Parliamentary Budget Office

PARLIAMENT OF THE REPUBLIC OF SOUTH AFRICA

Quarterly Economic Brief

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Boxes

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 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 Parliamentary Budget Office's (PBO) Quarterly Economic Bulletin (QEB) provides an update of the performance of the South African economy for the last quarter of 2019. The QEBs provide economic updates, particularly with regard to macroeconomic performance, based on the most recent quarterly and monthly data releases from organisations such as Statistics South Africa (StatsSA) and the South African Reserve Bank (SARB). Due to the Covid-19 pandemic and its hugely disruptive impact on the global economy and South African society the economic situation in April 2020 is totally different to January 2020.

This QEB will begin with a discussion of the outlook for the global and South African economy in the context of the Covid-19 pandemic. As we write this QEB, while in lock down, one thing we know is that no-one knows how severe the human and socio-economic impact of the pandemic will be. We are faced with huge uncertainties where the outcomes will be shaped by individuals and their actions to lower the infection curve, the actions of individual governments and collective action in the international community. The greater the effort and resources we invest in mitigating the impact on South African society now, particularly helping the poorest communities, the higher the socio-economic returns for our society as a whole.

Economic outlook and turmoil in financial markets

Most of the recent macroeconomic forecasts for South Africa attempting to take account of the impact of Covid-19 correctly come with warnings that they are tentative and generally have very large margins of error. Therefore, this QEB will not be reporting these early predictions. The focus is on interventions influencing the outcomes rather than reporting the forecasts at this stage of the pandemic.

The forecasts of international financial institutions and national organisations since the global financial crisis of 2008 have proven to be consistently inaccurate and all too often required updating within months of publication. One difficulty for the forecasts has been high levels of uncertainty in the global economy. Another problem is that most of these forecasts have generally depended on similar macroeconomic models based on mainstream economic thinking. The many weaknesses of mainstream economics and the inability of its practitioners to have predicted the 2008 global financial crisis is well known. Mainstream macroeconomics has undergone change, including mainstream economists' rediscovery that fiscal policy is effective and should be used by governments.

Mainstream macroeconomic forecasts have also suffered because they still do not adequately include the financial sector, the extent of the influence of finance and the impact of global integration of financial markets on domestic and national economies into their models. This problem with mainstream economics is particularly pertinent at present because there have been huge disruptions in domestic and international financial markets as a result of the responses to Covid-19.

The Institute of International Finance reported that emerging markets had record levels of portfolio outflows, i.e. outflows from equity and bond markets, of US$83.3 billion during March 2020. The IMF reported that capital outflows from South Africa during March 2020 were enormous amounting to approximately 2 per cent of GDP (US$5.9 billion). In other words, there has been enormous levels of capital flight from developing countries, including South Africa, that negatively affect the value of their financial assets. This withdrawal of capital also affects the real sectors because financial markets have become less liquid and more volatile. The outflows place pressure on developing countries' balance of payments and could force them to limit imports as they have less foreign exchange available. It also caused large rapid depreciation of currencies of developing countries, including the rand, as the outflows reduce available foreign exchange.

It is important to understand that the capital flows into and out of developing countries do not necessarily always reflect the state of health of those economies. But they do give a strong sense of the appetites and sentiments of financial corporations with access to capital searching for places to improve their short-term financial returns. When financial corporations panic they search for safety in developed country financial assets and withdraw capital from developing countries.

Developed countries have used monetary policy, such as quantitative easing, to substantially increase liquidity in their financial markets since the global financial crisis of 2008. For example, the United States Federal Reserve substantially increased the size of its balance sheet from well below US$1 trillion in 2006 to close to US$4.5 trillion in 2012 and injected more than US$2 trillion into financial markets since the global financial crisis of 2008. Much of this growth in availability of credit was used for increased activity in financial markets, including much speculation, and inadequately utilised to increase investment and productive capacity. For example, much debt has been used to fund share buybacks to increase share prices rather than increase investment over the past few years.

Some of the capital raised went into short-term financial flows to developing countries. In most cases, surges of short-term foreign financial inflows have led to stock market booms and overvalued exchange rates.

The coronavirus pandemic has set off high levels of anxiety and panic-driven activity in global financial markets. As a result, there is great uncertainty in financial markets. We cannot rule out scenarios where widespread pre-existing weaknesses in financial markets before Covid-19 could escalate into further crashes in stock markets, large loan defaults causing collapses in corporate debt and real estate markets, and the possibility of bank failures.

South Africa does not have adequate regulatory or other measures as precautions to manage volatile cross-border capital flows. As a result, we have already been negatively affected by massive capital outflows and could be affected by contagion from problems in financial markets elsewhere. The recent downgrade by the credit ratings agency Moody's of South Africa's domestically denominated sovereign debt while much anticipated has proven to be a sideshow during this time of remarkable turbulence in financial markets and the global economy.

Covid-19, South Africa and the global economy

The PBO's 2020 pre-Budget presentation to the joint Committees on Finance and Appropriations in the National Council of Provinces and the National Assembly on 25 February 2020 stated that there are several risks to the South African economy in an integrated global economy. The threats listed were:

- Global debt accumulation and growing risks of financial instability and crises;
- Increasing climate change events, e.g. flooding, droughts and fires;
- Global Epidemics, such as Covid-19;
- Poor performance of key economies – China, India, Europe etc.;
- High & rising levels of unemployment, inequality & instability;
- War and conflict events increasing.

It was pointed out that these risks are interrelated. Within a very short time of the spread of Covid-19 the interrelatedness of these risks became clear. The downturn in global economic activity has put key economies that were already performing poorly under even more pressure. This pressure has led to difficulties and panic in financial markets that has increased financial instability and the possibility of financial crises. The high and rising levels of unemployment and inequality have been made worse by the pandemic but also exacerbate the impact of the pandemic on society. Many commentators on the environment and the effects of global warming convincingly warn that Covid-19 is a preview of the troubles facing the globe as global warming increases.

At the time of the PBO's pre-Budget presentation, the name Covid-19 had just been given to the sickness caused by the novel coronavirus SARS-Cov-2. The World Health Organisation declared Covid-19 a pandemic only by 11 March 2020. Currently, we witness the widespread global growth of Covid-19. In response, many countries around the world, including South Africa, have implemented increased screening, testing, lock-downs and other responses to curb the spread of the infections. There is a determined approach to limit the spread of the pandemic and to "flatten the curve" at home and globally.

Covid-19 has caused a public health crisis. Unfortunately, this public health crisis occurs in the context of South Africa's already daunting and considerable socio-economic problems. Covid-19 in an environment with these extraordinary levels of inequality, mass unemployment, inadequate housing and shelter, poor access to sanitation and water services and not to mention the parlous state of much of the healthcare system will add to the pre-existing levels of suffering and early deaths of too many South Africans. This public health crisis has the potential to become a human rights crisis, particularly because the socio-economic rights of too many people who live in South Africa have remained unfulfilled.

Unfortunately, socio-economic rights are too often treated as separate from human rights. However, the pandemic once again painfully illustrates the warnings of the United Nations that socio-economic rights are equally important, indivisible and interrelated to civil and political rights, such as the right to life, freedom of speech, movement and assembly. We are conscious about the costs to the state as we respond to this crisis but we have to remember two things as we contemplate the costs:

•Government is responding to a public health crisis and a potential human rights crisis where the benefits associated with mitigation are not only hard to calculate in terms of money they are hard to see because we will not be able to tell how bad things would have gone if we did not implement those measures.

•The human toll and the cost to the country of the pandemic is more than what should have been incurred because not enough was spent on securing greater levels of socio-economic rights in the past.

While there are concerted efforts globally to respond to the humanitarian and economic impacts of the crisis uncertainty remains about what damage the pandemic will wreak and the period over which that damage will last. However, the key economies in the global economy were not doing well even before the pandemic. The global recovery from the 2008 global financial crisis that seemed to start from 2017 had clearly run out of steam during 2019. The declining levels of growth in Europe, India and China were of concern. The economic growth and employment experienced in the USA after the Trump tax breaks also seemed to be subsiding. Overall, the level of investment globally and in different regions has been sluggish since the global financial crisis of 2008.

The responses of developed economies to the global financial crisis of 2008 and the slow and halting post-crisis recovery and the sovereign debt crises in European countries was focused on using monetary policy. These monetary policy responses, included quantitative easing and other measures to increase liquidity and cheapen debt. The idea of increasing liquidity and lowering interest rates was to support the ongoing activities of business and increase investment. It was also hoped that these measures would help recovery in employment and support economic growth through increasing household consumption. However, the focus on monetary policy did not support increased productive investment but led to speculative activities in financial asset markets that led to occasional booms and busts. The monetary policy liquidity injections that kept interest rates low in many countries led to large and unsustainable levels of corporate debt. One could argue that this corporate debt was not productively used as it was used to support an unprecedented level of share buybacks that served to boost share prices. It also increased debt to low productivity services sectors, such as the gig economy, which includes ride sharing and food delivery businesses.

A large percentage of jobs created globally since the global financial crisis of 2008 was precarious, short-term contract, casual and gig economy jobs. They provided employment without job security and health and pension benefits. At the same time, the increased debt levels supported a resurgence in real estate asset markets that had been decimated at the time of the subprime crisis. The overall effect of this rise in debt levels that did not support productive investment and the creation of precarious employment was a surge in inequality.

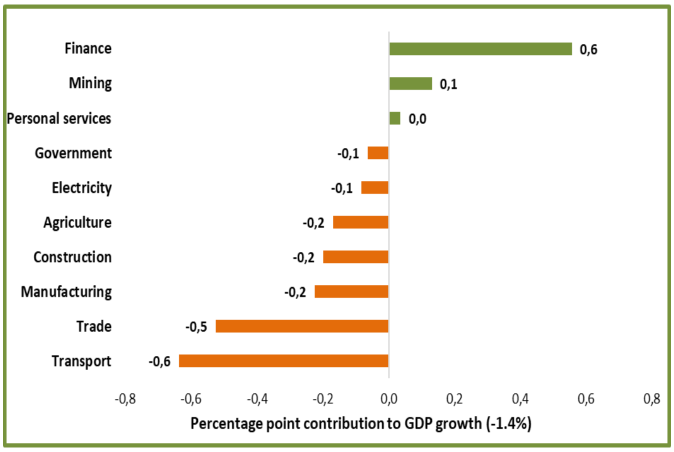
The South African economy, even though, there has not been very much accommodative monetary policy from the South African Reserve Bank, has also suffered from low levels of productive investment, high levels of speculative activities in the financial asset markets, growing unemployment, and increasingly precarious jobs that led to growing inequality. Therefore, South Africa and the rest of the world suffered from a problem of poor aggregate demand that put downward pressure on economic growth rates. It was widely recognized before the Covid-19 pandemic that monetary policy, particularly in countries with very low, zero and negative interest rates, had become less effective and that fiscal policy would be required to help countries avoid recession.

The economic impact of Covid-19 and the responses to it, particularly lock downs, has caused downward pressures on the productive economy by limiting the number of people that can work and the output side of the economy. It has also further reduced demand in the global economy as many businesses have closed, freight and transport has drastically declined, tourism has halted and many workers have lost their jobs. Developing economies, particularly those that export oil and other commodities have been severely affected. Value chains in countries, regions and globally have begun to break down as aggregate demand collapsed and government imposed lockdowns on non-essential economic activities.

Gross domestic product[1]

The South African economy entered a technical recession as real gross domestic product (GDP) in the fourth quarter of 2019 contracted by 1.4 per cent, following a contraction of 0.8 per cent in the third quarter. This is the second time that output has contracted for two successive quarters since the first quarter of 2018. According to the latest GDP figures, transport and trade were the main drags to overall economic activity. A simple indicator of a technical recession is two (or more) consecutive quarters of negative growth (real GDP quarter-on-quarter). The first recession since 1994 took place from the fourth quarter of 2008 until the second quarter of 2009. The second took place over the first and second quarters of 2018.

Figure 1: Sector percentage contribution to the fourth quarter GDP decline



Source: StatsSA

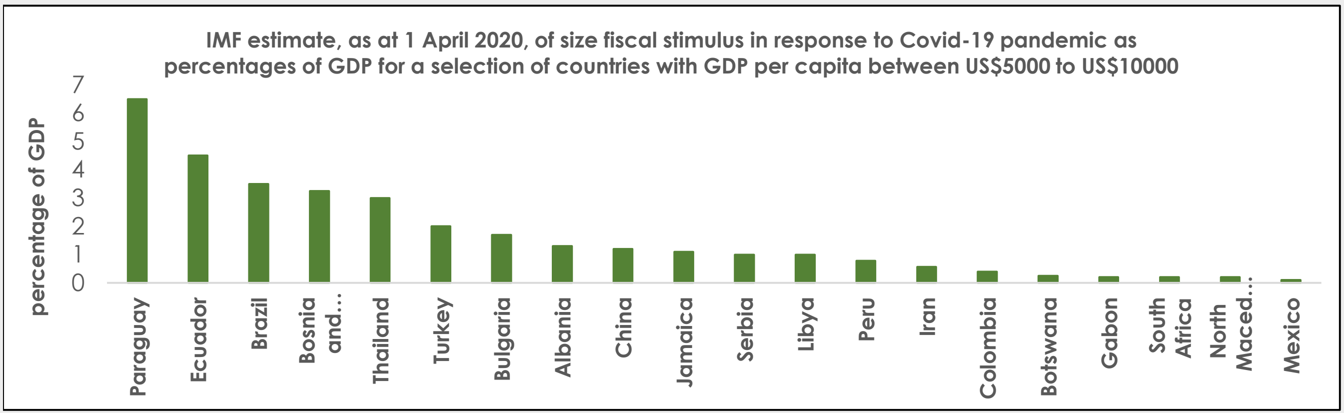
Seven of the ten industries of the South African economy contracted in the fourth quarter. Finance, mining and personal services made positive contributions to GDP, but insufficient to prevent the economy from entering a recession. The transport and communication sector (-0.6%) had the largest negative impact on the 1.4 per cent decline in quarterly GDP. A decrease in both freight and passenger transport constrained growth in the sector.

Trade, which declined by 3.8 per cent, was the second largest negative contributor to GDP after transport. The construction industry entered its sixth consecutive quarter of negative growth and has had only one quarter of positive growth since the beginning of 2017. Agriculture experienced its fourth consecutive quarter of negative growth, with negative growth of 7.6 per cent during the fourth quarter of 2019. Late rains and heatwave conditions across the country, affected the production of field crops. Production of horticultural products also declined in the fourth quarter of 2019. Flooding at some power stations and disruptions to coal deliveries caused by rain contributed to the electricity, gas and water supply industry's negative contribution to growth in the fourth quarter of 2019.

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

Box 1: South Africa's policy measures in response to the economic impact of Covid-19

The economic impact of the Covid-19 pandemic and measures to limit its health impacts, through efforts such as lock downs, will have very large negative economic implications for countries across the world. Huge numbers of businesses would be bankrupted and millions of workers will lose their jobs. At this very difficult time, we realise the important role of the state in mitigating the effects of crises, coordinating responses and investing resources to save lives, ease suffering, limit economic damage and to rebuild.



The International Monetary Fund (IMF) has compiled summaries of different countries' responses to the economic impact of the pandemic, such as measures to help workers and businesses. The IMF estimated amounts allocated to loans and grants used to respond to the economic impact of the pandemic by governments of 190 countries at the end of March 2020. They found that of the 69 countries with GDP per capital of US$10 000 or less, such as South Africa, only 29 allocated 1 per cent of GDP or more towards their responses to the pandemic. South Africa was not one of those countries. In fact, the IMF calculated South Africa's allocations as only 0.2 per cent of GDP. South Africa's response is on the very low end of the scale (see graph in this box). Most developed countries allocated at least 5 per cent of GDP. There are calls for developed countries to provide more help to poorer countries.

South African monetary policy measures

The 1 per cent interest rate cut by the South African Reserve Bank is seen as part of South Africa's monetary policy response. Other measures, such as increasing the number of repo auctions and the size of weekly refinancing operations when necessary, are aimed at increasing liquidity in South African financial markets. The SARB announced a programme to buy government securities in the secondary market at all different yields. They are implementing a programme to provide temporary relief on bank capital requirements and reduced the liquidity coverage ratio from 100 to 80 per cent to increase liquidity and reduce financial system risks. The SARB also supported banks to provide debt relief to borrowers for periods during the pandemic. These monetary interventions are relatively small compared to the monetary policy interventions by developed economies.

South African Tax relief measures

Employment Tax Incentive (ETI)

Under an extension of the 2013 Employment Tax Incentive Act, government expanded the ETI programme for a limited period of 4 months from 01 April 2020, by increasing amounts claimable by employers by R 500 in different categories, allowing monthly claims by employers on ETI and by accelerating payments of ETI reimbursements by reducing payment period from six months to monthly.

VAT relief

The Disaster Management Act No 57 of 2002 (of 25 March 2020) exempted 'essential goods' from Value Added Tax and rebate of customs duty. Essential goods include food products, cleaning and hygiene products, medical products, fuel and basic goods, such as electricity and airtime. The relief is intended to improve the cash position of the business importing these 'essential goods'. The business importing these 'essential goods' would not have to pay VAT during the lockdown period.

Support to industry by the Industrial Development Corporation and the Department of Trade, Industry and Competition

The Industrial Development Corporation (IDC) and the Department of Trade, Industry and Competition have compiled a package of more than R3 billion for industrial funding to help vulnerable businesses and fast-track funding to businesses that are considered vital for addressing the impact of the COVID-19 pandemic. This funding is only available to South African-owned businesses. A large part of the support amounting to R1.2 billion will be made available in the form of R500 million for trade finance to import essential medical products and R700 million for working capital, equipment and machinery. The remaining R1.8 billion will be used to support agriculture and food value chains to help secure food security; suppliers of primary energy with working capital to support energy security; SMMEs that provide components to auto-makers; businesses in the tourism sector; and providing necessary bridging capital to avoid disruptions in supply chains. The IDC as also announced that it will allocate R3 billion during the second quarter of 2020 for business support related to the Covid-19 pandemic.

Temporary Employment Relief Scheme

If Covid-19 is the direct cause of a company's financial distress that forces it to close down for 3 months or less it may benefit from the Temporary Employment Relief Scheme (TERS) if it is registered with the Unemployment Insurance Fund. TERS will be only for the cost of the salary of the employee and capped at R17 712 per month per employee. It will be paid according to the Unemployment Insurance Act's income replacement sliding scale. The provision requires that the wage must not fall below the minimum wage. Further, employees in self-quarantine qualify for sickness benefits.

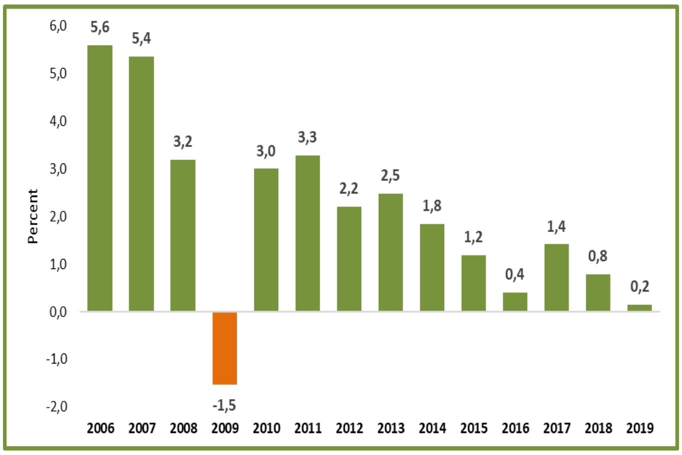
The Department of Agriculture, Land Reform and Rural Development

The Department of Agriculture, Land Reform and Rural Development allocated R1.2 billion to respond to COVID-19 pandemic and ensure sustainable food production. The support will be provided only to farmers that are within the current production season and have actively farmed for at least 12 months. These farmers have to be registered but they can be registered when the apply for help. Smallholder farmers with annual sales between R20 000 and R1 million and communal farmers will also qualify for this support. Priority is given to women, youth and disabled people

The National Empowerment Fund

The National Empowerment Fund has allocated R200 million for loans to black owned businesses to manufacture medical products, such as medical masks, sanitisers and dispensers and related priority products that help the healthcare sector during the pandemic. Black owned businesses will be able to apply for loans of between R500 000 to R10 million over a maximum term of 5 years.

Figure 2: Growth for 2019 the lowest since the 2008–2009 global financial crisis



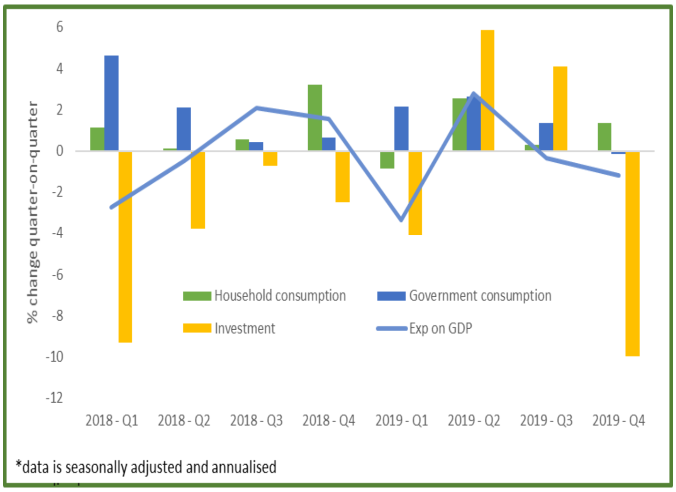
Source: StatsSA

The last quarter of 2019 GDP figure allows calculation of a full year GDP figure for 2019. GDP grew by 0.2 per cent in 2019, the lowest annual economic growth since 2009 when the economy contracted by 1.5 per cent because of the global financial crisis.

Expenditure on GDP

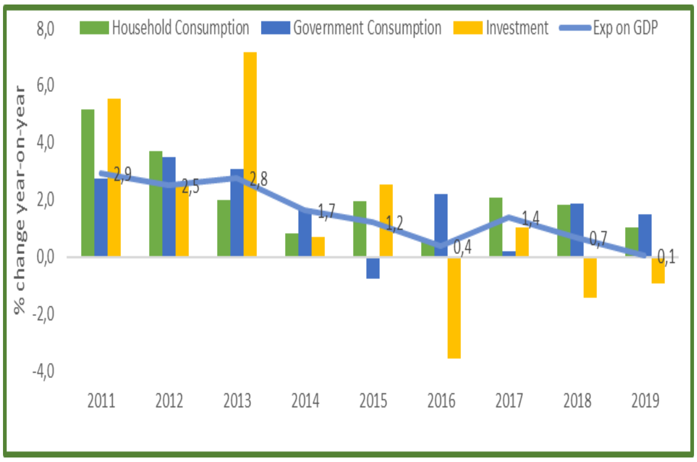
The real expenditure on GDP declined by 1.2 per cent in the fourth quarter of 2019 following a 0.4 per cent decline in the third quarter of 2019. The biggest drag on the fourth quarter of GDP growth was a contraction in South Africa's expenditure on investment by 10 per cent from the third to fourth quarters of 2019. This contraction in investment was the largest in four years following expansions of 4.1 per cent in the third quarter of 2019 and 5.8 per cent in second quarter of 2019. Household consumption expenditure expanded by 1.4 per cent in the fourth quarter of 2019 following a 0.3 per cent increase in the third quarter of 2019.

Figure 3: Quarterly sector performance



Source: StatsSA

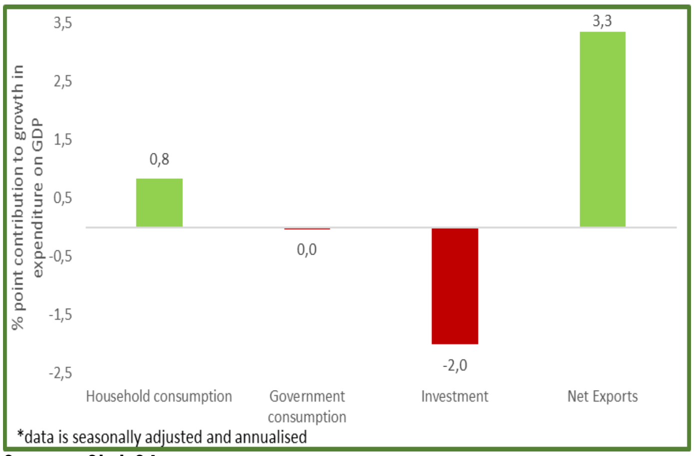
Figure 4: Annual sector performance



Source: StatsSA

The rate of annual real expenditure on GDP growth in figure 4 indicates a significant decline over the past decade. In 2011, the annual growth in real expenditure on GDP was 2.9 per cent. This growth rate declined to 0.1 per cent in 2019. In 2019, investment expenditure contracted by 0.9 per cent while expenditure on household consumption (1%) and government consumption (1.5%) expanded.

Figure 5: Sector contribution to negative fourth quarter GDP growth

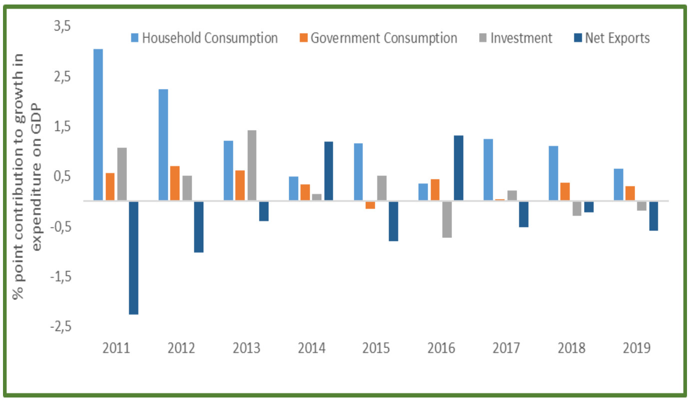


Source: StatsSA

Figure 5 shows the percentage contribution of different expenditure categories to the 1.2 per cent contraction in expenditure on GDP from the third quarter 2019 to the fourth quarter of 2019. Investment expenditure subtracted 2.2 per cent and net exports made a second consecutive positive contribution of 3.3 per cent to GDP growth during the fourth quarter of 2019.

The 3.3 per cent positive contribution by net exports was from an increase in exports of precious metals and stones and lower imports of machinery and equipment and vehicles and transport equipment.

Figure 6: Annual percentage contribution of sectors t to GDP



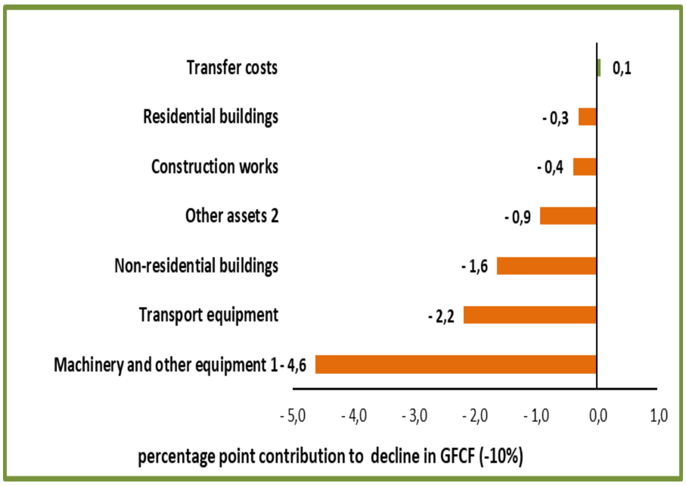
Source: StatsSA

Since 2011, Households' consumption expenditure, government expenditure and investment have been the main contributors to real GDP growth. Over the past two years the contribution from investment was negative and government consumption made only a small positive contribution to growth in real GDP. Household consumption contributed 0.6 per cent in 2019 to growth in real GDP from 1.1 per cent in 2018 and 1.3 per cent in 2017.

Investment

Gross fixed capital formation (GFCF) decreased by 10 per cent in the fourth quarter of 2019. This was after a 4.5 per cent increase in the third quarter. The decline in investments was due to the decrease in machinery and equipment, transport equipment, non-residential buildings and other assets.

Figure 3: Real Gross fixed capital formation by type of asset

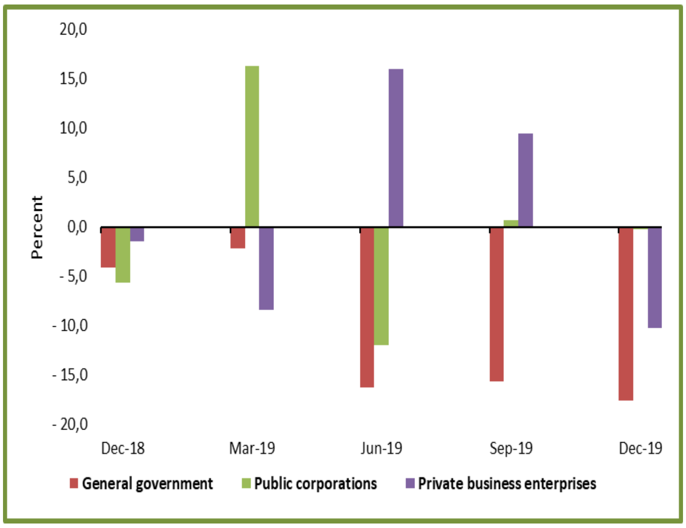


Source: StatsSA

The decline in investment, particularly of capital goods, will have a negative impact on South Africa's aging capital stock as a share of amortised machinery and equipment was not replaced. In other words, South Africa's potential to produce goods and services in the future has decreased.

Real gross fixed capital formation by private business declined by 10.3 per cent in the fourth quarter of 2019. This is after private business increased investment in the previous two quarters. Capital expenditure on transport equipment, construction works and machinery and equipment decreased in the last quarter of 2019. Declining public sector investment during the fourth quarter of 2019 means that real gross fixed capital formation by the public sector decreased for the third consecutive quarter. This decline was due to lower capital expenditure by general government. Gross fixed capital formation by government, which constituted 15 per cent of total investment in 2019, has contracted consistently over the last two years. It declined by 4.4 per cent in 2018 and an additional 8.9 per cent in 2019. Gross fixed capital formation by public corporations contracted by 0.3 per cent in the fourth quarter of 2019, after a marginal increase of 0.7 per cent in the third quarter.

Figure 4: Gross fixed capital formation by type of organisation



Source: StatsSA

Employment

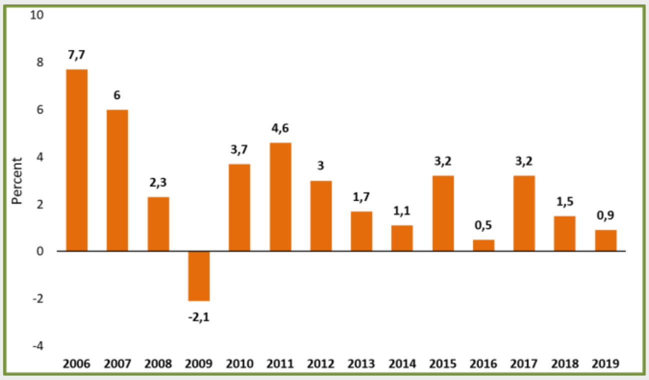
According to the Quarterly Labour Force Survey which measures formal and informal employment, the estimated official unemployment rate remained at 29.1 per cent (6.7 million people) in the fourth quarter of 2019. The labour force (37 686) grew by 0.2 per cent in the fourth quarter of 2019 while the number of people employed (45 260) also grew by almost the same rate of 0.3 per cent, resulting in an unchanged unemployment rate in the fourth quarter of 2019.

The broad unemployment rate, which includes discouraged job-seekers, increased by 7 percentage point (524 322) in the fourth quarter of 2019 compared to a year ago.

Box 2: Trends in household wages and income

Moderation in nominal wage growth in recent years has resulted in a slowdown in growth in nominal disposable income, which has negatively affected the ability of households to spend and borrow. Salaries and wages payable in cash or in kind drive the compensation of employees which, in turn, contributes almost 80 per cent to households' nominal disposable income (the other 20 percent comprises of property income, social benefits and current transfers received, according to South Africa's household disposable income statistics within the national accounts framework). Growth in households' nominal disposable income is a key driver of domestic demand. Lower household demand could lead to lower nominal consumption expenditure. Household consumption contributes about 60 per cent to South Africa's nominal gross domestic product (GDP).

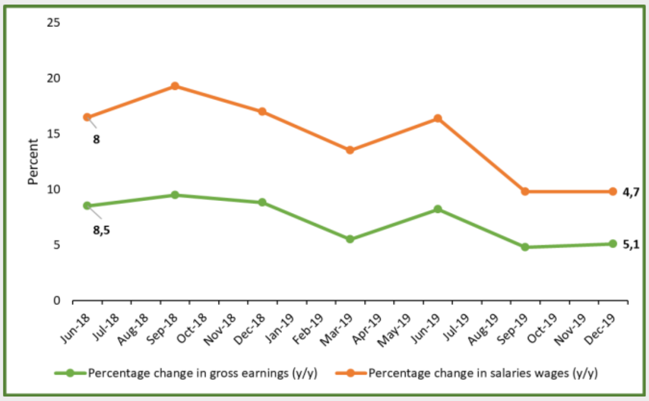
Figure 1: Percentage change in disposable income of households



Source: SARB

An analysis of the QES survey data (in figure 2) shows that year-on-year growth in the total nominal salaries and wages in the formal non-agricultural sector slowed notably from 8 per cent in the second quarter of 2018 to 4.7 per cent by the fourth quarter of 2019. A similar slowdown is depicted in the year-on-year trends in gross earnings which declined from 8.5 per cent in June 2018 to 5.1 per cent at the end of the fourth quarter of 2019.

Figure 2: Percentage change in nominal salaries and wages and gross earnings



Source: StatsSA

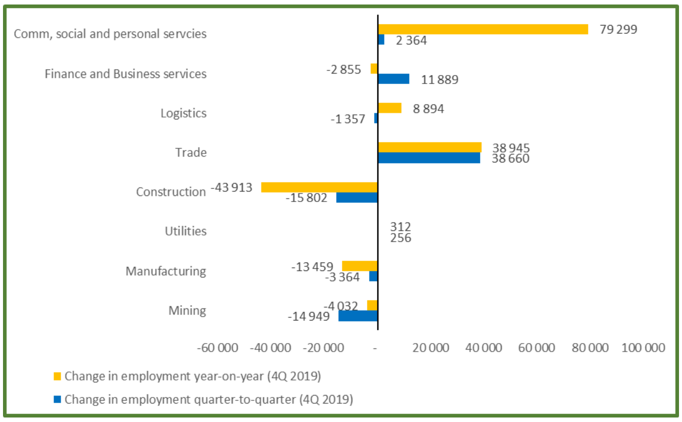
Table 1: Key labour statistics – Quarterly Labour Force Survey

	4Q 2018	3Q 2019	4Q 2019
Labour force ('000s)	**22 668**	**23 109**	**23 146**
Employed	16 529	16 375	16 420
Unemployed - official	6 139	6 734	6 726
Unemployed - broad*	9 706	10 272	10 381
Not economically active ('000s)	**15 466**	**15 474**	**15 581**
Discouraged job-seekers	2 841	2 793	2 855
Other (not economically active)	12 625	12 681	12 726
Unemployment rates			
Official unemployment rate (narrow)	27,1%	29,1%	29,1%
Broad unemployment rate*	37,0%	38,5%	38,7%
Unemployment Rates - Gender			
Male - official	25,1%	27,7%	27,2%
Female - official	29,5%	30,9%	31,3%
Unemployment Rates - Race			
Black African - official	30,4%	32,8%	32,4%
Coloured - official	21,6%	23,5%	24,9%
Indian/Asian - official	12,4%	13,3%	13,9%
White - official	7,6%	7,4%	7,6%
Youth**			
Unemployment rate - official	38,7%	41,9%	41,5%
Unemployment rate - broad*	50,1%	52,5%	52,4%

* The broad unemployment rate includes discouraged job seekers
** Youth is defined as age 15 - 34
Data: Quarterly Labour Force Survey, Stats SA

It has also increased by 0.2 percentage points to 38.7 per cent in the fourth quarter of 2019 compared to previous quarter. The unemployment rate for women increased in the fourth quarter while for males it decreased. Female unemployment increased by 0.4 to 31.3 per cent in the fourth quarter of 2019 from 30.9 per cent in the third quarter, while for males there was a 0.5 percentage point decrease from 27.7 per cent in the third quarter of 2019 to 27.2 per cent.

Figure 5: Sector contribution to employment – Quarterly Employment Survey (QES)

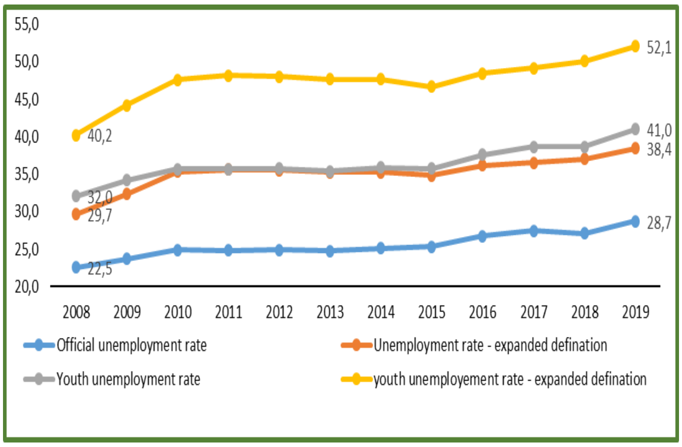


Source: StatsSA

According to the Quarterly Employment Survey (QES), which reports formal non-agricultural sector employment, employment increased by 17 697 jobs (a 0.2 per cent increase in employment) in the fourth quarter of 2019, or 63 191 (0.6 per cent) compared to the same quarter in 2018. Trade (38 660) and Finance and Business services (11 889) were the largest contributors to job creation whereas Construction (15 802) and Mining (14 949) made the largest negative contribution to employment growth in the fourth quarter of 2019.

Figure 6 shows that in 2008, the official unemployment rate was 22.5 per cent and 29.7 per cent by the broad definition. The official unemployment rate rose to 28.7 per cent in 2019 and 38.4 per cent according to the broad definition. The official youth unemployment rate rose from 32 per cent in 2008 to 41 per cent in 2019 or from 40.2 per cent in 2008 to 52.1 per cent in 2019 by the expanded definition. Overall, unemployment has increased over the past 5 years (2015 – 2019).

Figure 6: Trend in annual unemployment rate – official and broad rates



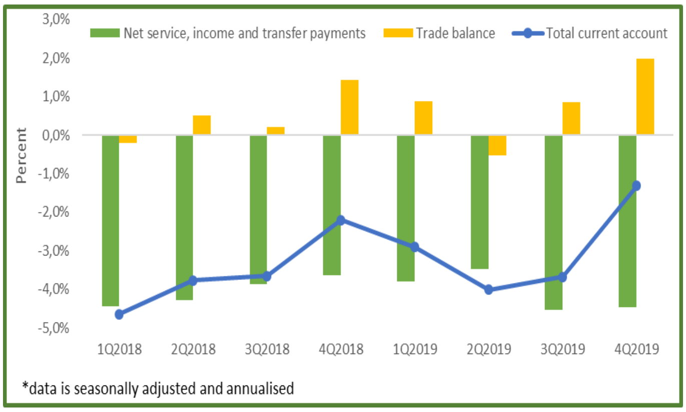
Source: StatsSA

Current Account

The deficit on the current account of the balance of payments narrowed by R120 billion from R188 billion in the third quarter of 2019 to R68.1 billion in the fourth quarter. As a ratio of GDP, the current account deficit narrowed by 2.4 percentage points from 3.7 per cent in the third quarter of 2019 to 1.3 per cent in the fourth quarter.

South Africa's trade surplus increased substantially from R44.0 billion in the third quarter of 2019 to R102.5 billion in the fourth quarter of 2019. This improvement in the trade balance is due to the increased value of merchandise exports while that of imports declined. Both prices and volumes in the value of merchandise exported increased while the value of imported goods was weighed down by lower import volumes. As a ratio of GDP, the trade surplus widened further by 1.1 per cent from 0.9 per cent in the third quarter of 2019 to 2.0 per cent in the fourth quarter of 2019.

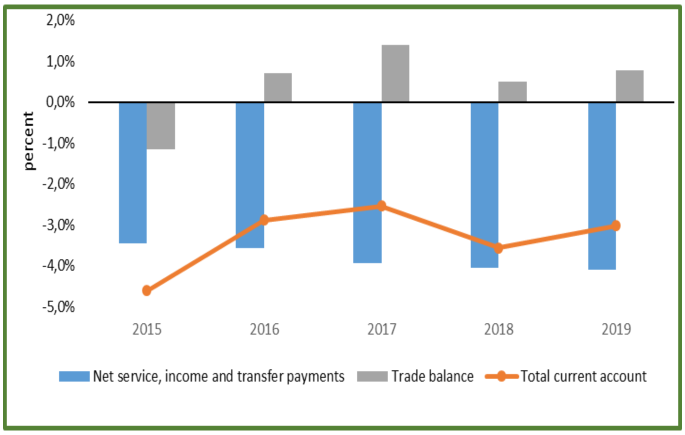
Figure 7: Change in the balance of the current account (as a percentage of GDP)



Source: StatsSA

Figure 8: Annual change in the balance of the current account (as a percentage of GDP)

Source: SARB



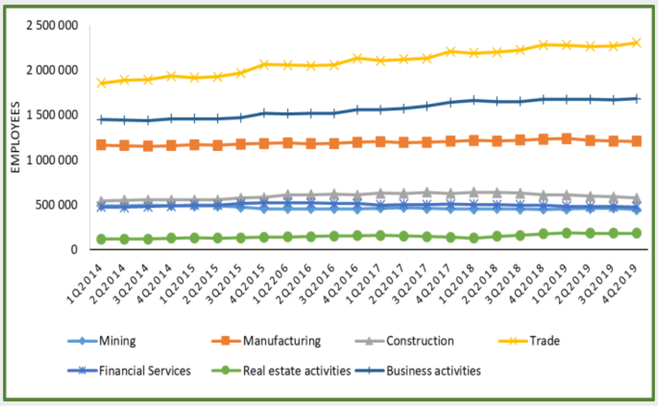
South Africa's trade balance moved from a deficit of R47.1 billion in 2015 to a surplus of R30.8 billion in 2016, a positive annual trade balance was sustained until 2019. The improvement in the trade balance was due to the value of merchandise exports increased, particularly minerals products, vehicle and transport equipment and platinum group metals while that of imports (agriculture) declined. As a ratio of GDP, the trade surplus moved from a deficit of 1.2 per cent in 2015 to a surplus of 0.7 per cent in 2016, a surplus which has been continued until 2019.

However, the current account balance remains in deficit due to the relatively large amount of negative financial transfers on the current account. The negative current account balance has to be offset by positive inflows on the financial account of the balance of payments. Therefore, the negative financial transfers on the current account may pose a serious problem at a time of the Covid-19 pandemic when there are large capital outflows on

Box 3: Trends in private sector employment

Private sector business enterprises (67 per cent) contribute the largest share of total formal non-agricultural employment, followed by the public sector (26 per cent) and public corporations (6.5 per cent). In 2019, many private sector companies reported their intentions to retrench workers due to selling, restructuring or closing down business units. These retrenchments contributed to stagnant employment in the private sector in all four quarters of 2019.

Figure 1: Private sub-sectors' contribution to employment



Source: StatsSA

Figure 1 shows sectoral contributions to private sector employment in all four quarters of 2019. Construction sector employment has been decreasing since the second quarter of 2018. The inability of the construction sector to create more jobs could be associated with retrenchments in the big construction companies, including Big Five and PPC Cement, which went through restructuring processes in 2019. Manufacturing, financial services and mining are sectors where companies reported their intentions to retrench workers during the course of 2019. These are sectors where employment numbers in these sub-sectors declined during 2019.

Whilst sub-sectors like trade and business services continued to increase employment overtime, it should be noted that many businesses face serious downside risks as a result of the coronavirus pandemic. The drastic measures of a country-wide lockdown enforced by the government, which significantly reduces economic activity to curb the spread of covid-19, will inevitably affect employment. Furthermore, the South African Reserve Bank (SARB) announced that they expect approximately 370 000 jobs to be affected as a result of the Covid-19 pandemic with private sector employment most affected.

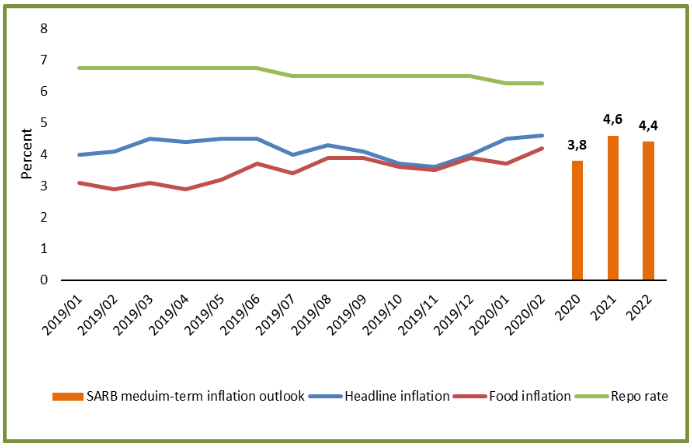
the financial account of the balance of payments. For example, South Africa's foreign exchange reserves could significantly decline and the country's ability to import could be curtailed even though we have a positive trade balance. The SARB has asked companies not to pay dividends in 2020. Lower outflows of dividends to foreign shareholders could ease pressure on the balance of payments by increasing reducing the current account deficit.

Inflation and monetary policy

Headline consumer price inflation (CPI) for all urban areas was 4.6 per cent in February 2020, up from 4.5 per cent in January 2020. Inflation on food and non-alcoholic beverages increased by 4.2 per cent year-on-year, from January's 3.7 per cent. The Monetary Policy Committee (MPC) of the South African Reserve Bank has noted that the global economic outlook has been revised downward due to the outbreak and spread of Covid-19. According to the MPC, the overall risks to the inflation outlook for the moment appear to be balanced. In the short term however, electricity pricing is of immediate concern, and there is the possibility of higher price volatility of goods and services as a result of sudden changes in demand and supply. The Bank's headline consumer price inflation forecast averages 3.8 per cent for 2020, 4.6 per cent for 2021, and 4.4 per cent in 2022.

Against this backdrop, the MPC decided to cut the repo rate by 100 basis points to 5.25 per cent per annum, with effect from the 20 March 2020. The MPC emphasised that monetary policy in this instance sought to ease financial conditions for households and firms in order to alleviate the short-term impact of Covid-19.

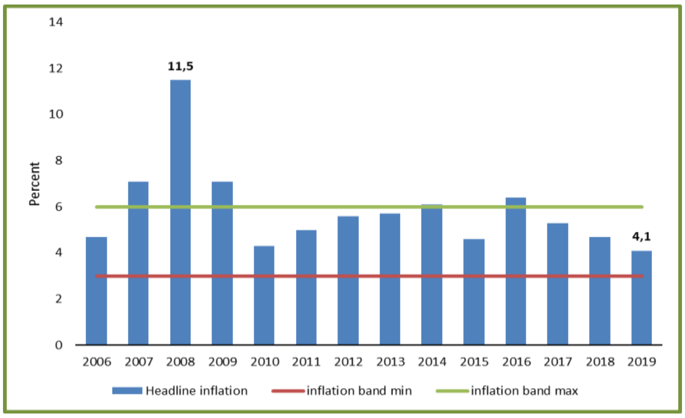
Figure 8: Inflation still within the Reserve Banks 3%-6% target range



Source: SARB

Figure 9 shows the annual changes in inflation since 2006. South Africa's inflation has generally remained within the inflation target range of the Reserve Bank. The inflation rate was outside the inflation band between the years associated with the peak of the global financial crisis, between 2007 and 2009.

Figure 9: Percentage change in annual headline inflation



Source: StatsSA, SARB

Sovereign ratings: Latest update

Sovereign ratings agency Moody's maintained its negative outlook and downgraded South Africa's long term foreign and local currency debt ratings to 'Ba1' from 'Baa3'. South Africa's Moody's credit ratings for sovereign domestic currency debt is now one notch below investment grade. Moody's gave the following as reasons for their downgrade:

- Structurally very weak growth and constrained capacity to stimulate the economy;
- A significant rise in government debt over the medium term;
- The risk that economic growth will prove even weaker and the debt burden will rise even faster and further than currently expected, weakening debt affordability and potentially, access to funding.

Fitch also took the decision to lower South Africa's long term foreign and local currency debt ratings further into non-investment grade by one notch to 'BB' from 'BB+' and maintained their negative outlook. According to Fitch, they downgraded South Africa further because they believe there is the lack of a clear path towards government's debt stabilisation and because of the expected impact of the coronavirus (COVID-19) shock on public finances and economic growth. Fitch announced in early April 2020 that the coronavirus outbreak and large drops in the oil price will lead to increased multi-notch sovereign downgrades during 2020. They expect developed and developing countries to be affected. They said that developing countries are more likely to be moved to a lower rating category as a result of a multi-notch downgrade.

Conclusion

While the extent of the impact of the Covid-19 pandemic cannot yet be known we do know that it is already causing much damage. The global economy was close to recession before the outbreak of the pandemic. South Africa's macroeconomic performance in terms of growth, employment and investment was low before the pandemic. As a result of the pandemic and measures to reduce its spread, South Africa's socio-economic problems related to unemployment, poverty and inequality will further deepen. We will lose many businesses, jobs and productive capacity. However, these measures are necessary to prevent even further harm.

The extent of the pandemic has raised questions not only about how to reduce economic damage and to support the poor and businesses during the crisis. It has also raised questions about long-held beliefs about economic policies and public finance. Governments across the world are asking how far government and central banks can go to respond to the current crisis. An initial comparison of the size of South Africa's response, partly drawing on work of the IMF, shows that we are the low end in terms of commitment of resources, even when compared to other developing countries.