Quarterly economic review

Summary and general comments

Economic developments during the first quarter of 1982 provided further evidence of the cyclical downswing in real economic activity which had begun in the third quarter of 1981. Real gross domestic product, which had still grown at a seasonally adjusted annual rate of about 5 per cent during the first nine months of 1981, increased only marginally in the fourth quarter and remained virtually unchanged in the first quarter of 1982. Although real gross domestic expenditure increased appreciably in the first quarter, after a decline in the last quarter of 1981, this increase was entirely due to a further rise in fixed and inventory investment. Real private and government consumption expenditure actually decreased during this period. The economic slowdown was also reflected in a lower rate of increase in non-agricultural employment in the fourth quarter of 1981 and in an increase in the number of registered unemployed Whites, Coloureds and Asians during the first quarter of 1982.

Despite these indications of a downward cyclical movement, economic activity, and in particular nominal domestic expenditure, remained at a high level. One result of this was a further sharp rise in the *value* of imports in the first quarter. At the same time, merchandise exports continued to be affected adversely by the recession in most industrial countries, while the gold price fell considerably further. Consequently, in the first quarter the current account of the balance of payments showed a deficit of R6,7 billion at a seasonally adjusted annual rate. Although the *volume* of imports, which had begun a cyclical decline in the fourth quarter of 1981, continued to decrease in the first quarter of 1982, it is clear that the balance of payments adjustment process still has to run its course.

Compared with the substantial deficit on the current account, the net inflow of capital not related to reserves was of negligible proportions in the first quarter. Total net gold and other foreign reserves, therefore, declined by no less than R1,4 billion during this period, bringing the decline during the past eighteen months to R4,7 billion. The sharp decrease in *net* foreign reserves during the first quarter partly reflected large-scale short-term foreign borrowing by the banking sector in order to support the foreign exchange reserves. In these circumstances, the rand depreciated sharply during the first quarter and also during the ensuing period. From the end of 1980 to the end of May 1982 the effective exchange rate of the rand declined by as much as 20 per cent.

This depreciation was a significant contributing factor to the sustained high rate of inflation. The import price component of production prices, for example, showed a sharply accelerating increase from the third quarter of 1981. The rate of increase in consumer prices decelerated slightly in the first quarter, but a notably higher rate of increase is expected in the second quarter, when consumer prices will show the full effect of recent indirect tax increases and upward adjustments in several administered prices. The increase of 16,5 per cent in consumer prices from April 1981 to April 1982 provides an indication of the still prevailing high rate of inflation.

An exceptionally strong growth in the money supply was experienced during the first quarter. At a seasonally adjusted annual rate, the broadly defined money supply (M2) increased by 41 per cent during this period, despite the contractionary effect of a substantial decline in the net gold and other foreign reserves of the monetary banking sector and a marked decrease in net bank credit to the government sector. The main reasons for the further monetary expansion were a substantial rise in bank credit to the private sector and an increase in liquidity preference which caused a shift from long-term deposits to shorter-term deposits offering higher rates of interest. In addition, there was a marked increase in the net "other" assets of the monetary banking sector, reflecting mainly losses on forward exchange transactions.

The continuing strong demand for bank credit in general reflected tight conditions in the broad financial markets and limited alternative sources of finance. More in particular, greater reliance was placed on bank credit as a means of supplementing reduced company cash flows and of financing a further, and to some extent an involuntary, build-up of inventories. Banking institutions were enabled to extend further bank credit on a large scale by a considerable expansion of their liquidity base, resulting mainly from increased bank advances to the Land Bank and Reserve Bank credit to the Government towards the end of 1981 and a considerable net inflow of short-term foreign capital in the first quarter of 1982. To a large extent, however, the substantial increase in bank credit to the private sector during the first quarter reflected "round-tripping" and the re-intermediation of credit transactions which had previously been contracted outside the banking system, especially during the third quarter and part of the fourth quarter of 1981.

Mainly as a result of the decline in the Reserve Bank's net foreign reserves and the seasonal flow of tax funds to the Government, the money market tightened considerably during the first quarter. In order to alleviate the tight market situation and the upward pressure on short-term interest rates, the Reserve Bank on 30 March reduced the supplementary cash reserves which banks are required to hold with the Bank. In addition, the Bank encouraged the increased use of foreign credits by quoting substantially reduced premiums on forward dollars. These measures, together with increased government expenditure at the beginning of the new fiscal year, resulted in a considerable easing of the money market during April and May. To offset the temporary expansionary effect of government expenditure on money market conditions and the money supply, however, the Reserve Bank engaged in substantial open-market sales of securities obtained from the Treasury through tap issues.

Tight conditions in the capital market during the first quarter led to a sharp rise in long-term fixed-interest security yields, a decline in turnover and prices in the share market, and limited mortgage lending. The value of real estate transactions, on the other hand, rose to a new high. In addition to a general tightening of the capital market, the fall in share prices also reflected greater realisation that a more pronounced slow-down of economic activity was imminent. New investment in long-term government stock and other fixed-interest securities during the first quarter was temporarily inhibited by expectations of a further increase in long-term yields. These expectations were, however, moderated considerably by the smaller than anticipated borrowing requirement of the Central Government in the 1982/83 fiscal year, and in April a climate more conducive to investment in long-term fixed-interest securities came into being. Existing large holdings of money market investments and less favourable opportunities for further investment in the share and real estate markets also induced long-term institutional investors with large contractually determined cash inflows to increase their investment in fixed-interest securities during April and May.

National accounts*

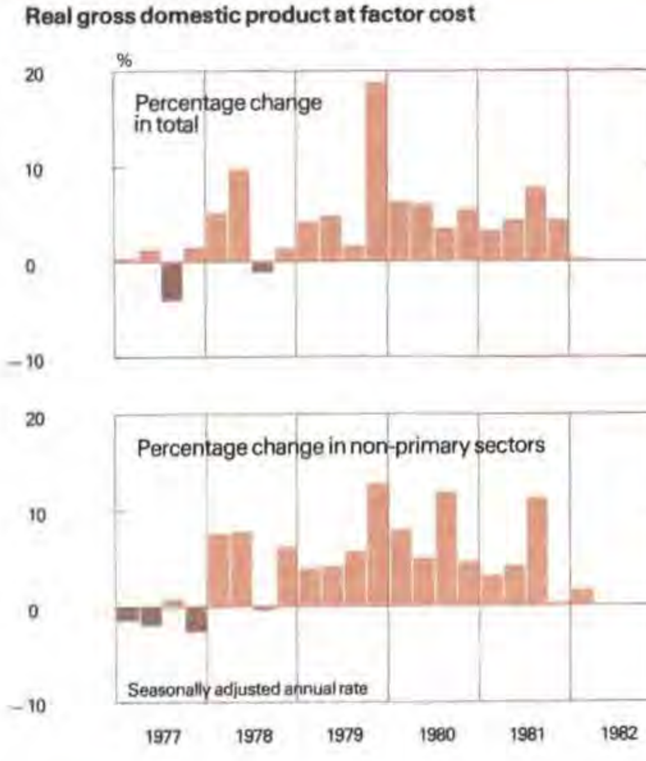
Little change in real gross domestic product

After having risen only marginally in the fourth quarter of 1981, real gross domestic product showed little change in the first quarter of 1982. The real value added by important sectors such as agriculture, mining, wholesale and retail trade declined in the first quarter, while the real product of manufacturing showed little change relative to the fourth quarter of 1981.

In the primary sectors, the decline in the real product of agriculture was related to adverse weather conditions, whereas the rather sharp decrease in that of non-gold mining was largely due to the weak foreign demand for metals and minerals. The decline in the real value added by gold mining, despite a fairly sharp increase in the tonnage of ore milled, reflected a lower volume of production resulting from a further decline in the grade of ore milled. In contrast with the decline in the real product of the agricultural and mining sectors, the combined real value added by the non-primary sectors increased moderately in the first quarter.

Looking at individual non-primary sectors, preliminary indications are that manufacturing production did not increase in the first quarter of 1982. The real value added

Real gross domestic product at factor cost



*Unless otherwise indicated, quarterly developments are based on seasonally adjusted data.

by the wholesale and retail trade actually declined in the first quarter, whereas that of the motor trade increased only marginally. These developments were all related to a lower level of real expenditure on durable and semi-durable consumer goods in the first quarter. In fact, the combined real product of industry and commerce already started to decline from the fourth quarter of 1981. Moderate increases were, however, recorded in the real product of the other non-primary sectors, namely the transport and financial sectors, mainly because of the continuing high levels of domestic demand and general financial activity.

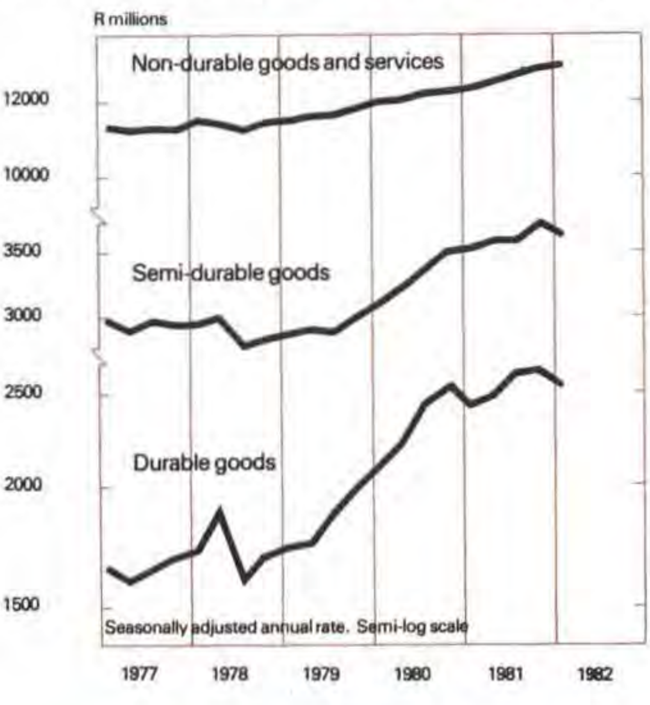
The gross domestic product at current prices declined in the first quarter of 1982. The gross operating surplus component decreased for the second consecutive quarter, reflecting the lower surpluses of agriculture and mining. The rate of increase in the other main component, namely remuneration of employees, was also lower than the average quarterly rate recorded in 1981.

Notable increase in real gross domestic expenditure

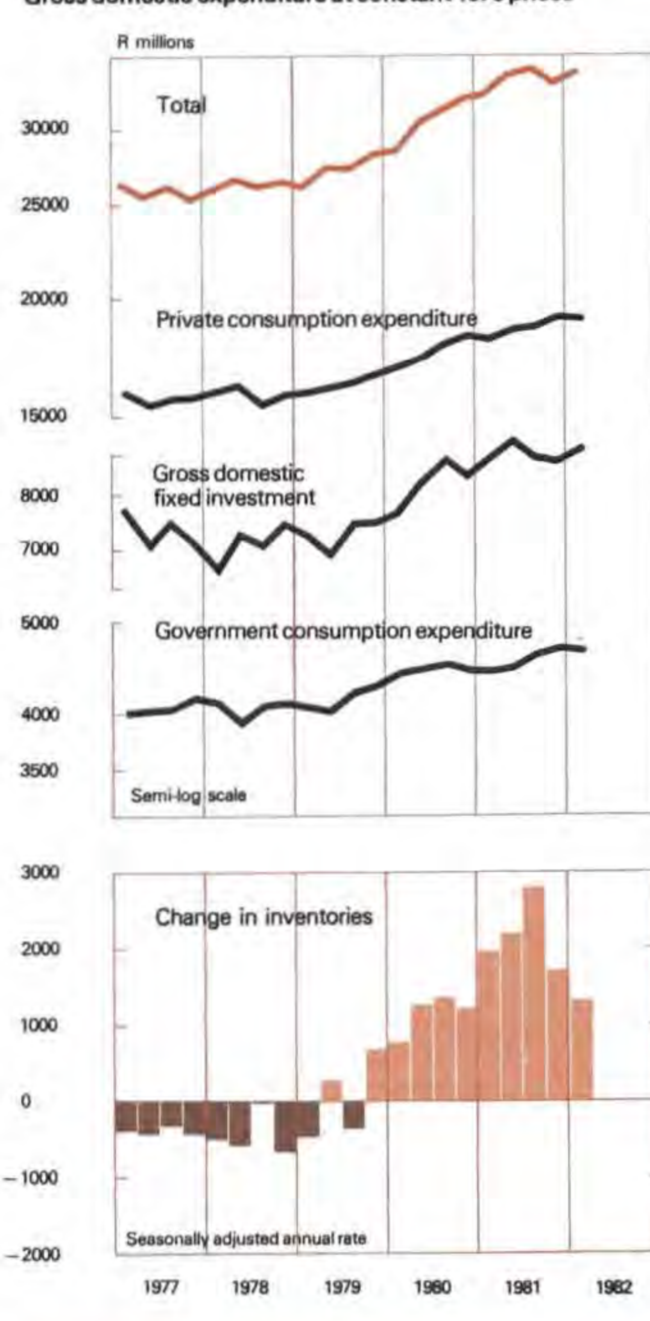
Following upon a substantial decline in the fourth quarter of 1981, real gross domestic expenditure increased notably in the first quarter of 1982. This increase was entirely accounted for by real fixed and inventory investment. In contrast, real government and private consumption expenditure showed small decreases in this period. At current prices, gross domestic expenditure exceeded gross national product by a substantial amount, indicating a large deficit on the current account of the balance of payments.

The upward trend in real private consumption expenditure since the middle of 1979 appeared to have been arrested in the first quarter of 1982, when further small increases in real outlays on non-durable goods and on services were more than neutralised by fairly large declines in real outlays on durable and semi-durable goods. In the durable goods category, a small increase in outlays on new motor cars was more than offset by a large decrease in outlays on furniture and household appliances. The decline in real outlays on semi-durable

Private consumption expenditure at constant 1975 prices



Gross domestic expenditure at constant 1975 prices



goods largely reflected a lower level of expenditure on clothing and footwear.

Real government consumption expenditure, which often shows large quarterly fluctuations, declined slightly in the first quarter. A small increase in real remuneration of employees was more than neutralised by a decrease in real expenditure on goods and other services.

In contrast with the decreases in private and government consumption expenditure, real gross domestic fixed investment rose further in the first quarter of 1982. In the private sector further increases were recorded by manufacturing and mining, but declines occurred in agriculture and in residential construction. The latter decline was related to the high cost and scarcity of funds, whereas the decrease in real agricultural fixed investment should be seen in relation to the sharp increases that occurred in the preceding four quarters. The persistent increase in real fixed investment in manufacturing since the middle of 1979, coupled with the slow-down in production towards the end of 1981 and the first quarter of 1982, caused the utilisation of production capacity in manufacturing to decline from a peak of 90,0 per cent in the third quarter of 1981 to 89,4 per cent in the first quarter of 1982, the lowest level since the fourth quarter of 1980.

After having decreased in the course of 1981, real fixed investment by public corporations rose moderately in the first quarter of 1982, mainly as a result of an increase in real outlays by Escom. The latter increase more than neutralised a decline in the real capital expenditure of Sasol. Despite a decrease in fixed investment by general government, increases in capital outlays by the South African Transport Services and by the Department of Posts and Telecommunications caused the real capital expenditure of public authorities to increase further in the first quarter of 1982.

A notable increase in real inventories again occurred in the first quarter of 1982. Diamond stocks rose further owing to a continuing weak demand, and agricultural stocks-in-trade remained at a high level, largely because the programme of exporting the maize surplus had not been completed. The further build-up of real industrial and commercial inventories was related to the slow-down of consumption expenditure in the first quarter, and was consistent with the past behaviour of these classes of inventories in similar stages of the business cycle. The ratio of real non-agricultural and non-strategic inventories to the comparable real gross domestic product increased further to 35,7 per cent in the first quarter of 1982, compared with the latest trough of 29,6 per cent in the fourth quarter of 1979.

Decline in gross domestic saving

Gross domestic saving declined substantially in the first quarter of 1982 to its lowest level since the fourth quarter of 1979. As a ratio of gross domestic product, it amounted to only 23 per cent in the first quarter of 1982, compared with an average ratio of 27½ per cent in the second half of 1981 and 33 per cent in the 1980 calendar year. At a seasonally adjusted annual rate, gross domestic saving amounted to about R17 100 million in the first quarter, no less than R6 700 million lower than gross fixed and inventory investment. This indicates that foreign funds were again employed extensively to supplement domestic savings in financing domestic investment.

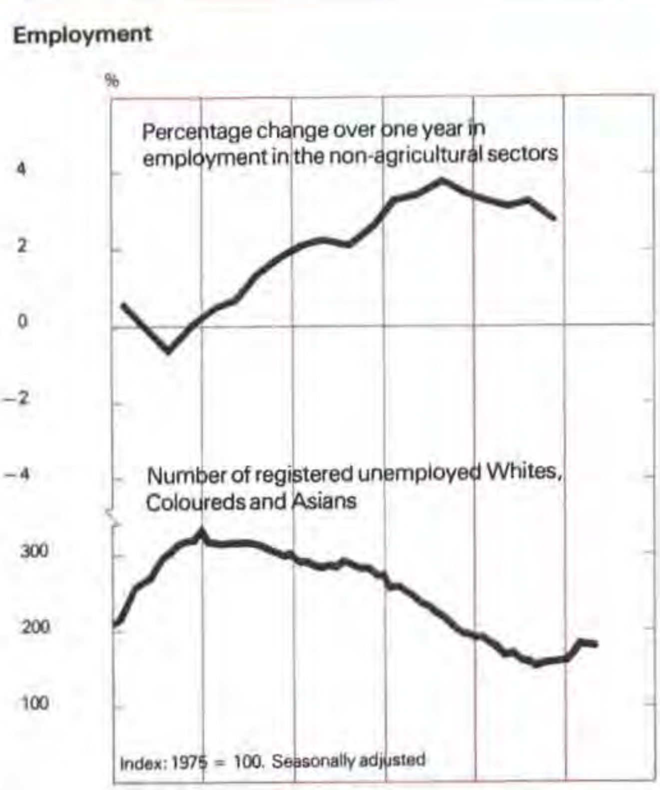
The different components of gross domestic saving showed divergent tendencies in the first quarter of 1982. Provision for depreciation and the saving of general government rose moderately, but personal and corporate saving declined markedly. The increase in provision for depreciation reflected the further rise in fixed investment, while the higher level of general government saving resulted largely from a peak in central government revenue during this period. Corporate saving declined to its lowest level since the fourth quarter of 1979, reflecting largely a decrease in corporate profits. Personal saving declined because the increase in private consumption expenditure at current prices exceeded the rise in personal disposable income. The ratio of personal saving to personal disposable income declined to a low level of only 6 per cent in 1981 and even fell below this level in the first quarter of 1982.

Employment and remuneration of labour*

Employment in the non-agricultural sectors of the economy increased by 2,9 per cent in 1981, compared with 3,3 per cent in the preceding year. Employment in the private and public sectors rose by 3,0 per cent and 2,5 per cent, respectively. Although the increase in employment slowed down in certain major sectors of the economy, such as manufacturing, mining, general government and financial institutions, employment in construction, trade, the South African Transport Services, electricity supply, insurance, local authorities and private road transport increased at higher rates.

The slower growth of real economic activity in the fourth quarter was also reflected in a lower rate of increase in non-agricultural employment. At a seasonally adjusted annual rate, the increase in non-agricultural employment decelerated from 3,4 per cent in the third quarter to 1,3 per cent in the fourth quarter. This slowdown occurred mainly in the private sector and was also reflected in the lower growth rates of ordinary and overtime hours worked in manufacturing and construction. On the other hand, the rate of increase in public-sector employment accelerated in the third and fourth quarters of 1981. Mirroring the declining rate of increase in total employment in the fourth quarter, the seasonally adjusted number of registered unemployed Whites, Coloureds and Asians increased from a low of 14 643 in August 1981 to 15 336 in December and 17 334 in April 1982. The unemployment rate among Blacks (ratio of unemployed to the economically active population) continued to decline throughout 1981, namely from 8,1 per cent at the end of 1980 to 7,1 per cent in November 1981.

Employment



*Statistics relating to employment and remuneration of labour are only available up to the end of 1981.

Labour productivity, as measured by the real gross domestic product per worker in the non-agricultural sectors of the economy, rose by 1,8 per cent in 1981, compared with 3,4 per cent in 1980. This lower increase reflected to some extent the physical inability of available production resources to sustain a further high rate of increase in economic activity, but was also due to a more pronounced slow-down of the growth in production than of the increase in employment.

In nominal terms, the average remuneration per worker rose sharply by 21 per cent in 1981, compared with 18 per cent in 1980. The higher rate of increase was the result of active competition for scarce skilled labour, a narrowing of the gap between the wages of skilled and unskilled workers, and inflation-induced upward adjustments in salary and wage scales in both the private and public sectors. In real terms, average salaries and wages per worker rose by 4,6 per cent in 1981, compared with 3,7 per cent in 1980. The rate of increase in the average real remuneration of White workers accelerated from 3,2 per cent in 1980 to 5,7 per cent in 1981, while that of other workers decelerated from 4,3 per cent in 1980 to 2,9 per cent in 1981.

Prices

The increase in consumer prices slowed down from a seasonally adjusted annual rate of 16,2 per cent in the third quarter to 14,6 per cent in the fourth quarter of 1981 and to 14,4 per cent in the first quarter of 1982. With the exception of housing costs, virtually all major components of the consumer price index recorded notably lower rates of increase in the first two months of 1982. From February to March, however, consumer prices rose sharply by 2 per cent, reflecting the increase in the general sales tax rate from 4 to 5 per cent on 1 March (which alone contributed 0,7 per cent to the total increase) as well as increases in the prices of various goods and services, such as transport equipment and services, furniture and household equipment, clothing, housing, education, recreation and personal care. During April the seasonally adjusted consumer price index rose by 1,9 per cent, mainly as a result of upward adjustments in petrol prices, postal tariffs, railway tariffs, air fares and certain other administered prices as well as in food prices and housing costs. It is expected that the rate of increase in consumer prices will show an acceleration in the second quarter because of the factors

Prices

noted above as well as the import surcharge of 10 per cent, which was introduced in February. From April 1981 to April 1982 consumer prices rose by 16,5 per cent.

The increase in production prices accelerated from a seasonally adjusted annual rate of 11,5 per cent in the third quarter of 1981 to 13,7 per cent in the fourth quarter and to 16,8 per cent in the first quarter of 1982. Prices of domestically produced goods and imported goods increased at annual rates of 16,8 and 17,2 per cent, respectively, during the first quarter of 1982. Prices of domestically produced basic metals and metal products, machinery, rubber and rubber products, leather products, processed food and electricity tariffs rose sharply in the first quarter, while the high rate of increase in the prices of imported goods was mainly due to the depreciation of the rand. From April 1981 to April 1982 production prices increased by 14,4 per cent.

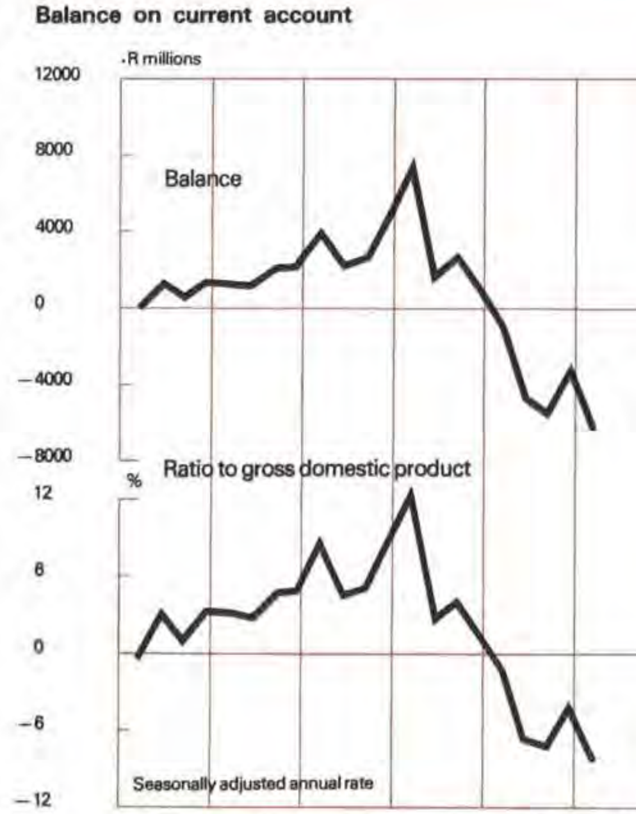
Balance of payments

Further deficit on current account

In the first quarter of 1982 the current account of the balance of payments continued to reflect the effect of a high level of domestic demand on imports as well as adverse external influences in the form of a decline in merchandise exports and a further fall in the price of gold. The deficit on the current account, which had decreased from R1 398 million in the third quarter of 1981 to R1 137 million in the fourth quarter, rose to R1 413 million in the first quarter of 1982. At a seasonally adjusted annual rate, the deficit increased from R3 630 million in the last quarter of 1981 to R6 700 million in the first quarter of 1982, or from 4,8 to 9,0 per cent of the gross domestic product.

Merchandise imports, seasonally adjusted, increased notably in the first quarter, but this increase was entirely due to price rises. Although price increases in the main industrial countries slowed down, the rise in import prices accelerated as a result of the further depreciation of the rand. The volume of merchandise imports, which had begun to show a cyclical decline in the fourth quarter of 1981, continued to decrease in the first quarter of 1982 and was in fact 7½ per cent below the

Balance on current account



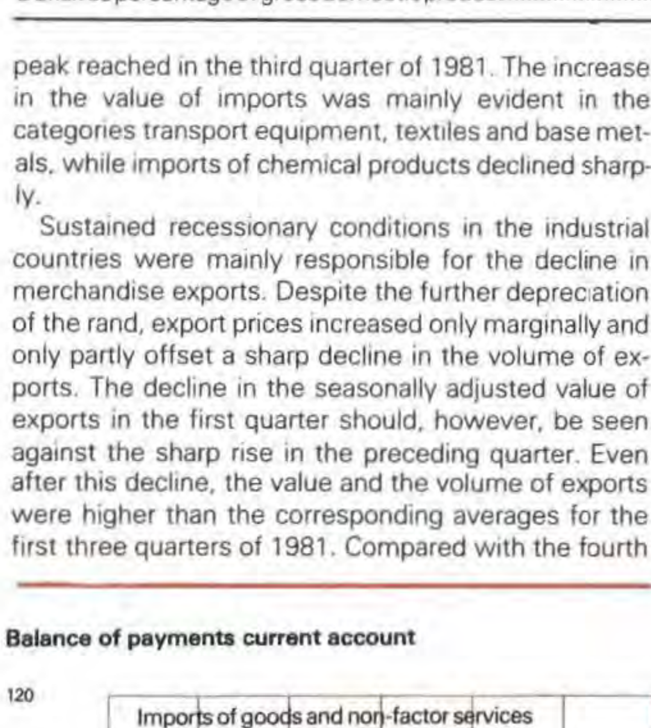
Current account of balance of payments
(Seasonally adjusted annual rate)
R millions

	1981				1982
	1st qtr.	**2nd qtr.**	**3rd qtr.**	**4th qtr.**	**1st qtr.**
Merchandise exports	8 840	9 000	8 720	10 760	9 430
Net gold output	8 490	7 610	8 380	8 870	6 970
Merchandise imports	−15 820	−18 230	−19 280	−19 360	−19 810
Net service and transfer payments	−2 780	−3 420	−3 680	−3 900	−3 290
Deficit on current account	**−1 270**	**−5 040**	**−5 860**	**−3 630**	**−6 700**
Deficit as percentage of gross domestic product	1,9	7,3	7,8	4,8	9,0

peak reached in the third quarter of 1981. The increase in the value of imports was mainly evident in the categories transport equipment, textiles and base metals, while imports of chemical products declined sharply.

Sustained recessionary conditions in the industrial countries were mainly responsible for the decline in merchandise exports. Despite the further depreciation of the rand, export prices increased only marginally and only partly offset a sharp decline in the volume of exports. The decline in the seasonally adjusted value of exports in the first quarter should, however, be seen against the sharp rise in the preceding quarter. Even after this decline, the value and the volume of exports were higher than the corresponding averages for the first three quarters of 1981. Compared with the fourth quarter of 1981, declines were recorded in exports of agricultural products, mineral products and processed food.

Balance of payments current account



Both volume and price declines were responsible for a marked decrease in the seasonally adjusted value of the net gold output in the first quarter of 1982. The price of gold on the London market fell from an average of US $420 per fine ounce in the fourth quarter of 1981 to an average of US $363 per fine ounce in the first quarter of 1982, or by about 13½ per cent. In terms of rand, the decrease was slightly lower at 11½ per cent, owing to the further depreciation of the rand against the US dollar. During the first five months of 1982 the price of gold averaged US $355 per fine ounce.

In contrast with changes in imports, exports and the net gold output, all of which contributed to the larger deficit on the current account of the balance of payments, net service and transfer payments to foreigners declined appreciably in the first quarter. Freight, merchandise insurance and dividend payments to foreigners were lower than in the preceding quarter, whereas investment income receipts from the rest of the world were notably higher. On the other hand interest payments to foreigners rose sharply in accordance with the increase in foreign debt.

Small net inflow of capital

A small net capital inflow of R59 million, excluding changes in liabilities related to reserves but including unrecorded transactions, was recorded in the first quarter. This net inflow was substantially less than the corresponding amount of R748 million in the fourth quarter of 1981. As shown in the accompanying table, a net long-term capital inflow of R672 million was almost offset by a net short-term capital outflow of R613 million. The net inward movement of long-term capital consisted mostly of foreign loans contracted by the Central Government, the South African Transport Services, the Department of Posts and Telecommunications, public corporations and the private sector. The net outflow of short-term capital during the first quarter was related to the somewhat lower domestic cost of trade financing, especially financing by means of bank overdrafts, in comparison with foreign costs.

During the first quarter the premium on forward dol-

Net capital movements not related to reserves
R millions

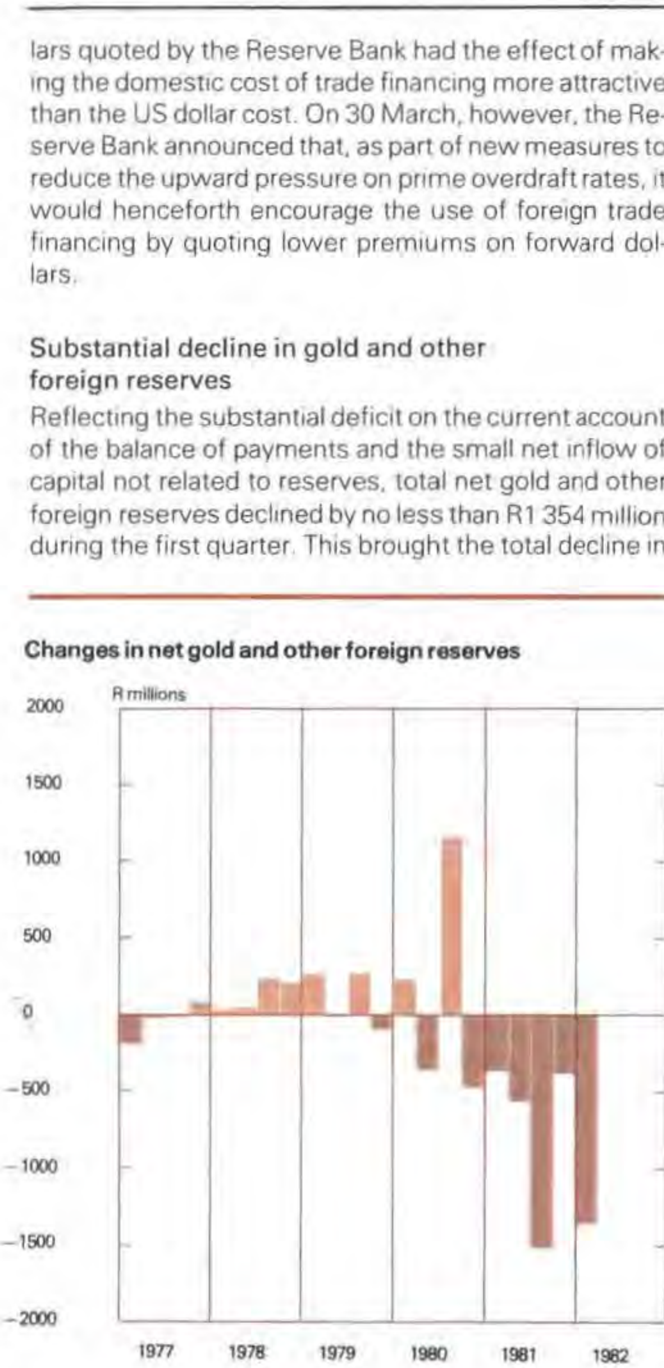
	1981				1982
	1st qtr.	2nd qtr.	3rd qtr.	4th qtr.	1st qtr.
Long-term capital					
Central government and banking sector	12	24	37	-67	285
Public corporations and local authorities	107	54	189	202	47
Private sector	31	51	-94	-189	-340
Total	150	129	132	-54	672
Short-term capital not related to reserves but including unrecorded transactions	-419	629	-257	802	-613
Total	**-269**	**758**	**-125**	**748**	**59**

lars quoted by the Reserve Bank had the effect of making the domestic cost of trade financing more attractive than the US dollar cost. On 30 March, however, the Reserve Bank announced that, as part of new measures to reduce the upward pressure on prime overdraft rates, it would henceforth encourage the use of foreign trade financing by quoting lower premiums on forward dollars.

Substantial decline in gold and other foreign reserves

Reflecting the substantial deficit on the current account of the balance of payments and the small net inflow of capital not related to reserves, total net gold and other foreign reserves declined by no less than R1 354 million during the first quarter. This brought the total decline in the net foreign reserves during the past eighteen months to R4 683 million. The short-term foreign liabilities of the banking sector rose by Rl 605 million during the first quarter. If this increase and negative valuation adjustments of R601 million, consisting mainly of the revaluation of the gold reserves at a lower price, are taken into account, the gross gold and other foreign reserves declined by only R350 million. At the end of March the gross foreign reserves amounted to R3 895 million. During April the gross gold and other foreign reserves of the Reserve Bank increased by R31 million, mainly because of the revaluation of the gold reserves at a higher price. The foreign exchange reserves of the Bank actually declined by R206 million.

Changes in net gold and other foreign reserves



Further depreciation of the rand

The effective exchange rate of the commercial rand remained almost unchanged during the first two months of 1982, but declined substantially during March and more moderately during April. From the beginning of May it decreased sharply and at the end of the month was 7,2 per cent below its level at the end of 1981. In particular, the rand depreciated markedly against the US dollar. It also depreciated sharply against the German mark, while the rates of depreciation against other major currencies were more moderate. From the end of December 1980 up to the end of May, the average value of the commercial rand declined by 20,1 per cent, while the depreciation of the rand against the US dollar amounted to no less than 31,0 per cent.

Changes in the exchange rate of the commercial rand
%

	Dec. 1981 to March 1982	Dec. 1981 to May 1982	Dec. 1980 to May 1982
Effective exchange rate	-4,4	-7,2	-20,1
US dollar	-9,0	-11,4	31,0
British pound	-2,3	-5,5	-8,0
German mark	-2,6	-8,0	-17,8
Swiss franc	-2,2	-2,2	-22,8
Japanese yen	2,0	-2,0	-17,5
French franc	-0,2	-4,9	-7,1

The financial rand also depreciated sharply during the first quarter of 1982, but then appreciated to the same extent during April and May. At the end of May the price of the financial rand was, therefore, exactly at its level at the end of 1981. The sharp depreciation of the commercial rand against the US dollar, however, narrowed the financial rand discount from 23,4 per cent at the end of 1981 to 13,7 per cent at the end of May.

Money and banking

Sharp increase in money supply

The strong monetary expansion of 1981 continued into 1982. The seasonally adjusted annual rate of increase in the broadly defined money supply (M2) accelerated from 20 per cent during the fourth quarter of 1981 to 41 per cent during the first quarter of 1982. Corresponding rates of increase in the narrowly defined money supply (M1) were 34 and 48 per cent, respectively. The substantial increase in M1 was accompanied by a marked change in its composition. As during the second half of 1981, non-interest-bearing demand deposits, or cheque deposits, with monetary banking institutions actually declined during the first quarter, while at the same time there was a substantial increase in interest-bearing call deposits with these institutions. The latter increase was mainly due to the relatively high rates of interest on such deposits and a generally larger liquidity preference that was related to expectations of an absolute or relative rise in long-term interest rates.

The renewed acceleration of the growth in M2, and more specifically in its M1 component, during the fourth quarter of 1981 and the first quarter of 1982, was accompanied by a significantly lower velocity of circulation. From the third quarter of 1981 to the first quarter of 1982 the velocity of circulation of M1 and M2, as measured by the ratio of the gross domestic product at current market prices to these two monetary aggregates, declined by 12 per cent and 9 per cent, respectively.

Monetary banks' short and medium-dated repurchase agreements with the non-bank private sector declined during the first quarter. If the amount of these agreements are included in the monetary aggregates, M2 and M1 increased at seasonally adjusted annual rates of 34 per cent and 45 per cent, respectively, during the first quarter.

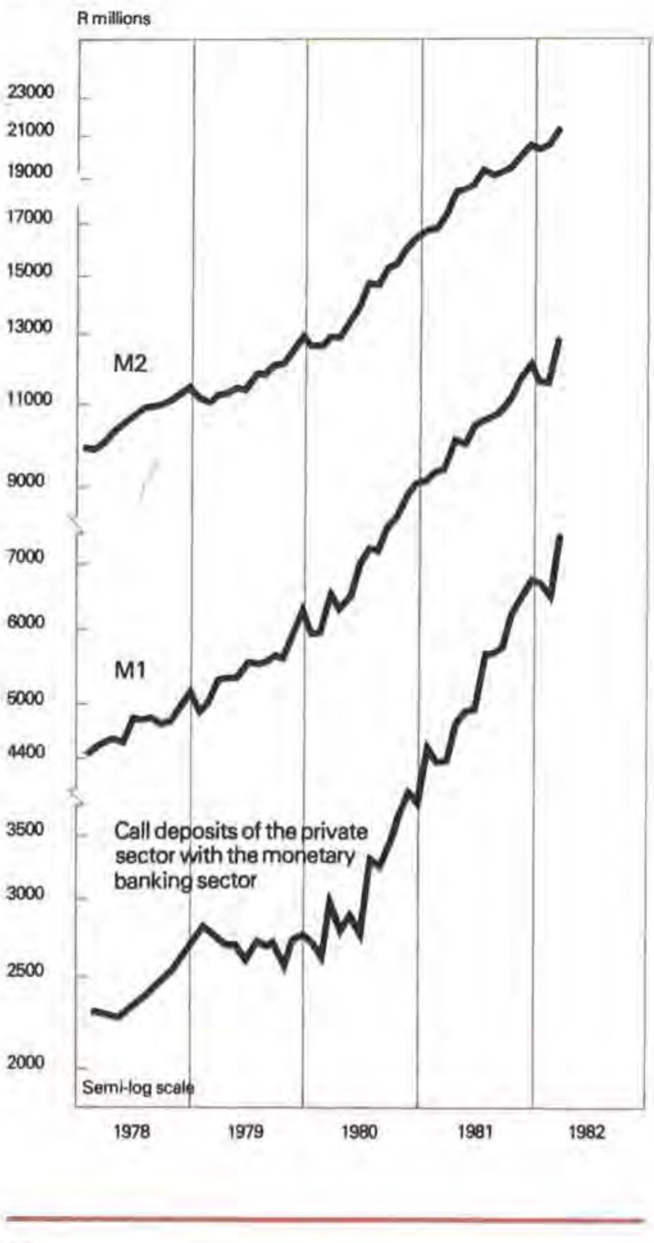
Causes of changes in M2
R millions

	Not seasonally adjusted			Seasonally adjusted	
	Year 1981	**4th qtr. 1981**	**1st qtr. 1982**	**4th qtr. 1981**	**1st qtr. 1982**
Net gold and other foreign reserves	−2 835	−389	−1 354	−246	−1 306
Claims on government sector:					
Gross claims	101	−239	−92	...	...
Government deposits (increase-, decrease+)	709	1 117	−1 124	...	...
Net claims	810	878	−1 216	656	−477
Claims on private sector	5 632	901	2 062	1 083	1 969
Long-term deposits (increase-, decrease+)	−134	−121	72	−248	172
Net other assets	617	7	1 317	...	...
Total changes in: M2	**4 090**	**1 276**	**881**	**930**	**1 765**
M1	2 876	1 193	626	768	1 117

Causes of changes in M2

As shown in the accompanying table, the main statistical "causes" of the further increase in M2 during the first quarter were a large increase in claims on the private sector and a decline in long-term deposits of the non-bank private sector with monetary banking institutions because of a shift towards shorter-term deposits offering higher rates of interest. In addition, there was a substantial increase in the net "other" assets of the monetary banking sector. Although a complete breakdown of this increase is not available, a major part of it consisted of exchange losses incurred by the Reserve Bank on forward exchange contracts. These losses are for the account of the Central Government and could be considered as claims on the government sector. The "other" assets of commercial banks also showed an appreciable rise. The decline in the net gold and other foreign reserves of the monetary banking sector continued to exert a strong contractionary influence on M2 and, in addition, net claims on the government sector declined moderately.

Money supply



Exceptionally large expansion of bank credit to the private sector

The seasonally adjusted annual rate of increase in bank credit to the private sector accelerated sharply from 23 per cent during the fourth quarter of 1981 to 41 per cent during the first quarter of 1982. A breakdown of the seasonally unadjusted increase during the first quarter, shows a notable further rise in hire-purchase credit, leasing finance and bills discounted. The latter declined during January and February but rose strongly in March, mainly as a result of the acquisition of bankers' acceptances by banking institutions after the announcement that required cash reserves with the Reserve Bank would be reduced from the end of March. In addition, "other" loans and advances expanded strongly during the first quarter, at a time when bank overdraft rates were lower than certain deposit and money market interest rates. This substantial rise was apparently due to "round-tripping" and the re-intermediation of credit transactions which had previously been contracted outside the banking system, and was probably also related to the financing of an involuntary build-up of inventories. Preliminary figures indicate, however, that the discounts, loans and advances of the five largest banking groups actually declined during April.

Changes in monetary banking sector's claims on the private sector
Not seasonally adjusted
R millions

	4th qtr. 1981	1st qtr. 1982
Reserve Bank, NFC and discount houses	−139	−93
Land Bank	275	−53
Other monetary banks:		
Deposits and investments	81	80
Bills discounted	62	318
Hire-purchase credit	699	349
Leasing finance	−93	252
Other loans and advances	16	1 209
Total	**901**	**2 062**

Moderate decline in bank liquidity

Banking institutions' excess holdings of liquid assets, which had increased appreciably during the last two months of 1981, declined moderately during the first quarter. Actual liquid asset holdings increased by R329 million, while required liquid assets rose by R540 million. The excess liquid asset ratio for all banking institutions declined from 3,4 per cent at the end of 1981 to 2,6 per cent at the end of March 1982. The increase in the banks' actual liquid asset holdings was due to an inflow of foreign funds and larger holdings of liquid bank-

Changes in discounts and advances of commercial banks, merchant banks and monetary general banks

kers' acceptances and liquid inter-bank deposits. This expansion of the banks' liquidity base was partly offset by a decline in net Reserve Bank credit to the government sector, after a sharp increase in this form of Reserve Bank credit had been an important cause of the considerable expansion of the liquidity base towards the end of 1981.

Money market

Conditions in the money market tightened considerably towards the January month-end and remained tight throughout the ensuing period up to early April. Subsequently, conditions were generally easier and tightened only slightly over the April and May month-ends. Severe shortages of funds were experienced over the January and February month-ends and during the larger part of March, before measures were introduced to help alleviate the tight market situation. The tight conditions up to the end of March were caused mainly by a decline in the net gold and other foreign reserves of the Reserve Bank and by the flow of funds to the Government over the January and February month-ends, together with a low level of government spending towards the end of the fiscal year. From April the customary higher level of government spending at the beginning of the new fiscal year contributed materially to an easing of the market.

Under these conditions, the discount houses remained indebted to the Reserve Bank from the end of December up to early April. The amount of accommodation increased substantially over the tight January and February month-ends and remained at a high level during most of March. On 30 March the Reserve Bank announced that, in order to alleviate the tight money

Short-term interest rates

market situation and to reduce the upward pressure on the banks' prime overdraft rates, the supplementary minimum cash reserves, which banks are required to hold with the Reserve Bank against their short-term liabilities to the public, would be reduced. In addition, the Reserve Bank would encourage the increased use of foreign credits by quoting lower premiums on forward dollars. The immediate effect of these measures was to reduce the amount of accommodation to discount houses from R983 million on 26 March to R428 million at the end of March. By 8 April all accommodation had been repaid. At the end of April and the end of May the discount houses were again accommodated by R494 million and by R473 million, respectively.

In addition to accommodating the discount houses, the Reserve Bank provided direct accommodation to several banking institutions at the end of February and during part of March. However, by 26 March this accommodation had been fully repaid.

Money market interest rates rose sharply from about the middle of January up to the end of March, before declining slightly in early April. During the remainder of April these rates remained fairly stable, but declined again slightly in May. The rate on three-month bankers' acceptances, for example, increased from 14,9 per cent on 15 January to 19,0 per cent on 26 March. On 2 April it decreased to 17,1 per cent and after having remained fairly stable during the rest of the month, it declined further to 16,7 per cent on 28 May. The Treasury bill tender rate rose consistently from 14,04 per cent on 31 December 1981 to 15,84 per cent on 19 March. Subsequently, it fluctuated around this level and amounted to 15,96 per cent on 28 May.

Open-market operations

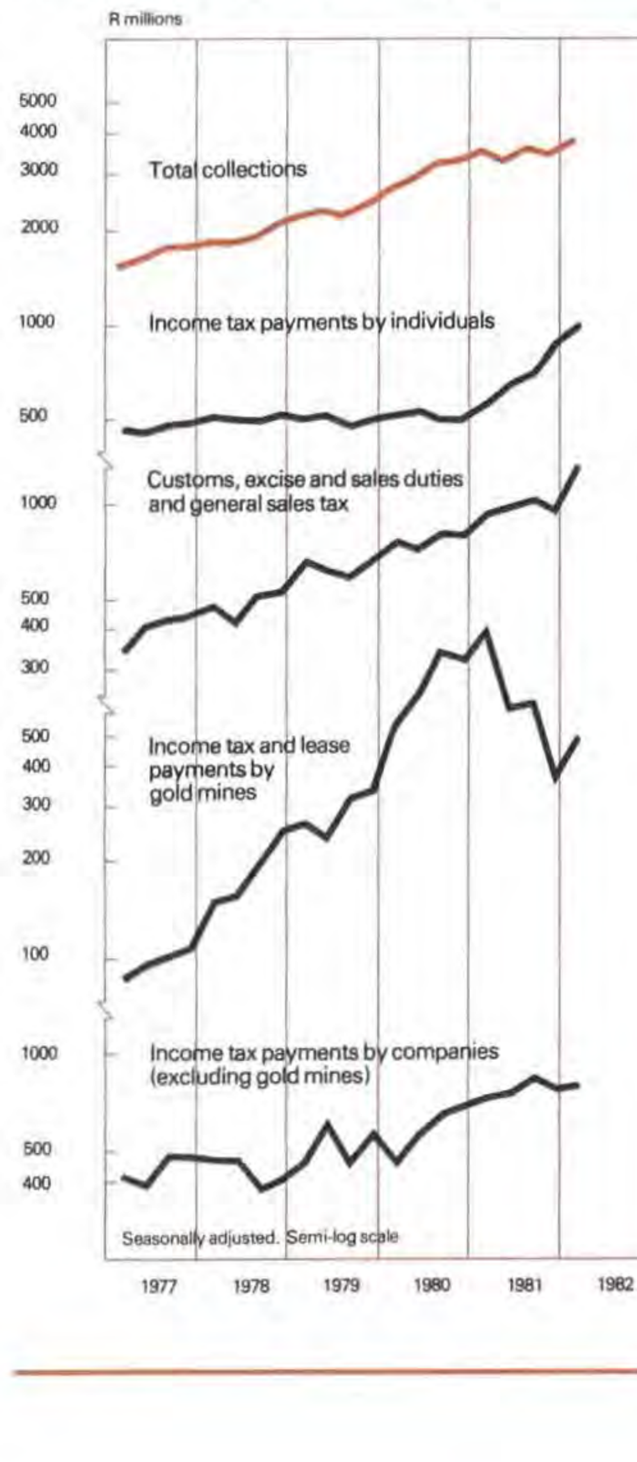
Open-market sales of government stock by the Reserve Bank during the first quarter amounted to R54 million. In April government stock to the value of R300 million, similar to that issued on a tender basis on 7 April, was issued on tap to the Reserve Bank. The Reserve Bank's open-market sales of government stock during April amounted to R260 million. In addition, special Treasury bills amounting to R37 million, maturing at the end of August, were sold by the Bank. During May further tap issues of government stock, totalling R500 million, were made to the Bank. The Bank's open-market operations during this period consisted of sales of medium and long-term government stock amounting to R438 million.

Government finance

Substantial decline in Exchequer's net indebtedness to banking sector during last quarter of 1981/82 fiscal year

Exchequer Account* issues during the last quarter of the 1981/82 fiscal year, i.e. the three months January to March 1982, were as much as 25 per cent higher than in the corresponding quarter of the preceding fiscal year. At the same time, however, tax and other revenue col-

Revenue collections — State Revenue Fund



*For the purpose of this analysis, the Exchequer Account was adjusted to take account of changes in the cash balance on, and the net borrowing from, the Paymaster-General Account and to incorporate the Stabilization Account.

lections reached their usual seasonal peak and were in fact 9 per cent above the exceptionally high peak in the corresponding quarter of the 1980/81 fiscal year. Revenue, in fact, exceeded issues by R237 million.

Overall government receipts were increased further by the non-bank private sector's net investment of R282 million in government securities, mainly by means of subscriptions to new issues and open-market purchases from the Reserve Bank. In addition, a net amount of R86 million was borrowed from the Public Debt Commissioners, while net drawings on foreign loans amounted to R302 million, including a drawing of R130 million on the International Monetary Fund. These borrowing operations, together with the Exchequer Account surplus, had the effect of reducing the Treasury's net indebtedness to the monetary banking sector by R907 million. This reduction was equal to the increase in the Treasury's net indebtedness to the monetary banking sector during the first nine months of the fiscal year.

Government stock issues

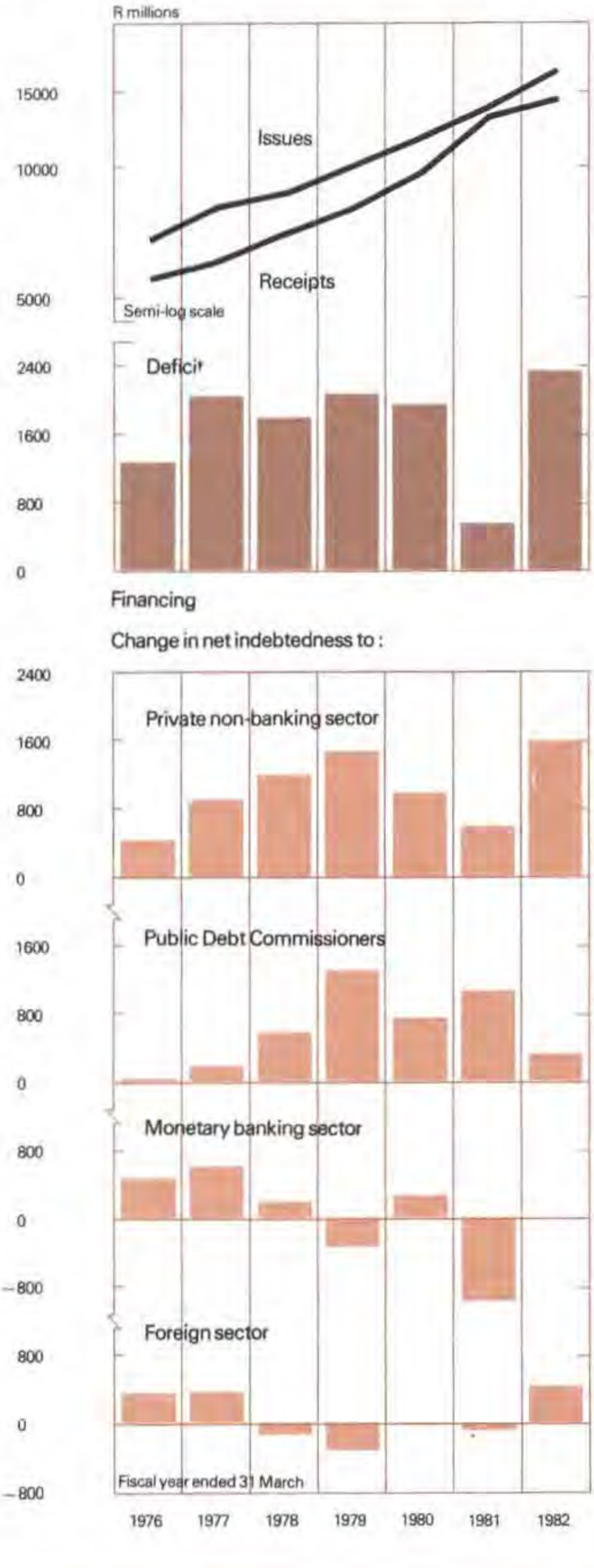
As in February, new government stock was issued on a tender basis during April. The average yields on the new series of stock with maturities of three, five and ten years were 15,10 per cent, 15,16 per cent and 14,72 per cent, respectively. These issues were well supported and applications of R1 036 million were received for the new stock of R400 million offered for subscription. In addition to the new issues, the Reserve Bank sold R260 million of the same stock, issued to it on tap by the Treasury. Despite the new issues and the Reserve Bank's open-market sales of government stock, government deposits declined substantially during April, reflecting a strong seasonal increase in government expenditure during this month.

Financial results for the 1981/82 fiscal year

Although central government revenue was estimated in the 1981/82 Budget to decline by 1 per cent, an increase of 8 per cent was actually recorded in the fiscal year. As had been foreseen, income tax and mining lease payments by gold mining companies declined sharply during 1981/82, namely by about R1 500 million or 41 per cent, as a result of the decline in the price of gold and an increase in production costs. This revenue loss was, however, more than compensated for by a considerable increase in other revenue. Reflecting the further sharp rise in domestic expenditure, imports, non-mining company profits and salaries and wages, receipts of customs and excise duties and income tax payments (excluding those by gold mines) rose by 37 per cent and 35 per cent, respectively, compared with original Budget estimates of 6 per cent and 20 per cent, respectively.

Exchequer issues to government departments during the 1981/82 fiscal year exceeded those in the pre-

Exchequer Account



State Revenue Fund — Revenue collections

	1981/82 Budget		Actual collections		
	R millions	Percentage change[1]	1980/81 R millions	1981/82 R millions	Percentage change
Indirect taxes[2]					
Customs duties[3]	850	16,0	733	1 185	61,7
Excise duties	1 385	11,4	1 243	1 506	21,2
General sales tax and sales duty	2 150	30,0	1 654	2 126	28,5
Total	4 385	20,8	3 630	4 817	32,7
Income tax and lease payments by gold mines	2 160	-40,5	3 633	2 131	-41,3
Other income tax payments	5 688	20,3	4 727	6 401	35,4
Other collections	1 652	-11,5	1 866	1 810	-3,0
Sub-total	13 885	0,2	13 856	15 159	9,4
Less transfers to neighbouring countries	725	32,8	546	733	34,2
Total revenue collections	**13 160**	**-1,1**	**13 310**	**14 426**	**8,4**

[1]Compared with actual collections during the 1980/81 fiscal year.
[2]Including amounts transferable to neighbouring countries in terms of Customs Union Agreements and to the Central Revenue Fund of South West Africa.
[3]Including surcharge on imports.

ceding fiscal year by 21 per cent. Original Budget estimates provided for an increase of 17 per cent. Despite the sharp rise in expenditure, the higher than expected revenue resulted in a deficit before borrowing of only R2 342 million, compared with the R2 707 million provided for in the Budget.

In financing this deficit, R329 million was obtained from the Public Debt Commissioners on a net basis. The Commissioners' gross new investment in government securities amounted to R1 199 million, but a substantial part of this amount represented the reinvestment of the proceeds of stock sold in the market. The non-bank private sector's contribution to the financing of the Exchequer Account deficit amounted to R1 588 million, including appreciable open-market purchases of government stock from the Reserve Bank. Net foreign borrowing totalled R425 million, of which R130 million consisted of a drawing on the International Monetary Fund. As mentioned earlier, the Treasury's net indebtedness to the monetary banking sector remained unchanged during the fiscal year as a whole; an increase during the first nine months of the fiscal year was exactly offset by a decline during the last three months of this period.

The 1982/83 Central Government Budget

In his presentation of the 1982/83 Budget, the Minister of Finance stated that while he was fully aware that the economy had entered the downward phase of the business cycle and that the rate of real economic growth would almost certainly be lower in the coming fiscal year, the decline in the gold price and other adverse external developments of recent months ruled out any possibility of "reflation" or "stimulation" of the economy at that time. On the contrary, the balance of payments adjustment process needed strong support from fiscal and monetary policies, even if this meant restraining demand at a time of slower real growth. The existing economic situation, therefore, called for firm control over government spending, the liquidity base of the banking system and the money supply.

The Minister was of the opinion that in recent months adjustments to the adverse external developments had come about largely via inflation and currency depreciation on the one hand, and increases in interest rates on the other. He stated that the Government considered it essential that fiscal policy should play its proper part in assisting the economy to make the necessary further adjustments. Recognition needed to be given to the "trade-off" which existed in the prevailing situation between higher interest rates, higher tax rates (or lower government spending) and exchange rate depreciation. In framing the Budget proposals, therefore, due consideration had been given to the need to achieve the optimal combination of tax rates, interest rates and spot and forward exchange rates required for dealing with the existing economic situation.

Against this background, the Budget sought to comply with three minimum requirements. Firstly, the increase in government spending would be restricted as much as possible without disrupting the provision of essential services. Secondly, in order to curb monetary demand and to prevent undue upward pressure on interest rates, the "deficit before borrowing" as a percentage of gross domestic product would be reduced to well below its average of 3,4 per cent over the past 22 years. Thirdly, this deficit would be financed in such a manner that not only the Exchequer, but also the government sector as a whole, would be able to avoid a net recourse to bank credit.

Aggregate expenditure during the 1982/83 fiscal year was estimated at R18 238 million, or 11,5 per cent more than the revised estimates of expenditure in 1981/82. Total revenue in 1982/83 was estimated at R15 858 million, an increase of 11 per cent in comparison with expected revenue receipts in 1981/82. Tax proposals for 1982/83 included the incorporation of the existing surcharge of 5 per cent on company tax into the basic rate of 40 per cent and the introduction of a surcharge of 10 per cent on the new basic rate of 42 per cent. The surcharge on income tax payable by gold and diamond mining companies was raised from 5 to 15 per cent. In addition, a 5 per cent compulsory loan levy, based on personal income tax, was imposed on individual taxpayers.

The deficit before borrowing in 1982/83 was estimated at R2 380 million, or 2,8 per cent of gross domestic product. Together with loan redemptions of R1 246 million, the total financing requirement came to R3 626 million. It was anticipated that this amount would be financed as follows:

	R millions
Foreign loans	250
Domestic loans:	
Public Debt Commissioners	1 290
Re-investment of maturing stock issues	614
New stock issues	800
Non-marketable securities	550
Loan levy on individuals	115
Use of available balances	7

Capital market

Substantially smaller increase in holdings of longer-term funds with non-contractual savings institutions

Reflecting the general scarcity of funds in the economy and levels of short-term interest rates that were higher than those of long-term rates, the seasonally adjusted holdings of longer-term funds with banking institutions, building societies, government saving schemes and participation mortgage bond schemes increased by only R92 million during the first quarter of 1982. During 1981 these holdings showed an average quarterly increase of R598 million.

Seasonally adjusted holdings of savings and long-term deposits with bankimg institutions actually declined by R73 million during the first quarter, compared with an average quarterly increase of R105 million during 1981. Building societies experienced an appreciable net outflow of funds during January and February, but their shares and deposits nevertheless showed a seasonally adjusted increase of R161 million during the first quarter as a whole. This net inflow of funds was considerably smaller than the quarterly average of R397 million in 1981. Government saving schemes recorded a net outflow of funds of R34 million during the first quarter, while funds invested with participation mortgage bond schemes increased by R38 million during this period.

As a result of active competition for funds, deposit interest rates rose further from the beginning of 1982. The accompanying table shows the increase in the more important rates during 1981 and the first five months of 1982.

Selected interest rates[1]
%

	1980 31 Dec.	1981 31 Dec.	1982 31 May
Ordinary savings deposits	3,50	4,00	4,00
Special savings deposits	5,50[2]	8,25[3]	8,75[3]
Fixed deposits:			
12 months	8,50	11,50	16,00
24 months	9,50	13,50	15,50
36 months	9,50	13,25	14,00
60 months	9,50	14,00	14,00
Building society shares:			
Indefinite period paid-up	8,00	11,50	14,00
Tax-free shares	7,00	8,75	9,50
Post Office Savings Bank certificates	7,00	8,75	9,50
National Savings Certificates[4]	7,50	9,00	9,00
Tax-free Treasury Bonds	7,00	8,75	9,50

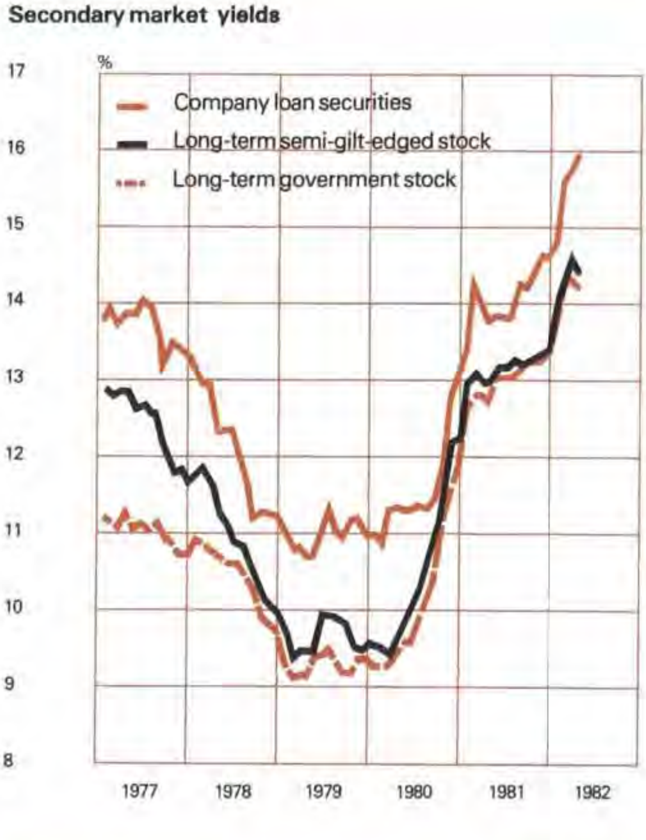
[1]Predominant rates.
[2]Deposits of less than R20 000.
[3]Deposits of up to R15 000.
[4]Average rate over full period of investment.

Levelling-off of sharp rise in fixed-interest security yields

The sharp rise in long-term fixed-interest security yields from March 1980 continued during the first quarter of 1982, but tended to level off during April and May. On the one hand, the fixed-interest security market was influenced by the smaller than expected borrowing requirement of the Central Government for the fiscal year 1982/83 and by the postponement of long-term stock issues by some public sector borrowers. On the other hand, long-term investors with a substantial cash inflow and already large holdings of money market investments displayed more interest in long-term fixed-interest securities as an investment outlet. Generally, investment in fixed-interest securities was encouraged by weaker expectations of a further rise in long-term interest rates and less favourable opportunities for further investment in the equity and real estate markets.

Greater interest in fixed-interest securities and portfolio adjustments were reflected in a sharp rise in the value of gilt and semi-gilt-edged securities traded on the stock exchange. The turnover in these securities in the first quarter of 1982 was more than double the amount in the fourth quarter of last year and also exceeded the previous record in the second quarter of 1981. The secondary market yield on long-term government stock rose from an average of 13,33 per cent in December 1981 to 14,30 per cent in March and amounted to 14,15 per cent in May. The corresponding change in the long-term yield on semi-gilt-edged stock of the highest grade was from 13,41 to 14,51 and 14,19 per cent. The yield on company loan securities increased from 14,58 per cent in December 1981 to 15,68 per cent in March and to 15,79 per cent in May.

Secondary market yields

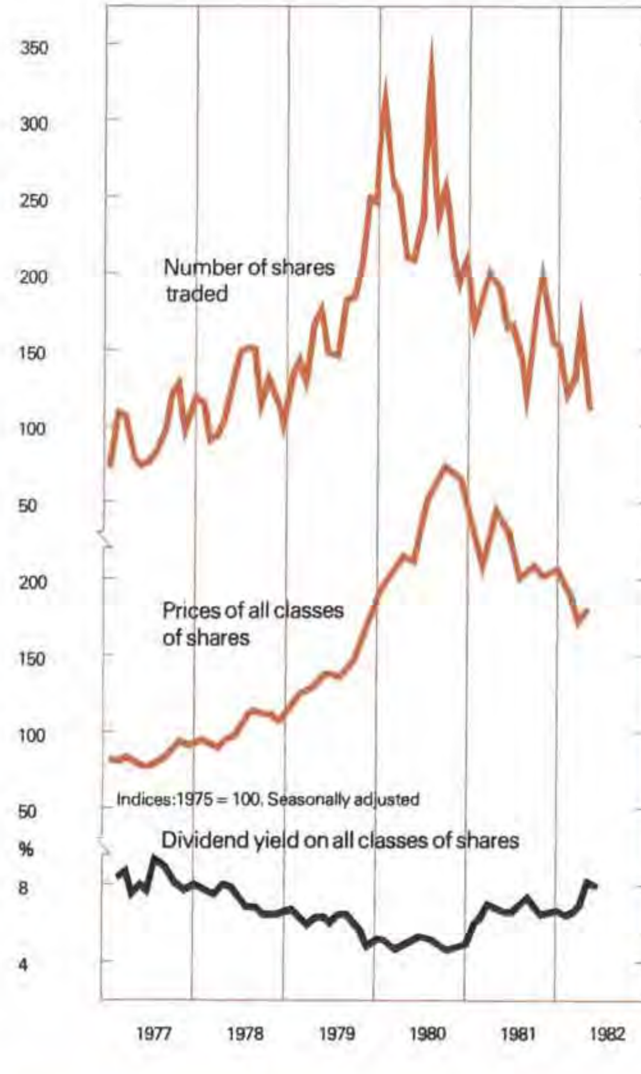


Decline in turnover and prices in share market

The sustained buoyancy of the share market during 1981 and January 1982 was followed by a sharp decline in turnover and prices during the three months from February to April. Factors contributing to this downward adjustment included a further decline in the price of gold, a further weakening of metal, mineral and other commodity prices in international markets, and a greater awareness of an imminent slow-down of economic activity in South Africa.

The average monthly turnover, in terms of the number of shares traded on the stock exchange, was 19 per

Stock exchange



cent lower during the first four months of 1982 than during the fourth quarter of 1981. Share prices were on average 20 per cent lower in April than in December 1981. This decline was evident in all classes of shares. Mining share prices fell by 23 per cent, while decreases of 20 per cent and 17 per cent were recorded in the prices of financial shares and industrial and commercial shares, respectively. Reflecting the sharp decline in share prices, the average dividend yield on all classes of shares rose from 6,54 per cent in December 1981 to 8,08 per cent in April 1982.

Restrained activity in mortgage market, but high level of activity in real estate market

The building societies' mortgage lending continued to be restrained by the general scarcity of funds. Nevertheless, the seasonally adjusted amount of new mortgage loans granted during the first quarter, namely R473 million, was slightly in excess of the quarterly average of R425 million in 1981. The seasonally adjusted amount of new mortgage loans actually paid out, however, fell from a quarterly average of R821 million in 1981 to R486 million in the first quarter. In order to maintain the amount of new mortgage lending at a fairly high level, the societies reduced their holdings of prescribed investments by R172 million during the first quarter.

The effect of the higher deposit interest rates on the margin between the building societies' borrowing and lending rates induced the societies to raise their mortgage rates by 1 per cent in February. After this increase, the home mortgage rates of the societies ranged from 13,25 to 15,25 per cent. The mortgage rate of participation mortgage bond schemes was also adjusted upwards from 14,9 per cent at the end of 1981 to 17,5 per cent at the end of April.

Owing to a high level of turnover in non-residential buildings, stemming from increased institutional investment in real estate, the seasonally adjusted value of real estate transactions rose to a new record level of R1 712 million in the first quarter. This figure was notably higher than the corresponding figure of R1 458 million in the preceding quarter and the quarterly average of R1 535 million in 1981.

Building societies