. Higher interest rates in major economies often trigger capital outflows from emerging market economies such as South Africa.

South Africa's bond performance since the beginning of 2022 indicates the negative impact of rising interest rates in the USA and other developed economies that cause capital outflows to those financial markets. Whilst bond auctions have remained fairly well subscribed, average clearing yields (the interest government has to pay to finance the budget deficit and refinance maturing debt) remained high, which indicates higher debt service costs for a given level of issuance.

Figure 5 Yield on SA 10-year bond

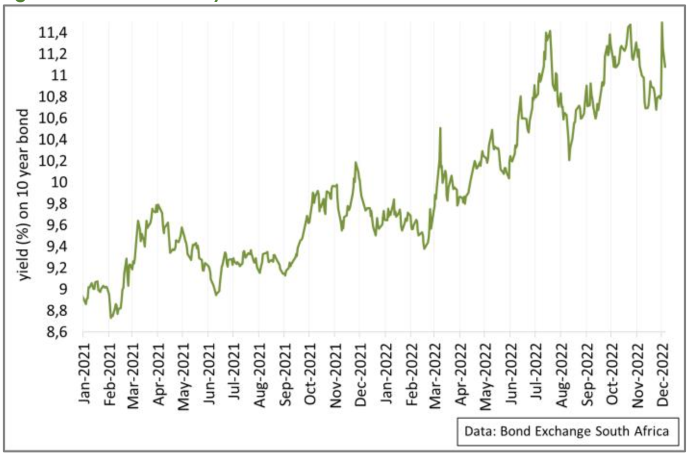
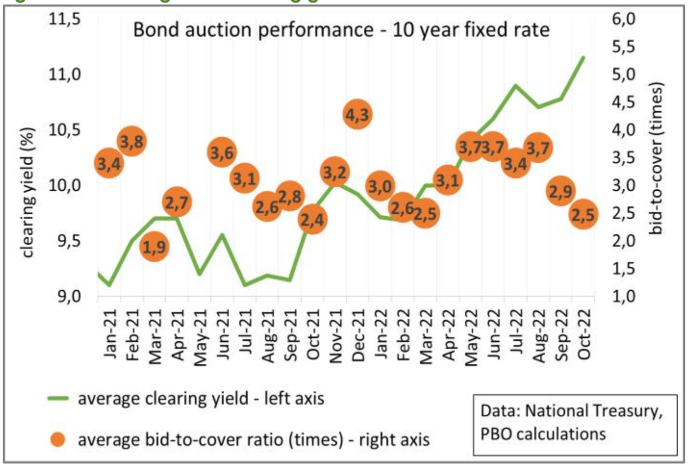
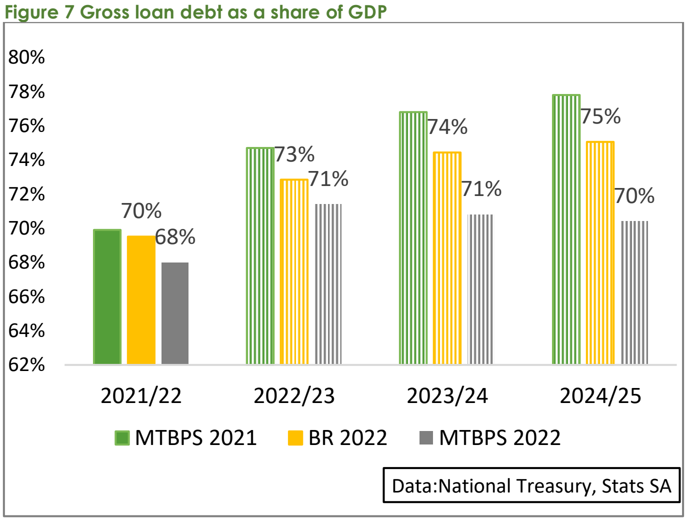


Figure 6 Increasing cost of issuing government debt



While the 2022 MTBPS expects debt to decline over the medium term, several risks remain elevated. Gross loan debt as a share of GDP is expected to remain at 71 per cent in 2022/23, and over the MTEF. This level is expected mainly due to better revenue projections that increase the primary balance and higher nominal GDP due to higher inflation. However, elevated long-term government bond yields, a weaker commodity price trajectory and poor GDP growth pose significant risks to debt reduction. Moreover, debt service costs continue to consume a significant share of government expenditure.

Figure 7 Gross loan debt as a share of GDP



Box 1: The extension of the Social Relief of Distress (SRD) grant

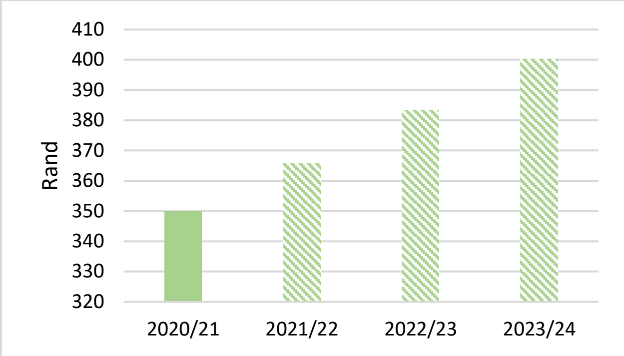
The extension of the covid-19 SRD grant (also known as the R350 grant) has provided a lifeline to many people in South Africa. Failure to address high, structural unemployment combined with inadequate social provision has caused the persistence of unemployment, poverty and inequality (UPI). The result has been long-term, cumulative negative impacts on households, communities and society. The majority of South Africans live in poverty and the grant has partially addressed the long-standing gap in social protection for the 18-59-year-old group. The extension of the SRD to March 2024 will temporarily extend this vital assistance to many individuals and households.

The Government allocated R44 billion to the Department of Social Development (DSD) in the 2022 Budget to support 10.5 million vulnerable people until the end of March 2023. Although the allocation, at that stage, was viewed as insufficient due to higher projected uptake. In an effort to remain within the budget allocation, the DSD proceeded to introduce new, tighter qualifying criteria with the intention of reducing the number of eligible applicants for the grant. One critical manipulation of the criteria was the introduction of a means test at the low level of income below R350 per month. This change caused a significantly lower uptake of the grant. Only 4.8 million people were approved for the grant in April 2022. On 16 August 2022, the DSD published amended regulations for the covid-19 SRD grant. Notably, the means test threshold was increased from R350 to R624 (the level of the Food Poverty Line). In August 2022, there were 13.5 million applications and 7.5 million people received the grant. This change that increased the number of approved grants means that the number of grantees is still substantially below the 10.9 million people that the DSD identified as potential beneficiaries of the programme. One disappointing consequence of these events is that, the DSD declared unspent funds and projected underspending of R1.8 billion in the 2022 MTBPS. A further R3.7 billion was shifted away from the DSD.

Grants have made a significant impact on poverty and hunger in South Africa. A study by Bhorat and Kohler (2021) on the fiscal incidence of the COVID-19 SRD grant suggests that the grant reduced poverty by 5.3 per cent amongst the poorest households, and household income inequality by 1.3 to 6.3 per cent depending on the measure in 2020. While the SRD grant has not been at the level of the food poverty line (R663), it has made an impactful contribution to household consumption and alleviated some suffering.

Due to the effect of inflation one would have expected an inflation coupled increase to at least R383.31 for 2022/23. Figure 8 below shows the inflation adjusted values of the SRD grant 2024.

Figure 8 Inflation-adjusted SRD grant value (2020-2024)



Source: PBO estimates based on National Treasury data

Inflation and monetary policy

South Africans are experiencing a heightened cost of living crisis. High Inflation continues to erode the spending power of poor and middle-income households. Headline consumer price inflation (CPI) was 7.6 per cent in October 2022. This level is 0.2 per cent lower than the 13-year high of 7.8 per cent recorded in July 2022. The largest contributors to the acceleration of inflation were transport and food prices. Transport costs increased by 17.1 per cent year-on-year. Food prices increased by 12 per cent year-on-year, the largest increase since January 2009. The largest contributors to the high food price increase were oil and fats (25.7%) and bread and cereals (19.5%).

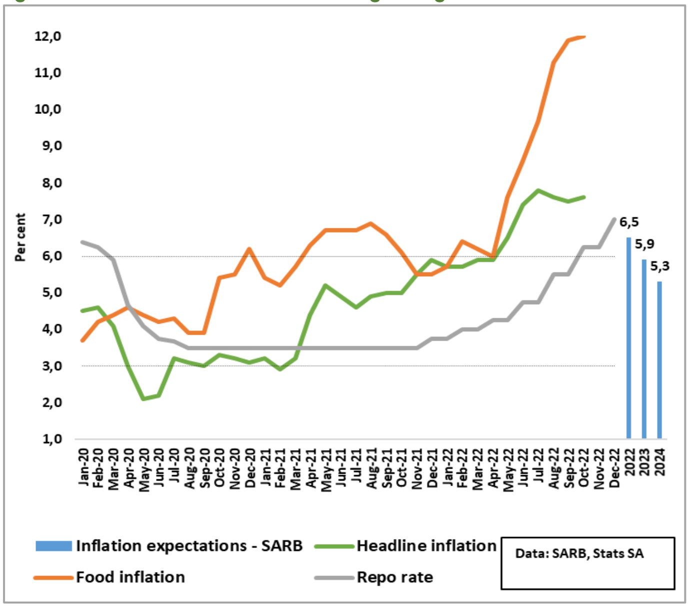
Increasing inflation is particularly devastating to lower-income households who spend the majority of their income on necessities. The average cost of the Household Food Basket, in the Household Affordability Index published by the Pietermaritzburg Economic Justice & Dignity Group (PMBEJD) is R4 835.96. The cost of the average household food basket has increased by R563.52 (13.2%) from November 2021 to November 2022.

Inflationary pressures continue to be fuelled by the ongoing geopolitical conflicts between Russia and Ukraine, which have resulted in supply chain disruptions and higher crude oil prices. Inflationary pressures are not only being driven by supply-side shocks. Part of the inflation can be attributed to profit-push which is when companies increase prices higher than their increasing costs.

In response to the relatively high inflation and rapid interest rate hikes by advanced economy central banks, the SARB's Monetary Policy Committee (MPC) decided to increase the repurchase rate by another 75 basis points to 7.0 per cent at their November 2022 meeting.

For households, with lower incomes, who have access to credit, higher interest rates are further reducing their household disposable incomes. The impacts of higher interest rates are also disproportionately felt by SMMEs.

Figure 9 Inflation breached the SARB's target range



Domestic economic outlook

The 2022 MTBPS presented an improved fiscal outlook relative to the 2022 Budget Review. As a result of higher-than-expected corporate income tax collections and continued fiscal consolidation, the government expects to achieve a primary budget surplus in 2023/24 for the first time in 15 years.

In terms of economic performance, the outlook for GDP growth over the medium term is relatively poor. The National Treasury lowered its growth forecast for 2022 to 1.9 per cent, down from the 2.1 per cent forecast in the Budget Review in February. There is little support for economic development in the 2022 MTBPS with aggregate demand and investment likely to remain low. Load-shedding, higher interest rates and efforts to achieve a primary budget surplus will likely hurt small businesses and the poorest households.

Table 4 Revised SA growth outlook

GDP growth outlook - calender year*	2022	2023	2024
National Treasury - Budget 2022	2,1%	1,6%	1,7%
National Treasury - MTBPS 2022	1,9% ↓	1,4% ↓	1,7%
South African Reserve Bank - January 2022	1,7%	1,8%	2,0%
South African Reserve Bank - September 2022	1,9% ↑	1,4% ↓	1,7% ↓
IMF - World Economic Outlook - January 2022	1,9%	1,4%	-
IMF - World Economic Outlook - October 2022	2,1% ↑	1,1% ↓	
Reuters Consensus Forecast - January 2022	2,0%	1,8%	2,0%
Reuters Consensus Forecast - September 2022	1,9% ↓	1,5% ↓	1,8% ↓
*Growth projections correspond to publication date and not forecast date			
Data: National Treasury, South African Reserve Bank, International Monetary Fund			

Box 2: Restructuring of global supply chains and its impact on developing countries

Increased globalisation and the increased integration of large, low wage countries such as China and India into the global economy over the past few decades have led to intensified globalisation of supply chains. Many countries moved production and sourcing of intermediate inputs offshore to these lower cost countries. As a result, many countries, including South Africa, have become more dependent on imports of capital, intermediate and final products and services from abroad. The negative side of these developments became evident even before the global financial crisis of 2008 when global imbalances caused by unbalanced global trade and financial flows became a serious concern. Countries, such as the USA, had become net importers with large trade deficits while China, Japan and Germany had developed massive trade surpluses. These trade imbalances required massive net financial flows from the trade surplus countries to the trade deficit countries. As a result, China, Germany, Japan and many other countries became massive purchasers of US financial assets, including US Treasury Bonds but also private debt. The result of this global imbalance was a world with increased financial systemic risks and exacerbated contagion risks across the globe. It also meant more speculative, short-term financial flows to emerging economies, including South Africa, that increased their vulnerability to financial crises and contagion.

The other serious consequence of the ongoing global economic imbalance has come sharply and painfully to light since the impact of the Covid-19 pandemic. The development of global supply chains has increased the risk to companies operating and sourcing intermediate and final products in the supply chains. An important problem is that global markets have become very concentrated with a few lead corporations dominating most of the global markets. The dominance of global lead corporations in global supply chains and global product markets has increased. However, it is not only dominance by lead corporations but also the cascading of increased market dominance by firms within value chains as well. For example, there have been major supply disruptions in the automobile, white goods and other manufacturing sectors where large global original equipment manufacturers of cars, major appliances and many other products that include electronics, have been forced to reduce supply of cars, dishwashers and many other products because of disruptions to production caused by shortages of microchips. The production of microchips, which is an important link in a number of global value chains, is an extremely concentrated global sector. There are similar levels of concentration in other key sectors that provide inputs to global value chains, including in chemicals, steel, food and beverages, fertilisers, and others.

After years of offshoring and sourcing inputs from abroad, there are concerted efforts in developed countries to respond to these risks in supply chains by producing more in their domestic economies and diversifying the sources of inputs they require for their businesses. There also seems to be realignment of value chains that seem more closely aligned to geopolitical conflicts and alliances. The developing countries now face the prospect of ongoing inflation due not only to ongoing supply chain disruptions but also due to efforts by developed economies to reorient global supply chains due to geopolitical concerns. At the same time, the increase in interest rates (in developed countries and developing countries) puts further pressure on developing countries that are still limping after Covid-19, particularly those that have increased public debt. In face of these problems, and the other 'polycrisis' concerns, building economic and financial resilience of households in domestic economies and the pursuit of industrial policy and strengthening regional economic alliances and value chains has become increasingly urgent.