Quarterly economic review

Introduction

As discussed in some detail in the Reserve Bank's *Annual Economic Report* of 1992, the downturn in economic activity deepened further in the first half of 1992. The rate of decrease in real gross domestic product therefore accelerated from ½ per cent in both 1990 and 1991 to annualised rates of 2 and 2½ per cent in the first two quarters of 1992. Although this acceleration was caused mainly by poor agricultural conditions, the real value added by the other sectors nevertheless decreased, at an annualised rate of almost 1 per cent, in the first half of 1992. Uncertainty arising from political developments and internal unrest in the country created a climate that was not conducive to domestic economic growth, while export growth was hampered by the slow and hesitant economic recovery in the major industrialised countries.

The recession not only deepened, but also became more widespread throughout the economy. In the first half of 1992 decreases were registered in the value added by most of the economic sectors such as agriculture, non-gold-mining, manufacturing, construction and wholesale and retail trade. These negative contributions to domestic output were offset somewhat by only small increases in gold-mining output and in the value added by transport, finance and general government.

Real gross domestic expenditure has shown a distinct declining trend since the second quarter of 1988 – i.e. from even before the downturn in economic activity. In the second quarter of 1992 real gross domestic expenditure declined at a seasonally adjusted and annualised rate of 6½ per cent because of declines in real private consumption expenditure and real gross domestic fixed investment, and the reversal of the build-up of inventories in the preceding quarter. Consumption expenditure by general government continued to increase, albeit at a lower rate.

Households' consumption expenditure in the second quarter of 1992 was constrained by factors such as a decline in real personal disposable income, the increased number of unemployed people, a general lack of job security, the heavy burden of existing consumer debt and a decline in the net wealth of households. In particular, real private consumption expenditure on durable consumer goods fell rapidly, while real outlays on non-durable goods and services also continued to contract. However, real expenditure on semi-durable goods rose slightly in both the first and the second quarter of 1992.

Much more disconcerting has been the substantial decrease in gross domestic fixed investment. From a high in the fourth quarter of 1989 until the second quarter of 1992 real gross domestic fixed capital formation declined by almost 19 per cent. Moreover, the largest part of capital expenditure was used to replace existing assets and not to extend the production capacity of the economy. Net domestic fixed investment as a ratio of gross domestic product therefore declined to only 1 per cent in the second quarter of 1992, compared with average ratios of 14½ per cent in the 1970s and 8 per cent in the 1980s. This low level of current investment has serious implications for future economic growth.

The domestic savings ratio also weakened further in the second quarter of 1992. The low level of domestic savings in this quarter reflected continuing net dissaving by general government because of a sustained high level of current government expenditure and lower than expected government revenue, as well as a decline in net saving by the corporate sector because of lower profits. Net saving by households improved marginally because the decline in real private consumption expenditure exceeded the decline in real personal disposable income.

The deepening of the recession also seriously affected the availability of employment in the formal sectors of the economy. Despite an estimated decrease of 200 000 employment opportunities from the beginning of the downturn until the first quarter of 1992, the rate of increase in nominal salaries and wages per worker declined only moderately from very high levels. Real wages therefore continued to rise, contributing to the persistent and relatively high rate of price inflation. The impact of the severe drought on food prices and fears arising from the increase in the relative size of the budget deficit that financial discipline may wane, prevented a meaningful decrease in inflation. However, encouraging signs have appeared recently that the rate of price increases is beginning to recede.

As could be expected, the decline in economic activity led to a decrease in the volume of merchandise imports, which was countered somewhat by higher agricultural imports in the second quarter of 1992 because of the drought. A rise in the volume of merchandise exports continued to support the level of domestic production and, together with a small decline in net service and transfer payments, offset a sharp decrease in the value of net gold exports. The result of these developments was that a surplus on the current account of the balance of payments of nearly 2 per cent of gross domestic product was still recorded in the second quarter of 1992.

This surplus was accompanied by a net outflow of capital of R1,9 billion. The renewed large capital outflow was mainly caused by an outflow of short-term capital related to political uncertainties and social unrest, while the outflow of long-term capital declined to only a small amount. The net gold and other foreign reserves therefore decreased moderately in the second quarter of 1992, after having risen fairly consistently from the beginning of 1990. The total gross gold and other foreign reserves nevertheless had risen to a level above the equivalent of two months' imports of goods and services at the end of July 1992. The healthy overall balance of payments position facilitated the maintenance of a relatively stable real effective exchange rate of the rand during the first seven months of 1992.

The twelve-month growth rates of almost all the monetary aggregates decelerated significantly further from the beginning of 1992 and most of the monthly growth rates of M3 were well within the guideline range. A low demand for credit and the relatively high cost of borrowing caused the growth in credit extended to slow down sharply in the first half of 1992. In particular, the growth in hire-purchase credit and overdrafts contracted substantially, while mortgage advances and leasing finance continued to rise at relatively high rates.

In the financial markets, the money market was at first characterised by a high level of liquidity. Since May 1992 tighter conditions have been experienced, which could mainly be attributed to a sharp increase in government deposits, reflecting substantial sales of government stock. In the capital market, trading activity bore little relation to the pace of activity in the real economy in the first half of 1992. New record levels were registered in the turnover of public-sector stock and in the trade in derivative instruments, while share prices also rose to new record levels. The continued political impasse, mass action, the weakening economy and worse than expected financial results of certain companies subsequently had a profound effect on capital market activity in July and August 1992. Share prices softened, stock prices rose sharply, higher trading volumes were generally recorded, and activity on the derivative markets increased further.

Long-term interest rates declined sharply in the first eight months of 1992, reflecting more optimistic inflation expectations, a softening of short rates, a weaker than expected real economy and the lowering of Bank rate. The gradual decline in money market interest rates since early 1990 also gathered momentum in the first eight months of 1992 as money market participants became convinced that inflation rates would subside and anticipated a lowering of Bank rate. At the end of August 1992 the rate on three-month liquid bankers' acceptances was 3,5 percentage points below the Reserve Bank's rediscount rate for such acceptances.

In the area of public finance, the public-sector borrowing requirement improved moderately in the second quarter of 1992 (i.e. in the first quarter of fiscal 1992/93) because cutbacks and rationalisation programmes by non-financial public enterprises led to surplus funds being available for lending to other sectors. However, the borrowing requirement of general government deteriorated markedly. Although all levels of general government, with the notable exception of local authorities, were responsible for this increase in the general government's borrowing requirement, the deficit before borrowing on especially the Exchequer Account increased sharply. Exchequer revenue fell considerably short of the budgeted amount, while Exchequer issues remained at fairly high levels. The lower revenue collections of the government were mainly caused by disappointing proceeds from value-added and income tax, reflecting the deepening of the recession.

In a statement on 3 September 1992, the Minister of Finance and of Trade and Industry indicated that these lower tax proceeds will lead to a larger deficit before borrowing on the Budget for fiscal 1992/93 than originally projected, because efforts to raise additional revenue at this juncture would be counter-productive. Fortunately, the bond market seemed capable of financing these larger government borrowing requirements from non-monetary sources without materially affecting interest rate movements. However, the Minister also stated that it was important that the growth in consumption expenditure of general government be restrained in favour of a much higher rate of fixed investment in new productive capacity, and that a process has already been set in motion to achieve spending guidelines incorporating these principles for fiscal 1993/94.

Economic conditions during the first half of 1992 indicate clearly that the smaller but at least further increase in the volume of South Africa's exports will be unable to neutralise the effects of the poor agricultural conditions, and of the decreases in real private consumption expenditure and real domestic fixed investment. It can therefore readily be predicted that the real gross domestic product will again decline in 1992, and that this rate of decrease could amount to about 1½ per cent. It is, however, considerably more difficult to predict at what point in time a lower turning-point of the business cycle will be reached. An upturn in economic activity will depend on factors such as agricultural conditions in the forthcoming season in the summer rainfall area, the extent of growth in the economies of major industrialised countries and world trade, and on domestic political developments.

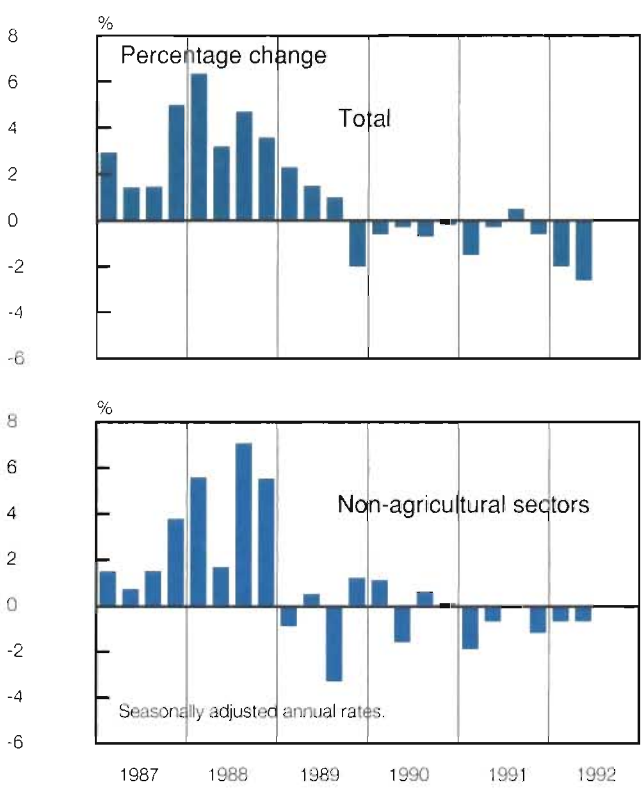
Domestic economic developments

Domestic production

The deepening in the downturn of real economic activity during the first half of 1992 is clearly reflected by developments in *aggregate real domestic output*. After having declined by ½ per cent in both 1990 and 1991, real gross domestic product contracted at annualised rates of 2 and 2½ per cent in the first two quarters of 1992. This accelerated decrease in real gross value added was mainly due to poor agricultural conditions in a large part of the country. Excluding the value added by agriculture, the real gross domestic output of the other sectors declined at an annualised rate of almost 1 per cent in the second quarter of 1992 – i.e. at about the same rate as in the preceding quarter as well as in 1991 as a whole.

The real value added by the *agricultural sector* changed from positive growth at an annualised rate of 5 per cent in the fourth quarter of 1991 to negative annualised rates of 17 per cent in the first quarter of 1992 and 28 per cent in the second quarter. The failure of the maize crop was largely responsible for the lower agricultural output. The drought also caused severe damage to other field crops and horticultural production. Current estimates show that the production of grain sorghum, sunflower seed, soya beans and dry beans will be more than halved in the 1991/92 season.

Real gross domestic product

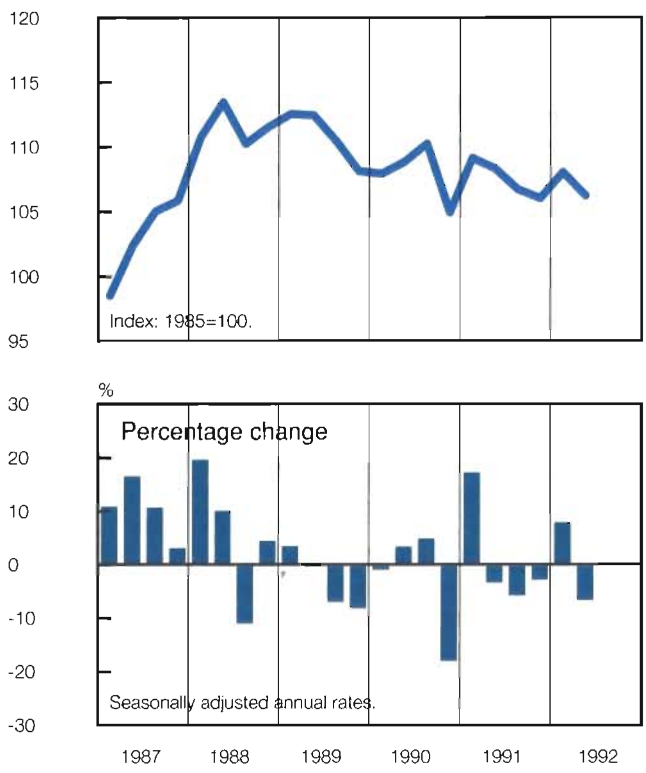


In contrast to these developments, the real value added by the *mining industry* continued to rise over the past four quarters. The annualised rate of increase in real mining output rose from ½ per cent in the third quarter of 1991 to 1 per cent in the fourth quarter and to approximately 1½ per cent in the first two quarters of 1992. This rise in the real value added by mining was mainly the result of a corresponding increase in gold production. In the second quarter of 1992 the real output of gold mines was 2½ per cent higher than in the corresponding quarter of 1991 because of an increase in the quantity and quality of ore milled. Production by a new mine, which came into operation in the second half of 1991, was also responsible for an increase in diamond output; this increase was countered by declines in the real value added by other mines on account of the low international demand for commodities.

The real value added by the *secondary sectors* contracted at an annualised rate of 2½ per cent in the second quarter of 1992; this was almost equal to the rate of decline in the first quarter of 1992 and slightly higher than the average annual rate of decrease of 2 per cent in 1991 as a whole. This further decline in the output of the secondary sectors was extensive and even the value added by the sector supplying electricity, gas and water receded at an annualised rate of 2 per cent in the second quarter of 1992. The real output of the construction industry contracted at an annualised rate of 9 per cent, while the rate of decline in manufacturing output decreased slightly from an annualised rate of 2½ per cent in the first quarter of 1992 to nearly 2 per cent in the second quarter. All these secondary sectors were therefore seriously affected by the decline in real domestic demand coupled with only a sluggish upturn in world output growth. Politically inspired worker actions, such as mass demonstrations, stay-aways, strikes and sporadic violence, as well as a large number of public holidays, also caused a drop in production in the second quarter of 1992.

Real value added by the *tertiary sectors*, which until the third quarter of 1991 showed a distinct but moderately increasing trend in the current recession, began to decrease slightly at annualised rates of less than ½ per cent from the fourth quarter of 1991. This decrease was, however, mainly confined to a contraction in the real value added by commerce, while moderate increases were still recorded in the real output of transport, finance and general government. The real value added by commerce, which had started to decline from the beginning of 1991, contracted further at annualised rates of approximately 2½ per cent

Real gross domestic expenditure



in the first two quarters of 1992. The rates of increase in the value added by the other tertiary sectors varied between ½ and 1 per cent.

Domestic expenditure

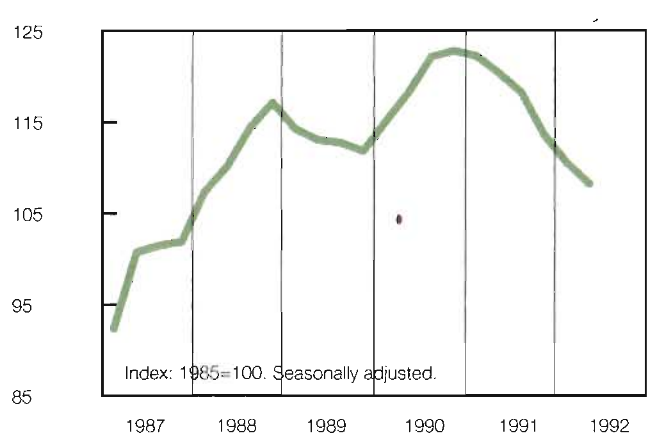
Manifesting the severe recessionary conditions in the economy, *aggregate real gross domestic expenditure* has shown a downward trend since the second quarter of 1988. Owing mainly to an involuntary build-up of inventories, real domestic expenditure rose at an annualised rate of 8 per cent in the first quarter of 1992. This unexpected increase in domestic expenditure was reversed again in the second quarter of 1992 when total expenditure declined at an annualised rate of 6½ per cent.

The contraction in total real gross domestic expenditure in the second quarter of 1992 resulted from further declines in real private consumption expenditure and real gross domestic fixed investment, and the reversal of the build-up of inventories in the preceding quarter. *Consumption expenditure by general government* increased further, albeit at a lower rate of 2½ per cent against quarter-to-quarter changes at annualised rates of 4 per cent and 3 per cent in the fourth quarter of 1991 and the first quarter of 1992. Real expenditure on intermediate goods and services by general government continued to rise sharply, but the rate of increase in real remuneration of government employees fell back from an annualised rate of 4½ per cent in the first quarter of 1991 to about ½ per cent in the second quarter of 1992.

Real outlays on *private consumption expenditure*, which began to decline in the second quarter of 1991, again decreased in the second quarter of 1992. The rate of contraction in real consumption expenditure by households amounted to an annualised figure of 3 per cent in the second quarter of 1992; this was slightly less than the revised estimated decline of 3½ per cent in the first quarter of 1992 and brought the total decline in real outlays on consumer goods and services to about 2 per cent in the year ended June 1992. Households' consumption expenditure was held back by factors such as a decline in real personal disposable income, the increased number of unemployed people, a general lack of job security, the heavy burden of existing consumer debt and a decline in the net wealth of households.

In particular, real private consumption expenditure on *durable consumer goods* continued to fall rapidly in the second quarter of 1992. Real expenditure on durable consumer goods decreased at an annualised rate of 8 per cent in this quarter, compared with 10½ per cent in the first quarter of 1992 and almost 15 per cent in the fourth quarter of 1991. This decline occurred despite a decrease in finance charges on households' credit transactions and the recent amendments to the Credit Agreements Act, which were specifically introduced to support the depressed automobile industry. The amendments entailed a reduction from 15 to 10 per cent in the minimum deposit required for the purchase of a new motor

Real durable consumption expenditure



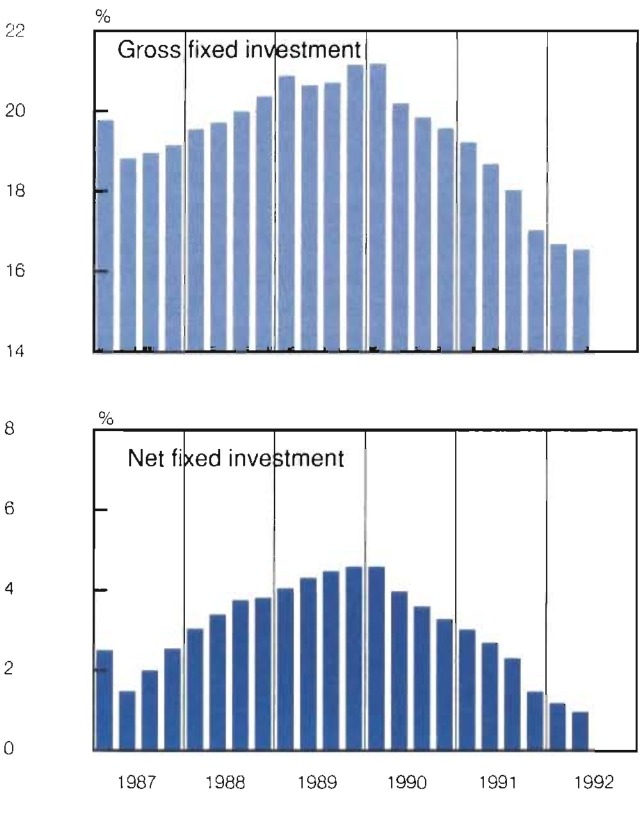
vehicle and the extension of the repayment period from 42 months to 54 months.

Real consumer outlays on *non-durable goods and services* also still contracted. Moreover, the rate of decrease in consumer purchases of non-durable goods (seasonally adjusted and annualised) accelerated sharply from 1½ per cent in the second quarter of 1991 to 3½ per cent in the first quarter of 1992 and to as much as 4½ per cent in the second quarter. In contrast to these developments, real expenditure on *semi-durable goods* rose at an annualised rate of ½ per cent in both the first and the second quarter of 1992. The turnaround in this type of consumer expenditure was probably related to more aggressive marketing by the clothing and footwear trade and to the availability of less expensive imported goods.

The rate of decrease in total *real gross domestic fixed investment* slowed down slightly in the second quarter of 1992 to an estimated annualised rate of about 4 per cent; real fixed investment decreased at an annualised rate of 6½ per cent (revised figure) in the first quarter of 1992 and by 8½ per cent in 1991 as a whole. From a high in the fourth quarter of 1989 until the second quarter of 1992 real gross fixed capital formation declined by almost 19 per cent. As a ratio of gross domestic product, fixed investment contracted from a peak of 21 per cent to only 16½ per cent over the same period. If depreciation allowances are taken into account, net domestic fixed investment as a ratio of gross domestic product decreased from an already low level of 4½ per cent in the fourth quarter of 1989 to only 1 per cent in the second quarter of 1992. At present, the production capacity of the economy is therefore scarcely being extended; by far the larger part of fixed investment outlays is used to replace existing assets. This low net investment ratio can be compared with average ratios of 14½ per cent in the 1970s and 8 per cent in the 1980s.

As shown in the accompanying table, the decline in fixed investment since the beginning of 1990 took place in all the main institutional sectors. However, the rate of decrease in investment by the *public sector* (public corporations and public authorities) was considerably higher than the rate of decrease in investment by the private sector, clearly indicating the contraction in expenditure on the infrastructural development of the country and the existing surplus production capacity in some of the public utility companies.

Fixed investment as percentage of gross domestic product



Decrease in real gross domestic fixed investment from the fourth quarter of 1989 to the second quarter of 1992

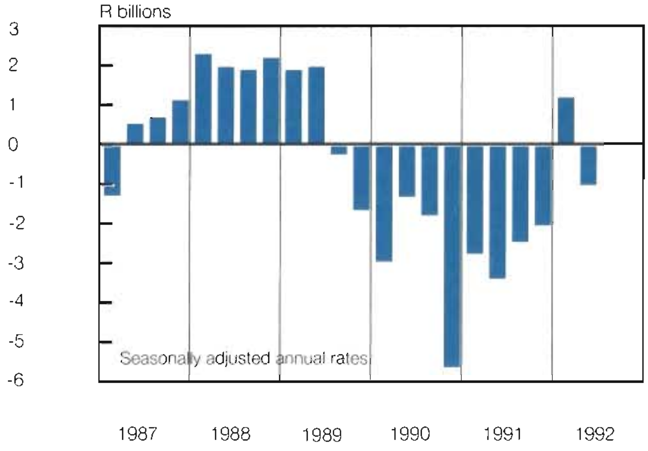
%

Private sector	-9½
Public corporations	-52½
Public authorities	-22
Total fixed investment	**-19**

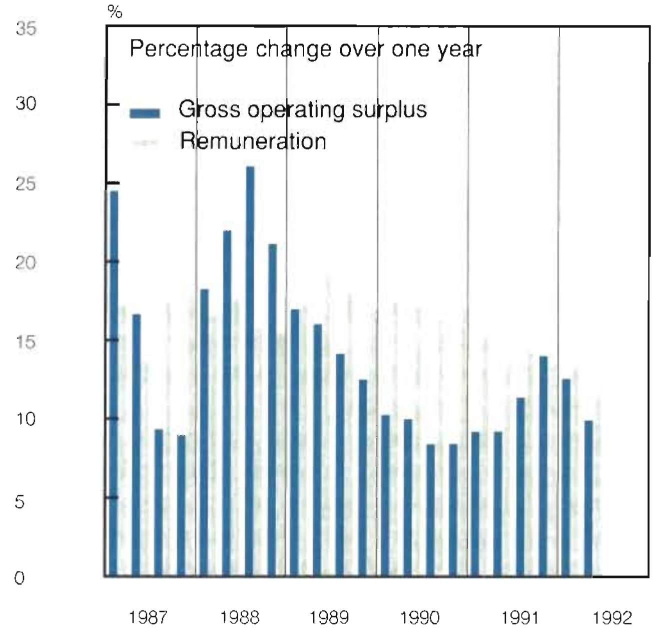
In the second quarter of 1992 fixed investment by public corporations increased somewhat from its very low base, while real fixed investment expenditure by public authorities continued on its downward trend. Decreases in the real outlays on capital expenditure by Transnet, Telkom and the South African Post Office in the latter sector outweighed a somewhat moderate increase in capital spending by general government.

Real fixed investment in the *private sector* decreased further at an annualised rate of nearly 2 per cent in the second quarter of 1992; in the preceding four quarters the rate of decrease in this aggregate was slightly higher, varying between 2 and 3 per cent. With the exception of the mining sector, the real fixed capital formation of all the other economic sectors declined. Significant declines were recorded in the investment expenditure of agriculture and manufacturing. Despite the generally depressed state of the mining sector, capital expenditure on several large mining projects caused this sector's real capital formation to rise at an annualised rate of 2½ per cent in the second quarter of 1992.

Change in real inventories



Gross operating surplus and remuneration



The decumulation of *inventories* in the second quarter of 1992 was mainly due to a drawing-down of inventories in private manufacturing and wholesale trade. This brought the ratio of industrial and commercial inventories to gross domestic product to a level of 18 per cent, compared with approximately 18½ per cent in 1991 as a whole. Increases were, however, recorded in the real inventory levels in the mining sector and in agricultural stocks-in-trade. The increase in the latter was mainly related to the early harvesting of the current maize crop and stockpiles of imported maize. Despite these increases, the ratio of inventories (excluding strategic stocks and livestock) to the gross domestic product deteriorated further to 23½ per cent in the second quarter of 1992, which was substantially lower than the ratio of 29 per cent in the second quarter of 1989 – i.e. at the beginning of the current downswing in economic activity.

Factor income and domestic saving

The growth in aggregate nominal factor income over a period of twelve months continued to slow down to 10½ per cent in the second quarter of 1992; in the first quarter of 1992 it has amounted to 12 per cent. This decline was partly due to a decrease in the year-on-year rate of increase in total nominal labour remuneration from 13½ per cent in the first quarter of 1992 to 12½ per cent in the second quarter. In addition, the growth in the gross operating surplus over twelve months also slowed down from 12½ per cent in the first quarter of 1992 to 10 per cent in the second quarter.

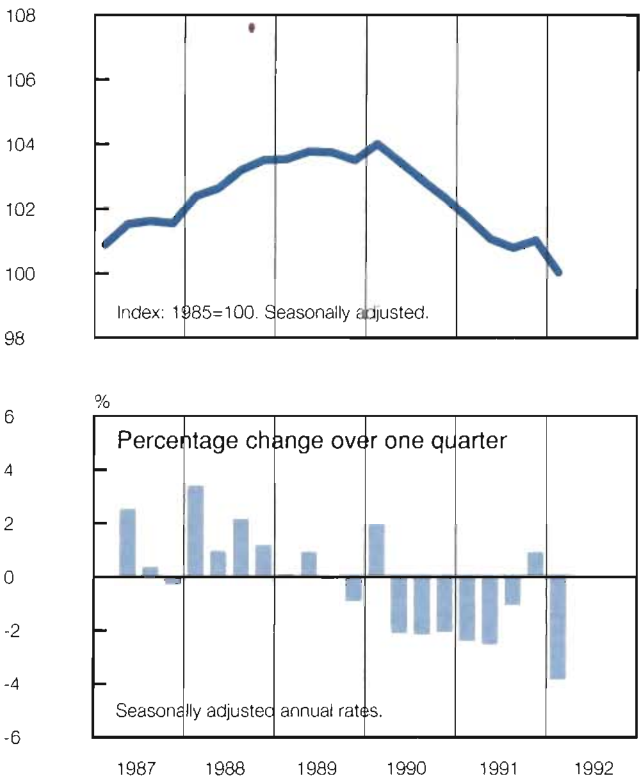
The ratio of gross *domestic saving* to gross domestic product weakened to about 18 per cent in the second quarter of 1992 from 18½ per cent in the first quarter and approximately 19 per cent in calendar 1991. This low level of gross domestic saving reflected continued net dissaving by the general government because of a sustained high level of current government expenditure and lower than expected government revenue. Net saving by the corporate sector also declined because of dividend pay-outs being maintained in the face of declining company profits.

Net saving by households improved marginally and the ratio of personal saving to personal disposable income strengthened from an average of 2 per cent in 1991 to 3 per cent in the first half of 1992. This could be attributed to a fairly marked decline in households' real consumption expenditure, which exceeded the decline in aggregate real personal disposable income.

Employment

Total employment in the non-agricultural sectors of the formal economy reacted strongly to the cyclical downturn in economic activity and declined by 0,5 and 2,0 per cent in 1990 and 1991, respectively. This decline started in the third quarter of 1989 and accelerated to 2,5 per cent (seasonally adjusted and annualised) in the second quarter of 1991 before subsiding moderately to 1,1 per cent in the third quarter. Large increases in employment by the public authorities in the fourth quarter of 1991 then caused total employment in the non-agricultural sectors of the economy to increase at a seasonally adjusted and annualised rate of 0,9 per cent. In the first quarter of

Non-agricultural employment



1992 total employment declined markedly again by 3,9 per cent – the highest quarterly rate of decline recorded during the current downswing.

The effect of the lower level of economic activity on employment was felt largely in the non-agricultural *private sector* of the economy. Total employment by private enterprises declined by 0,7 and 3,4 per cent in 1990 and 1991. The quarter-to-quarter rate of decrease accelerated from a seasonally adjusted and annualised rate of 0,4 per cent in the first quarter of 1989 to a peak of 5,2 per cent in the first quarter of 1991; it then slowed down to only 0,1 per cent in the fourth quarter. A large number of labour retrenchments in mining, manufacturing, construction and retail trade then caused the rate of decrease in private-sector employment to accelerate significantly to a seasonally adjusted and annualised rate of 4,6 per cent in the first quarter of 1992. Preliminary information for the second quarter indicates that employment in manufacturing, construction and electricity generation declined further.

In contrast to these developments, employment by the *public authorities* increased at rates of 0,1 per cent in 1990 and 1,6 per cent in 1991. On a quarterly basis declines in the labour force of this sector in some quarters were followed by increases in subsequent quarters. More recently, quarter-to-quarter rates of increase (seasonally adjusted and annualised) amounting to 0,6 and 3,3 per cent in the last two quarters of 1991, were followed by a decline in employment of 2,1 per cent in the first quarter of 1992.

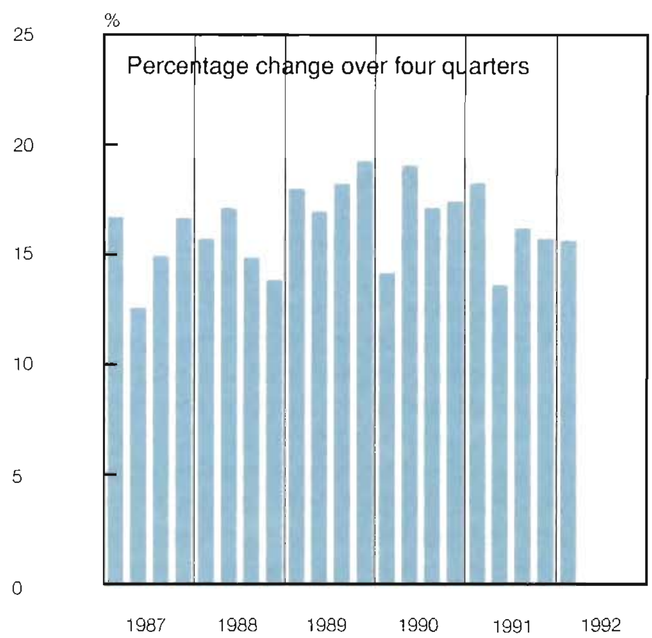
As could be expected, the seasonally adjusted total number of *registered unemployed workers* increased with the declining level of formal employment in the non-agricultural sectors of the economy. The average level of unemployed workers in 1991 was 10,4 per cent higher than during the second half of 1990, and the average for the first three months of 1992 was 14,3 per cent higher than in the corresponding period of 1991.

Labour costs and productivity

Despite a loss of approximately 200 000 employment opportunities from the beginning of the downturn of economic activity until the first quarter of 1992, the rate of increase in *nominal salaries and wages per worker* in the non-agricultural sectors of the economy declined only moderately from 18,0 per cent in 1989 to a still high level of 15,8 per cent in 1991. The year-on-year rate of increase in nominal remuneration per worker also amounted to as much as 15,7 per cent in the first quarter of 1992.

During this period the increases recorded in the nominal remuneration per worker employed by the *public authorities* were consistently higher than those

Nominal remuneration per employee in non-agricultural sectors



of workers in the private sector. From the first quarter of 1989 to the first quarter of 1991 the nominal salaries and wages per worker employed by the public authorities generally increased at rates close to and sometimes even higher than 20 per cent; the rate of increases then slowed down considerably in 1991. The year-to-year rate of increase in the nominal salaries and wages per worker employed by the public authorities therefore declined from a peak of 21,9 per cent in 1989 to 17,3 per cent in 1991. In the first quarter of 1992 the remuneration per worker employed by public authorities was 16,2 per cent higher than in the corresponding quarter of 1991.

The rate of increase in nominal salaries and wages per worker in the non-agricultural *private sector* of the economy fluctuated between 16 and 17 per cent in 1988 to 1990, but then declined substantially to 14,8 per cent in 1991. In the first quarter of 1992 it reaccelerated again to a year-on-year rate of 15,4 per cent, from 13,8 per cent in the fourth quarter of 1991. Available information for the second quarter points to a deceleration of the wage increases in manufacturing, construction and electricity generation.

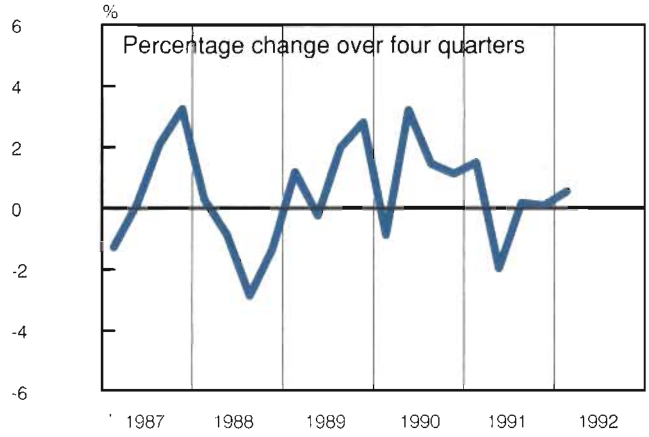
The slower growth in nominal salaries and wages per worker was mainly responsible for a decline in the rate of increase in the *real wage* per worker (as deflated by the non-agricultural gross domestic product deflator) from 2,3 per cent in 1989 to 1,2 per cent in 1991 and to a year-on-year rate of 1,7 per cent in the first quarter of 1992. None the less, the real wage per worker continued to increase in a period of low economic growth and a substantial decline in employment, indicating a serious structural problem in the South African economy and contributing to the persistently high price inflation.

The rate of increase in real *labour productivity* in the non-agricultural sectors simultaneously declined sharply from 2,3 per cent in 1988 to only 0,4 per cent in 1990 before rising moderately again to 1,3 per cent in 1991. This increase in productivity already started in the third quarter of 1990, and the year-on-year rate of increase in real output per worker accelerated from 1,2 per cent in that quarter to 1,9 per cent in the second quarter of 1991; it then slowed down to 0,3 per cent in the fourth quarter of 1991 before reaccelerating to 1,0 per cent in the first quarter of 1992.

The rapid increases in the nominal salaries and wages per worker coupled with the relatively poor performance of labour productivity, resulted in high rates of increase in *nominal unit labour costs*. However, the rate of increase in nominal labour costs per unit of physical output declined from 17,1 per cent in 1989 to 16,5 per cent in 1990 and more noticeably to 14,4 per cent in 1991. In the first quarter of 1992 nominal unit labour costs were 14,7 per cent higher than in the corresponding quarter of 1991.

The rate of increase in the *real unit labour costs* (as deflated by the price deflator for the non-agricultural gross domestic product) declined from 1,4 per cent in 1989 to 1,2 per cent in 1990. In 1991 real labour costs per unit of physical output decreased by 0,1 per cent. The year-on-year rate of increase in real unit labour costs receded substantially from 3,2 per cent in the second quarter of 1990 to 1,5 per cent in the first quarter of 1991. Real labour costs per unit of physical output then fell by 2,0 per cent in the second quarter of 1991 before rising again, albeit at low rates of 0,2, 0,1 and 0,7 per cent, in the ensuing three quarters.

Real unit labour costs in non-agricultural sectors



Prices

As discussed in some detail in the Reserve Bank's *Annual Economic Report for 1992,* various factors stood in the way of lower price inflation. In the first half of 1992 the more important factors were the impact of the severe drought on food prices, continued high increases in nominal unit labour costs and expectations of persistently high inflation. Statistical factors, such as the effect of value-added tax introduced in October 1991 and the implementation of a new weighting structure in the calculation of the consumer price index in August 1991, also affected the official published rate of increase in the consumer price index.

The quarter-to-quarter rate of increase in the *prices of imported goods* declined from a seasonally adjusted and annualised rate of 10,9 per cent in the third quarter of 1991 to a negative rate of 0,7 per cent in the first quarter of 1992; it then reaccelerated to 9,6 per cent in the second quarter. In the first half of 1992 the rate of increase in the prices of imported goods over periods of twelve months rose from negative levels of 1,9 and 0,9 per cent in January and February to a positive figure of 5,9 per cent in May and June. These rates, measured over twelve months, were mainly influenced by the low rates of increase which had been recorded a year earlier in the aftermath of the conflict in the Middle East.

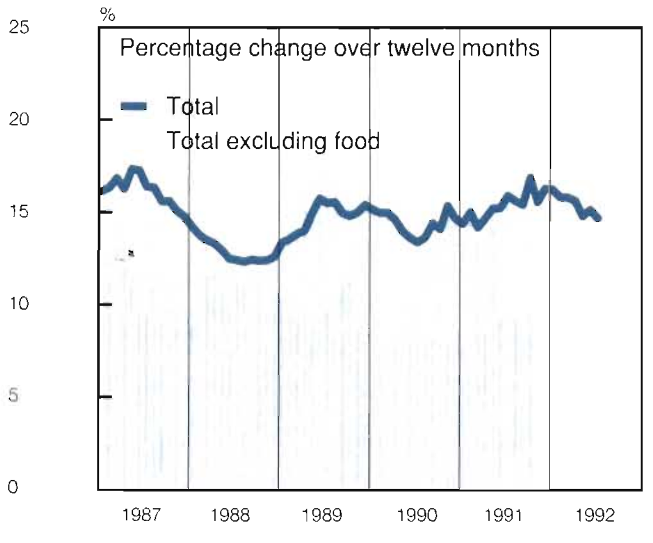
The quarter-to-quarter rate of increase in the *prices of domestically produced goods* also declined from a seasonally adjusted and annualised rate of 12,0 per cent in the third quarter of 1991 to 3,7 per cent in the first quarter of 1992, and then rose again to 12,3 per cent in the second quarter. The rate of increase in the prices of domestically produced goods over periods of twelve months accelerated from its most recent low point of 8,5 per cent in February 1992 to 10,1 per cent in June, mainly owing to the impact of the drought. The poor agricultural conditions caused the rate of increase over periods of twelve months in the production prices of unprocessed food to rise from 9,7 per cent in February 1992 to 22,9 per cent in June, and the rate of increase in prices of processed food from 9,2 to 11,2 per cent over the same period.

As a result of these movements in its main components, the quarter-to-quarter rate of increase in the *all-goods production price index* declined from a seasonally adjusted and annualised rate of 12,5 per cent in the third quarter of 1991 to 3,2 per cent in the first quarter of 1992; it then rose again to 11,4 per cent in the second quarter. The rate of increase over twelve months in the all-goods production price index declined, on balance, from a peak of 14,6 per cent in November 1990 to 6,7 per cent in both January and February 1992 before rising again to 9,2 per cent in June 1992.

The quarter-to-quarter rate of increase in the overall *consumer price index* declined from a seasonally adjusted and annualised rate of 18,8 per cent in the fourth quarter of 1991 to 12,8 per cent in both the first and second quarter of 1992. This lower rate of increase was brought about by lower rates of increase in the prices of consumer goods and services. The quarter-to-quarter rate of increase in the prices of consumer goods declined from a seasonally adjusted and annualised rate of 21,1 per cent in the fourth quarter of 1991 to 14,8 per cent in the second quarter of 1992, whereas the corresponding rate of increase in the prices of consumer services declined from 16,6 per cent to only 9,3 per cent over the same period.

The rate of increase in the overall consumer price index over periods of twelve months receded from its most recent high of 16,8 per cent in October 1991 to 14,8 per cent in May 1992, rose somewhat to 15,1 per cent in June and decreased again to 14,6 per cent in July. These recent changes in the overall consumer price index were also affected by high and accelerating increases in the prices of food. If food and non-alcoholic beverages are excluded from the representative basket of consumer goods and services, consumer price inflation over periods of twelve months subsided from a high of 15,4 per cent in July 1991 to only 11,8 per cent in June 1992 and to 11,0 per cent in July.

Consumer prices

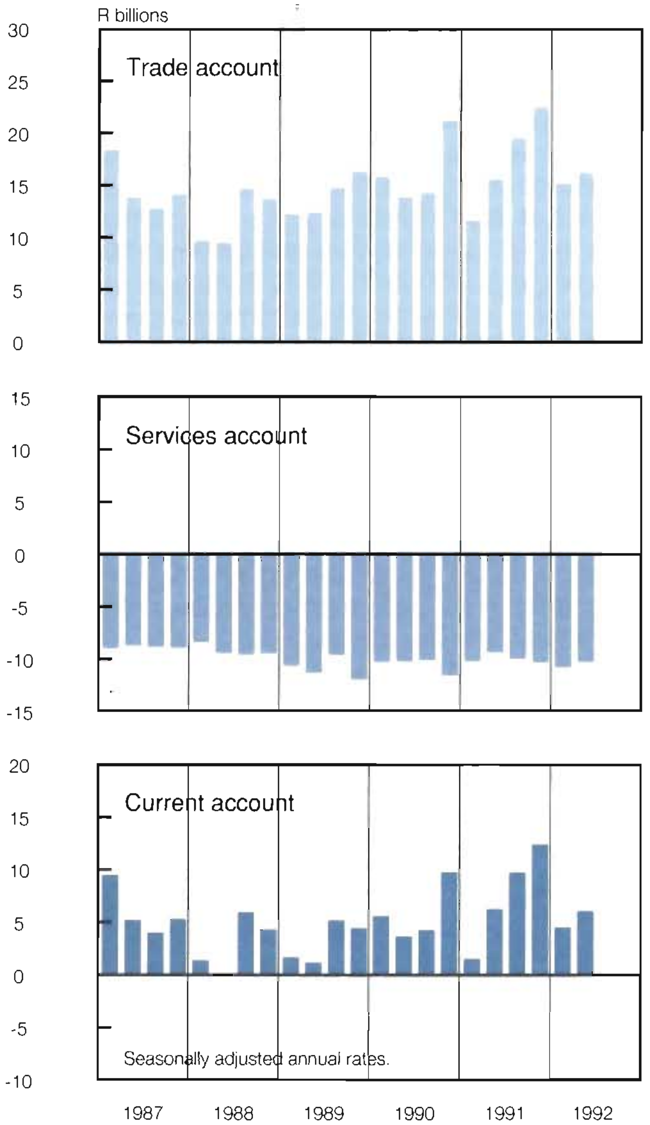


Balance of payments

Current account

The surplus on the current account of the balance of payments (seasonally adjusted and annualised), which had weakened from a quarterly average amount of R11,0 billion in the second half of 1991 to R4,5 billion in the first quarter of 1992, rose somewhat to R6,0 billion in the second quarter of 1992. As a percentage of gross domestic product, the surplus on the current account amounted to 1,9 per cent in the second quarter, compared with 2,5 per cent in 1991 and 4,3 per cent recorded in 1986 – i.e. during the advanced stage of the previous downswing in the business cycle.

Balance of payments : Current account

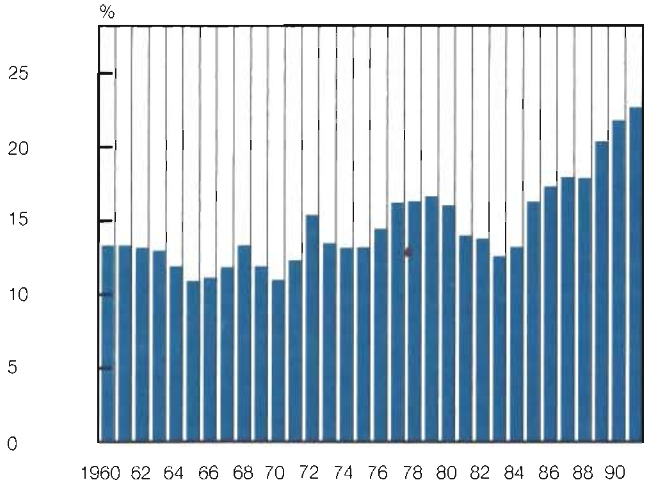


The increase in the surplus from the first to the second quarter of 1992 was the result of higher merchandise exports and lower service and transfer payments to non-residents, which more than offset a substantial decline in net gold exports.

The value of *merchandise exports* (seasonally adjusted and annualised) rose from R47,6 billion in the first quarter of 1992 to R49,4 billion in the second quarter. This increase was partly a matter of a 2½ per cent rise in export prices which benefited from an increase in international commodity prices. Prices on international commodity markets, which had decreased sharply from the middle of 1988, started to rise again towards the beginning of 1992 and in the second quarter were 3 per cent above the average level of the first quarter of 1992. The rise in the value of exports was, however, also due to an increase of 1½ per cent in the volume of goods exported. The rise in volumes reflected a very *strong* export performance by manufactured goods (particularly chemical products, machinery and electrical equipment, and transport equipment) as well as by certain mining products. Exports of agricultural products also remained on a high level because of increased fruit and wine exports.

Although the growth in the volume of merchandise exports moderated considerably from the beginning of 1991, the proportion of real exports to real gross domestic product continued to increase sharply to very high levels. After having reached a low point of only 13 per cent in 1983, the volume of exports as a percentage of real gross domestic product rose to 22 per cent in 1990, 23 per cent in 1991 and 24 per cent in the first half of 1992. The level of these ratios can be compared with averages of 12 and 14 per cent in the 1960s and 1970s. The lower growth in the South

Real merchandise exports as percentage of gross domestic product



Balance of payments on current account
Seasonally adjusted annual rates

R billions

	1991					1992	
	1st qr	2nd qr	3rd qr	4th qr	Year	1st qr	2nd qr
Merchandise exports	41,8	45,9	48,6	47,3	45,9	47,6	49,4
Net gold exports	17,3	20,0	20,1	21,2	19,6	18,1	16,0
Merchandise imports	–47,5	–50,2	–49,1	–45,9	–48,2	–50,5	–49,1
Net service and transfer payments	–10,1	–9,5	–9,9	–10,3	–9,9	–10,7	–10,3
Balance on current account	**1,5**	**6,2**	**9,7**	**12,3**	**7,4**	**4,5**	**6,0**

African economy during the 1980s was therefore accompanied by an increasingly higher proportion of goods exported despite sanctions and trade boycotts. This rise in the volume of exports prevented domestic production from declining even further (the increase in exports was also probably partly due to low economic growth) and enabled the country to maintain a surplus on the current account of the balance of payments required for the repayment of foreign debt.

The value of *net gold exports*, which had declined from a seasonally adjusted and annualised rate of R21,2 billion in the fourth quarter of 1991 to R18,1 billion in the first quarter of 1992, shrank further to R16,0 billion in the second quarter. This more recent sharp decrease was a combination of both price and volume declines. The average fixing price of gold declined from US$351 per fine ounce in the first quarter of 1992 to $339 in the second quarter, or from R992 to R963 per fine ounce. Towards the end of July the gold price recovered momentarily to almost $360 per fine ounce, owing to fears that South Africa's gold production could decline because of stay-aways and mass actions. When it became evident that gold production would not be seriously affected, the gold price fell again to $340 per fine ounce on 31 August.

After having reached a new record value of R50,5 billion (seasonally adjusted and annualised) in the first quarter of 1992, *merchandise imports* declined moderately to R49,1 billion in the second quarter. This level of imports was nevertheless still 2 per cent higher than the quarterly average of 1991. The imports of agricultural products arising from the drought were mainly responsible for the high import volume in the second quarter of 1992. The seasonally adjusted and annualised value of agricultural products (mainly maize) more than doubled from R1,1 billion in 1991 to R2,4 billion in the second quarter of 1992.

Mainly reflecting higher oil prices, import prices rose by 1½ per cent in the second quarter of 1992, following a decline of 1 per cent in the first quarter. A decline of 1 per cent in the average effective exchange rate of the rand from the first to the second quarter was also responsible for this rise in import prices. However, in the second quarter of 1992 import prices were only 4 per cent higher than in the corresponding quarter of 1991. This lower rate of increase than in the prices of domestically produced goods explains to some extent why imported products were substituted for domestic goods.

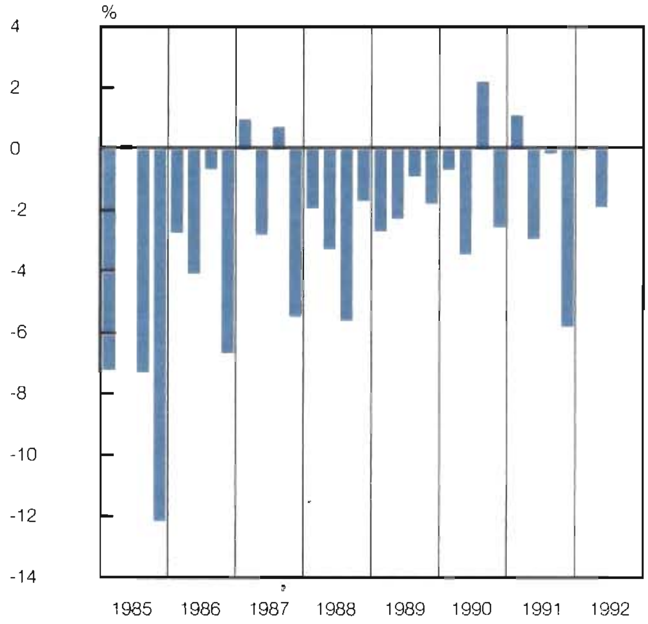
Net *service and transfer payments* to non-residents declined marginally from a seasonally adjusted and annualised value of R10,7 billion in the first quarter of 1992 to R10,3 billion in the second quarter. This decline was caused by a drop of R1,4 billion in service payments, which outstripped a decline of R1,0 billion in service receipts. Higher payments for freight and merchandise insurance in the second quarter were fully offset by lower interest and dividend payments to non-residents, whereas lower interest and dividends received on foreign investments resulted in a decline in service receipts from the rest of the world.

Capital account

The *total net outflow of capital* not related to reserves, which had fallen from R4,7 billion in the fourth quarter of 1991 to only R21 million in the first quarter of 1992, rose again to R1,9 billion in the second quarter. This renewed large capital outflow was mainly caused by a large outflow of short-term funds; the outflow of long-term capital declined to only a small amount.

The net outflow of *long-term capital* improved considerably over the twelve-month period to June 1992. Largely reflecting borrowing on international capital markets, the net outflow of long-term capital decreased from R1,4 billion in the third quarter of 1991 to R0,3 billion in the first quarter of 1992 and to only R37 million in the second quarter. The proceeds of debt issues on the European capital market of Telkom, Eskom and the Industrial Development Corporation to the amount of R0,8 billion were mainly responsible for a

Capital movements not related to reserves as percentage of gross domestic product



further inflow of capital to the public sector in the second quarter of 1992. This brought the net inflow of long-term capital to the public sector to R1,8 billion in the first half of 1992, against an inflow of R0,2 billion in 1991 as a whole. The net outflow of long-term capital from the private sector declined from the high figure of R1,3 billion in the first quarter of 1992 to R0,9 billion in the second quarter. This outflow represented foreign debt repayments, an increase in long-term assets related to export trade and net sales by non-residents of securities quoted on the Johannesburg Stock Exchange (these sales are recorded on a gross basis and do not cause a loss of foreign reserves; their counterparts are shown as inflows against other components of the capital account).

Short-term capital (excluding reserve-related liabilities but including unrecorded transactions) changed from a small net inflow of capital of R0,3 billion in the first quarter of 1992 to a net outflow of capital to the amount of R1,8 billion in the second quarter. This fairly large outflow of short-term funds is likely to have occurred mainly towards the end of the second quarter and could be ascribed to renewed political uncertainty and social unrest. Preliminary indications are that this outflow of short-term capital changed to an inflow again in July 1992.

Foreign reserves

The net outflow of capital not related to reserves exceeded the surplus on the current account of the balance of payments, with the result that South Africa's total *net gold and other foreign reserves* decreased by R0,5 billion in the second quarter of 1992. However, during the first half of 1992 the total net reserves still rose by R1,5 billion, after having risen by R1,4 billion during 1991 as a whole.

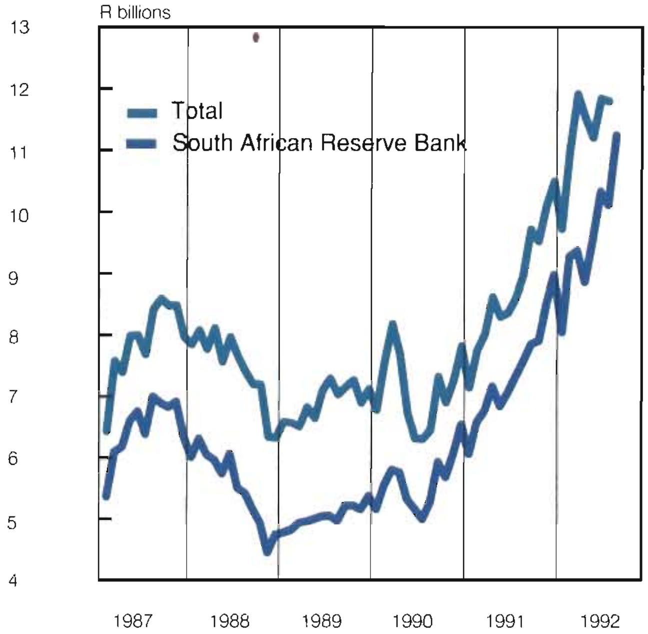
South Africa's total *gross gold and other foreign reserves* rose by R266 million in the second quarter of 1992 and pushed the level of the gross reserves to R11,8 billion at the end of the quarter. During the

Net capital movements (not related to reserves)

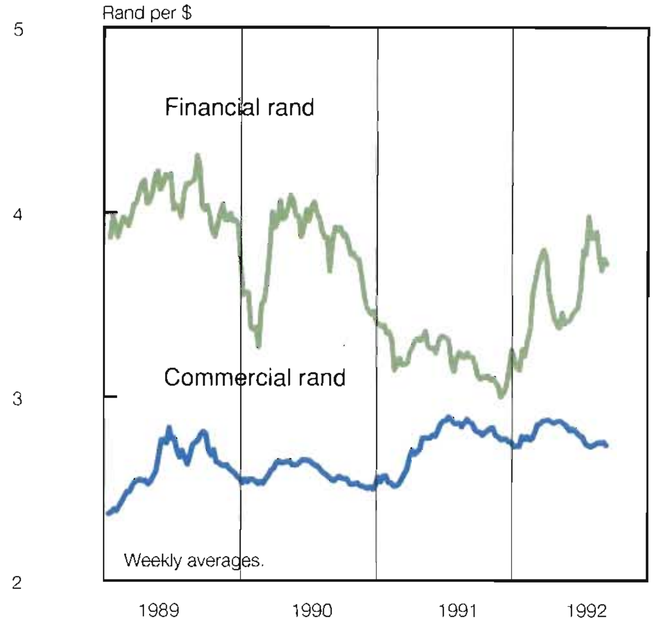
R millions

	1991					1992	
	1st qr	2nd qr	3rd qr	4th qr	Year	1st qr	2nd qr
Long-term capital							
Public authorities	–167	116	–398	346	–103	941	303
Public corporations	188	345	–183	–20	330	55	540
Private sector	–604	–787	–774	–768	–2 933	–1 283	–880
Total long-term capital	–583	–326	–1 355	–442	–2 706	–287	–37
Short-term capital, including unrecorded transactions, but excluding reserve-related liabilities	1 362	–1 748	1 258	–4 217	–3 345	266	–1 819
Total capital movements, excluding liabilities related to reserves	**779**	**–2074**	**–97**	**–4 659**	**–6 051**	**–21**	**–1 856**

Gross gold and other foreign reserves



Exchange rates



ensuing two months the gross reserves of the Reserve Bank rose further by R1,4 billion to a level of R11,5 billion at the end of August. The gold reserves of the Reserve Bank at the end of this month amounted to 6,7 million fine ounces, up from 6,4 million fine ounces at the end of December 1991 and from a low of 3,1 million fine ounces at the end of 1989.

Exchange rates

Concern about developments in the world's major economies resulted in *volatile financial markets* during the first eight months of 1992. The interest rate differential between the United States and Germany widened further when the American discount rate was lowered in early July 1992 to its lowest level since 1963, and when the Bundesbank increased its discount rate on 20 July to its highest level since the 1930s. This large interest rate differential and the relatively low economic growth in many industrial countries caused the dollar to continue on its downward trend which had started in the second quarter of 1992. Despite central bank intervention, the dollar reached a historic low of DM1,4063 on 26 August 1992.

Changes in exchange rates of the rand
%

	31 Dec '91 to 31 March '92	31 March '92 to 30 June '92	30 June '92 to 31 Aug '92	31 Dec '91 to 31 Aug'92
Weighted average	–0,7	–0,4	–1,6	–2,7
US dollar	–4,7	3,9	1,2	0,2
British pound	2,8	–5,2	–3,0	–5,5
German mark	3,5	–3,9	–6,4	–6,9
Japanese yen	1,1	–2,0	–0,6	–1,5
Netherlands guilder	3,4	–3,8	–6,4	–6,9
Italian lira	3,1	–3,8	–5,3	–6,0
Financial rand	–9,7	–6,5	–0,9	–14,8

Owing to the weak performance of the dollar, the rand appreciated against the dollar but depreciated against all the other major currencies from the beginning of the second quarter. In the period 20 March 1992 to 20 July 1992 the rand appreciated by more than 6 per cent against the dollar to R2,72 per dollar - its highest level against the US currency since 17 April 1991. It then depreciated again moderately to R2,74 per dollar on 31 August 1992. Historic lows were, however, recorded in the rand's exchange rates against the other major currencies.

The net result of these movements in the exchange rates of the rand was that the *nominal effective exchange rate* of the rand declined by only 0,4 per cent in the second quarter of 1992 and by a further 1,6 per cent up to the end of August 1992. This brought the total decline in the nominal effective exchange rate of the rand to 2,7 per cent since the beginning of 1992. The *real effective exchange rate* of the rand also remained relatively stable. In July 1992 the real effective exchange rate of the rand was only 0,9 per cent above its level in December 1991 and 1,6 per cent higher than in December 1990.

At first the *financial rand* was also relatively stable following the outcome of the referendum in March 1992, and the financial rand discount fluctuated between 14 and 22 per cent from the end of March 1992 to 19 June 1992. However, events at Boipatong on 17 June, the suspension of the negotiations for a new constitution and the instigation of mass actions, caused the financial rand to drop sharply from R3,63 to R4,07 per dollar on 9 July 1992. The financial rand subsequently appreciated again to R3,72 per dollar and a discount of 26 per cent on 31 August.

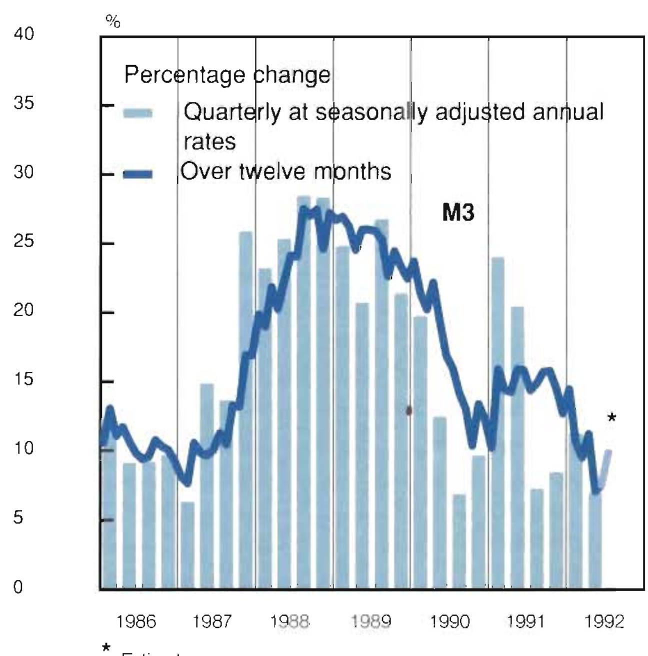
Financial markets

Money supply

The twelve-month growth rates of almost all the monetary aggregates decelerated significantly during the first six months of 1992. At the beginning of the year these rates were still affected by the regulatory changes under the Deposit-taking Institutions Act, which came into force in February 1991. When these effects were no longer reflected in the twelve-month growth rates of the aggregates, this rate of increase in the *broadly defined money supply (M3)* declined from 14,4 per cent in January 1992 to 10,6 per cent in February 1992; it then receded even further to 7,5 per cent in June. Preliminary estimates indicate that the growth rate in M3 over periods of twelve months rose again to 9,9 per cent in July 1992. The declining tendency in the growth in M3 during the first half of 1992 was also confirmed by the growth in the quarterly average value of M3 (seasonally adjusted and annualised), which contracted from 8,5 per cent in the fourth quarter of 1991 to 7,0 per cent in the second quarter of 1992.

Sharp fluctuations in monthly values of M3 at times caused the growth in this aggregate to move above the upper limit of the guideline range of 10 per cent. However, most of the monthly growth rates were generally well within the guideline range and closer to the lower limit of the range of 7 per cent. This is clearly

Money supply



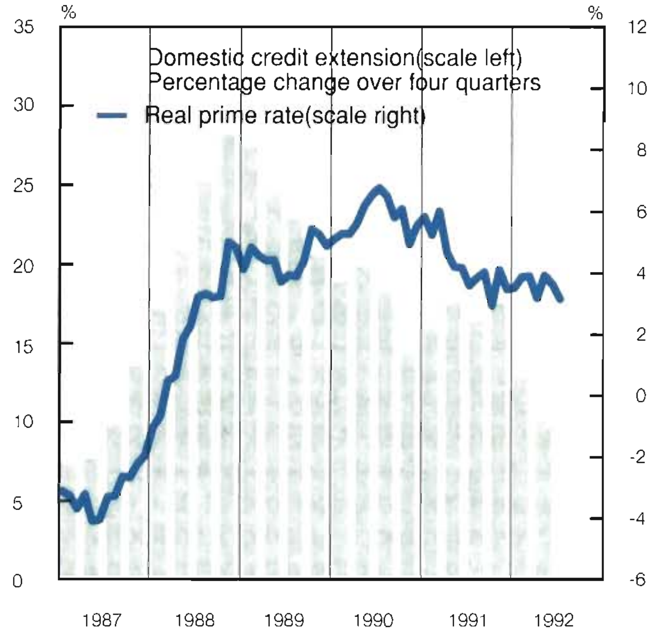
* Estimate.

illustrated by the rate of increase in M3 as measured for guideline purposes of 7,7 per cent (seasonally adjusted and annualised) from the fourth quarter of 1991 to June 1992. Preliminary estimates indicate that this rate then rose again to 10,2 per cent in July 1992.

The rates of increase in the *narrower monetary aggregates*, with the exception of M1A, also displayed a declining tendency during the first six months of 1992. The rates of increase in M1 and M2 over periods of twelve months fluctuated downwards from 14,8 and 16,1 per cent in December 1991 to 11,1 and 11,8 per cent, respectively, in June 1992. In contrast to these developments, the corresponding growth rate in M1A increased from 17,7 per cent in December 1991 to 18,7 per cent in June 1992. This was mainly due to a shift from longer-term deposits to cheque and transmission deposits, leading to an increase in the relative share of cheque and transmission deposits in total domestic private sector deposits from 12,2 per cent in June 1991 to 14,2 per cent in June 1992.

In a *statistical or accounting sense* the main counterpart of the R6,9 billion increase in M3 in the first half of 1992 was a R5,0 billion increase in the claims of the monetary institutions on the private sector. An increase of R1,5 billion in the net gold and other foreign reserves and a R2,5 billion increase in net other assets and liabilities, were countered to some extent by a drop of R2,1 billion in monetary institutions' net claims on the government sector.

Real prime rate and domestic credit extension



Credit extension by monetary institutions

The twelve-month growth rate in *total credit extended* by monetary institutions to the domestic private sector continued to decrease in the first half of 1992. This rate of increase fell back from 14,5 per cent in December 1991 and 15,6 per cent in January 1992 to 10,8 per cent in February, when the effect of the regulatory changes under the Deposit-taking Institutions Act was no longer reflected in this growth rate; it then fluctuated downwards to only 9,0 per cent in June 1992.

The low demand for credit related to the depressed economic conditions and the relatively high cost of borrowing, was also reflected in the quarterly growth rates of credit extension. The seasonally adjusted and annualised rate of increase in the quarterly average of monetary institutions' claims on the domestic private sector receded from a recent peak of 23,4 per cent in the first quarter of 1991 to 11,1 per cent in the fourth quarter and even further to only 4,4 per cent in the first quarter of 1992; it then rose again to 11,1 per cent in the second quarter. Similarly, the rate of increase over four quarters in the quarterly average value of credit extension by monetary institutions to the domestic private sector (seasonally adjusted) declined from 17,6 per cent in the fourth quarter of 1991 to 10,1 per cent in the second quarter of 1992. These recent lower growth rates in credit extension were, however, also due to disintermediation that could be explained by a widening of the margins between lending and deposit rates of monetary institutions.

An *analysis* of monetary institutions' claims on the domestic private sector *by type of credit* extended reveals that the lower growth in credit extension was mainly due to a contraction of the growth rate in hire-purchase credit and overdrafts. The twelve-month rate of increase in hire-purchase credit shrank from the already low level of 6,7 per cent in December 1991 to only 2,2 and 1,3 per cent in March and June 1992, respectively. The rate of increase in "other loans and advances" (mainly overdrafts) over periods of twelve months similarly receded from 12,6 per cent in December 1991 to 7,0 per cent in March 1992 and to only 0,2 per cent in June.

The slower growth in these types of credit was partly due to a switching to mortgage advances and leasing finance because of the comparatively favourable interest rates and cash flow advantages that are associated with such financing. Lower capital requirements against mortgage advances also encouraged deposit-taking institutions to promote this kind of credit extension. The twelve-month growth rate in mortgage advances accordingly rose from 14,7 per cent in December 1990 to 18,0 per cent in December 1991; an increase in precautionary savings of households then probably caused this growth rate to recede somewhat to 17,2 per cent in June 1992. However, the growth in leasing finance remained buoyant and the rate of increase in this aggregate over a period of twelve months rose from 20,6 per cent in December 1991 to 24,4 and 23,3 per cent in March and June 1992.

Money market conditions and Reserve Bank operations in the money market

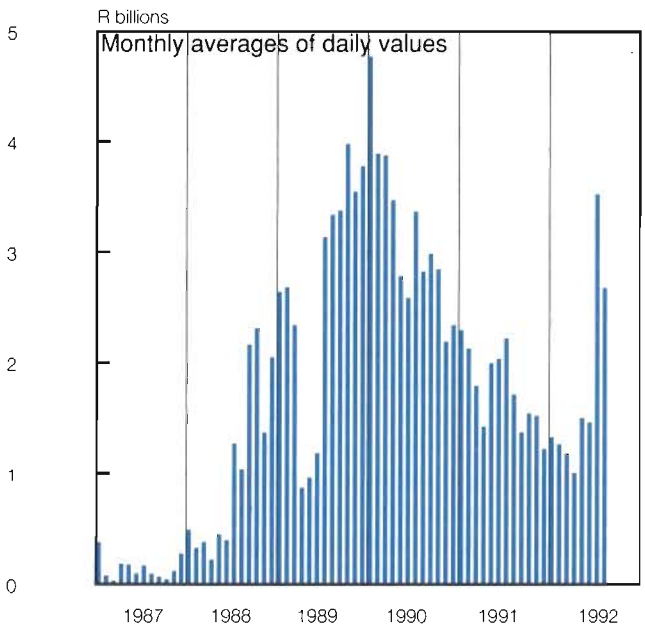
Money market conditions continued to ease during the first four months of 1992, but became markedly tighter thereafter. The average daily *level of accommodation* at the discount window decreased from R1,2 billion in December 1991 to R1,0 billion in April, but increased sharply to R1,5 billion in May and R3,5 billion in July 1992; it then decreased again to R2,7 billion in August. The amount of accommodation at month-ends decreased from R2,8 billion in December 1991 to R1,2 billion in February 1992, and then advanced sharply to R4,0 billion in July; in August 1992 it receded again to the December level of R2,8 billion.

The changes in money market conditions were more clearly reflected in the data on *money market liquidity before Reserve Bank intervention*. The average daily level of money market liquidity before Reserve Bank intervention increased from a money market deficit of R0,7 billion in January 1992 to a money market surplus of R1,4 billion in April, and then reverted to deficits of R3,3 billion and R1,3 billion in July and August, respectively. The net effect of autonomous influences on money market conditions (i.e. changes in banknotes in circulation, government deposits, gold and foreign exchange reserves and the financing of the Land Bank) resulted in a decrease in the money market deficit before Reserve Bank intervention of R1,4 billion during the first eight months of 1992.

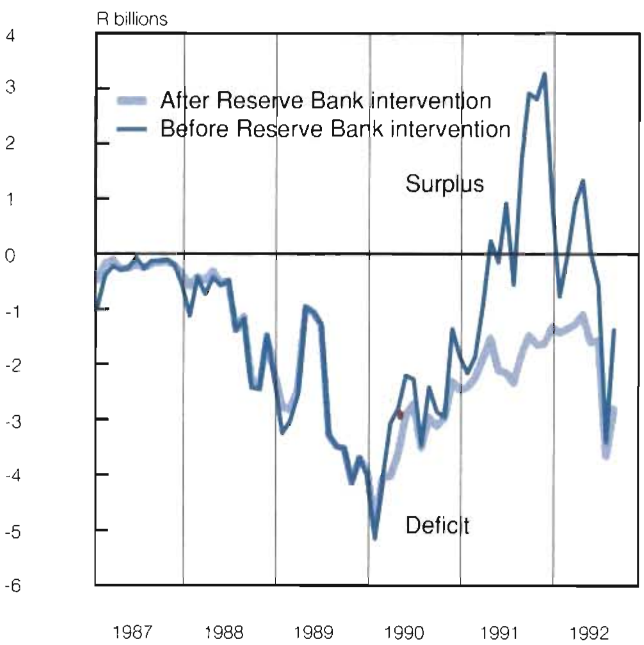
The tighter conditions experienced in the money market from May 1992 could mainly be attributed to a sharp increase in *government deposits* with the Reserve Bank. The monthly average of the daily balances on the Exchequer, Paymaster-General and Stabilisation Accounts with the Reserve Bank increased from R10,9 billion in April 1992 to R15,6 billion in July. If the proceeds from the sales of special short-dated Treasury bills are excluded, the tightening effect of the increase in these deposits amounted to R7,3 billion from the end of March 1992 to the end of July. This sharp increase in government deposits was mainly the result of vigorous selling of government stock during this period. In August 1992 the government deposits with the Reserve Bank declined by R5,3 billion on account of the transfer of R3,8 billion from the Stabilisation Account to the Gold and Foreign Exchange Contingency Reserve Account (with no effect on money market liquidity) and the redemption of government stock of R3,1 billion.

The tighter money market conditions during the first eight months of 1992 were partly offset by a net decrease in *banknotes in circulation* and the improvement in the overall balance of payments position. Banknotes in circulation declined by R0,6 billion and the increase in the *net gold and foreign*

Accommodation at the discount window



Money market deficit



exchange reserves of the Reserve Bank to the extent that this affected the money market, amounted to R1,6 billion over this period. Since April the Reserve Bank and the Corporation for Public Deposits purchased *Land Bank promissory notes* of R2,5 billion, causing a further net increase in money market liquidity of R1,0 billion in their transactions with the Land Bank during the first eight months of 1992.

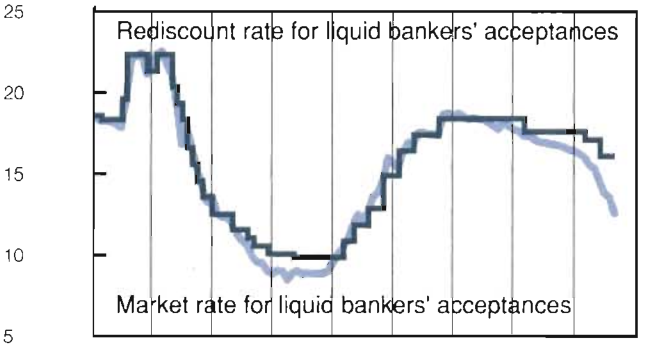
The *Reserve Bank's operations* in the money market during the first seven months of 1992 consisted mainly of foreign exchange intervention swaps with major banking institutions and the issuing of special short-dated Treasury bills. The combined utilisation of these facilities rose from a peak outstanding amount of R1,8 billion in January 1992 to R3,9 billion in both March and April and then dropped to R1,9 billion in June. During June the Reserve Bank also issued its own special bills amounting to R0,5 billion. An additional cash reserve requirement of 1 per cent of deposit-taking institutions' short-term liabilities to the public (in addition to the existing 4 per cent) removed a further R0,9 billion from the money market in July 1992.

In July the Reserve Bank undertook transactions to alleviate tight conditions which had developed during that month. The Bank allowed deposit-taking institutions to place special foreign exchange deposits with the Reserve Bank to the amount of R0,7 billion and entered into repurchase agreements on behalf of the Corporation for Public Deposits to a maximum outstanding amount of R1,0 billion. All these agreements were terminated by 3 August 1992.

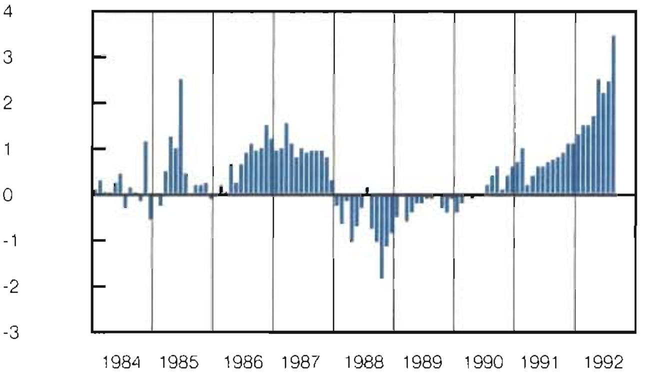
Net sales of government stock by the Reserve Bank rose from R1,2 billion in the first quarter of 1992 to R10,3 billion in the ensuing four months, i.e. the first four months of fiscal 1992/93. In August the net sales of government stock by the Reserve Bank amounted to only R0,5 billion. The Bank's trading of *government stock options* also rose from a monthly average of R4,2 billion in January 1992 to R7,1 billion in July and R6,8 billion in August. The monthly average of these transactions in the first eight months of 1992 amounted to R5,2 billion, as against R2,0 billion in 1991.

From 20 March 1992 until 5 June 1992 the Reserve Bank also issued *Treasury bills* for six and nine months in addition to the ordinary three-month bills at the weekly tender. The weekly offer of Treasury bills of three months' currency was reduced from R200 million to R100 million, and R100 million of each of the other two types of bills were issued for a total amount of R300 million per week. Since 5 June 1992 the Bank has only issued Treasury bills for three and six months, to an amount of R150 million each, at the weekly tender.

Rediscount and market rate for 3-month liquid bankers' acceptances



Margin between discount rate and market rate for 3-month liquid bankers' acceptances



Money market interest rates

The gradual decline in money market interest rates since early 1990 gathered momentum in the first eight months of 1992. This acceleration in the decline in money market rates was due to a lower demand for funds, and two reductions of one percentage point each and expectations of a further lowering of Bank rate. The declining trend in short-term interest rates was clearly reflected in the rate of *three-month liquid bankers' acceptances*, which declined rapidly from 16,40 per cent at the end of December 1991 to 13,80 per cent at the end of June 1992 and further to 12,50 per cent at the end of August. In the first eight months of 1992, the rate on three-month liquid bankers' acceptances has therefore declined by 3,90 percentage points. At the end of August the rate on three-month bankers' acceptances was 3,50 percentage points below the Reserve Bank's rediscount rate for such acceptances, clearly indicating the market's expectation of a further lowering of Bank rate. Since July 1990 the Reserve Bank's rediscount rate for liquid bankers' acceptances has consistently exceeded the market rate on these acceptances – i.e. for a period of twenty-six months.

Most *other money market interest rates* also softened fairly sharply in the first eight months of 1992. For example, the predominant rate for interbank call money of clearing banks decreased from 16,00 per cent at the end of 1991 to 13,50 per cent at the end of August 1992, or by 2,50 percentage points. The three-month Treasury bill tender rate declined even more steeply from 16,13 per cent to 12,03 per cent over the same period, or by 4,10 percentage points.

The *prime lending rate* of deposit-taking institutions followed the changes in Bank rate, being reduced by 1 percentage point to 19,25 per cent on 1 April 1992 and to 18,25 per cent on 6 July 1992. The inflation-adjusted prime lending rate of deposit-taking institutions fluctuated around 3,5 per cent in the first seven months of 1992 if it is deflated by the current inflation rate in every month. Based on the *expected* underlying inflation rate, the level of the real prime lending rate was probably somewhat higher.

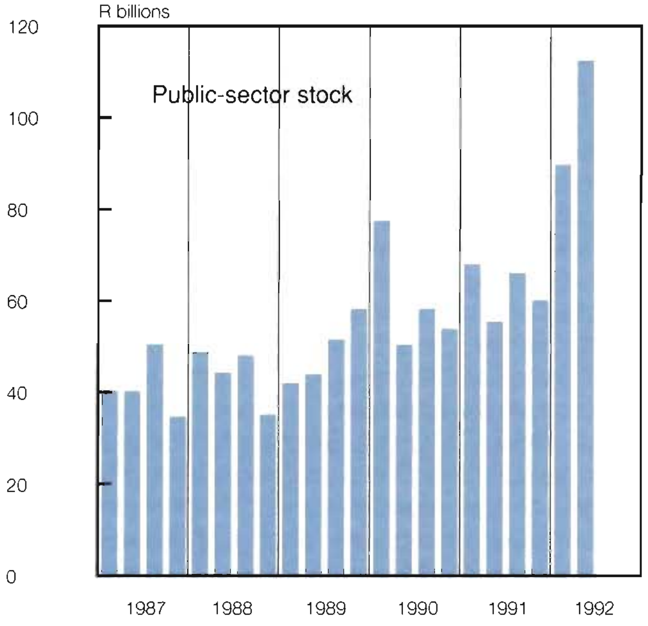
Capital market developments

In many instances during the first eight months of 1992 trading activity in the capital market bore little relation to the pace of real economic activity. Activities remained buoyant in most of the capital markets, and share prices reached new record levels in June. Political actions, worse than expected financial results of certain companies and declines in the share prices on international markets in July and August, resulted in a significant softening in share prices, a sharp rise in stock prices, generally continued high levels of activity, and a considerable increase in activity on the derivative markets as expectations diverged.

The value of *public-sector stock* traded on the Johannesburg Stock Exchange, which had fluctuated around an average quarterly amount of R62,3 billion in 1991, rose sharply to R89,5 billion in the first quarter of 1992 and to R112,3 billion in the second quarter. The monthly average value of public-sector stock traded subsequently increased further from R37,4 billion in the second quarter of 1992 to R74,2 billion in July and August. The sharp increase in trading activity in public-sector stock during the first eight months of 1992 was caused mainly by the softening of interest rates as long rates moved down in tandem with short rates. Rates on long-dated stock continued to fall because institutions readjusted their positions and bought public-sector stock at the expense of equities. The shift from equities to gilts, which had started in the first quarter, maintained its momentum despite a short-lived recovery in the equity market during the second quarter.

Net purchases of public-sector stock by *non-residents* increased from R616 million in the fourth quarter of 1991 to R823 million in the first quarter of 1992, and then fell back to R253 million in the second quarter of 1992. In July 1992 sales of public-sector stock by non-residents exceeded purchases (for the first time since September 1988) by an amount of R77 million. Non-residents' net sales of shares contracted from R1 134 million in the fourth quarter of 1991 to R695 million and R413 million in the first and second quarter of 1992. The markedly weaker financial rand

Stock exchange transactions

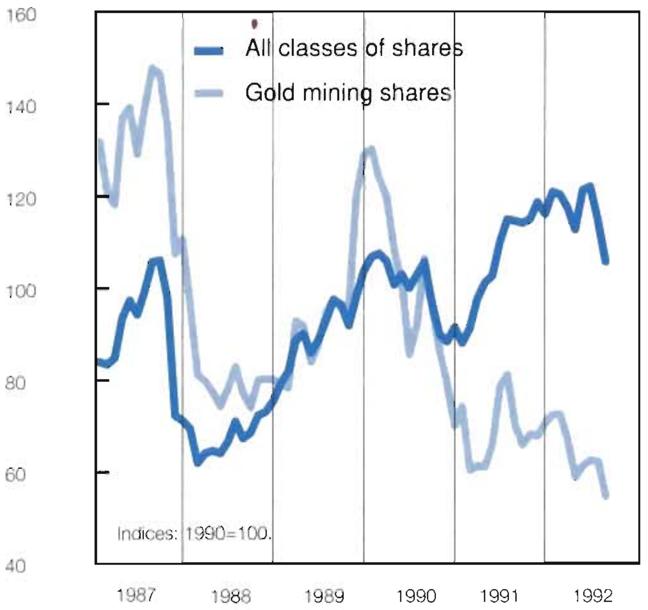


then boosted non-residents' purchases of shares, leading to net purchases of R124 million in July 1992.

After having increased from R4,9 billion in the fourth quarter of 1991 to R5,5 billion in the first quarter of 1992, the value of *shares traded* on the Johannesburg Stock Exchange fell back to R5,0 billion in the second quarter. Trading activity increased significantly in July and August 1992, when the average monthly value of shares traded increased to R2,1 billion; in the second quarter of 1992 the monthly average amounted to R1,7 billion. Institutional investors continued to dominate share trading activity, but market activity gained further momentum because of the amendment to the Stock Exchanges Control Act in July 1992, which now allowed bear sales at the last sale price recorded.

Owing to increases in the *share prices* of all the main classes of shares, with the exception of gold-mining shares, the average price level of all classes of shares rose by 5,1 per cent from December 1991 to June 1992. The share prices of gold mines decreased by 11,7 per cent during this period as a result of a lower gold price and increasing concern about the profitability of these mines. In July and August 1992 negative sentiment engulfed the equity market as mass action on the political front, a sudden floundering of some of the major international equity markets and a switch from equities to fixed-interest stock, drove share prices down. The average monthly level of all classes of shares therefore fell by 13,3 per cent in these two months.

Share prices



Net new borrowing by the *public sector* through *issues of fixed-interest securities* peaked at R4,9 billion in the fourth quarter of 1991, fell back to R0,5 billion in the first quarter of 1992 and then rose substantially to R11,3 billion in the second quarter. This high level of net new issues in the first quarter of the new fiscal year was greatly facilitated by the favourable borrowing climate in the market.

The value of new issues of fixed-interest securities (including convertible preference shares and debentures) and ordinary shares by listed *private-sector* companies rose from R1,4 billion in the second half of 1991 to R2,2 billion in the first half of 1992. Similarly, the value of new issues of *ordinary shares* by listed private-sector companies increased from R3,7 billion in the second half of 1991 to R4,3 billion in the first half of 1992. Both new issues of fixed-interest securities and ordinary shares in July moved to substantially lower levels.

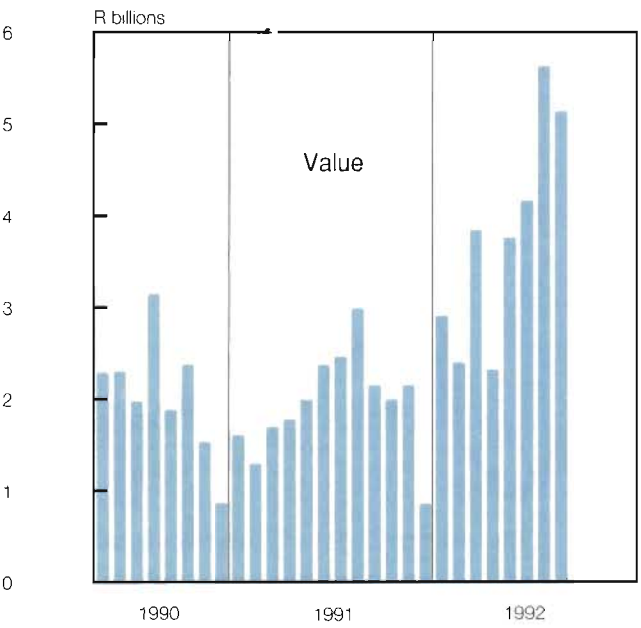
In the *mortgage market* the average amount of mortgage advances paid out by deposit-taking institutions and mutual building societies during the first six months of 1992 amounted to R2,5 billion per month, which was slightly higher than in the previous year. Most deposit-taking institutions began offering flexible bond facilities and introduced computerised procedures to speed up the process of loan approval during 1992. This allowed approved clients access to less expensive financing, which is not necessarily earmarked for real estate purposes only and therefore reduced the relationship between an increase in financial institutions' holdings of mortgage bonds and an increase in the value of real estate transactions.

In contrast to the rise in mortgage advances, the value of *real estate transactions* contracted from a quarterly average of R7,3 billion in 1991 to R7,1 billion and R6,1 billion in the first two quarters of 1992. The number of transactions in fixed property fell back by 17,2 per cent in the first half of 1992, while the average value of property transactions rose by 8,9 per cent to R133 000.

The value of transactions in *futures contracts* rose from a relatively low R5,0 billion in the fourth quarter of 1991 to R9,1 billion and R10,2 billion in the first and the second quarter of 1992, respectively. In July 1992 an all-time monthly high of R5,6 billion was recorded in transactions in futures contracts, following a weakening in share prices and uncertainty arising from political actions; this high level of activity contracted only moderately to R5,1 billion in August. Contracts in share indices represented 85,1 per cent of the total value of futures contracts during the first eight months of 1992. The mark-to-market value of all index futures contracts for June, September and December 1992 was below the Johannesburg Stock Exchange's spot price from the middle of May 1992, throughout most of June, as well as the last two weeks of July – indicative of a bear market.

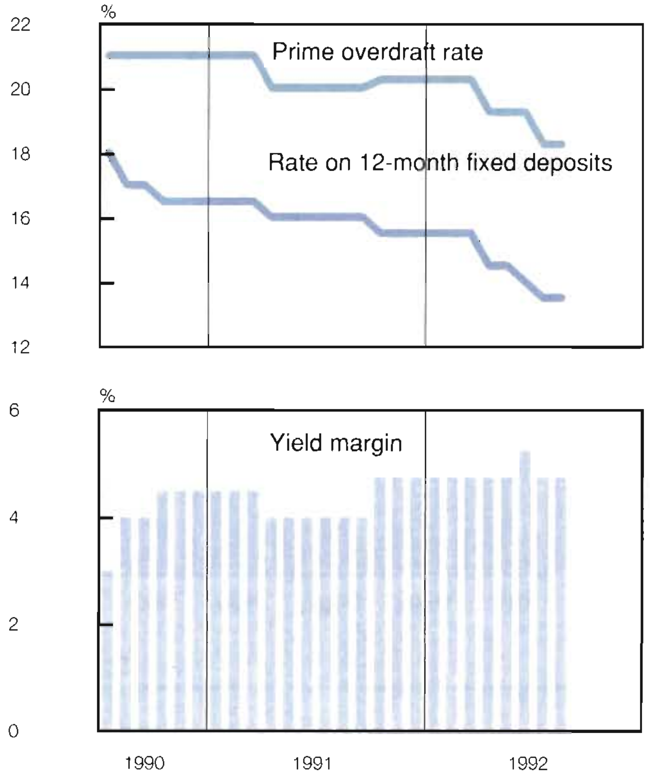
After the opening of the Johannesburg Stock Exchange's *Traded Options Market* on 24 January

Futures exchange transactions



1992, activity was at first brisk but then weakened progressively from March to May: the 395 contracts with an underlying value of R3,6 million in February 1992 decreased to 70 contracts with an underlying value of only R0,7 million in May. In the next month no options were traded, but in July increased volatility in the underlying equity market and the listing of the Gencor option created renewed interest in the Traded Options Market, resulting in 1 503 contracts with an underlying value of R6,1 million. In the bond market, gilt options were heavily traded in July 1992 because the increase in activity in the underlying market and the concomitant change in yields caused divergent expectations regarding future changes.

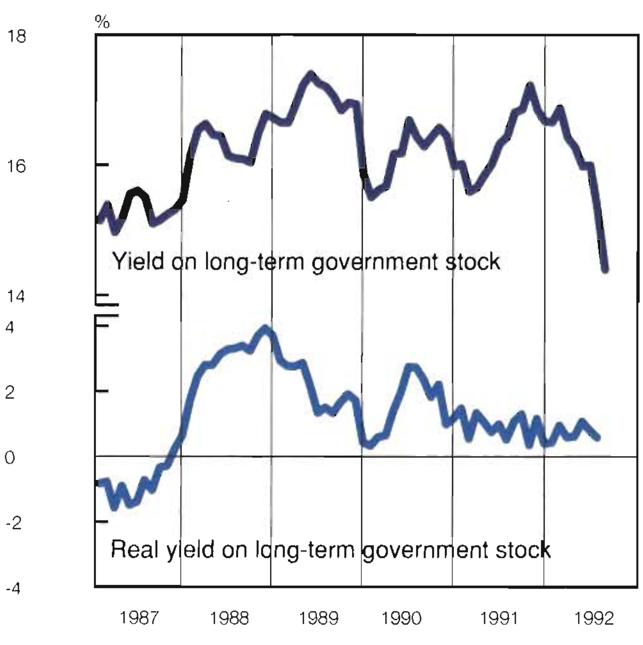
Margin between prime overdraft rate and rate on 12-month fixed deposits



Capital market yields and interest rates

The monthly average yield on long-term government stock eased gradually from a peak of 17,2 per cent in October 1991 to 16,9 per cent in February 1992, and then declined more rapidly to 15,3 per cent in July and to 14,4 per cent in August 1992. The decrease of long rates in the first eight months of 1992 reflected the softening in short rates following the increase in market liquidity, expected lower inflation rates, a weaker than expected real economy and the lowering of Bank rate. Concern about the equity market and substantial institutional buying of securities also contributed to the drop in long rates. The monthly average *real* yield on government stock also softened from 0,9 per cent in February 1992 to only 0,6 per cent in July.

Capital market yields



The deposit-taking institutions' predominant bond rate was reduced gradually during the first eight months of 1992 based on expected reductions of Bank rate. The bond rate was first reduced by 1,0 percentage point to 19,0 per cent from 2 March 1992 and later by a further 1,0 percentage point with effect from 1 July 1992. In August deposit-taking institutions announced a further reduction of their predominant mortgage bond rate to 17,25 per cent with effect from 1 September 1992. This reflected comfortable margins and an expected further lowering of Bank rate.

The deposit-taking institutions also lowered their longer-term deposit rates further during the first eight months of 1992. After having reduced their *twelve-month deposit rate* from a peak of 16,5 per cent in March 1991 to 15,5 per cent in October 1991, deposit-taking institutions lowered this rate further by 1,0 percentage point in April 1992 following the Bank rate reduction on 23 March 1992. This rate was subsequently brought down further, to 14,0 per cent, in June 1992 and to 13,5 per cent in July. In view of the fact that lending rates did not decline to the same extent, the margin between the twelve-month deposit rate and the predominant prime overdraft rate of clearing banks widened from 4,75 percentage points in

January 1992 to 5,25 percentage points in June before narrowing again to 4,75 percentage points in August 1992. The twelve-month deposit rate provided a negative before-tax real yield of 0,99 per cent to depositors in July 1992.

Lower dividends of many companies and the high level of share prices depressed the *dividend yield* on all classes of shares from 3,36 per cent in April 1992 to 3,15 per cent in June. The *earnings yield* on all classes of listed shares (excluding gold-mining shares) also decreased, from 7,83 per cent to 7,28 per cent, over the same period. The dividend yield on all classes of shares firmed to 3,58 per cent and the earnings yield to 8,12 per cent in August as a result of the decline in average share prices.

After having remained unchanged since 27 July 1990, the maximum permissible *finance charges rates*, as determined in terms of the Usury Act, were reduced with effect from 29 May 1992 from 29 to 28 per cent in respect of money lending, credit and leasing transactions for amounts of more than R6 000 (but not exceeding R500 000), and from 32 to 31 per cent in respect of transactions for amounts up to R6 000.

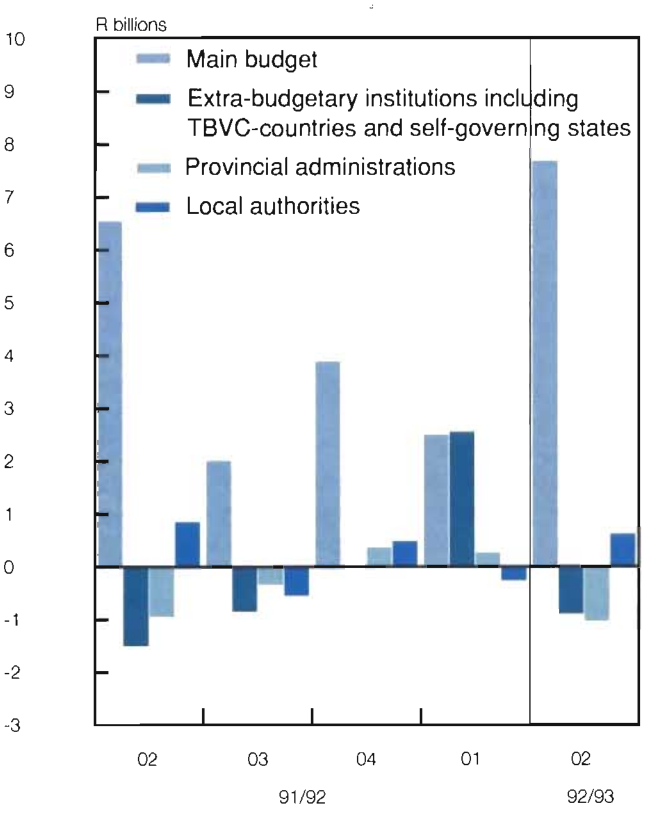
Public finance

Public-sector borrowing requirement

The public-sector borrowing requirement (i.e. the deficit before borrowing and debt repayment of the consolidated Central Government, provincial administrations, local authorities and the non-financial government enterprises and public corporations) in the June quarter of 1992 (the first quarter of fiscal 1992/93) amounted to R5,7 billion; in the corresponding quarter of fiscal 1991/92 the public-sector borrowing requirement had been higher at R6,1 billion. As a ratio of gross domestic product, this borrowing requirement was equivalent to 7 per cent in the June quarter of 1992, compared with 8½ per cent in the corresponding quarter of 1991 and 5½ per cent for the full fiscal year 1991/92.

Cutbacks and other rationalisation programmes by *non-financial public enterprises* led to a turnaround of their borrowing requirement from a deficit of R1,2 billion in the first quarter of fiscal 1991/92 to a small surplus of R0,7 billion in the first quarter of fiscal 1992/93. However, the borrowing requirement of the *general government* (i.e. the deficit before borrowing and debt repayment of the consolidated Central

General government: Borrowing requirements

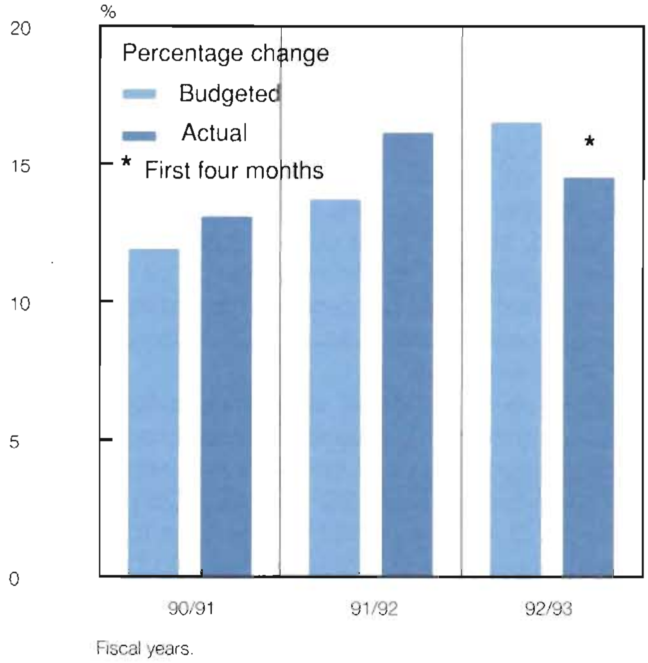


Government, provincial administrations and local authorities) amounted to R6,3 billion (8 per cent of gross domestic product) in the first quarter of fiscal 1992/93; this was significantly higher than the deficit of R5,0 billion (7,0 per cent of gross domestic product) in the first quarter of 1991/92.

As illustrated in the accompanying graph, a high public-sector borrowing requirement in the first quarter of the fiscal year is a normal seasonal characteristic of general government finance. In comparison with the first quarter of fiscal 1991/92, all levels of general government, with the notable exception of local authorities, were responsible for the rise in the borrowing requirement of general government in the first quarter of fiscal 1992/93. The deficit before borrowing on the Main Budget increased from R6,6 billion in the first quarter of fiscal 1991/92 to R7,7 billion in the first quarter of fiscal 1992/93, while the surpluses of extra-budgetary institutions (including the TBVC countries and self-governing states) and provincial administrations available for lending to other sectors declined from R2,4 billion to R1,9 billion over the same period. In contrast to these developments, the deficit before borrowing of local authorities was equal to R0,6 billion in the June quarter of 1992, compared with R0,9 billion in the corresponding quarter of 1991.

The increase in the borrowing requirement of general government was due to the fact that the rate of increase in expenditure of general government was considerably higher than the rate of increase in general government revenue. The expenditure of general government rose from R24,1 billion in the first quarter of fiscal 1991/92 to R27,4 billion in the first quarter of fiscal 1992/93, or at a rate of 13,6 per cent; general government revenue rose from R19,6 billion to R21,6 billion, or by 10,2 per cent, over the same period. In particular current expenditure rose by 17 per cent from the first quarter of fiscal 1991/92 to the first quarter of fiscal 1992/93, but this increase was partly countered by a moderate contraction of capital expenditure. The relatively low rate of increase in general government revenue could mainly be attributed to the low rate of increase in tax collections by the Central Government.

Budgeted and actual Exchequer issues to government departments



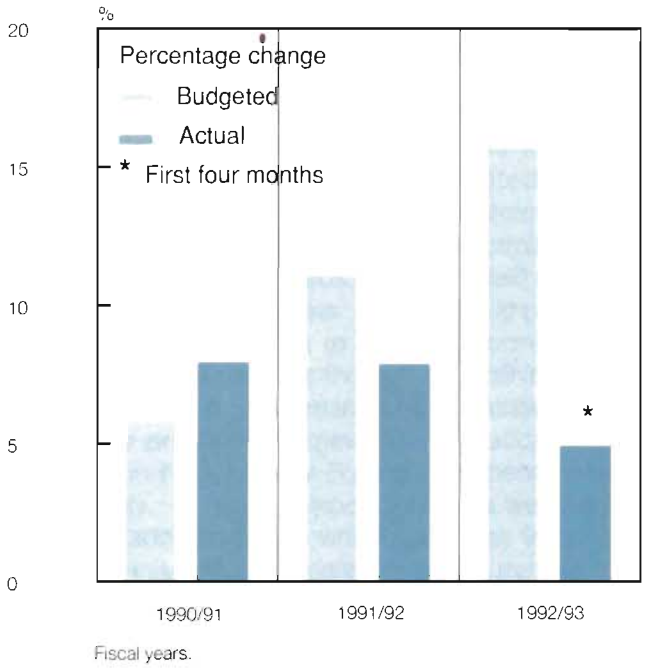
Exchequer Account

The sharp rise in general government expenditure took place mainly in the expenditure on the Exchequer Account. In the first quarter of fiscal 1992/93 the year-on-year rate of increase in Exchequer issues (after adjustment for changes in the balance on the Paymaster-General Account) amounted to 13,0 per cent. If expenditure in July 1992 is also taken into account, this rate of increase was slightly higher at 14,5 per cent. Although this rate of increase in Exchequer issues exceeded the increase in government revenue, it was nevertheless fairly low in comparison with corresponding increases in previous years and well within the increase budgeted for 1992/93: the average year-on-year rate of increase in the corresponding period of the preceding five fiscal years was equal to 16,2 per cent, and expenditure was budgeted to rise by 16,5 per cent for fiscal 1992/93 as a whole.

The year-on-year rate of increase in Exchequer receipts (excluding proceeds from privatisation), which had decelerated from 16,5 per cent in the third quarter of fiscal 1991/92 to 8,3 per cent in the final quarter, rose by only 8,9 per cent in the first quarter of fiscal 1992/93. In July 1992 even lower revenues were collected, with the result that the year-on-year rate of increase slowed down to only 4,9 per cent. This rate of increase was substantially lower than the budgeted increase of 15,7 per cent for fiscal 1992/93 and the average year-on-year rate of increase of 18,5 per cent for the corresponding period in the preceding five fiscal years.

The shortfall in Exchequer revenue was to a large extent the result of the downturn in economic activity which had become more severe and was lasting longer than had been anticipated at the time the Budget was presented in March 1992. This is clearly reflected by the proceeds from value-added tax in the first four months of fiscal 1992/93, which were no less than 22,0 per cent below the proceeds from general sales tax in the corresponding period of the preceding year. The proceeds from income tax in the first four months of fiscal 1992/93 also rose at a rate considerably lower

Budgeted and actual Exchequer receipts



than budgeted. Revenue from customs and excise duties, however, increased at a much higher rate than the budgeted amount for the full fiscal year, largely because of the higher than expected receipts from the fuel levy.

Percentage increase in government revenue

	Budgeted increase, fiscal year 1992/93	Actual increase, first four months 1992/93
Exchequer receipts	15,7	4,9
Customs and excise duties....	28,4	51,0
Inland revenue	14,0	-1,1
Income tax	16,7	4,8
Value-added tax	9,9	-22,0

The deficit on the Exchequer Account before borrowing and debt repayment in the first four months of fiscal 1992/93 came to R8 449 million, or about 53,0 per cent of the deficit budgeted for the fiscal year as a whole. The deficit for the corresponding period of fiscal 1991/92 was equivalent to 55 per cent of the deficit budgeted for that year. The deficit of R8 449 million, plus the discount of R1 867 million on new government stock issues, was financed by funds obtained from:

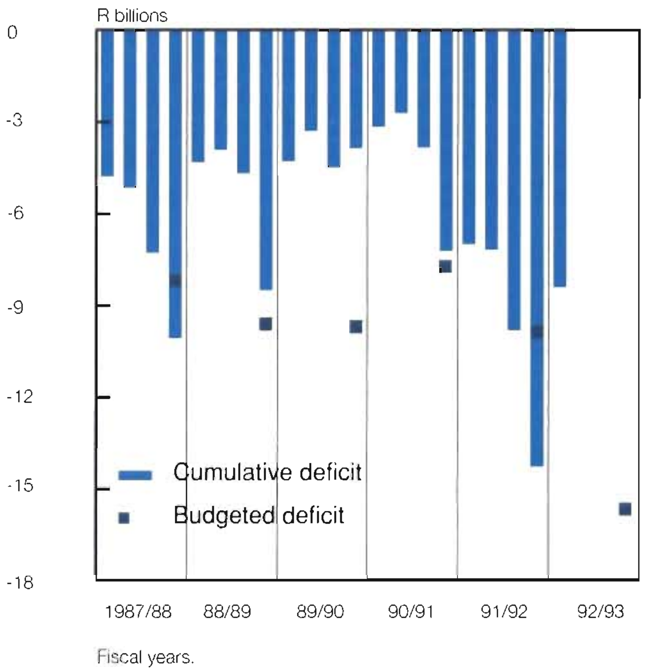
	R millions
Public Investment Commissioners	5 437
Non-monetary private sector	9 450
Monetary institutions:	–5 535
Corporation for Public Deposits	182
Other monetary institutions	–5 717
Foreign sector	964
Total gross financing	10 316
Less: Discount	1 867
Total net financing.....................................	**8 449**

The borrowing instruments utilised in the financing of the Exchequer deficit were as follows:

	R millions
Government stock (including discount)	14 022
Treasury bills	2 671
Foreign loans..	879
Non-marketable securities	8
Increase in available cash balances	-7 264
Total financing of Exchequer deficit	10 316
Less: Discount	1 867
Total net financing.....................................	**8 449**

New government stock issued for the financing of the government deficit amounted to R14 901 million in the first four months of fiscal 1992/93, of which R879 million was raised on international capital markets and R14 022 million domestically. This represented 80,6 per cent of the government's total budgeted financing

Deficit before borrowing



requirement of R18 495 million for fiscal 1992/93. The large share of the fiscal deficit was financed in the first four months of the current fiscal year because circumstances favoured sales of new government stock at this stage.