Quarterly economic review

Introduction

The *downswing* in the South African economy, which had started in March 1989, continued in the first five months of 1991. The economy has, therefore, now been in an economic downswing for 27 months. This is considerably longer than the average length of 17 months of such cyclical contractions since the beginning of the 1940s. Moreover, the composite leading business cycle indicator as yet does not show any signs that the economy is approaching the end of the downturn.

Although longer than most previous periods of contraction, the current downswing has been *relatively mild* - especially in comparison with the previous two recessionary phases. This is not only clearly illustrated by the extent of the downward movement of the composite coincident business cycle indicator, but also by various other indicators of real economic activity. In fact, the coincident business cycle indicator declined by only 5½ per cent in the first seven quarters of the current downswing, compared with 20½ per cent over the corresponding period of the 1984/86 downward phase and 19 per cent from the peak to the trough (six quarters) of the downswing of 1981/83.

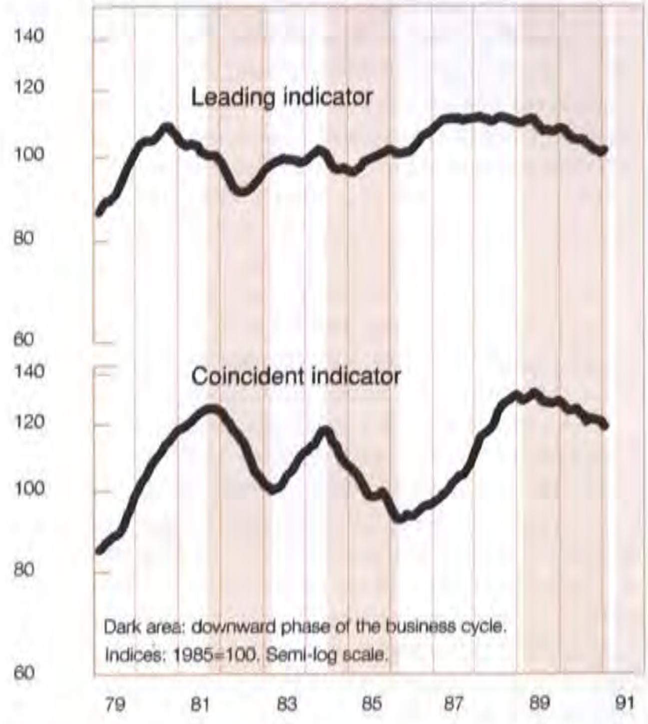
This relative mildness of the current downswing was to a large extent due to the fact that the largest part of it took place during a period of prolonged world economic growth leading to a continuous and fairly vigorous expansion in the volume of South African exports. In addition, real private consumption and real fixed investment expenditure have remained fairly buoyant. In fact, real private consumption expenditure has continued to increase throughout the current downswing and real fixed investment declined by an annualised rate of only 1 per cent from the upper turning-point of the cycle to the first quarter of 1991.

As explained in detail in previous issues of this *Quarterly Bulletin*, the buoyancy of real private consumption expenditure was mainly due to relatively high wage increases, a redistribution of income to lower-income groups with a high propensity to consume, the unwillingness of consumers to accept lower living standards, and the replacement demand for durable consumer goods. The relatively high level of real fixed investment in the current downswing was, in turn, mainly related to the ongoing high level of consumption expenditure, investment spending for replacement purposes and the development of the Mossgas project.

However, recently a slightly sharper and more dispersed downturn in economic activity became discernible. This was probably largely the result of lower economic growth in some industrialised countries, which resulted in a levelling-off in the growth of South African exports. Fortunately, this downturn in world economic growth is generally expected not to last very long. In addition, the moderate deepening of the recession could also be attributed to slower growth in real private consumption expenditure probably because of sustained decreases in personal disposable income per capita, the already low level of personal savings, an increasing reluctance to make use of more credit and a postponement of expenditure on durable goods by Black households in view of the violence in Black townships.

Despite these factors, the real gross *domestic product* declined by only 1 per cent in the first quarter of 1991, which broadly equalled the rate of contraction in the year 1990. The first quarter of 1991 was the sixth consecutive quarter in which an actual contraction in real output was reported. This further

Business cycle indicators



contraction in real gross domestic product occurred mainly in mining, manufacturing and wholesale and retail trading activities; small increases, however, were still recorded in the real value added by agriculture, financial services, general government and transport enterprises.

Preliminary estimates for the first quarter of 1991 also show that total real gross *domestic expenditure* increased substantially from its relatively low level in the previous quarter. In particular, a further – although lower – rate of increase was recorded in real spending by households on consumer goods and services, while real government consumption expenditure rose significantly. Even more important was the considerably smaller decline in inventories, after substantial destocking had taken place in the fourth quarter of 1990. On the other hand, real gross domestic fixed investment continued to decline in the first quarter of 1991, in accordance with the low level of economic activity and the availability of excess production capacity. However, the rate of decrease in real fixed investment receded from a quarter-to-quarter annualised figure of 5½ per cent in the fourth quarter of 1990 to only about 3½ per cent in the first quarter of 1991.

The higher domestic demand and lower domestic production found expression in a substantial decline in the surplus on the *current account of the balance of payments* from a seasonally adjusted and annualised rate of R9,7 billion in the fourth quarter of 1990 to R1,5 billion in the first quarter of 1991. As pointed out in more detail below, this change in the surplus from a very high to a very low quarterly figure was partly due to exceptional circumstances largely related to the crisis in the Middle East. It therefore seems more appropriate to compare the *average* surplus on the current account over the past *two* quarters (which amounted to a seasonally adjusted and annualised figure of R5,6 billion) with the R4,2 billion surplus of the third quarter of 1990. Nevertheless, the substantial deterioration which occurred on the current account during the first quarter of 1991 was the result of a sharp increase in the volume and a moderate rise in the prices of imported goods, combined with decreases in the values of merchandise exports and net gold exports.

The net outflow of capital not related to reserves of R1,8 billion in the fourth quarter of 1990 changed to a net *inflow of capital* of approximately R0,8 billion in the first quarter of 1991. This inflow of capital was mainly related to the higher value of imports, resulting in an increase in trade and project financing from trading partner countries. Public corporations also continued to be net borrowers of long-term funds on foreign capital markets. At the same time further repayments were made on foreign debt in terms of the standstill arrangements with creditor banks as well as on maturing bearer bonds and notes.

The net inflow of capital and the small surplus on current account were responsible for an increase of R1,8 billion in the total net *foreign reserves* in the first quarter of 1991. The improvement in the foreign reserves enabled the Reserve Bank to repay nearly all of its remaining foreign liabilities related to reserves. Despite these debt redemptions, the *total* gross gold and other foreign reserves still increased by R1,4 billion in the first quarter of 1991 to a level of R8,7 billion at the end of March. In April-May the gross foreign reserves held by the Reserve Bank declined moderately again by R99 million.

These favourable developments on the balance of payments were accompanied by a relatively stable effective *exchange rate* of the rand. However, the rand depreciated considerably against a very strong US dollar, which contributed to a substantial narrowing of the financial rand discount from about 25 per cent at the beginning of 1991 to 14,1 per cent on 31 May.

The lower domestic production also resulted in a sharp decline of the rate of growth in *employment* in the non-agricultural sectors. At the same time the rate of increase in nominal wages per worker declined marginally, but it still amounted to 16,7 per cent in 1990, which was notably in excess of the inflation rate. Moreover, the higher real wage per worker was accompanied by a substantial decrease in non-agricultural labour productivity, resulting in a sharp increase in real unit labour costs.

The continuing relatively high rates of increase in labour costs remained an important inhibiting factor in bringing the *inflation rate* in South Africa more in line with those of major trading partner countries. In addition, the crisis in the Persian Gulf also caused both the production and the consumer price indices to rebounded to higher levels in the second half of 1990. Petrol and related fuel price reductions in November and December 1990 were subsequently followed by a downward fluctuating movement in the rate of increase in prices during the first four months of 1991. The levels of the rates of increase in the consumer and production prices in April 1991 was nevertheless still higher than at their lower turning-points in July 1990.

On the *monetary front*, developments were influenced by the coming into force of the Deposit-taking Institutions Act on 1 February 1991. First in anticipation of the Act and later as a result of changes introduced by the Act, repurchase agreements (not included in the monetary aggregates) were converted into ordinary deposits (included in the monetary aggregates). These conversions therefore led to an acceleration in the statistically measured growth of the money supply and bank credit as from November 1990, which became more pronounced in February 1991. They were also mainly responsible for the fact that in February 1991 M3 moved above the upper limit of the new money supply guidelines of 8 to 12 per cent for the 1991 "guideline" year.

Developments in the *financial markets* were characterised by a considerable easing of the money market during the first five months of 1991, despite short-term intervention by the Reserve Bank to drain excess liquidity. Shortly after the reduction of the Bank's accommodation rates as from 11 March 1991, short-term rates started moving downward again.

Trading activity in the secondary *capital market* also recovered considerably, but the amount of funds raised by the public sector from new issues in the primary market declined sharply. The value of real estate transactions remained on a high level and the decline in the average level of share prices since the beginning of 1990 was halted; most share prices, in fact, strengthened markedly during the period February to May 1991. Capital market yields and lending rates fluctuated along a slightly downward trend during the first quarter of 1991, while deposit rates (with the exception of tax-free investments) were reduced by only ½ percentage point in April.

In the area of *government finance*, the rate of increase in Exchequer issues accelerated substantially in the March quarter of the fiscal year. At the same time the rate of increase in Exchequer receipts also rose considerably. This resulted in a deficit before borrowing and debt repayments of R2 170 million, compared with a surplus of R1 408 million in the first quarter of 1990.

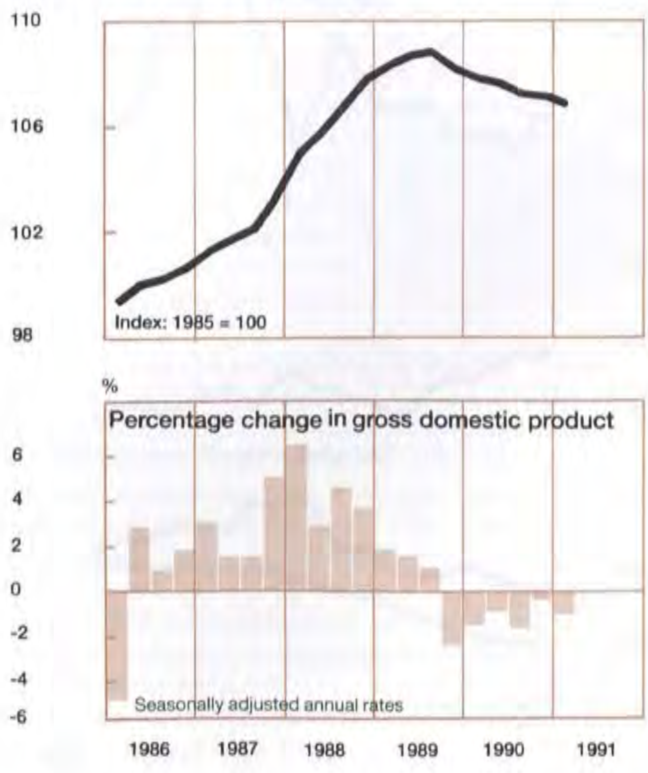
Domestic economic developments

Domestic production

The relative mildness of the current downturn in economic activity referred to in the introduction is clearly illustrated by developments in domestic production. After real gross domestic product had increased by 4 per cent in 1988, it still rose by 2 per cent in 1989 – the first calendar year falling mainly in the downward phase of the business cycle. Ten months of economic contraction were then followed by a decline of 1 per cent in real output in 1990. This decline was largely concentrated in the primary sectors (especially agriculture). Although manufacturing production also declined moderately during the year, the value added by the non-primary sectors declined by less than ½ per cent in 1990.

In the first quarter of 1991 real gross domestic product fell further at an annualised rate of 1 per cent. Domestic production has therefore now declined for six consecutive quarters, and available statistics are as yet not indicating any turn-around in the near future. With the exception of the fourth quarter of 1989, when a substantial decline in agricultural production was mainly responsible for a

Real gross domestic product

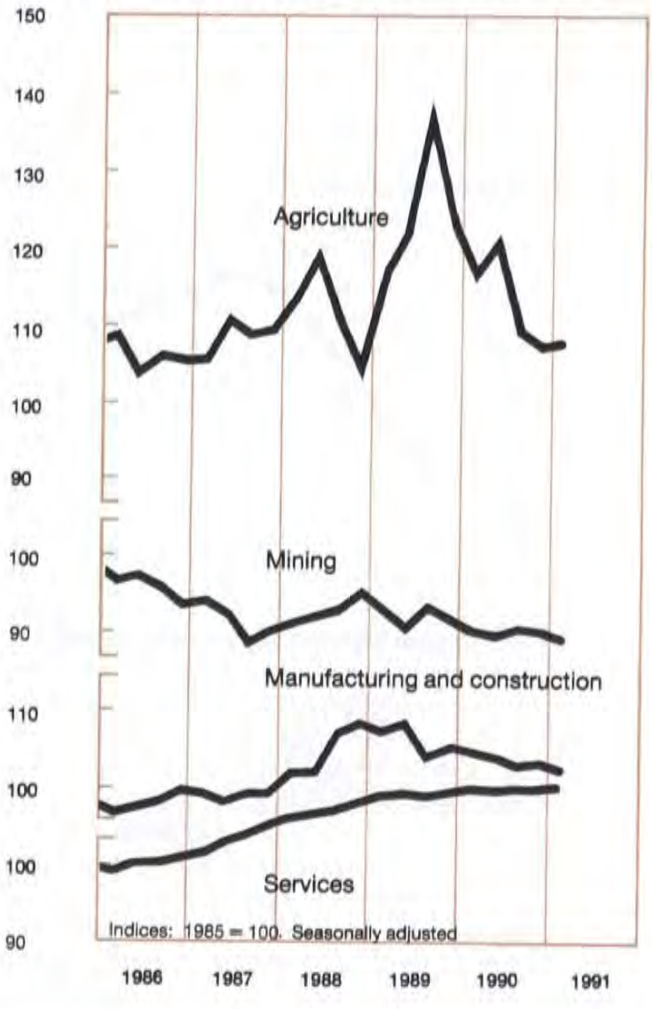


decline in real output at an annual rate of 2½ per cent, the subsequent annualised rates of decline varied between ½ and 1½ per cent in the next five quarters.

Sectoral production estimates show that the further decline in real gross domestic product in the first quarter of 1991 was particularly evident in the real value added by the *mining* sector. This was due to a substantial decline in gold production and a lacklustre performance by the rest of the mining industry. The gold-mining industry was adversely affected by the deteriorating dollar price of gold. Other factors such as the high level of production costs, a decline in payable ore reserves and rationalisation programmes to minimise unprofitable operations, led to a drop in the throughput of ore which more than offset a slight increase in the average grade of ore milled in the first quarter of 1991.

On the other hand, *agricultural* production improved marginally in the first quarter; this improvement stemming mainly from an increase in horticultural production. This modest revival in agricultural output occurred after a sharp declining trend in the previous five quarters; as a result, value added by agriculture in the first quarter of 1991 was still 22 per cent below the high point of the third quarter of 1989. The net outcome of these developments was a total contraction at an annual rate of some 2 per cent in the primary sector's total real output in the first quarter of 1991.

Components of real gross domestic product



The real value added by the *secondary sector* also contracted in the first quarter of 1991, at an annualised rate of some 3 per cent. This followed a rate of *increase* of 5 per cent in the previous quarter. Accordingly, real output in the secondary sector in the first quarter of 1991 was only ½ per cent lower than in the corresponding quarter of 1990. Declines were recorded in all the main sub-sectors of the secondary sector in the first quarter of 1991, i.e. in manufacturing, construction, and electricity, gas and water.

Output decreases in *manufacturing* were recorded mainly in the sub-sectors clothing, non-metallic mineral products, base metals, and machinery and transport equipment, while the production of food, paper and printing and chemical products increased. The decline in the real output of the *construction* industry reflected mainly the downturn in residential construction and the generally sluggish conditions prevailing in civil engineering.

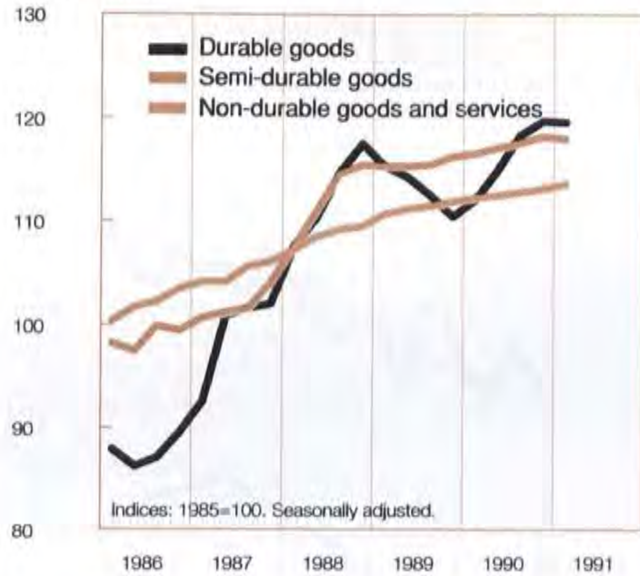
Real value added by the *tertiary sectors* is estimated to have increased slightly in the first quarter of 1991, i.e. at an annualised rate of approximately ½ per cent. However, lower wholesale and retail trade sales resulted in a marginal decline in the real output of commerce. In the case of the other sectors, namely transport, finance, general government, and community, social and personal services, positive growth rates varied between ½ and 2 per cent.

Domestic expenditure

Real gross domestic expenditure decreased even before the start of the downturn in economic activity, and contracted for four consecutive quarters from the second quarter of 1989 to the first quarter of 1990. In the middle quarters of 1990 this contraction was, however, reversed and aggregate real domestic expenditure increased at annualised rates of approximately 3 and 4 per cent in the second and third quarter respectively. This was mainly the result of sustained moderate growth in real private consumption expenditure and a slowdown in the decumulation of inventories. Notwithstanding the continuing high level of total real consumption expenditure, real gross domestic expenditure then reversed its course again and decreased sharply in the fourth quarter of 1990 as a result of a further

Real gross domestic expenditure

Components of real private consumption expenditure



decline in real gross domestic fixed investment and a substantial decumulation of inventories.

Current estimates suggest that the quarter-to-quarter change in aggregate real gross domestic expenditure turned positive again in the first quarter of 1991. This could be attributed in particular, to further increases in real consumption expenditure by households and the general government. In addition, the decline in real stocks slowed down significantly, while the rate of decline in real gross domestic fixed investment eased to some 3½ per cent from 5½ per cent in the third and the fourth quarter of 1990.

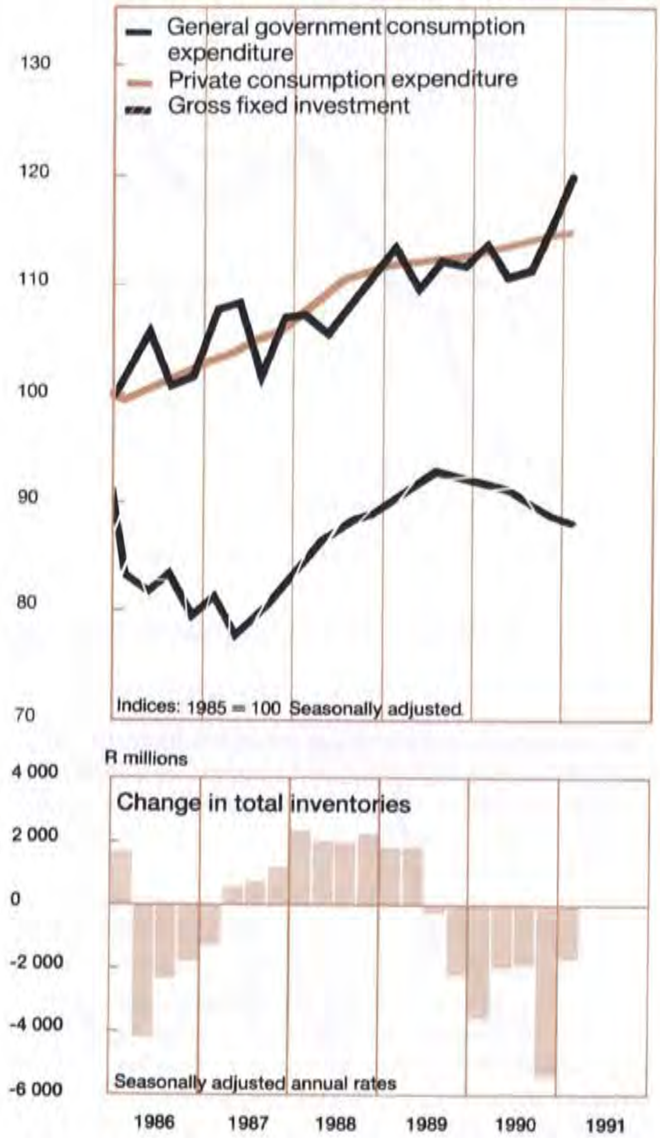
The quarter-to-quarter rate of increase in real *private consumption expenditure* remained surprisingly brisk throughout calendar 1990, and annualised growth rates varied between 2 and 2½ per cent for the four quarters. Estimates for the first quarter of 1991 show a further increase in real outlays by households, albeit at a lower rate of about 1 per cent. This slowdown in real consumption expenditure by households stemmed from a virtually sideways movement in real outlays on durable and semi-durable goods, whereas real expenditure on non-durable goods and on services still showed an increase at a rate of about 1½ per cent.

As already discussed at length in previous *Quarterly Bulletins*, the continued growth in consumption expenditure reflects the increasingly consumption-orientated nature of the South African society and was especially evident in expenditure on certain kinds of *durable consumer goods*, with the notable exception of personal transport equipment. In particular, furniture sales increased substantially in the second half of 1990. In the first three months of 1991, however, a contraction in expenditure on furniture and transport equipment resulted in a moderate decline in outlays on durable goods despite continued increases in expenditure on audio equipment and other appliances.

What seems to be the end of the buoyancy in expenditure on durable goods could probably mainly be attributed to a natural levelling-off in expenditure on durable goods following the satisfaction of the pent-up demand of the boom period in the second half of 1990. Other factors, such as the cooling-down of the economy, the retrenchment of labour in several economic sectors and the high level of violence in townships, could also have led to a more conservative attitude in respect of expenditure on luxury goods.

Real *consumption expenditure by general government* rose again substantially in the first quarter of 1991. Following an increase at an annualised rate of 16 per cent in the fourth quarter of 1990, real outlays by general government rose at an even higher rate of 19½ per cent in the first4 quarter of 1991. This surge in general government expenditure occurred almost entirely in real outlays on intermediate goods and services. Real remuneration of employees (as measured by the change in employment) showed little change from the level attained in the fourth quarter of 1990. The further substantial increase in government expenditure brought the total expansion in real government consumption expenditure in the fiscal year 1990/91 as a whole to 2½ per cent. In fiscal 1989/90 this increase had amounted to less than 2 per cent.

Main components of real gross domestic expenditure



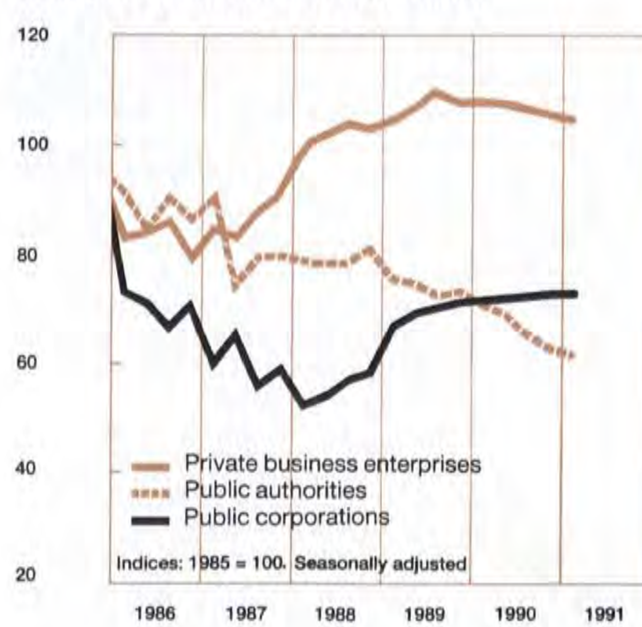
After total real *gross domestic fixed investment* had reached a recent high in the third quarter of 1989, it continued to decline throughout 1990 and in the first quarter of 1991. These contractions in six consecutive quarters could be attributed to declines in the real capital formation of the private sector and public authorities, which more than offset an increase in such expenditure by public corporations.

As already indicated, the decline in aggregate real gross domestic fixed investment decelerated in the first quarter of 1991 to an estimated annualised rate of 3½ per cent, compared with an average quarterly rate of decline of 5½ per cent in the last half of 1990. The main factors responsible for this slower growth included, firstly, a smaller decline in real fixed investment by the private sector, which has been on a downward trend since the fourth quarter of 1989. Secondly, a notable increase in real outlays on fixed investment by Transnet prevented an acceleration in the rate of contraction of fixed investment by public authorities. Thirdly, real fixed investment by public corporations increased somewhat further.

Real fixed capital formation by the *private sector* declined at an annualised rate of some 3½ per cent in the first quarter of 1991, *vis-à-vis* a decline of more than 4½ per cent in the previous quarter. A sectoral analysis shows that declines in the sectors agriculture, commerce and finance outweighed increases in investment by mining and manufacturing. Various factors had combined to produce this further decline in private-sector fixed investment, including successive droughts and increasing levels of farm debt, uncertainties regarding political developments and the land ownership issue, the downturn in economic activity, unrest in the townships, disharmony in management/labour relations and high interest rates.

Real fixed capital formation by the *public sector* shrank at an annualised rate of approximately 3½ per cent in the first quarter of 1991, after having declined at a rate of 6½ per cent in the previous quarter. This was the net result of a further downward movement in real fixed investment by the general government which exceeded the increase recorded by public corporations, whereas fixed investment by government business enterprises remained virtually

Real gross domestic fixed investment



unchanged. In the case of general government, real expenditure on fixed investment by the central government and local authorities declined in the first quarter, while provincial administrations registered an increase from the low recorded in the fourth quarter of 1990.

The decline in the decumulation of *inventories* in the first quarter of 1991 followed a drawing-down of total inventories in the fourth quarter of 1990 of nearly R5,5 billion (seasonally adjusted and at an annualised rate). The further decline in inventories in the first quarter of 1991 could be attributed mainly to a decline in the net foreign balance, which was again mainly due to higher import volumes. A sectoral analysis shows that lower rates of inventory decumulation could be observed mainly in the industrial and the commercial sectors and in diamond stocks-in-trade. Inventories held by the mining sector actually increased.

Despite the decline in the drawing-down of real industrial and commercial inventories, the ratio of these inventories to real gross domestic product in the first quarter of 1991 remained almost unchanged at the low level of 18½ per cent which had been reached in the fourth quarter of 1990.

Factor income

Aggregate nominal factor income at market prices increased at a seasonally adjusted and annualised rate of 10 per cent from the fourth quarter of 1990 to the first quarter of 1991. Although this rate of increase was slightly higher than that of the previous quarter, it was still well below the average annual rates of increase of 17½ and 13 per cent recorded in 1989 and 1990. The further moderate increase in factor income was the net result of a slower growth in the remuneration of employees combined with a rise in the rate of increase in the total gross operating surplus.

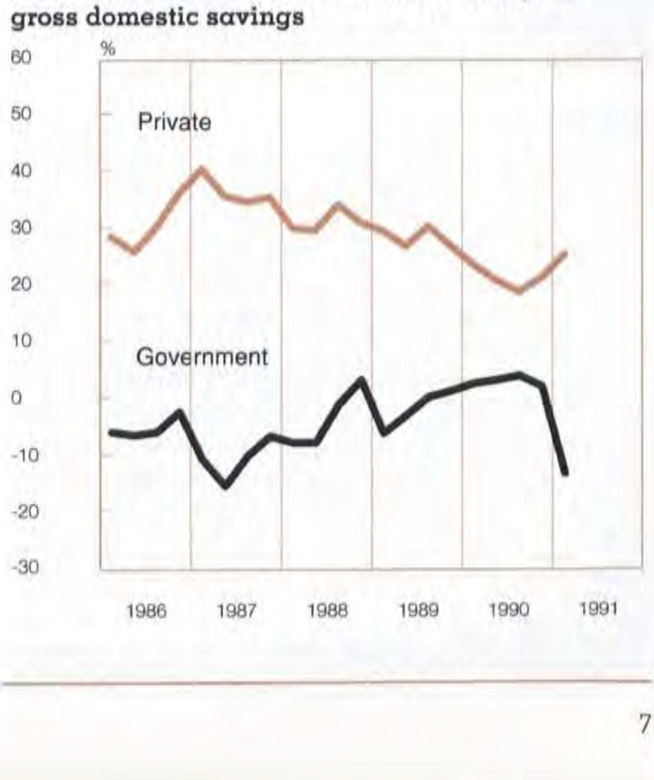
The quarter-to-quarter growth in total *labour remuneration* seasonally adjusted and annualised, receded from 23 per cent in the second quarter of 1990 to 13 per cent in the fourth quarter and to almost 11 per cent in the first quarter of 1991. A sectoral analysis shows that this slowdown in the rate of increase in the remuneration of employees was broadly based, but it was especially evident in the mining and manufacturing sectors. Rationalisation programmes introduced by several mines led to a considerable reduction in their labour force, while employment in manufacturing enterprises as well as in most other sectors was adversely affected by the lower level of production. The recession thus not only had an adverse impact on new job creation, but also led to a decline in existing job opportunities. A further, more structural, contributing factor to this moderation of the rise in labour remuneration was the increasing mechanisation undertaken to contain labour costs and to make enterprises less vulnerable to sporadic industrial actions, general stay-aways and unrealistic wage demands.

After the quarter-to-quarter rate of growth in the total nominal *gross operating surplus* of business enterprises had shrunk from an annualised level of 13 per cent in the first quarter of 1990 to a negative figure of 1½ per cent in the fourth quarter, it rose again to 11 per cent in the first quarter of 1991. This acceleration occurred despite the weak performances of the operating surpluses of mining and construction enterprises, and reflected sound results from a number of companies involved mainly in manufacturing, commerce, electricity, gas and water and finance. The gross operating surplus of the agricultural sector also recovered somewhat, following substantial decreases in the preceding two quarters.

Domestic saving

The *domestic savings ratio* (i.e. the ratio of gross domestic saving to gross domestic product), which had receded from a recent peak of 23½ per cent in the third quarter of 1989 to 21 per cent in the third quarter of 1990 and 21½ per cent in the fourth quarter, dropped to slightly less than 19 per cent in the first quarter of 1991. This ratio can be compared with an average of 24½ per cent in the 1980s. The further decline in the domestic savings ratio in the first quarter of 1991 stemmed mainly from dissaving by general government combined with a lower level of personal saving, which outweighed a small rise in corporate saving.

Ratio of government and personal savings to gross domestic savings



For six consecutive quarters from the third quarter of 1989 to the fourth quarter of 1990 the *general government* made positive contributions to net domestic saving because of relatively low growth in current government expenditure and sharp increases in government revenue. In the fourth quarter of 1990 current government expenditure began to rise sharply, leading to considerably lower, but still positive, saving by the general government. A further substantial increase in current government expenditure and a lower level of proceeds from direct taxes transformed this positive saving into dissaving again in the first quarter of 1991.

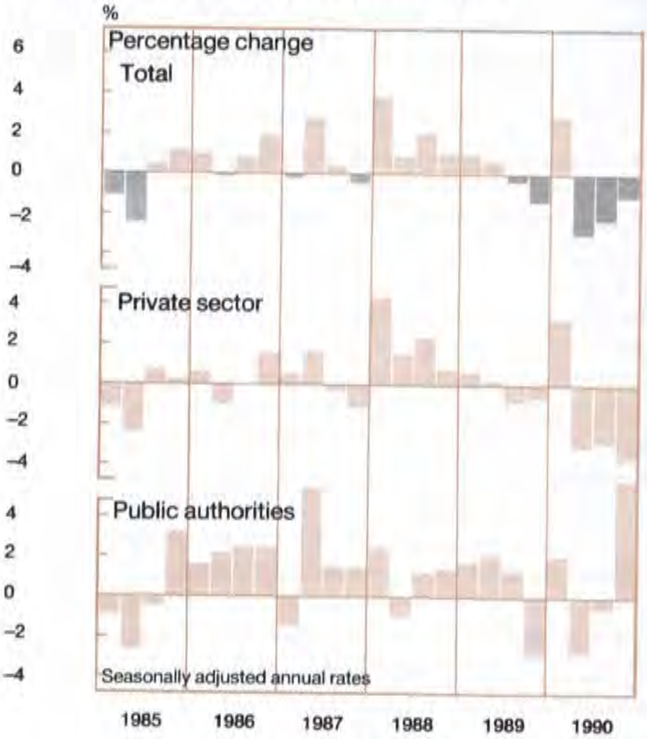
In addition, net saving by the *household* sector, which had increased fairly sharply in the fourth quarter of 1990, contracted again in the first quarter of 1991. Personal saving as a ratio of personal disposable income also receded again, namely from 2 per cent to 1½ per cent over the same period. This further decrease in household saving could be attributed to a small decline, at an annualised rate of less than ½ per cent in personal disposable income and to the unwillingness of households to accept lower living standards by cutting back on consumption expenditure. In the first quarter of 1991 the seasonally adjusted and annualised level of household saving was therefore 35 per cent below its high point in the fourth quarter of 1988.

In contrast to these developments, corporate saving increased marginally in the first quarter of 1991 following a distinct declining trend in 1990. This moderate improvement in corporate saving was associated with the rise in the nominal gross operating surplus of business enterprises and was to a large extent concentrated in certain sectors such as manufacturing, commerce and finance. The annualised quarter-to-quarter rate of increase in the operating surpluses of these sectors still varied between 9 and 16 per cent in the first quarter of 1991.

Employment

*Total employment** in the non-agricultural sectors of the economy expanded at a relatively modest average annual rate of 1,2 per cent in the cyclical upswing from 1986 to 1988. This was followed by an even lower, but still positive, increase of 0,7 per cent in the early downswing year 1989. However, with the protracted downturn in economic activity, employment in these sectors actually decreased at a rate of 0,4 per cent in 1990. During the course of 1990 employment in the non-agricultural sectors still increased at a seasonally adjusted and annualised rate of 2,8 per cent in the first quarter, but then decreased at rates of 2,8, 2,3 and 0,9 per cent in the subsequent three quarters. Available data for the first quarter of 1991 indicate further decreases in the number of persons employed in manufacturing, construction and electricity generation.

Employment in non-agricultural sectors



Employment in the non-agricultural *private sector* declined by 0,6 per cent in 1990, compared with an increase of 0,5 per cent in 1989. Like total non-agricultural employment, private-sector employment rose at a remarkably high seasonally adjusted and annualised rate of 3,2 per cent in the first quarter of 1990, but then decreased at disturbingly high rates of 3,0, 2,8 and 3,6 per cent in the next three quarters, owing mainly to contractions in the staff of construction, mining, wholesale trading, and electricity generation.

Total employment by *public authorities* also increased, at a seasonally adjusted and annualised rate of 1,8 per cent, in the first quarter of 1990, before decreasing at rates of 2,5 and 0,8 per cent in the next two quarters. However, it then increased sharply again at a rate of no less than 5,9 per cent in the final quarter of 1990 as a result of staff increases in the central government, provincial administrations, and the governments of the self-governing territories. Despite this sharp rise, total employment by public authorities for the year 1990 as a whole was still 0,1 per cent lower than in 1989.

Indicative of the lower demand for labour, the ratio of *overtime hours* to normal hours worked in

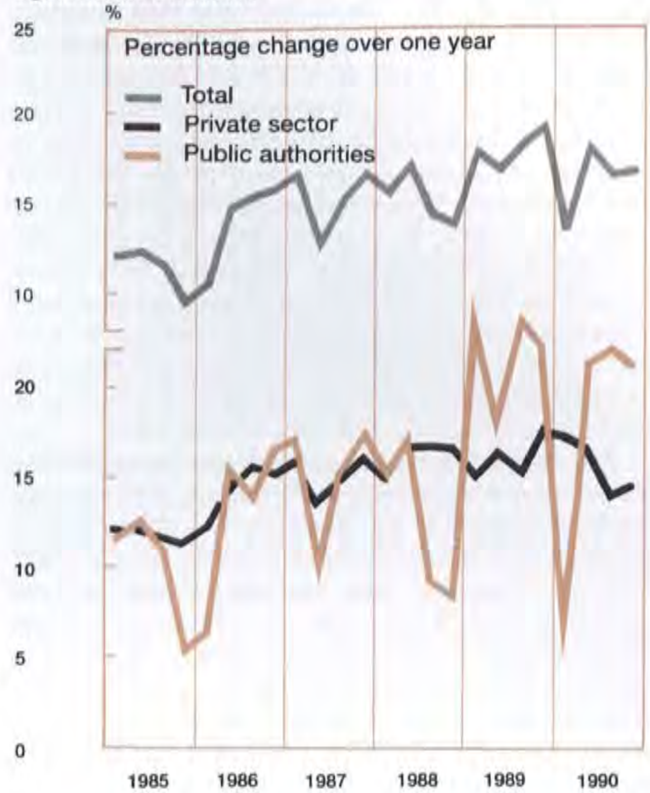
*All the seasonally adjusted data in respect of employment and labour costs and productivity have been revised.

manufacturing enterprises declined from the third quarter of 1989 through January 1991. In the construction industry this ratio has declined, on balance, from the second quarter of 1989.

As could be expected under these circumstances, the seasonally adjusted *total number of registered unemployed workers* more than doubled from a recent low point of 109 600 in January 1989 to 276 800 in December 1990, but then fell quite sharply to 190 500 in January. As has already been stated in previous quarterly surveys, this sharp rise in registered unemployment since mid-1990 has probably been affected to a large extent by the adoption of a new method of measuring the number of unemployed as from July 1990. The decline in January 1991 was mainly due to technical factors, and preliminary data indicate that a further increase in unemployment occurred in February.

The seasonally adjusted number of unemployed workers in the *White, Coloured and Asian population groups* also doubled, namely from 42 700 in December 1989 to 95 800 in December 1990. In January it declined substantially to 67 400. This decline was probably also due to technical factors and preliminary information for February suggests that the unemployment in these population groups has again increased sharply.

Average remuneration per worker in non-agricultural sectors



Labour costs and productivity

The rate of increase in the average amount of *nominal* salaries and wages per worker in the non-agricultural sectors of the economy accelerated from 11,4 per cent in 1985 to 18,0 per cent in 1989 - the highest increase since 1982. It then receded moderately to 16,7 per cent in 1990. However, this lower growth occurred mainly in the first quarter of 1990, when the increase in nominal wages per worker, measured over four quarters, amounted to 13,5 per cent. The year-on-year rate of increase in the average nominal wage per worker then accelerated disturbingly to 18,2 per cent in the second quarter and to slightly lower rates of 16,6 and 16,8 per cent in the third and fourth quarter of 1990.

These higher rates of increase in nominal wage packets were mainly the result of adjustments in the remuneration structure of a large number of employees in the civil service. Consequently, the year-on-year rate of increase in the nominal salaries and wages per employee of *public authorities* rose from only 5,6 per cent in the first quarter of 1990 to 21,5, 22,2 and 21,2 per cent in the final three quarters of the year. For the past two years workers employed by public authorities have been awarded higher wage increases than those of private-sector workers, thereby reversing the trend that prevailed from 1985 to 1988.

Despite the worsening employment conditions in the formal non-agricultural private sectors of the economy, the year-to-year rate of increase in the nominal wage per worker in the *private sector* decelerated only marginally from 16,3 per cent in 1989 to 16,1 per cent in 1990. The year-on-year rate of increase in the nominal wage per worker in the private sector nevertheless declined from 18,0 per cent in the fourth quarter of 1989 to 14,1 and 14,6 per cent in the third and fourth quarter of 1990. However, available data for the first quarter of 1991 indicate accelerations in wage increases in manufacturing, construction and electricity generation. The reluctance of employees to accept more fully justified wage increases under current conditions is confirmed by reports of wage claims by labour unions that have remained generally higher than the current and expected inflation rate.

The rate of increase in the *real* wage per worker in the non-agricultural sectors, which amounted to 2,2 and 2,9 per cent in 1988 and 1989, slowed down to 2,0 per cent in 1990. During the course of 1990 the year-on-year rate of change in the real wage per non-agricultural worker initially fell back to −1,3 per cent in the first quarter, but then reached a positive level of 3,7 per cent in the second quarter. It then receded again to positive levels of 2,6 and 1,9 per cent in the third and fourth quarter.

After real non-agricultural *labour productivity* had improved by only 0,8 per cent in the first year of the current cyclical downswing, it remained unchanged in 1990. Measured over four quarters, labour productivity continued to decline at first; the rates of decline amounted to 0,8 and 0,6 per cent in the first and the second quarter of 1990. It then recovered moderately (at year-on-year rates of increase of 0,8 and 0,5 per cent) in the third and fourth quarter. This weak performance of labour productivity was, of course, partly a cyclical phenomenon, but it was also the result of a sharp increase in the number of man-days lost because of strikes and work stoppages. The number of man-days lost due to strikes and work stoppages increased from 1,5 million in 1989 to 2,0 million in 1990.

The acceleration of nominal wage increases and the simultaneous weaker performance of labour productivity resulted in an alarming rate of increase in *nominal unit labour costs* of 17,2 per cent in 1989. This rate of increase then contracted slightly to a still high figure of 16,3 per cent in 1990. During the course of 1990 the year-on-year rate of increase in the nominal unit labour costs behaved rather erratically, but declined on balance from 18,9 per cent in the second quarter to 16,2 per cent in the fourth quarter.

Decreases were recorded in *real unit labour costs* from 1985 to 1988, before these costs rose sharply again by 2,1 per cent in 1989 and by 1,7 per cent in 1990. These increases were mainly due to the deterioration in labour productivity. The year-on-year rate of increase in real labour costs per unit of physical output declined sharply from 4,3 per cent in the fourth quarter of 1989 (the highest rate of increase since the fourth quarter of 1984) to 0,4 per cent in the first quarter of 1990. It then reaccelerated to 4,3 per cent in the second quarter, before falling back again to 1,4 per cent in the fourth quarter.

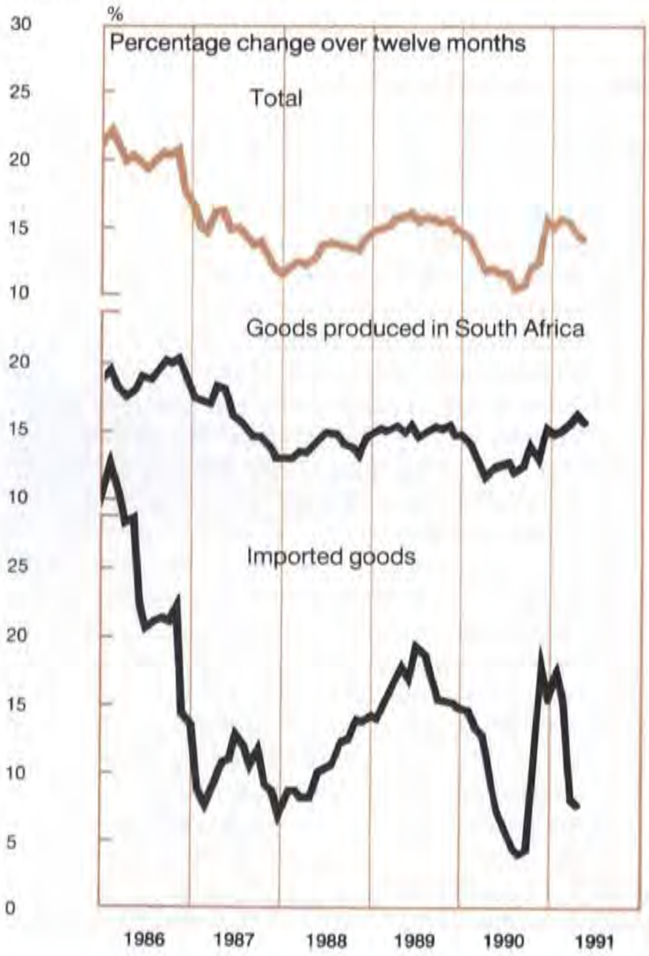
Inflation

After the rate of inflation showed encouraging signs of subsiding, the invasion of Kuwait by Iraq led to a substantial surge in import prices of oil and other petroleum products. The direct and secondary effects of these higher prices were reflected in increases in the more important domestic price indices. With the exception of the price index for imported goods, the end of the Gulf War and the return of international oil prices to pre-war levels have as yet not been reflected in any significant declines in the rates at which the prices of domestically produced goods and consumer goods and services have increased. Higher real labour costs, sustained inflationary expectations and substantial increases in the prices of foodstuffs prevented the rate of increase of both the production and the consumer price index from declining to anywhere near their lower levels in July 1990.

The generally stable effective exchange rate of the rand and the lowering of import surcharges in April 1990 contributed to a dramatic decline in the *quarter-to-quarter* rate of increase in the *prices of imported goods* from a seasonally adjusted and annualised rate of 25,4 per cent in the second quarter of 1989 to only 0,1 per cent in the third quarter of 1990. As a result of the initial impact of the Middle East crisis on international oil prices, this rate of increase then accelerated spectacularly to an all-time high of 59,4 per cent in the fourth quarter. It then dropped in a similar spectacular fashion to only 4,4 per cent in the first quarter of 1991.

Measured over a *period of twelve months*, the slowdown in the rate of increase in import prices from 19,3 per cent in June 1989 to only 4,1 per cent in August 1990 was also reversed, mainly because of the higher oil prices. In November this rate of

Production prices



increase amounted to 19,1 per cent. It subsequently fluctuated considerably, but on balance showed a declining trend and amounted to 15,3 per cent in February 1991, before declining sharply to 8,3 per cent in March and 7,6 per cent in April.

The higher international oil prices and consequent higher domestic fuel prices were also to an important extent directly and indirectly responsible for the acceleration in the rate of increase *from quarter to quarter* in the *prices of domestically produced goods* from a seasonally adjusted and annualised rate of 9,5 per cent in the first quarter of 1990 to 19,0 per cent in the fourth quarter. This rate of increase then receded again to 14,3 per cent in the first quarter of 1991.

Measured over *periods of twelve months*, the rate of increase in the prices of domestically produced goods accelerated from a lower turning-point of 11,3 per cent in March 1990 to 15,1 per cent in November. Despite the fuel price reductions, the secondary effects of the initial oil price increases and their influence on inflationary expectations caused this rate of increase to fluctuate around this higher level, and it amounted to 15,2 per cent in April 1991.

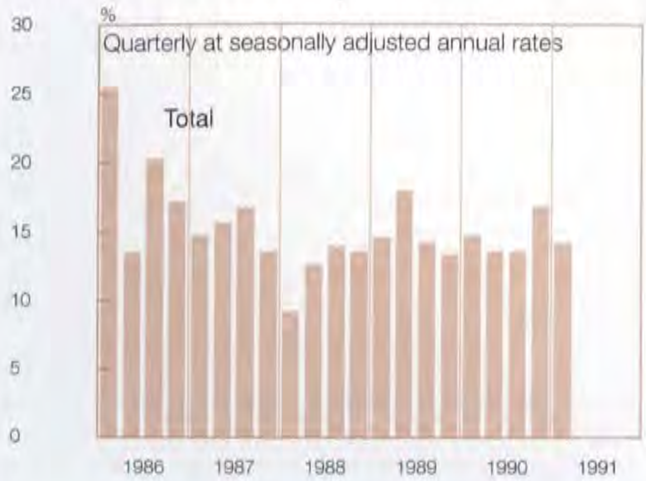
In a pattern similar to the increase in the prices of domestically produced goods, the *quarter-to-quarter* rate of increase in the *total production price index*, seasonally adjusted and annualised, climbed from a low point of 9,6 per cent in the first quarter of 1990 to 25,4 per cent in the fourth quarter, and then receded to 13,0 per cent in the first quarter of 1991. The rate of increase in the total production price index over *periods of twelve months* also accelerated, namely from 10,3 per cent in July 1990 to 15,8 per cent in November, and then fluctuated downwards to 13,8 per cent in April 1991.

Notwithstanding the resurgence of inflation in the prices of domestically produced and imported goods in the second half of 1990, the *year-to-year* rate of increase in the total production price index decelerated quite significantly from 15,2 per cent in 1989 to 12,3 per cent in 1990 - the lowest average annual rate of increase since the 8,4 per cent recorded in 1984.

In contrast to this encouraging improvement in production price inflation, the rate of increase in the monthly average *consumer price index* declined only marginally from 14,7 per cent in 1989 to 14,4 per cent in 1990.

The *quarter-to-quarter* rate of increase in the consumer price index accelerated from a seasonally adjusted and annualised rate of 13,5 per cent in both the second and third quarter of 1990 to 16,8 per cent in the fourth quarter, but then receded again to 14,1 per cent in the first quarter of 1991. This lower rate of increase was brought about by sharply reduced increases in the prices of consumer goods and more modest increases in the prices of consumer services.

Consumer price index



The rise in food prices accelerated again in the first quarter of 1991 and higher rates of increase were also recorded in the prices of alcoholic beverages and tobacco, new vehicles, furniture, health care and transport services.

The rate of increase in consumer prices measured over *periods of twelve months* accelerated on balance from a recent low point of 13,3 per cent in July 1990 to 15,3 per cent in November. It then came down to 14,1 per cent in March 1991, due mainly to reductions in the prices of liquid fuels that were announced in November and December 1990.

A further reduction in the prices of petrol and oil after the Budget in March as well as lower home-owners' costs arising from lower mortgage bond rates were, however, unable to prevent an acceleration in the year-on-year rate of increase in consumer prices to 14,6 per cent in April. This higher rate in April was primarily the result of substantial increases in the prices of foodstuffs, footwear and health and certain other services.

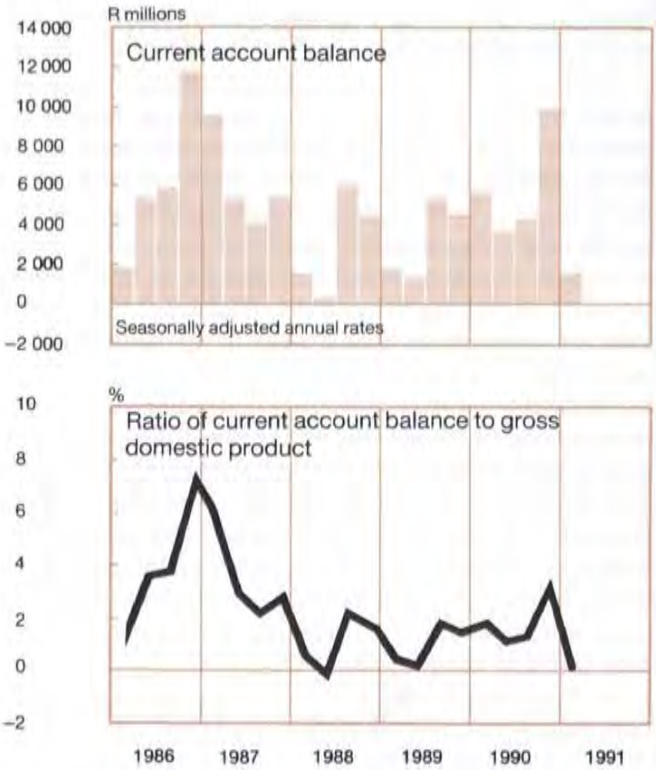
Balance of payments and exchange rates

Current account

The *surplus on the current account* of the balance of payments declined dramatically from its very high seasonally adjusted and annualised level of R9,7 billion in the fourth quarter of 1990 to R1,5 billion in the first quarter of 1991. This low surplus on the current account was exceptional because it occurred at a stage when domestic economic activity had already been in a downward phase of the business cycle for eight quarters, whereas the level of the surplus was comparable to those recorded at around the peak of the cycle at the beginning of 1989. Moreover, the deterioration in the current account was the combined result of a substantial increase in the value of merchandise imports and a decrease in the values of merchandise exports and net gold exports – developments which were out of line with the normal cyclical pattern.

The large surplus of the fourth quarter of 1990 and the small surplus of the first quarter of 1991 were, however, influenced by *extraordinary circumstances* related to a large extent to the crisis in the Persian Gulf. The second-highest ever surplus of the fourth quarter was largely the result of a drawing-down of inventories in order to keep the imports of mineral products at a low level. In the first quarter of 1991, however, the imports of mineral products increased again considerably. At the same time the sharp increase in the value of imports was also augmented by the purchase of a new macro jet aircraft by the South African Airways, while exports were adversely affected by poor agricultural conditions. From an analytical point of view it therefore seems more appropriate to evaluate the size of the surplus by comparing the average quarterly figure of R5,6 billion for the period October 1990 to March 1991 with the surplus of R4,2 billion in the third quarter of 1990.

Balance of payments



The higher *imports* of mineral products and transport equipment (the new Boeing) were mainly responsible for an increase of about 10 per cent in import *volumes* during the first quarter of 1991. Import *prices* rose by about 2½ per cent in the same quarter, on account of a 1 per cent decline in the average effective exchange rate of the rand and a moderate increase in the inflation rates of South Africa's main trading partner countries. The value of

Balance of payments on current account
Seasonally adjusted annual rates

R billions

	1990				1991
	1 st qr	2nd qr	3rd qr	4th qr	1st qr
Merchandise exports	41,7	39,5	42,8	45,5	41,8
Net gold exports	17,8	18,5	18,0	18,0	17,3
Merchandise imports	−43,6	−44,1	−46,5	−42,2	−47,5
Net service and transfer payments	−10,3	−10,3	−10,1	−11,6	−10,1
Balance on current account	**5,6**	**3,6**	**4,2**	**9,7**	**1,5**

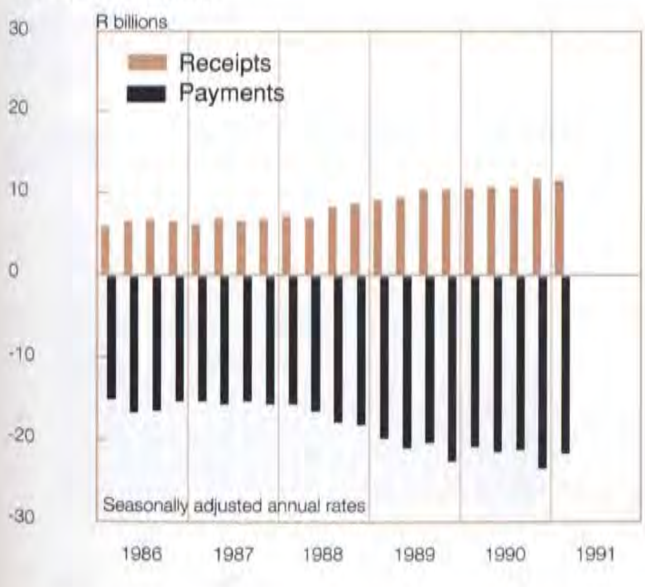
merchandise imports (at a seasonally adjusted and annualised rate) therefore grew from R42,2 billion in the fourth quarter of 1990 to R47,5 billion in the first quarter of 1991, or by 12½ per cent.

Both volume and price declines contributed to a decrease of 8 per cent in the value of *merchandise exports* from the fourth quarter of 1990 to the first quarter of 1991. Export *volumes* declined by about 4½ per cent, mainly because of the decrease in the exports of mineral products, reduced agricultural exports in anticipation of a poor maize crop, and lower exports of precious stones and metals related to the general decline in economic activity in most industrial countries. Export *prices* were affected detrimentally by a further decline in international commodity prices.

During the first quarter of 1991 the value of *net gold exports* declined by 3½ per cent to a seasonally adjusted and annualised amount of R17,3 billion. Although the average US dollar price of gold declined from $380 per fine ounce in the fourth quarter of 1990 to $370 in the first quarter of 1991, the rand price dropped only marginally from R962 to R957 per fine ounce, reflecting the depreciation of the rand against the US dollar. The larger part of the decline in the value of net gold exports in the first quarter could therefore be ascribed to a drop in the volume of net gold exports. In April – May 1991 the average dollar price of gold receded further to $358 per fine ounce, but the rand price strengthened to R990.

In contrast to these developments on the current account of the balance of payments, *net service and transfer payments* to non-residents improved during the first quarter of 1991. However, this decrease occurred from the exceptionally high level of R11,6 billion (seasonally adjusted and annualised) which these payments had reached in the fourth quarter of 1990, to R10,1 billion in the first quarter of 1991 – i.e. to a level comparable with that of the first three quarters of 1990, which averaged R10,2 billion. These fluctuations in net service and transfer payments over the past two quarters were to a large extent the result of changes in international oil prices. The high average oil price during the fourth quarter of 1990 led to substantially higher travel and transport payments to non-residents, followed by a decline in this type of service payments when oil prices dropped again to levels prevailing before the Persian Gulf crisis. The lower deficit on the services account during the first quarter also reflected lower interest payments on foreign debt, which were related to the declining outstanding foreign debt position and generally lower international interest rates, as well as to lower dividend payments on foreign investment because of the lower level of domestic economic activity and company profits.

Services account



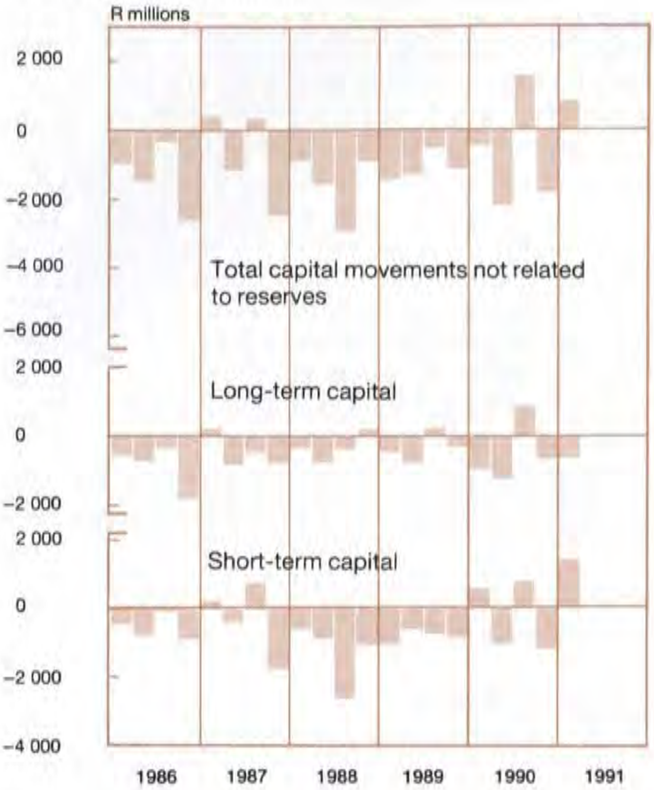
Capital movements

The net outflow of capital not related to reserves of R1,8 billion in the fourth quarter of 1990 was transformed into a net inflow of R0,8 billion in the first quarter of 1991. This *inflow* of capital was recorded despite repayments of approximately US$200 million on foreign debt in terms of the Third Interim Debt Arrangements with foreign creditor banks and the redemption of maturing bearer bonds and notes. These repayments were mainly responsible for a further net outflow of long-term capital amounting to some R0,6 billion in the first quarter of 1991.

In particular, *public authorities and private sector enterprises* made fairly large repayments on foreign long-term loans. However, the outflow of long-term funds reported for the private sector also includes net sales of securities by non-residents; because these transactions have to be concluded in financial rand they do not lead to a decrease in the country's foreign exchange holdings. The reported long-term capital outflow of the private sector was, therefore, to some extent offset by inflows recorded against other items in the capital account which are affected by these financial rand transactions.

Public corporations continued to be net borrowers of long-term funds on foreign capital markets during the first quarter of 1991. These institutions again became net borrowers of foreign long-term capital from the fourth quarter of 1988 and have since then nearly uninterruptedly recorded quarterly net inflows of long-term capital. Moreover, the net inflow of long-term capital of public corporations increased substantially from R436 million in 1989 to R890 million in 1990. In the first quarter of 1991 pub-

Net capital movements



lic corporations were again net borrowers of long-term funds to an amount of R188 million, which was somewhat less than the quarterly average of about R240 million in 1990. From the fourth quarter of 1988 to the first quarter of 1991 the inflow of long-term capital to public corporations totalled no less than R1 660 million.

By far the largest part of the inflow of capital in the first quarter of 1991 consisted of *short-term capital*, including unrecorded transactions but excluding reserve-related liabilities. This inflow amounted to some R1,4 billion, compared with a net outflow of approximately R1,2 billion in the fourth quarter of 1990. This large inflow of short-term capital occurred mainly in the form of trade financing, reflecting the increased value of merchandise imports and the relatively favourable conditions pertaining to foreign borrowing in comparison with the cost of domestic funding.

Foreign debt

South Africa's *total outstanding foreign debt* decreased further during 1990 to US$19,4 billion at the end of the year from $20,6 billion at the end of 1989. Valued at the dollar's exchange rates vis-à-vis other currencies as on 31 August 1985, the total outstanding debt of the country amounted to $16,4 billion on 31 December 1990, as against $18,2 billion at the end of 1989 and $23,7 billion at the start of the standstill arrangements. As a percentage of the exports of goods and services, South Africa's foreign debt also improved from 79 per cent at the end of 1989 to 70 per cent at the end of 1990. This last-mentioned ratio can be compared with an average figure of 255 per cent for all developing countries in the Western Hemisphere.

From 31 August 1985 to 31 December 1990 the total *affected debt* (i.e. the total debt under the so-

Net capital movements (not related to reserves)

R millions

	1990				1991
	1st qr	2nd qr	3rd qr	4th qr	1st qr
Long - term capital					
Public authorities	–206	–673	47	–328	–167
Public corporations	473	–35	279	173	188
Private sector	–1 204	–482	495	–484	–604
Total long-term capital	–937	–1 190	821	–639	–583
Short-term capital, including unrecorded transactions, but excluding reserve-related liabilities	531	–1 000	694	–1 154	1 362
Total capital movements, excluding liabilities related to reserves	**–406**	**–2 190**	**1 515**	**–1 793**	**779**

called standstill net) also shrank substantially, namely from \$13,6 billion to \$6,6 billion. Valued at the exchange rates of 31 August 1985, the affected debt decreased by \$7,7 billion over this period to an outstanding amount of \$5,9 billion at the end of 1990. This substantial reduction in affected debt was the combined result of repayments made in terms of the three interim debt arrangements concluded with foreign creditor banks, as well as of "debt overdue" which was converted into medium and long-term loans outside the net, and of debt-equity swaps. In particular, no less than \$4,7 billion of affected debt was converted into longer-term loans outside the standstill net up to 31 December 1990.

These conversions also led to a considerable improvement in the *maturity structure* of South Africa's foreign debt and were mainly responsible for the increase in the *non-affected debt* of the country from \$10,1 billion at the end of August 1985 to \$12,8 billion at the end of 1990. Valued at the exchange rates prevailing on 31 August 1985, the non-affected debt at the end of 1990 amounted to \$10,6 billion.

Foreign reserves

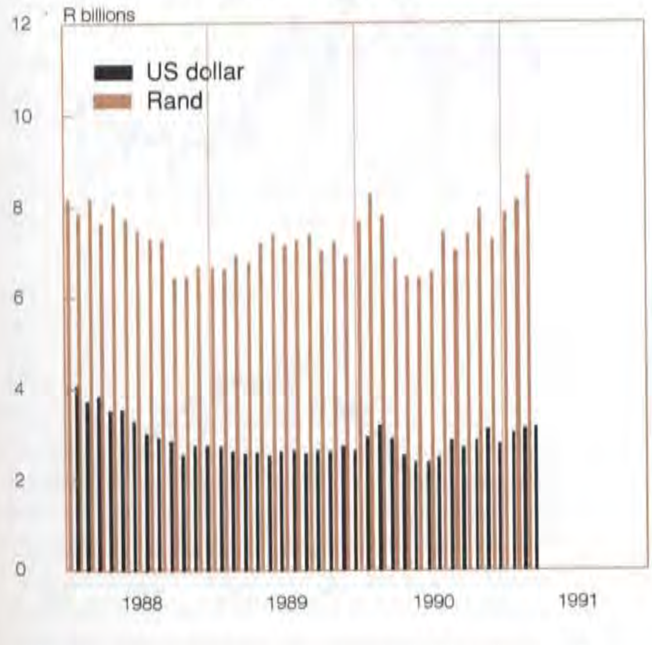
The inflow of capital not related to reserves together with the surplus on current account of R973 million (neither annualised nor seasonally adjusted), resulted in an increase of R1,8 billion in the total *net gold and other foreign reserves* in the first quarter of 1991. This substantial improvement was achieved on top of the increase in total net foreign reserves of R2,9 billion during 1990 as a whole. The improved foreign reserve position enabled the Reserve Bank to make further repayments on its liabilities related to reserves and by the end of March 1991 nearly all the short-term foreign loans of the Reserve Bank had been redeemed. Despite these redemptions, the total *gross* gold and other foreign reserves still rose by R1,4 billion in the first quarter of 1991 to a level of R8,7 billion at the end of March. In April and May the gold and other foreign reserves held by the Reserve Bank decreased again, on balance, by R99 million to R7,2 billion at the end of May 1991.

Exchange rates

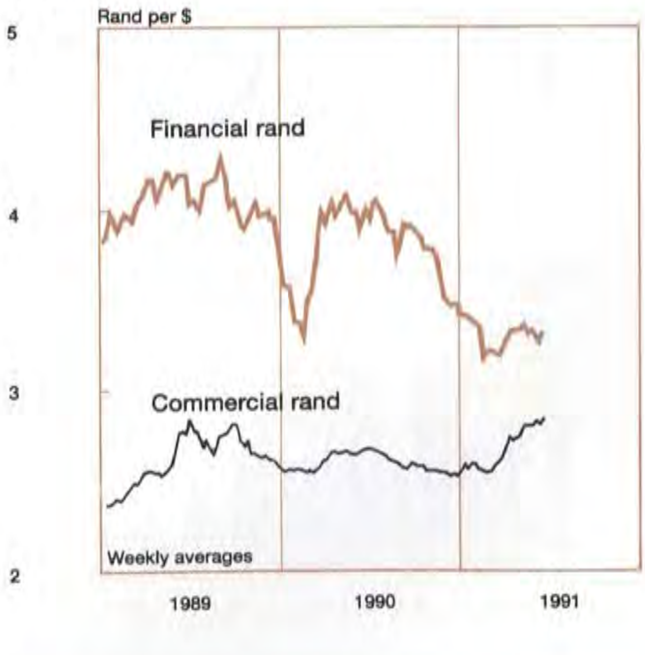
With the prospects of a quick end to the hostilities in the Middle East, the *US dollar* started appreciating from its lower turning-point of DM1,4474 per dollar on 12 February 1991 to a rate of DM1,7095 per dollar on 31 May, or by 18,1 per cent. Over the same period the rand depreciated sharply against the dollar, *viz* from R2,52 per US dollar to R2,81. However, the rand appreciated against all the other major currencies during this period, with the exception of the Japanese yen.

The *effective exchange* rate of the rand during the first two months of 1991 remained more or less unchanged and then declined moderately in the next three months. At the end of May 1991 it was, therefore, some 2,9 per cent below its previous low point on 18 September 1989.

Gross gold and other foreign reserves



Exchange rates



Changes in exchange rates of the rand

%

	18 Sept 1989 to 31 May 1991	12 Feb 1991 to 31 May 1991
Weighted average ...	-2,9	-3,2
US dollar ...	0,5	-10,4
British pound ...	-9,0	3,4
German mark ...	-12,4	5,8
Swiss franc ...	-13,4	5,5
Japanese yen ...	-5,3	-3,4
French franc ...	-11,8	5,3
Financial rand ...	23,3	-3,1

Having reached a new high of R3,07 per US dollar on 6 February 1991, the *financial rand* weakened again to R3,28 per dollar on 31 May 1991. The deterioration of the financial rand was, however, somewhat smaller than the depreciation of the commercial rand against the dollar. As a result, the financial rand discount narrowed from 17,8 per cent on 6 February 1991 to 14,1 per cent on 31 May. This narrowing of the discount was in sharp contrast with developments in 1990 when the financial rand also improved significantly after the opening of Parliament by the State President but weakened again subsequently, eventually showing discounts in excess of 30 per cent.

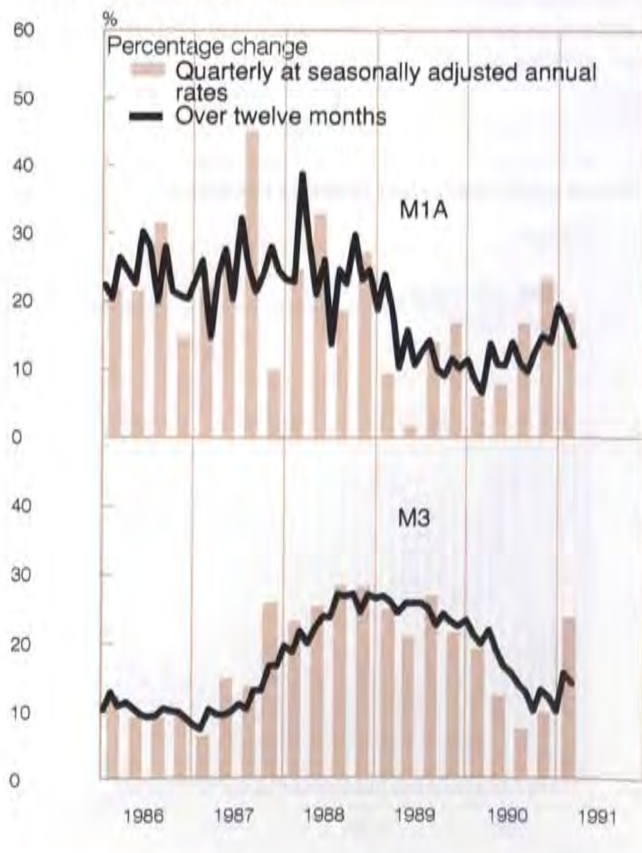
Financial markets

Money supply

The rate of increase in the broadly defined *money supply* (M3), which had decelerated considerably since the second half of 1988, fluctuated around somewhat higher levels at the end of 1990 and during the beginning of 1991. Measured over a period of twelve months, the growth rate of M3 receded from a cyclical peak of 27,5 per cent in August 1988 to only 10,2 per cent in October 1990. This slower growth in M3 was mainly due to the cyclical slowdown in economic activity and sustained high and relatively stable money market interest rates.

The twelve-month rate of increase in M3 rose moderately in the last two months of 1990, before returning to 10,2 per cent in January 1991. In February 1991 this rate rose markedly to 15,8 per cent, followed by 14,4 per cent in March and a preliminary estimated 15,0 per cent in April. These higher rates could be attributed to a considerable extent to the new regulations under the Deposit-taking Institutions Act, which became operative from 1 February 1991. First in anticipation of, and subse-

Monetary aggregates



quently in the wake of, these changes, repurchase agreements (which are not included in M3) were converted into conventional deposits (which are included in M3). If allowance is made for these conversions, the estimated underlying rate of increase in M3 remained relatively low. From its new peak in February 1991, the seasonally adjusted and annualised rate of increase in M3 was also relatively low, amounting to only 9,4 per cent up to April.

With the financial system in the process of settling down to these new regulations, as well as to further regulatory changes announced in April, the movements in the statistically measured M3 in the first half of 1991 should clearly not be taken to be indicative of developments in the real economy. This is substantiated by the marked decline in M3's income velocity of circulation, which fell by 2,9 per cent from the fourth quarter of 1990 to the first quarter of 1991.

The new regulations were also mainly responsible for the fact that in February 1991 M3 moved above the upper boundary of the *new money supply guidelines* of 8 to 12 per cent for the 1991 "guideline" year. At the end of February 1991 the value of M3 exceeded the upper limit of the guideline cone by 4,8 per cent; the extent of this overshoot declined somewhat to 3,5 per cent at the end of March and then increased slightly to a preliminary estimated 4,3 per cent in April.

The implementation of the Deposit-taking Institutions Act also had an important effect on the *narrower monetary aggregates*. Among these other aggregates, the twelve-month rate of growth in M1 and M2 similarly accelerated considerably from 1,7 and 12,0 per cent in January to 18,1 and 17,6 per cent in February and then amounted to 9,5 and 16,8 per cent in March. Even the growth rate of the more transactions-related M1A money supply picked up, apparently because some short-term repurchase agreements were converted into cheque and transmission deposits. Accordingly, the rate of increase in M1A measured over twelve months rose from 14,3 per cent in December 1990 to 19,5 per cent in January 1991, but then declined to 17,2 per cent in February, and to 13,6 per cent in March.

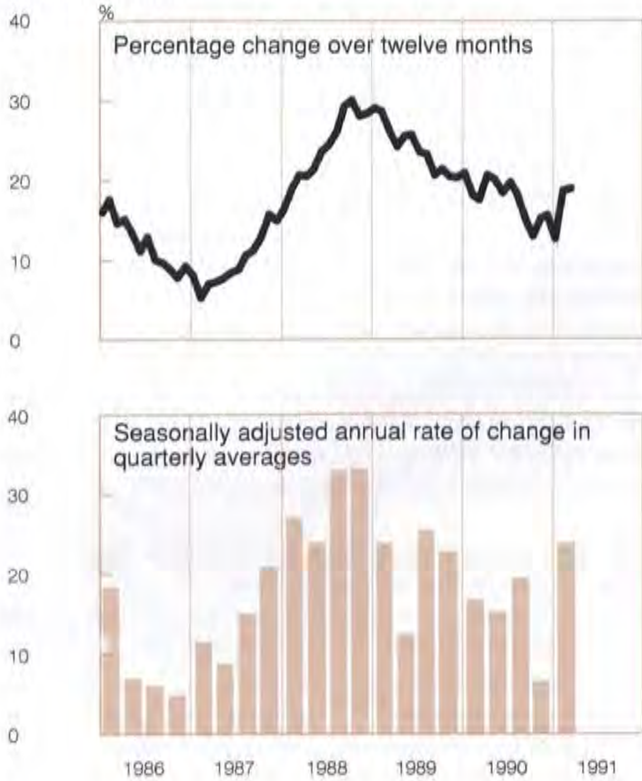
In an accounting sense, the main statistical counterpart of the seasonally adjusted increase of R9,0 billion in M3 during the first quarter of 1991 was an increase of R9,0 billion in monetary institutions' claims on the domestic private sector. To a considerable extent, this was also a reflection of the new regulations, which caused assets that had previously been sold temporarily to other parties under repurchase agreements and had not been included in monetary institutions' assets, to be brought back onto these institutions' balance sheets. The monetary system's net gold and other foreign reserves rose by R1,0 billion during the first quarter of 1991, but net claims on the government sector declined by R3,7 billion.

Credit extension by monetary institutions

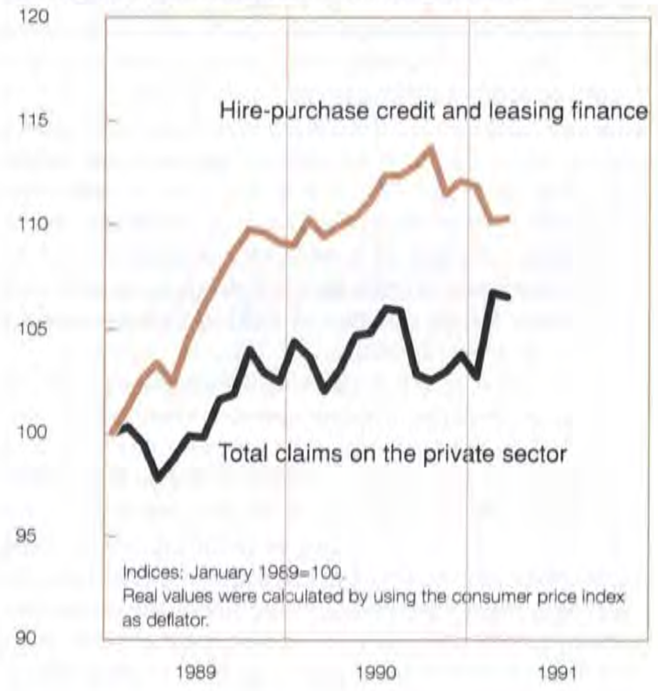
The twelve-month rate of increase in monetary institutions' claims on the *domestic private sector* receded on balance from a high point of 30,2 per cent in October 1988 to 12,9 per cent in January 1991. This rate subsequently accelerated again to 19,0 per cent in February and 19,2 per cent in March, because of the reintermediation of assets previously treated as off-balance-sheet items already referred to. Similarly, the seasonally adjusted and annualised rate of increase in the quarterly average of monetary institutions' claims on the domestic private sector rose from only 6,7 per cent in the fourth quarter of 1990 to 24,0 per cent in the first quarter of 1991.

In contrast to these developments, *hire-purchase credit and leasing finance* rose on average by only R113 million (or less than 0,4 per cent) per month in the first quarter of 1991, whereas this kind of credit had increased by some R339 million per month during 1990. Since these types of credit are well correlated with spending on consumer durables and capital goods, their behaviour underlined the fact that real expenditure in the economy remained under downward pressure, in spite of the apparently

Claims of monetary institutions on domestic private sector



Real total claims on the private sector and hire-purchase credit and leasing finance



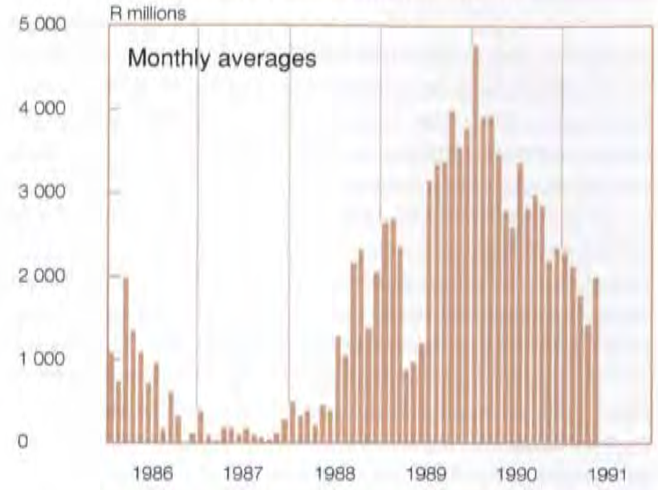
brisk rate of expansion recorded by overall credit extension. In real terms, however, hire-purchase credit and leasing finance still increased at fairly buoyant rates until the third quarter of 1990. Actual declines were then recorded in the volume of this type of credit during the ensuing six months.

Monetary institutions' *mortgage advances* continued to increase strongly during the first quarter of 1991. This was supported by factors such as the increase in the amount of government employees' mortgage loans qualifying for interest subsidisation (from R50 000 to R70 000 as from 1 January 1991), the active promotion of such loans by certain institutions and slower repayments of capital. In the first quarter of 1991 monetary institutions' mortgage holdings rose by R2,1 billion, i.e. by about the same amount as the average quarterly increase in 1990.

Money market conditions and Reserve Bank operations in the money market

Markedly easier conditions prevailed in the money market during the first five months of 1991. The average daily level of *accommodation* at the Reserve Bank's discount window dropped from a high point of R4,8 billion in January 1990 to R2,3 billion in both December 1990 and January 1991. It then continued to decline to R1,4 billion in April, after which it increased slightly to R2,0 billion in May. The amount

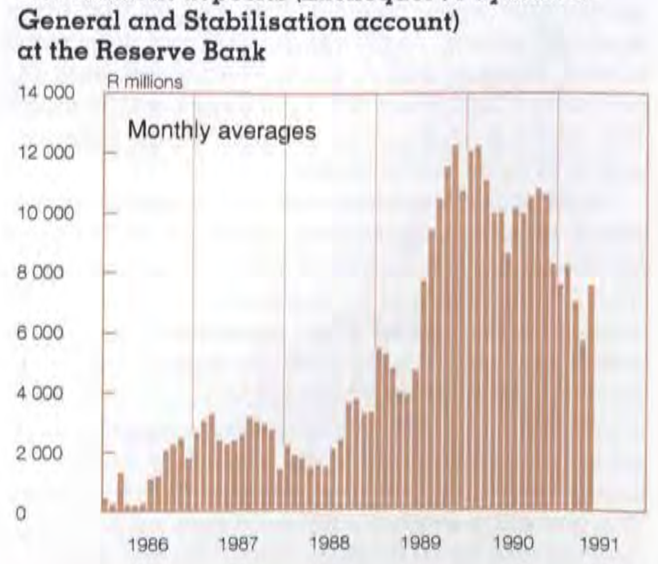
Accommodation at the discount window



of accommodation at month-ends showed a similar declining tendency and during the course of April the accommodation at the window at times declined sharply.

This easing of the money market was mainly caused by the substantial increase in the net gold and other foreign reserves of the Reserve Bank (referred to above) and by a decline in the Treasury's deposits with the Bank. The monthly average of the daily balances on the Exchequer, Paymaster-General and Stabilisation accounts with the Reserve

Government deposits (Exchequer-, Paymaster-General and Stabilisation account) at the Reserve Bank



Bank declined from R8,2 billion in December 1990 to R7,0 billion in March 1991. It then declined further to R5,7 billion in April, but rose to R7,5 billion in May. The part of these deposits sterilised in the Exchequer's Stabilisation Account was increased from R2,1 billion in January 1991 to R3,7 billion on 14 March and was kept at this level up to the end of May.

In contrast to these developments, the average daily amount of *notes in circulation* remained fairly stable during the first five months of 1991 and no major money market influences were exerted from this source. Deficits on the Reserve Bank's *forward exchange cover*, on the other hand, also added to the liquidity in the money market. Money market conditions were also eased further by the reduction in the amount of *cash reserves* that banks have to hold with the Reserve Bank. This reduction, which was caused by the lowering from 5 to 4 per cent of the cash reserve requirement against the banks' short-term liabilities and the abolition of the 2 per cent cash reserve requirement against their medium-term liabilities, is being phased in over a period of four months from 21 March 1991.

The easing effects of these developments on the money market were partly countered by the Reserve Bank through *foreign exchange intervention swaps*. Monthly peaks in the volume of such swaps amounted to R0,9 billion in January and February, R1,9 billion in March and R1,4 billion in both April and May. The Reserve Bank also issued special very *short-dated Treasury bills*, to a peak amount of R1,5 billion in April and R1,0 billion in May. At the end of May an amount of R1,0 billion of such paper was still outstanding. On 15 May 1991 the Bank also entered into a reverse-repurchase agreement with a bank, which amounted to R0,5 billion and fell due on 23 May 1991.

Net *sales of government stock* by the Reserve Bank declined from R1,2 billion in the fourth quarter of 1990 to R0,6 billion in the first quarter of 1991, but then rose again to R1,2 billion in April and R1,4 billion in May 1991. The Bank's gross transactions in government stock amounted to as much as R13,3 billion in the first five months of 1991, compared with only R5,2 billion in the corresponding period of 1990 - an indication of the Bank's efforts to increase the marketability of government stock.

Other operations of the Reserve Bank included activities in *government stock options*. The average monthly amount of traded options contracts was increased from R0,3 billion in the first half of 1990 to R1,2 billion in the fourth quarter and to R1,2 billion in the first five months of 1991. The amount of Treasury bills offered at the *weekly tender* was also increased from R100 million per week to R130 million per week from 5 April 1991 and to R150 million from 30 May 1991.

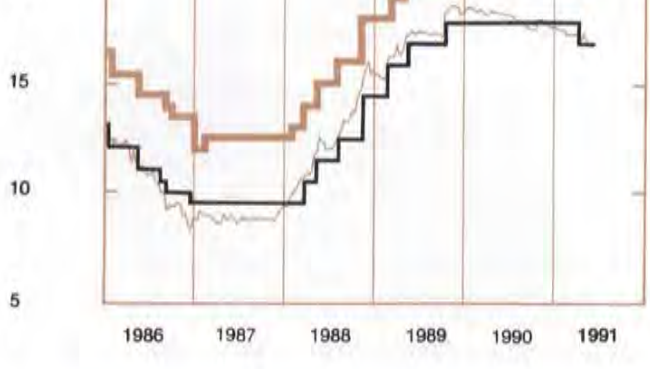
Money market interest rates

Money market interest rates continued to decline in the first two months of 1991 on the strength of expectations of a lowering of Bank rate. The market rate on *three-month liquid bankers' acceptances* declined from 17,70 per cent at the end of December 1990 to 17,25 per cent on 23 February 1991. This decline to 1,05 percentage points below the Reserve Bank's rediscount rate for such paper was indicative of the market's expectations of a reduction in Bank rate of at least 1 percentage point.

The rate on three-month liquid bankers' acceptances firmed again to 17,40 per cent on 28 February, but resumed its retreat after Bank rate was reduced from 18 to 17 per cent as from 11 March 1991. On 18 April it stood at 17,10 per cent, which was 0,40 percentage points below the Bank's rediscount rate for liquid bankers' acceptances. On 17 April and again on 24 April circulars on undesirable funding practices were issued to all deposit-taking institutions by the Registrar of Deposit-taking Institutions. These circulars created uncertainty in the market regarding their full implications and initially led to a rate range of 17,05 to 17,50 per cent being quoted for liquid bankers' acceptances. After this issue was resolved, the bankers' acceptance rate continued to decline to 16,80 per cent on 30 May, which was 0,70 percentage points below the Reserve Bank's rediscount rate for liquid bankers' acceptances.

In response to the reduction in Bank rate, the *inter-bank rate* declined from 19,25 per cent at the

Short-term interest rates



end of February to 17,75 per cent at the end of March. It continued to decline to 17,00 per cent at the end of April – clearly reflecting the markedly easier conditions prevailing in the money market. In May it firmed somewhat again to 17,25 per cent.

Capital market developments

Trading activity in the *secondary capital markets*, which had reached record heights in the first quarter of 1990 but then fell significantly in the rest of the year, recovered markedly again in the first quarter of 1991. After having declined from the exceptionally high level of R77,3 billion in the first quarter of 1990 to R53,7 billion in the fourth quarter, the value of *public-sector stock* traded on the Johannesburg Stock Exchange increased to R67,9 billion in the first quarter of 1991. Similarly, the value of *shares traded* on the stock exchange strengthened to R4,9 billion in the first quarter of 1991 after having been more than halved from a record R8,6 billion in the first quarter of 1990 to R3,5 billion in the fourth quarter. On a monthly basis the value of shares traded continued to increase throughout the first four months of 1991, but there was a distinct downward trend in the value of public-sector stock traded from a peak of R24,6 billion in January to R17,5 billion in April.

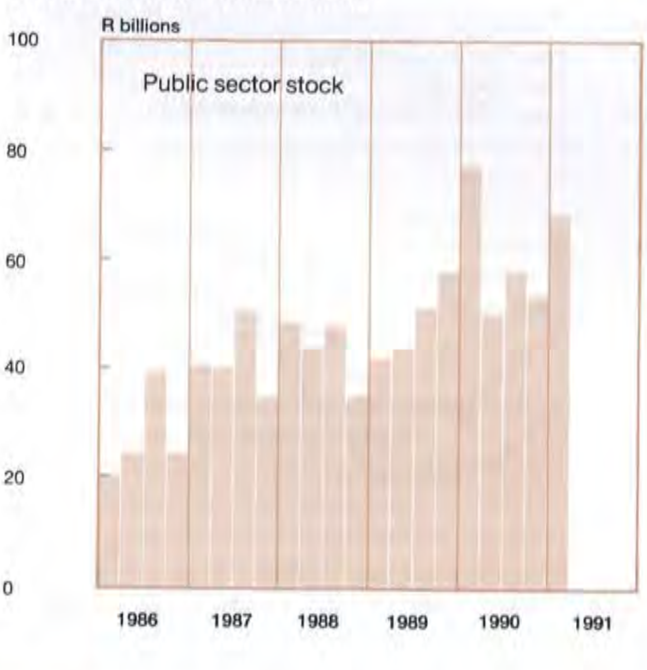
The declining tendency in the value of *transactions by non-residents* on the stock exchange was also reversed in the first four months of 1991. Net average monthly purchases of interest-bearing *stock* by non-residents increased from R51 million in the fourth quarter to R130 million during January to April 1991. Net sales of *shares* by non-residents increased over the same period from R188 million to R303 million.

With the exception of the third quarter of 1990, when they were net purchasers of South African securities (stocks plus shares) on the Johannesburg Stock Exchange, non-residents were net sellers, on balance, of these securities from the beginning of 1990 up to the first four months of 1991. In contrast to the first two months of 1990, non-residents' response to the marked strengthening of the financial rand was fairly limited in the first few months of 1991.

The average price level of all classes of shares, which had declined by 18 per cent from the all-time high point in February 1990 to January 1991, subsequently strengthened by 10 per cent up to March 1991. Share prices continued to rise throughout April and May 1991. In general, the level of *share prices* firmed in all the main categories, with the exception of gold-mining shares. In particular, industrial and commercial share prices gained 15 per cent in the first quarter of 1991. However, the average monthly price level of gold-mining shares declined by no less than 46 per cent during 1990 and by a further 12 per cent in the first three months of 1991, in response to the market's unease about the present and expected future profitability of gold mines.

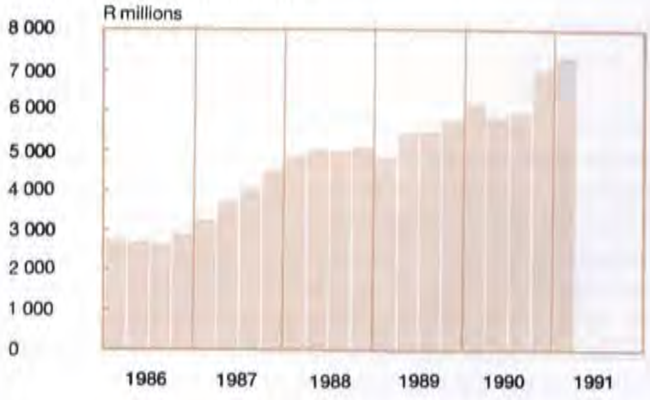
The monthly total value of deals in *futures contracts*, which had declined sharply in the last part of 1990, improved somewhat again in early 1991. In

Stock exchange transactions

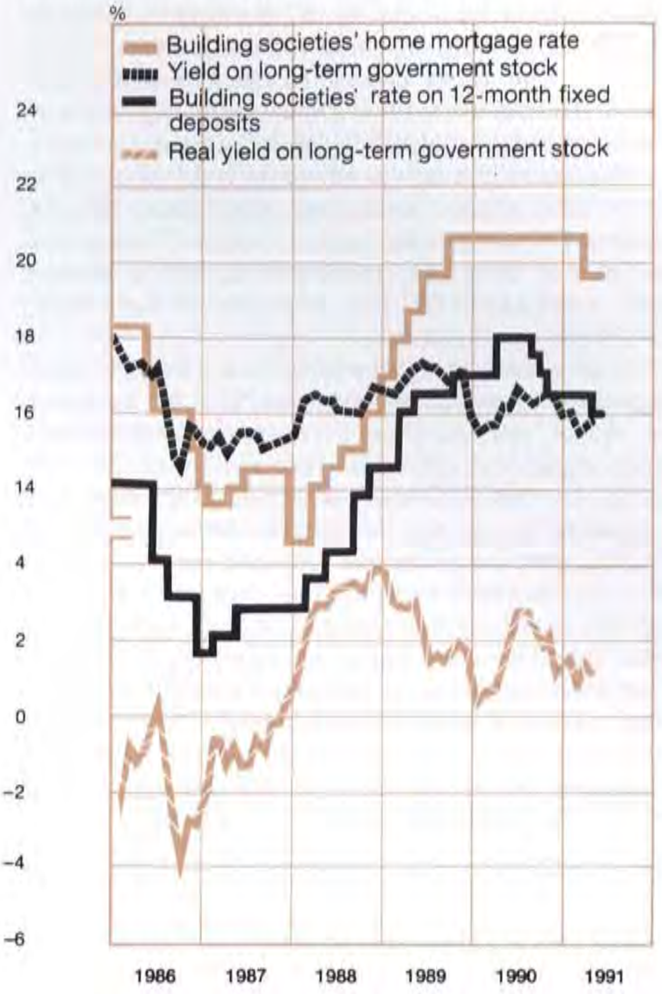


Share prices

Real estate transactions



Capital market interest rates and yields



response to uncertainties created by the crisis situation in the area surrounding the Persian Gulf, the value of these deals reached a record level of R3,1 billion in August 1990 before dropping sharply to R0,9 billion in December. In the first few months of 1991 the value of transactions in futures contracts increased substantially again to R1,9 billion in May.

In the *primary capital markets*, the amount of funds raised by public-sector borrowing entities declined sharply from R5,2 billion in the second quarter of 1990 to R1,4 billion in the fourth quarter and then eased further to R1,3 billion in the first quarter of 1991. The amount of funds raised by private-sector companies through new issues of fixed-interest securities decreased from R316 million in the fourth quarter of 1990 to R106 million in the first quarter of 1991. The value of new issues of ordinary shares by listed private-sector companies also fell over the same two quarters, namely from R1,7 billion to R0,3 billion.

In the *mortgage market* the amount of mortgage loans *paid out* by the building societies increased slightly from R2,2 billion in both the third and the fourth quarter of 1990 to R2,3 billion in the first quarter of 1991. The increase in the banks' and building societies' *holdings* of mortgage loans rose from R1,9 billion in the fourth quarter of 1990 to R2,0 billion in the first quarter of 1991.

The value of *real estate transactions*, on the other hand, increased impressively from R5,8 billion in the third quarter of 1990 to R6,9 billion in the fourth quarter, and to R7,3 billion in the first quarter of 1991.

Capital market yields and interest rates

Reflecting a generally declining trend in capital market yields and lending rates, the average monthly yield on *long-term government stock* eased from 16,7 per cent in June 1990 to 16,0 per cent in December, and somewhat further to 15,6 per cent in February and March 1991. It then firmed slightly to 15,8 per cent in April. This declining trend and the increase in the measured inflation rate resulted in a decline in the *real* yield on long-term government stock from its most recent high point of 2,7 per cent in July 1990 to 1,1 per cent in April 1991.

In contrast to these developments, the building societies' predominant *home mortgage rate*, which had been raised to 20,75 per cent in October 1989 from its previous level of 19,75 per cent, was maintained at this level up to February 1991. This was the longest period in which no change was made in this rate since the period October 1975 – March 1979. Following the Reserve Bank's moderate reduction in accommodation rates, the building societies lowered their home mortgage rate in March 1991 to 19,75 per cent.

The monthly average *dividend yield* on all classes of listed shares eased somewhat from 6,3 per cent in November 1990 to 6,1 per cent in January 1991. It then firmed again slightly to 6,2 per cent in February before decreasing again to 5,9 per cent in March. The relatively sharp decline in March was a reflection of the improvement in the average level of share prices on the Johannesburg Stock Exchange.

The monthly average *earnings yield* on all classes of listed shares (excluding gold-mining shares) declined from 15,4 per cent in October 1990 to 14,0 per cent in December, recovered slightly to 14,3 per cent in February 1991, but decreased sharply again to 13,3 per cent in March.

In contrast to the general declining trend in lending rates, long-term *deposit rates* (with the exception of those on tax-free investments) remained unchanged during the first three months of 1991. For example, the twelve-month deposit interest rate quoted by banks and building societies was kept at 16,5 per cent from October 1990 and was reduced to 16,0 per cent only in April 1991. However, the rates on tax-free investments with building societies, the Post Office Savings Bank and the Treasury, which had been raised to 11,5 per cent in March 1990 from their previous level of 10,0 per cent, were adjusted further to 12,0 per cent in March 1991. Both these increases arose from the gradual phasing-out of the tax concessions applicable to these deposits.

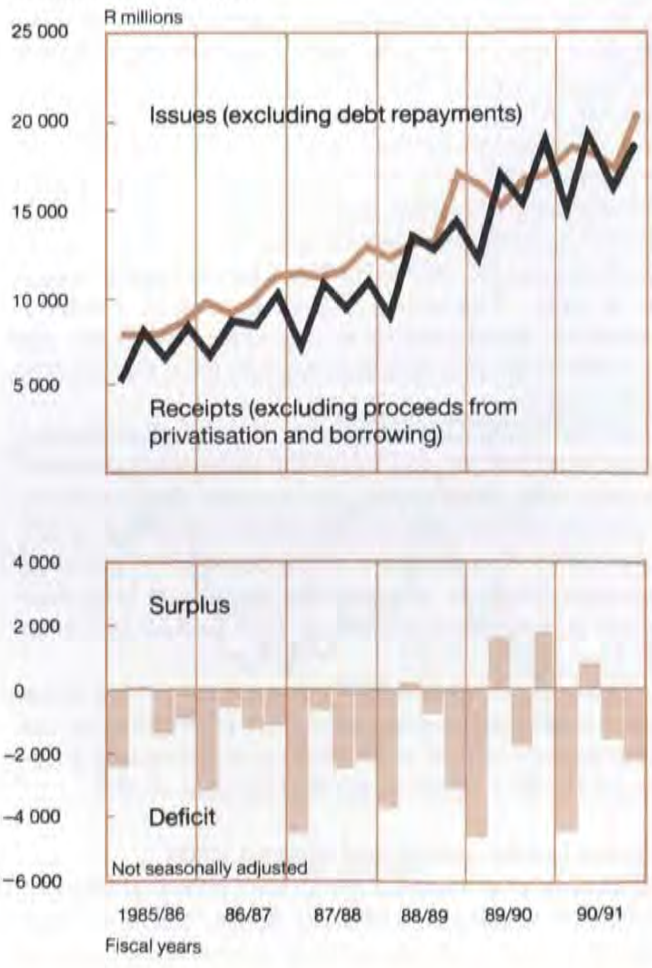
Government finance

Exchequer Account in final quarter of fiscal 1990/91

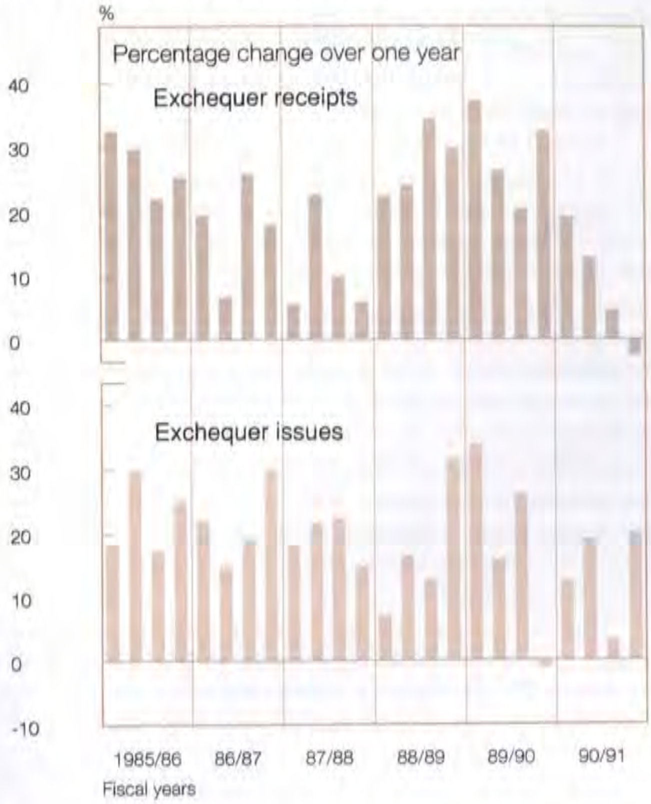
A marked acceleration in Exchequer *issues* was reported during the March or final quarter of fiscal 1990/91. The year-on-year rate of increase in Exchequer issues (after the usual adjustment for changes in the balance on the Paymaster-General Account) increased from only 3,4 per cent in the December quarter of fiscal 1990/91 to as much as 20,1 per cent in the March quarter. In the final quarter of the fiscal year 1989/90 these issues declined by 1,0 per cent, but in the March quarter of fiscal 1988/89 they increased by as much as 31,5 per cent.

In contrast to this much higher rise in Exchequer issues, *receipts* on the Exchequer Account (excluding the proceeds from the privatisation of enterprises in the public sector) actually decreased in the March quarter of fiscal 1990/91. After the year-on-year rate of increase in Exchequer receipts had declined

Exchequer Account



Exchequer receipts and issues



sharply from 19,1 per cent in the June quarter of fiscal 1990/91 to 4,6 per cent in the December quarter, it dropped to a negative figure of 2,5 per cent in the March quarter. This distinct declining tendency in the growth of government revenue was to a large extent the result of lower increases in company taxation, despite an increase in the effective company tax rate, and was probably mainly related to a lower growth in company profits. In addition, customs and excise receipts actually declined during fiscal 1990/91 because of a reduction in the surcharge on certain imports as from 15 March 1990.

The Exchequer deficit before borrowing in the March quarter of fiscal 1990/91 amounted to R2 170 million, or about 3,2 per cent of gross domestic product. This deficit plus the transfers to the Stabilisation Account (R3 792 million in total) were financed by means of new government stock issues (R3 168 million) and Treasury bills (R1 350 million). This allowed the Exchequer to redeem non-marketable debentures (R21 million) and foreign loans (R78 million) and also to increase its available cash balances (R627 million).

Outcome of the Budget for fiscal 1990/91

Notable features of the actual outcome of the Central Government's Budget for the fiscal year 1990/91 included, firstly, a high degree of discipline in the face of strong spending pressures by the authorities over their expenditure. Secondly, government revenue was again underestimated for the fiscal year, but to a much smaller extent than in the previous fiscal year. Lastly, these revenue and expenditure developments resulted in a deficit before borrowing in fiscal 1990/91 that was very close to the original Budget estimates.

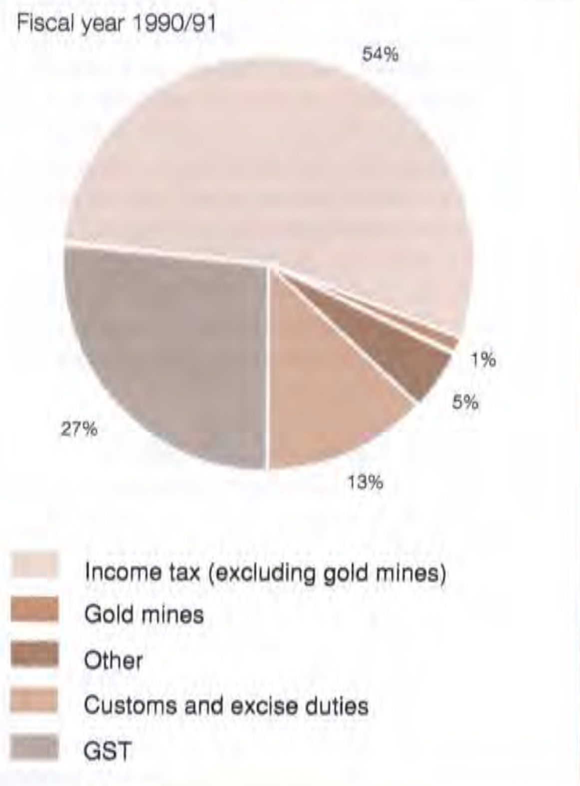
Actual Exchequer *issues* to government departments (on a basis comparable to the Budget figures) increased by 13,1 per cent to R74,4 billion in fiscal 1990/91. This could be compared with the Budget estimate of increases in these issues of 11,9 per cent, after taking into account the amount of R1,0 billion that had been set aside for unforeseen spending needs. This reserve, augmented by a further R1 bil-

State Revenue Fund collections, 1990/91

	Budget[1]		Actual collections	
	R millions	Percentage changes[2]	R millions	Percentage change[2]
Total collections from gold mines	1 264	-6,1	826	-38,6
Other income tax collections	34 761	10,6	36 455	16,0
General sales tax	18 532	12,5	17 977	8,6
Customs and excise duties[3]	7 871	10,2	8 587	-2,5
Other receipts	2 510	-14,0	3 284	-12,5
Total collections	**64 938**	**5,8**	**67 129**	**8,6**

1 Second and final print.
2 Compared with actual collections during the fiscal year 1989/90.
3 Excluding amounts transferable to neighbouring countries but including the surcharge on imports and the fuel levy.

Composition of government revenue



lion, was eventually used mainly to expand protection services. Other additional expenditure was incurred mainly for the reduction of capital backlogs in education, land purchases for urbanisation, and government debt servicing costs.

Despite these additional outlays, government expenditure in real or inflation-adjusted terms decreased by about 1,0 per cent in fiscal 1990/91. The extent of overspending by the Central Government came to only 2,0 per cent of the original Budget estimate, compared with the low figure of 1,2 per cent in fiscal 1989/90 and an average overspending ratio of 5,1 per cent in the ten fiscal years from 1980/81 to 1989/90. The ratio of government expenditure to gross domestic product nevertheless increased slightly from 27,4 per cent in fiscal 1989/90 to 27,5 per cent in fiscal 1990/91.

Total government *revenue* (also on a basis comparable with Budget projections) in fiscal 1990/91 exceeded the Budget estimates by R2,2 billion, or by 3,4 per cent; in fiscal 1989/90 the actual government revenue was 12,2 per cent higher than the Budget figure. The year-to-year rate of increase in government revenue amounted to 8,6 per cent in fiscal 1990/91, as against 5,8 per cent provided for in the Budget. Because of this relatively small rise in nominal government revenue, the ratio of government revenue to the gross domestic product declined from 25,7 per cent in fiscal 1989/90 to 24,8 per cent in fiscal 1990/91. In real terms government revenue decreased by 4,9 per cent.

As shown in the accompanying table, lower-than-budgeted increases in revenue were recorded in respect of gold mining tax and from general sales tax. These lower collections could mainly be attributed to a lower-than-expected gold price and a lower level of economic activity than had been foreseen. In contrast to these developments, income tax collections from individuals and non-gold-mining companies exceeded the Budget estimates to a considerable extent, mainly because of higher-than-expected wage increases and more effective tax collection procedures. The higher-than-estimated receipts from customs and excise duties were realised despite lower-than-budgeted collections from the fuel levy.

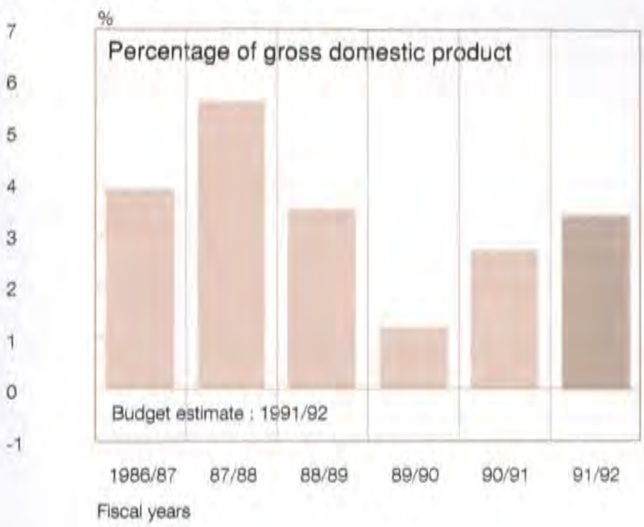
The *deficit before borrowing* and debt repayment in fiscal 1990/91 amounted to R7 267 million, or about 2,7 per cent of gross domestic product. In the Budget for 1990/91 allowance had been made for a larger deficit of R7 994 million or 2,8 per cent of gross domestic product. After taking the discount of R2 966 million on new government stock into account, the total deficit amounted to R10 233 million, which was financed from the following sources:

	R millions
Public Debt Commissioners	4 201
Non-bank private sector	4 432
Banking sector:	
Corporation for Public Deposits	505
Other banks	9 013
Foreign sector	-79
Total gross financing	18 072
Less payments to:	
IDT	2 000
South African Reserve Bank	3 000
Government pension funds	1 000
Development Bank of Southern Africa	216
Less transfers to the Stabilisation Account	1 623
Total net financing of deficit and discount	**10 233**

The Government Budget for 1991/92

In his presentation of the Budget for the fiscal year 1991/92 to Parliament on 20 March 1991, the Minister of Finance stated that the *theme* of the Budget was "equity through growth and stability". The Minister described "equity" as actions conducted by the Government on the revenue side in the fairest possible manner and on the expenditure side as actions

Deficit before borrowing



to give those in real need a chance to survive. The crucial issue in the Budget was to ensure the proper balance between the pressing needs for welfare augmentation and the no less urgent need for more rapid economic growth.

The aspects of the Budget that served to create a climate for growth and employment were summarised by the Minister as the reinforcement of the downward trend in inflation, the maintenance of a relatively stable exchange rate of the rand, the promotion of a climate conducive to investment, the support of institutions that are contributing to job creation, and the promotion of small businesses. The Minister also noted some aspects of the Budget that were intended to create a climate for stability such as increased social spending, the extension of the Police Force and the maintenance of fiscal discipline.

In accordance with the pressing needs of a growing part of the population, a large part of government funds was allocated to a strengthening of the share of social services in total government *expenditure* from 38,7 per cent in fiscal 1990/91 to 40,5 per cent in fiscal 1991/92. In particular, the Minister announced considerable increases in the expenditure on education and on social assistance allowances. Relatively small increases in spending on housing and health were explained by the Minister as being made possible by large expenditure on housing by the Independent Development Trust and rising private-sector expenditure on curative health services for that portion of the population that can afford to pay cost-related tariffs. Considerable cuts in expenditure on defence were announced in the Budget, a large part of which unfortunately had to be devoted to the maintenance of internal law and order. The Minister also provided for a significant increase in the remuneration of civil service employees.

On the *revenue* side of the Budget, the main feature was the announcement of the introduction of Value Added Tax (VAT) as from 30 September 1991 at a rate of 12 per cent to replace the existing general sales tax of 13 per cent. Other tax proposals for fiscal 1991/92 included increased excise duties, a further phasing-out of the surcharge on imports of especially capital and intermediate goods, an increase in the fuel levy, reductions in marketable securities tax rates and the stamp duty, the introduction of a new tax on interest received by deposit-taking institutions, a revised tax formula to lower taxes on gold mines, the reduction of the tax rate on companies from 50 to 48 per cent, the reduction of the maximum marginal tax rate for married men from 44 to 43 per cent, separate taxation of married women's investment income and an increase in the SITE ceiling to R50 000.

Government expenditure, including a contingency reserve of R1,2 billion, was budgeted to increase in fiscal 1991/92 by 13,7 per cent and government revenue by 11,1 per cent. Identified capital expenditure was estimated at R5,4 billion, or about 1,8 per cent of the expected gross domestic product. In view of the more rapid rise in expenditure than in revenue, the *deficit before borrowing* was projected to increase from R7 267 million in fiscal 1990/91 to R10 118 million in fiscal 1991/92, or from 2,7 to 3,4 per cent of the prospective gross domestic product. It was further proposed that this deficit be financed mainly by the issue of new government stock and by the use of available balances.

Budget of 1991/92

	R millions
Revenue	74 866
Expenditure	84 984
Deficit (before borrowing)	10 118
Financing (net of debt repayment):	
New government stock issues	9 181
Non-marketable securities	–185
Foreign loans	3
Sale of assets	950
Use of available balances	2 003
	11 952
Less: Transfers and payments	1 834
Total net financing	10 118

Exchequer account in April 1991

In April 1991, i.e. in the first month of fiscal 1991/92, Exchequer issues (after the usual adjustment for changes in the balance on the Paymaster-General Account) were 28,3 per cent higher than in April 1990. Exchequer receipts also increased more rapidly than provided for in the Budget and, compared with the same month of the previous year, rose by 16,1 per cent. The deficit before borrowing in April 1991 amounted to R2 726 million, exceeding the deficit in April 1990 by as much as R1 022 million or 60 per cent.