Quarterly economic review

Introduction

Economic developments in the first nine months of 1993 and especially in the third quarter of the year indicate that the prolonged recession in the South African economy of 1989-93 has bottomed out and that the economy has started to recover somewhat. The annualised rate of change in real gross domestic product not only turned around from negative to positive levels, but also accelerated from a still low 1½ per cent in the first quarter of 1993 to a very high 8 per cent in the third quarter. After having declined for three consecutive calendar years, real gross domestic product is therefore likely to show a small positive growth rate in 1993.

Although no mean achievement, the mainstay of this improved economic performance has been the substantial increase in agricultural production to more normal levels after having been adversely affected in 1992 by one of the most severe droughts in the country's history. This higher agricultural output made a large direct contribution to an increase in total domestic product, but was also in an indirect manner (through linkages with other production sectors) partly responsible for more widespread growth in the economy. Supported by a continued fairly good export performance and a higher gold price, the rise in agricultural production in the third quarter of 1993 contributed to positive growth rates in nearly all the more important economic sectors, with the notable exception of gold mining, construction, wholesale trade and accommodation services.

Various other positive developments also augur well for the future economic growth of the country, including the lifting of sanctions and establishment of new trade links with some countries; the normalisation of relations with international organisations, such as the International Monetary Fund and the International Bank for Reconstruction and Development; the final agreement concluded with South Africa's foreign creditor banks regarding the repayment of so-called affected debt; the greater financial stability achieved in the country; and the prospects of increased investments because of the introduction of tax-deductible accelerated depreciation allowances and the need to replace machinery and equipment.

A vigorous revival of economic activity over the short term will, however, probably be hampered by certain negative factors which may continue to have a significant influence on the economy. Firstly, the prospects for growth in the industrial countries still seem limited at this stage, which may hold back the growth in South African exports. Secondly, uncertainty regarding the outcome of political negotiations and ongoing internal unrest could probably continue to lead to a postponement of investment decisions. Thirdly, large fixed repayment obligations to foreign creditors may also restrict a more stimulatory macro-economic policy stance and thus prevent increases in output if this external constraint is not alleviated by the inflow of new foreign capital. Finally, important impediments to rapid economic growth still exist in the domestic production structure, which could have an adverse effect on the sustainability of such growth.

The improved economic conditions in the first nine months of 1993 were accompanied by sharp fluctuations in real gross domestic expenditure caused by changes in inventory levels. A fairly steady increase in final domestic demand, however, supported the acceleration in domestic output. Real private consumption expenditure continued to show positive rates of increase over this period, and increased somewhat faster in the third quarter of 1993. This mainly reflected higher levels of real personal disposable income and pre-emptive buying by consumers in anticipation of price increases of certain durable goods arising from the depreciation of the rand. Real consumption expenditure by general government also rose slightly, while total real gross domestic fixed investment rose marginally in the third quarter of 1993 after having contracted substantially in the preceding three years.

Despite the increase in domestic output, South African enterprises remained very cost-conscious and continued with rationalisation programmes leading to further labour-shedding. The lower levels of employment and higher production resulted in a considerable increase in labour productivity. The rates of increase in real remuneration per worker none the less still exceeded the rise in productivity, with the result that real unit labour costs continued to increase. If this carries on for a long period of time it could seriously affect the country's ability to compete internationally.

Considerable further success was nevertheless achieved in obtaining more stable financial conditions in the country during the first nine months of 1993. This was evident in the increases of both the producer and the consumer price indices. In addition to restrictive monetary policy measures, the downward drift in consumer price inflation was strongly aided by slower rates of increase in the cost of home ownership and in the prices of food; both these categories have initially been responsible for the inertia experienced in bringing price inflation down to lower levels.

The growth in both money supply and bank credit also slowed down further in the first half of 1993, but increased somewhat in the third quarter. The recovery in economic activity and concomitant higher income did not bring about a proportionate increase in the demand for money and credit because it was mainly related to improved agricultural output, i.e. it occurred in a sector with high and rising outstanding debt. Some other factors were also responsible for the lower growth in money supply and bank credit to the private sector, viz. the still low level of economic activity, the considerable overfunding of the government, the relatively high cost of borrowing, the increased flexibility in the use of mortgage financing facilities, disintermediation, and regulatory changes to the liquid asset and the cash reserve requirements.

Although the growth in money supply moved below the lower boundary of the money supply guidelines in the first nine months of 1993, the Reserve Bank continued to pursue a fairly restrictive monetary policy stance. No steps were taken to force the money supply back into the guideline range, because of the priority given to the protection of the foreign reserves of the country and to the objective of price stability. The Reserve Bank therefore applied monetary targeting in a discretionary manner and, as stated on various occasions, did not adhere to a rigid monetary rule. However, in view of the greater financial stability in the economy and the possible normalisation of South Africa's relations with the International Monetary Fund, the Reserve Bank reduced Bank rate from 13 to 12 per cent on 28 October 1993.

The total gross gold and other foreign reserves declined sharply to an alarmingly low level of only five weeks' imports of goods and services at the end of September 1993. This decrease was recorded despite the fact that the current account of the balance of payments remained relatively strong (with sharp fluctuations at times) throughout the first nine months of 1993. Unfortunately, this surplus was offset by a large net outflow of capital, mainly in the form of short-term funds. Continued leads and lags in foreign payments and receipts fostered by the strength of the US dollar on international foreign exchange markets, internal unrest and uncertainty created by socio-political developments, and the ready availability of domestic finance, persisted in favouring this outflow of capital.

The weakening in the overall balance of payments position led to a decline of 8,7 per cent in the nominal effective exchange rate of the rand from the end of December 1992 to 18 November 1993. Because this decrease was considerably larger than the differences in the inflation rates between South Africa and its main trading-partner countries, the real effective exchange rate of the rand also declined sharply.

In the financial markets, money market conditions remained relatively tight during the first nine months of 1993, but eased somewhat in October. The Reserve Bank accordingly concentrated on preventing the market from becoming too restrictive and on smoothing out shorter-term fluctuations. The capital market was characterised by substantial increases in trading of stocks, derivatives and shares, while real estate transactions rose slightly in the third quarter of 1993.

The general downward movement in money market interest rates, which had already started at the beginning of 1990, continued in the first ten months of 1993 but at a much slower pace than in 1992. The downward trend in money market rates from the middle of 1992 was based mainly on an expected lowering in Bank rate in an environment of a low demand for funds. Capital market rates, particularly the yield on long-term government stock, at first moved to higher levels in the first four months of 1993, but then contracted sharply again in the ensuing period up to October 1993.

The public-sector borrowing requirement amounted to 7,3 per cent of gross domestic product in the first half of fiscal 1993/94, which was substantially lower than the deficit of 10,3 per cent of gross domestic product in the first half of fiscal 1992/93. This improvement was mainly due to a reduction in transfers by the central government; in fiscal 1992/93 large extraordinary transfers had been made to the Gold and Foreign Exchange Contingency Reserve Account and to the civil service pension funds.

An increase in interest payments in the first seven months of fiscal 1993/94 caused Exchequer issues to rise to levels in excess of the budgetary provision for the year as a whole. On the other hand, the rate of increase in Exchequer receipts came close to the projected growth rate for the full fiscal year. Higher-than-expected receipts from value-added tax and customs and excise duties offset lower-than-expected income tax receipts from companies and individuals. As a ratio of gross domestic product, the deficit on the Exchequer Account before borrowing and debt repayment nevertheless still came to the high level of 8,2 per cent in the first half of fiscal 1993/94.

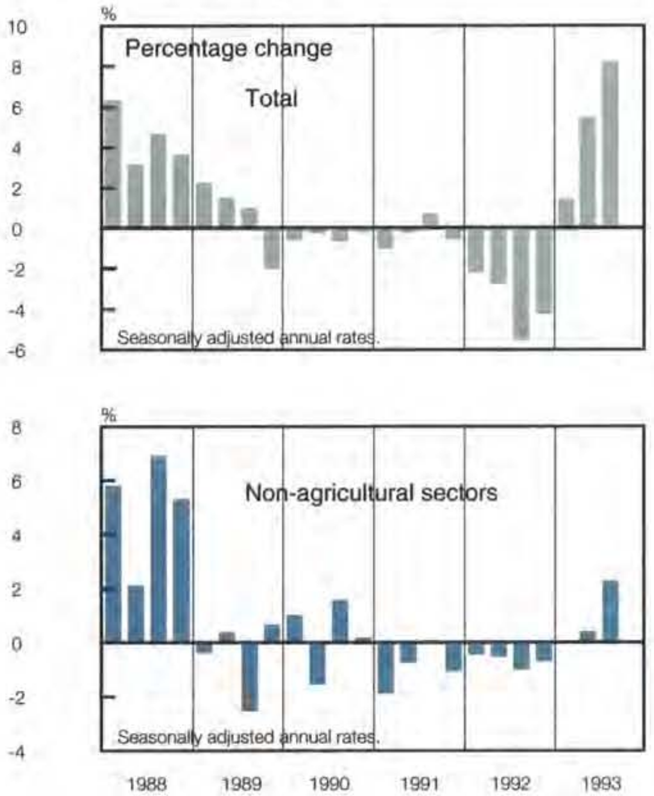
Domestic economic developments

Domestic output

After having declined at seasonally adjusted and annualised rates of 5½ per cent and 4½ per cent in the last two quarters of 1992, the growth rates in *real gross domestic product* turned positive from the beginning of 1993 and increased substantially from 1½ per cent in the first quarter to 5½ per cent in the second quarter and to 8 per cent in the third quarter. This was the first time since 1988 that the country experienced three consecutive quarters of positive economic growth. Even so, the level of aggregate output in the first nine months of 1993 was still about ½ per cent below that in the corresponding period of the preceding year.

The remarkable recovery in domestic output during the first three quarters of 1993 was mainly due to relatively favourable weather conditions and a substantial increase in *agricultural output*. In the third quarter of 1993 the level of agricultural output had returned to more or less the average output level of 1991 – i.e. to the levels that prevailed before the drought of 1992.

Real gross domestic product



The increase in real gross domestic product was, however, not only due to the substantially higher volume of agricultural output. If agricultural production is excluded, the total real output of the *non-agricultural sectors* rose by 2½ per cent in the third quarter of 1993, compared with a rate of increase of ½ per cent in the second quarter of 1993 and of approximately zero in the first quarter of the year. Moreover, this recovery in domestic output embraced a large number of sectors in the third quarter of 1993. With the exception of mining and construction, positive growth was reported in all the other major economic sectors.

Having increased at annualised rates of 2½ and 2 per cent in the first two quarters of 1993, the real value added by the *mining sector* receded at an annualised rate of 1 per cent in the third quarter. Technical problems experienced in the production of some divisions of gold-mining companies contributed to a decrease in the throughput and physical output of gold mines. The decline in gold production more than offset an increase in the production of other minerals and metals.

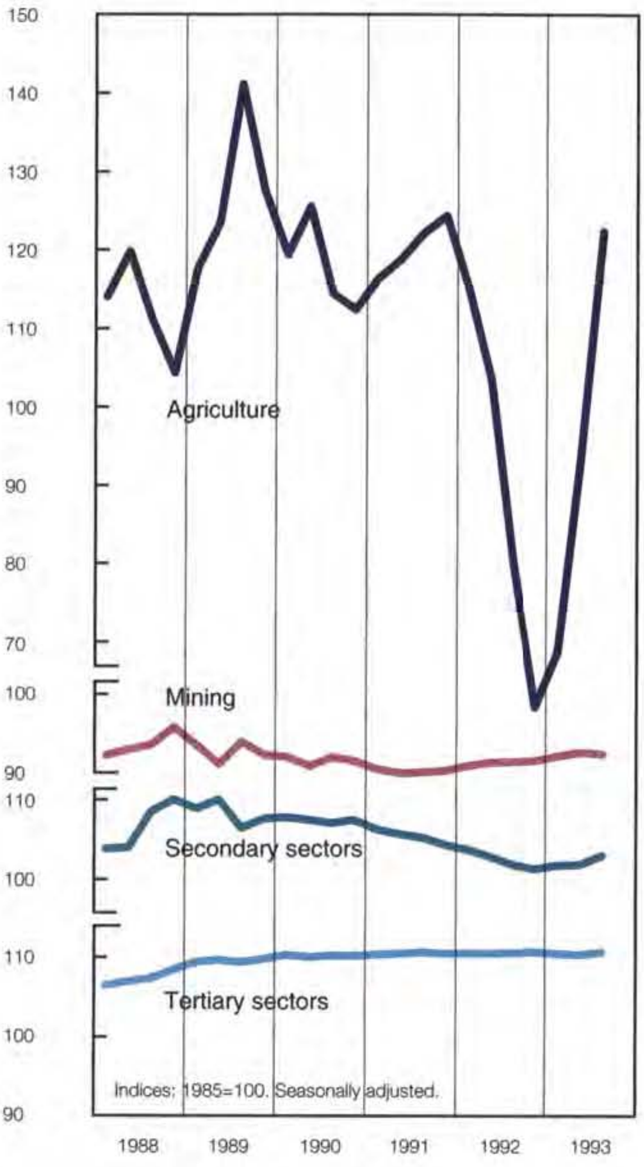
The real output of the *construction industry* continued to decline fairly sharply in the third quarter of 1993 to a level that was nearly 3 per cent below its value in the second quarter of 1993. The other two secondary sectors, however, performed exceptionally well in the third quarter of 1993. The real value added by the sector supplying *electricity, gas and water*, which had increased at annualised rates of 4½ per cent in the first quarter of 1993 and 5½ per cent in the second quarter, rose further at a rate of 5½ per cent in the third quarter. This was partly due to an increase in domestic demand, but was also brought about by a further rise in electricity sold to neighbouring countries.

The real output of the *manufacturing sector* increased at an annualised rate of 5½ per cent in the third quarter of 1993, following a moderate contraction in the preceding quarter. This increase in total manufacturing output reflected increases in real output by the subsectors producing food, wood products and furniture, chemical products, and machinery and transport equipment. Various factors probably contributed to the improvement in manufacturing production, including:

- the increase in the volume of manufactured goods exported in the first nine months of 1993;
- the much more aggressive marketing approach of local companies;
- the increase in inventories;
- the higher agricultural output, which had positive linkages with some manufacturing enterprises; and
- fewer disruptions of production because of mass demonstrations, stay-aways and other forms of labour unrest.

The real value added by the *tertiary sectors*, which had declined at an annualised rate of ½ per cent in both

Components of real gross domestic product



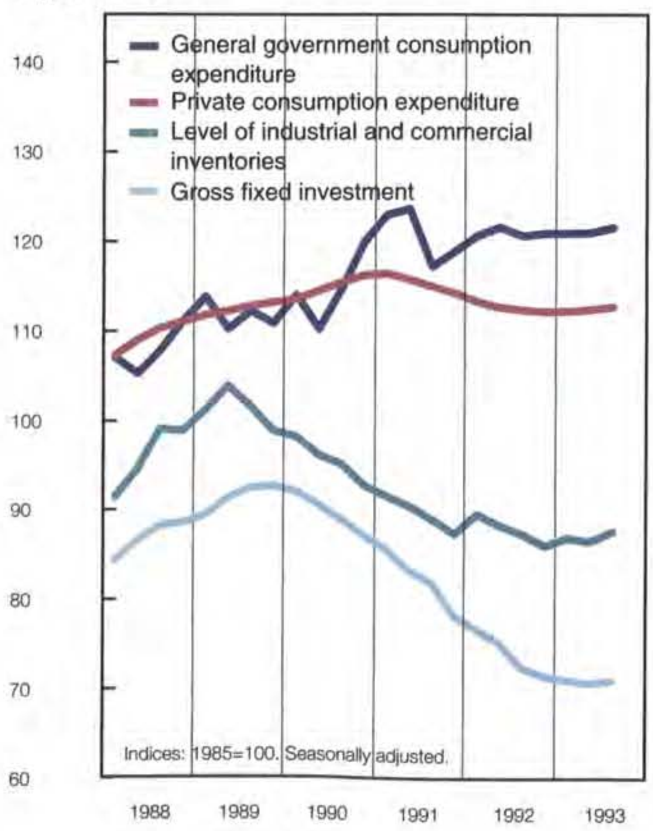
the first and second quarter of 1993, rose by 1 per cent in the third quarter. This increase stemmed from positive growth in the real value added by the sectors commerce, finance and insurance, and transport, storage and communication. A noticeable increase in the real growth of the motor trade, combined with a slight increase in the real value added by retail trade, neutralised further output decreases in the other subsectors of commerce, namely wholesale trade and catering and accommodation services. The increase in the real value added by the financial sector mainly reflected the buoyancy of trading activities on the Johannesburg Stock Exchange, whereas the larger maize crop and the larger foreign trade volumes in the first three quarters of 1993 led to an increase in activity in the transportation sector.

Domestic expenditure

The quarter-to-quarter rate of change in *total real gross domestic expenditure* fluctuated sharply in the first three quarters of 1993: in the first quarter real expenditure increased at an annualised rate of 9½ per cent, but it then contracted at a rate of 12 per cent in the second quarter before rising again at a rate of 15½ per cent in the third quarter. These sharp fluctuations could be ascribed mainly to changes in real inventories, which were affected to a large extent by fluctuations in foreign trade volumes. The level of real domestic expenditure in the first three quarters of 1993 was nevertheless still about ½ per cent lower than in the corresponding period of 1992.

Real *private consumption expenditure* rose further in the third quarter of 1993 at an annualised rate of 1 per cent; in the previous two quarters it had increased at a rate of only ½ per cent. The increase in real consumer outlays in the third quarter mainly reflected increases in household spending on semi-durable and

Main components of real gross domestic expenditure



non-durable goods and on services, while real expenditure on durable consumer goods remained virtually at the level of the preceding quarter. An increase in real outlays on personal transport equipment, owing largely to pre-emptive buying by consumers in anticipation of large price hikes, was offset almost completely by declines in real outlays on household appliances and recreational and entertainment goods. In the first three quarters of 1993 the number of new motor vehicles sold was 7 per cent higher than in the corresponding period of 1992.

Real *consumption expenditure by general government* showed almost no change in the first two quarters of 1993, but rose strongly in the third quarter. This increase was mainly due to an increase in real government purchases of intermediate goods and services, while the total real labour remuneration of general-government employees receded moderately.

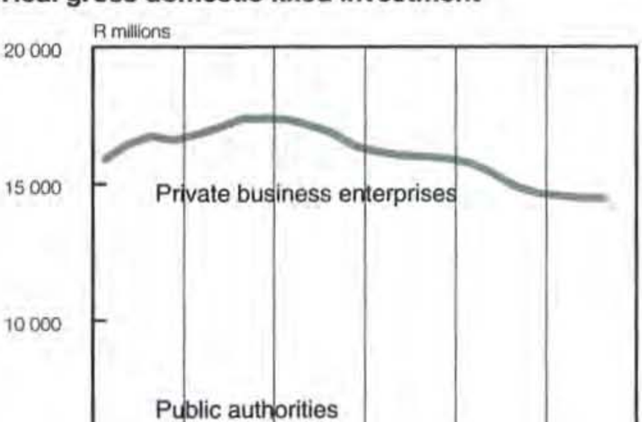
Total real *gross domestic fixed investment* levelled out in the second quarter of 1993 and, after fourteen consecutive quarters of contraction, actually rose at an annualised rate of 1½ per cent in the third quarter. This increase followed more moderate annualised rates of decline of 2½ and 2 per cent in the first two quarters of 1993. The level of real capital formation in the first nine months of 1993 was nevertheless still 5 per cent below that of the corresponding period of 1992.

The increase in aggregate real fixed investment in the third quarter of 1993 took place in the *public sector*: the real capital formation by public-sector entities rose at an annualised rate of 6 per cent, compared with rates of decline of 2½ and 1 per cent in the preceding two quarters. The higher level of real fixed capital expenditure by the public sector reflected increases in capital outlays of the central government, Transnet, Telkom and Eskom. In fact, sustained increases have been reported in the real fixed investment of Telkom and Eskom since the beginning of 1993 because of extensions to the telecommunications network of the country and the electrification of low-cost housing areas.

The real fixed investment of the *private sector*, however, continued to decline during the first nine months of 1993, but at a considerably lower rate than in 1992. After having contracted at a rate of 5½ per cent in 1992, the annualised rate of decline in the real fixed investment slowed down progressively to 2½ per cent in the first quarter of 1993, 2 per cent in the second quarter and to less than ½ per cent in the third quarter. This apparent bottoming-out of the downward movement in private-sector investment was probably related to the upgrading of existing production capacity (particularly in mining), the start of spending on a number of major capital projects encouraged by tax-deductible accelerated depreciation allowances and the need to replace machinery and equipment.

Real *inventory investment* rose fairly sharply in the third quarter of 1993 owing to a significant increase in agricultural stocks-in-trade resulting from the relatively large maize crop and an increase in real industrial and commercial inventories. The rise in industrial and commercial inventories may be interpreted as indicative of the fact that manufacturers and traders are positioning themselves to meet a strengthening of total demand. However, this conclusion is contradicted by the change in the ratio of industrial and commercial inventories to non-agricultural gross domestic product, which declined from an average of 17½ per cent in the first two quarters of 1993 to about 17 per cent in the third quarter. Relative to aggregate real product levels, inventories were thus still being reduced in the third quarter.

Real gross domestic fixed investment



Factor income

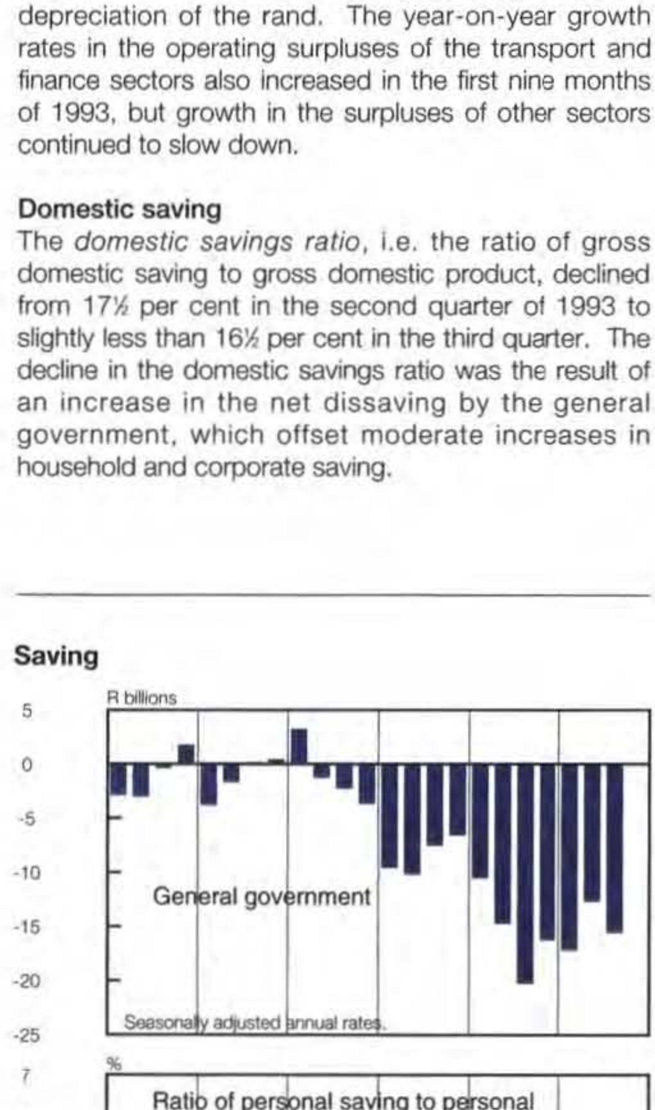
Despite a further decrease in the growth of nominal labour remuneration, the year-on-year rate of increase in *nominal factor income* accelerated from 9½ per cent in the first quarter of 1993 to 14 per cent in the third quarter. The rate of increase over four quarters in total *nominal labour remuneration*, however, slowed down from 11 per cent in the first quarter of 1993 to 9 per cent in the third quarter. This downward movement was evident in almost all the major sectors of the economy. Although this is a normal characteristic of the economy when the downturn begins to bottom out, these recent developments could also be ascribed to factors such as the high level of unemployment, a continued relatively restrictive monetary policy, the slowdown in the rate of inflation, a decline in existing job opportunities and more realistic wage demands by some trade unions.

The growth over four quarters in aggregate nominal *gross operating surplus*, on the other hand, rose sharply from 8 per cent in the first quarter of 1993 to 15 per cent in the third quarter. This significant increase in the gross operating surplus was mainly due to the improvement in the operating surpluses of farmers and the mines, who benefited from larger crops, an increase in the dollar price of gold and the depreciation of the rand. The year-on-year growth rates in the operating surpluses of the transport and finance sectors also increased in the first nine months of 1993, but growth in the surpluses of other sectors continued to slow down.

Domestic saving

The *domestic savings ratio*, i.e. the ratio of gross domestic saving to gross domestic product, declined from 17½ per cent in the second quarter of 1993 to slightly less than 16½ per cent in the third quarter. The decline in the domestic savings ratio was the result of an increase in the net dissaving by the general government, which offset moderate increases in household and corporate saving.

Saving



The dissaving by *general government* rose from an annualised level of R12,3 billion in the second quarter of 1993 to R15,7 billion in the third quarter. This deterioration of the balance on the current account of general government stemmed mainly from increases in interest paid on public debt and consumption expenditure, which outpaced a moderate increase in aggregate tax receipts and other current government revenue.

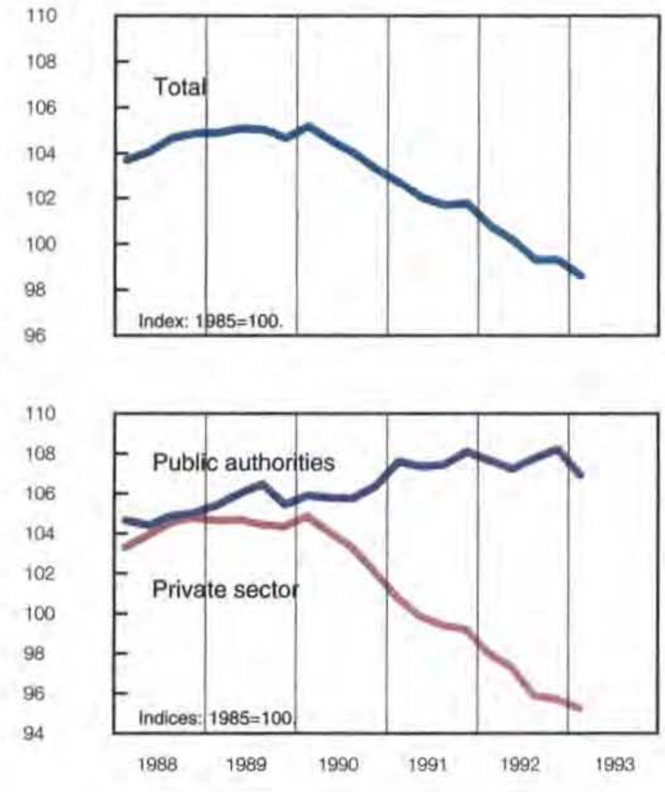
Net saving of the *private sector* (the corporates and households) as a percentage of gross domestic product rose marginally from 5½ per cent in calendar 1992 and 6 per cent in the second quarter of 1993 to 6½ per cent in the third quarter. In the corporate sector increased savings were reported in those sectors showing healthier financial results, such as agriculture, mining and finance. The ratio of personal saving to personal disposable income edged up from an average of less than 2½ per cent in the first two quarters of 1993 to about 3 per cent in the third quarter. A further increase in real personal disposable income (real income from property as well as adjustments in labour remuneration) exceeded the increase in current expenditure by households, and was responsible for the rise in household saving.

Employment

Despite the increase in domestic output, the generally low level of economic activity forced South African enterprises to become much more cost-conscious. Labour-shedding continued to take place in an environment of keen international competition and greater flexibility in the labour market. After having declined by 2,1 per cent in both 1991 and 1992, *total employment* in the formal non-agricultural sectors of the economy contracted by a further 2,8 per cent at a seasonally adjusted and annualised rate in the first quarter of 1993. (Latest information made available by the Central Statistical Service.)

The rate of decrease in employment in the non-agricultural *private sector* accelerated from 0,9 per cent in 1990 to 3,6 per cent in 1991, before moderating somewhat to 3,1 per cent in 1992. High rates of decrease in private-sector employment were recorded in almost every calendar quarter since the start of the recession. More recently, however, the quarter-to-quarter decrease in private-sector employment slowed down significantly from seasonally adjusted and annualised rates varying between approximately 3 and 6 per cent in the first three quarters of 1992, to 0,8 per cent in the fourth quarter and 1,9 per cent in the first quarter of 1993. The higher rate of decrease in the first quarter of 1993 was brought about by continued staff retrenchments in the construction industry, mining and the motor trade. Increases in employment were, however, reported by the manufacturing sector, wholesale and retail trade, banks and private road transportation. Information available for the second

Non-agricultural employment



quarter of 1993 indicates further reductions of personnel in the mining industry.

The rate of increase in total employment by *public authorities* slowed down from 1,6 per cent in 1991 to 0,1 per cent in 1992. Quarterly rates of change in employment by public authorities fluctuated widely and increases at seasonally adjusted and annualised rates of 2,0 and 1,7 per cent in the last two quarters of 1992 were followed by a large decline at a rate of 4,7 per cent in the first quarter of 1993. The public sector nevertheless remained a net creator of job opportunities in the formal economy during the current recession: from the first quarter of 1989 to the first quarter of 1993 employment by public authorities increased by 23 400 persons, while employment in the private sector declined by 351 600 persons.

The seasonally adjusted total number of *registered unemployed* persons increased throughout the recession of 1989-93. In 1992 the total number of registered unemployed was 16,2 per cent higher than in 1991 and in the first seven months of 1993 it was 16,4 per cent above the level in the corresponding period of 1992. In July 1993 the seasonally adjusted total number of registered unemployed workers amounted to 330 700.

Labour costs and productivity

Although the rate of increase in the average monthly *total nominal remuneration* per worker in the non-agricultural sectors declined from a recent high of 18,3 per cent in 1989 to 15,6 per cent in 1992, it remained relatively high given the rising number of unemployed. The year-on-year rate of increase in nominal remuneration per worker declined more significantly from 19,4 per cent in the fourth quarter of 1989 to 13,8 per cent in the second quarter of 1991; it then accelerated somewhat to 16,5 per cent in the second quarter of 1992 before declining again to 13,4 per cent in the first quarter of 1993. These high rates of increase were recorded even though labour unions were willing to accept more realistic wage adjustments under the current supply and demand conditions in the labour market. The continued high rates of increase in wages per worker could probably be ascribed to a change in the composition of the employed labour force because retrenchments have been relatively heavy among the more unskilled and relatively low-paid workers. This is confirmed by data on the total wage bill, which increased at much lower rates.

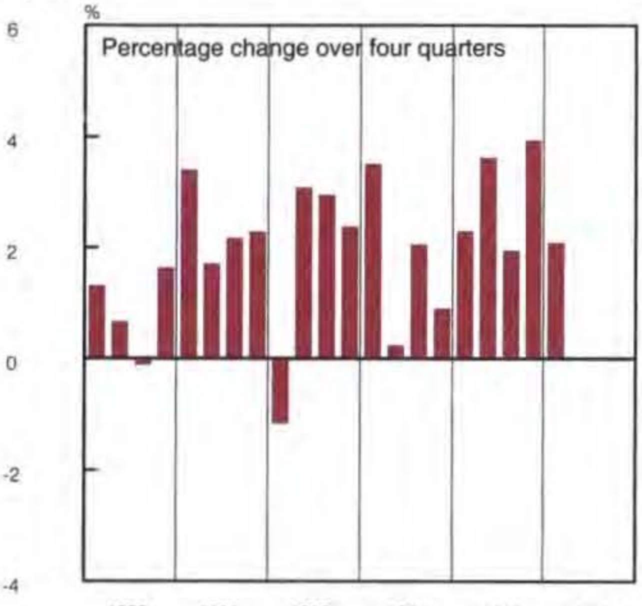
The rate of increase in the average monthly nominal remuneration per worker in the *private sector* declined only moderately from rates of more than 16 per cent in the period 1988-90 to 15,6 per cent in 1992. After having recorded year-on-year rates of increase of more than 15 per cent in most of the calendar quarters of 1992, the rise in total private-sector remuneration per worker declined to 13,0 per cent in the first quarter of 1993.

The rate of increase in the average monthly nominal remuneration per worker employed by *public authorities* declined more significantly than that of the private sector, viz. from 21,9 per cent in 1989 to 15,2 per cent in 1992, and to a year-on-year rate of 14,0 per cent in the first quarter of 1993. The workers employed by public authorities have nevertheless still received higher average salary and wage increases than their counterparts in the private sector during the past four years.

As a result of the generally high rates of increase in the nominal remuneration of workers, the rate of increase in the *real remuneration* per worker in the non-agricultural sectors of the economy (as deflated by the price deflator for the non-agricultural gross domestic product) remained positive and actually accelerated from 1,6 per cent in 1991 to 3,0 per cent in 1992. In the first quarter of 1993 the year-on-year rate of increase in real wage per worker came to 2,1 per cent. These figures indicate a continued squeeze on the operating surpluses or profits of business enterprises.

The rate of increase in the real non-agricultural *labour productivity* rose from only 0,5 per cent in 1990 to 1,4 per cent in 1991 and 1992. The year-on-year rate of increase in real labour productivity also

Real remuneration per worker in non-agricultural sectors



accelerated from 0,5 per cent in the fourth quarter of 1991 to 1,8 and 1,7 per cent in the fourth quarter of 1992 and the first quarter of 1993. This acceleration in productivity was aided to some extent by the contraction in the number of man-days lost due to strikes and work stoppages since 1990. Productivity also rose over this period because reductions in the labour force were larger than reductions in total output.

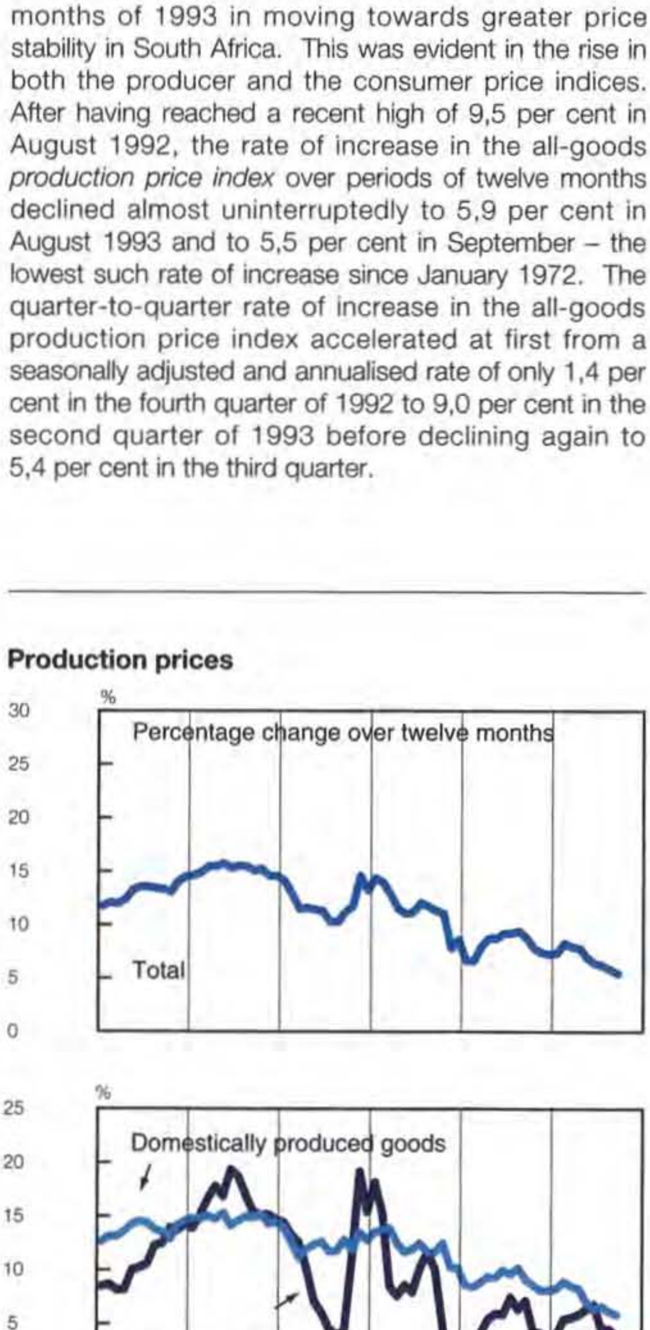
The rate of increase in *nominal unit labour costs* in the non-agricultural sectors of the economy declined continuously from a high of 17,2 per cent in 1989 to 14,0 per cent in 1992 because of lower rates of increase in the remuneration of workers and improvements in labour productivity. Measured over a period of four quarters, the rate of increase in nominal labour costs per unit of physical output declined, on balance, from a high of 19,9 per cent in the fourth quarter of 1989 to 11,5 per cent in the second quarter of 1991; it then accelerated to 15,2 per cent in the second quarter of 1992 before receding again to 11,5 per cent in the first quarter of 1993.

As a consequence of the continued high rates of increase in the nominal remuneration of workers and the significant progress that has been achieved in lowering inflation, *real unit labour costs* continued to increase at relatively high rates. After having increased by only 0,2 per cent in 1991, real labour costs per unit of physical output (as deflated by the price deflator for non-agricultural gross domestic product) rose by 1,5 per cent in 1992. The year-on-year rate of increase in real unit labour costs also accelerated from a negative level of 1,7 per cent in the second quarter of 1991 to a positive figure of 2,5 per cent in the second quarter of 1992; it then contracted to only 0,5 per cent in the third quarter, accelerated to 2,1 per cent in the fourth quarter of 1992 and declined again to 0,4 per cent in the first quarter of 1993.

Prices

Considerable success was achieved in the first nine months of 1993 in moving towards greater price stability in South Africa. This was evident in the rise in both the producer and the consumer price indices. After having reached a recent high of 9,5 per cent in August 1992, the rate of increase in the all-goods *production price index* over periods of twelve months declined almost uninterruptedly to 5,9 per cent in August 1993 and to 5,5 per cent in September – the lowest such rate of increase since January 1972. The quarter-to-quarter rate of increase in the all-goods production price index accelerated at first from a seasonally adjusted and annualised rate of only 1,4 per cent in the fourth quarter of 1992 to 9,0 per cent in the second quarter of 1993 before declining again to 5,4 per cent in the third quarter.

Production prices

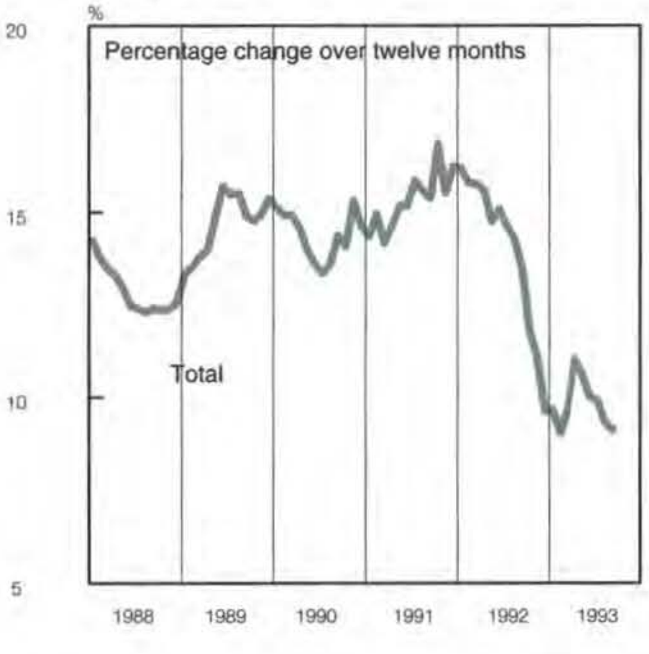


The rapid acceleration in the quarterly rise in the production price index was caused mainly by the sharp depreciation of the rand against the currencies of nearly all South Africa's main trading partners. As a result of this lower external value of the rand, the rate of increase in the *prices of imported goods* over periods of twelve months rose from a low of 3,1 per cent in December 1992 to 6,8 per cent in June 1993; it then moderated somewhat to 4,5 per cent in July and August and to 3,8 per cent in September.

The rate of increase in the *prices of domestically produced goods* over periods of twelve months has been sliding downwards since May 1989, when it amounted to 15,4 per cent. Although this downward movement was halted temporarily by the Gulf War towards the end of 1990, this inflation rate moved downwards to only 6,2 per cent in August 1993 and to 5,9 per cent in September.

The rate of increase in the overall *consumer price index* measured over twelve months, which had dropped from a high of 16,8 per cent in October 1991 to 9,6 per cent in December 1992 (the first single-digit rate of increase since June 1978), slowed down further to 9,0 per cent in February 1993. The slowdown in inflation was then interrupted briefly in March by sharp increases in education fees and in April by an increase of 4 percentage points in the value-added tax rate, increases in other indirect taxes and a rise in the price of petrol; this pushed the twelve-month rate of increase in the consumer price index back to 11,0 per cent in April. In subsequent months adherence to a relatively strict anti-inflationary monetary policy and the low level of economic activity gave cause for inflation expectations to subside noticeably and for wage settlements to become much more moderate than in previous years. Accordingly, the rate of increase over twelve months in the overall consumer price index declined to 9,1 per cent in September 1993.

Consumer prices



The downward drift of consumer price inflation since October 1991 was strongly aided by significant reductions in the rates of increase in the cost of home ownership. From April 1993 the consumer prices of food and non-alcoholic beverages over periods of twelve months also started to increase at lower rates than the overall price index. If the cost of home ownership and the prices of food and non-alcoholic beverages are excluded from the consumer price index, the rate of increase in the prices of the other components of the index measured over a period of twelve months still amounted to 12,9 per cent in September 1993. This high rate of increase in the prices of these other components was influenced in particular by a substantial rise in the prices of new vehicles because of the weak rand.

The quarter-to-quarter rate of increase in the consumer price index increased sharply from a seasonally adjusted and annualised rate of only 4,7 per cent in the fourth quarter of 1992 to 17,6 per cent in the second quarter of 1993 mainly because of the implementation of the indirect tax proposals contained in the Budget for 1993/94; however, it then slowed down again to 7,4 per cent in the third quarter. In this more recent quarter, sharply lower rates of increase were recorded in the prices of consumer goods as well as services. However, the prices of services, especially education fees and medical costs, have risen considerably faster than the prices of goods since March 1993.

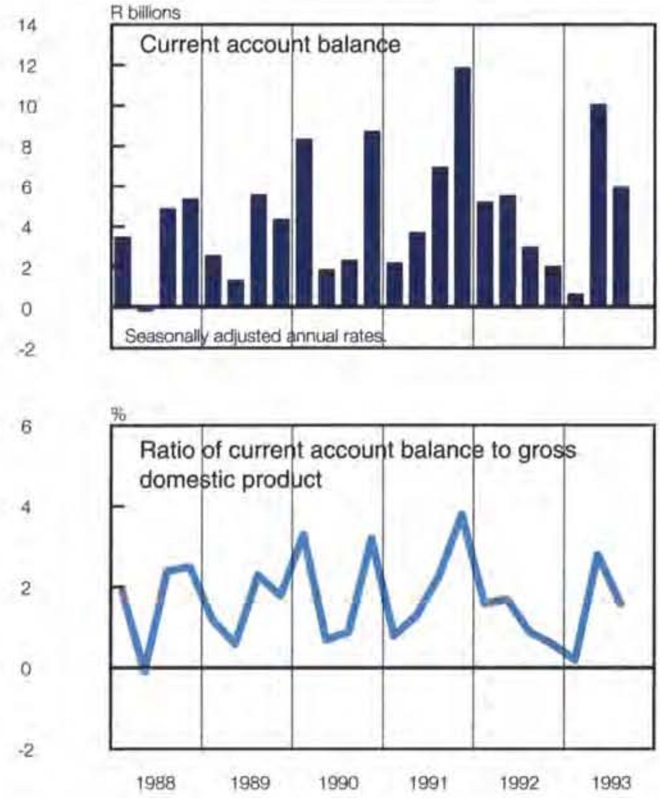
Foreign trade and payments

Current account

A surplus at a seasonally adjusted and annualised rate of R5,9 billion was recorded on the current account of the balance of payments in the third quarter of 1993. Although this surplus was significantly smaller than the exceptionally large figure of R10,1 billion in the second quarter of 1993, it was still slightly above the quarterly average seasonally adjusted and annualised surplus of R5,4 billion in the first half of 1993. Notwithstanding the higher level of economic activity in South Africa, the cumulative surplus in the first nine months of 1993 amounted to R5,1 billion; this was significantly more than the surplus of R3,9 billion for 1992 as a whole. As a ratio of gross domestic product, the surplus on the current account increased from just more than 1 per cent in 1992 to 1½ per cent in the first nine months of 1993.

The persistently good and even improved performance of the current account balance during a period in which the domestic economy recovered somewhat, was a reflection of the low level from which the economy started to grow and the effect of a substantial increase in agricultural output on imports and exports. A sharp decrease in the imports of agricultural goods limited the rise in the value of merchandise imports in the first nine months of 1993. At the same time the value of both the net gold exports and merchandise exports rose sharply, neutralising a significant increase in net service and transfer payments to non-residents.

Balance of payments



The value of *merchandise imports* rose from a seasonally adjusted and annualised rate of R53,4 billion in the fourth quarter of 1992 to R59,7 billion in the third quarter of 1993. This substantial increase was mainly the result of a sharp rise in the prices of goods imported: in the first nine months of 1993 the index value of merchandise import prices was 8½ per cent above its level in the corresponding period of the preceding year. Import prices rose sharply, despite marginally lower international oil prices and only moderate increases in the prices of goods in most of South Africa's main trading partner countries. The

Balance of payments on current account
Seasonally adjusted annual rates

R billions

	1992				1993		
	2nd qr	3rd qr	4th qr	Year	1st qr	2nd qr	3rd qr
Merchandise exports	49,6	49,5	49,4	49,0	47,2	56,2	54,8
Net gold exports	16,7	20,4	18,2	18,4	21,1	22,2	24,5
Merchandise imports	–49,2	–55,4	–53,4	–51,9	–56,4	–56,1	–59,7
Net service and transfer payments	–11,6	–11,5	–12,2	–11,6	–11,2	–12,2	–13,7
Balance on current account	**5,5**	**3,0**	**2,0**	**3,9**	**0,7**	**10,1**	**5,9**

depreciation of the rand was therefore mainly responsible for the sharp increase in the value of imports.

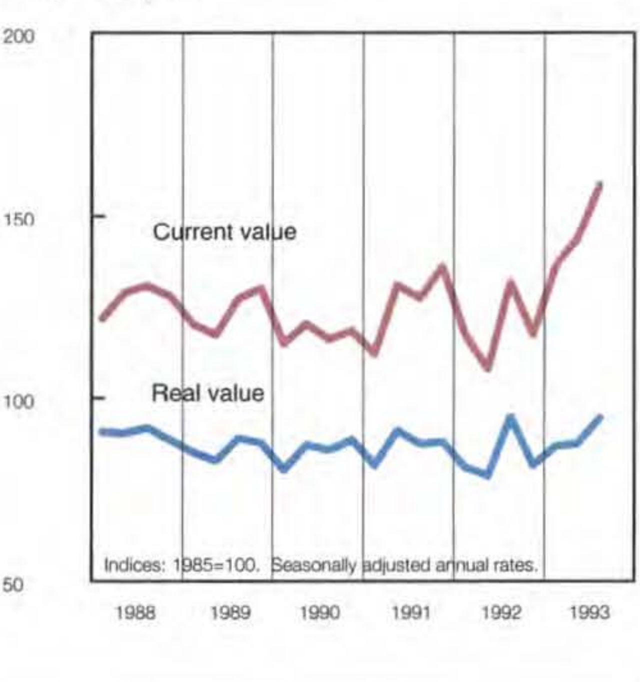
After having increased sharply in the second half of 1992 owing to the imports of agricultural goods, the volume of merchandise imports fluctuated around this higher level in the first nine months of 1993. Lower imports of agricultural products were offset by increases in most of the other main categories of imported goods, and particularly by pronounced increases in the imports of chemical products, machinery and electrical equipment, transport equipment and precious stones.

The value of *net gold exports* (seasonally adjusted and annualised) rose persistently from R18,2 billion in the fourth quarter of 1992 to R24,5 billion in the third quarter of 1993, reflecting a rise in the dollar price of gold and a depreciation of the rand against the dollar. The average fixing price of gold rose from US$329 per fine ounce in January 1993 to $392 in July 1993 – the highest monthly average since August 1990; it then dropped to $355 per fine ounce in September 1993 before recovering somewhat to $364 in October. In rand terms, the average fixing price of gold per fine ounce amounted to R1 010 in January, to R1 313 in July and to R1 233 in October.

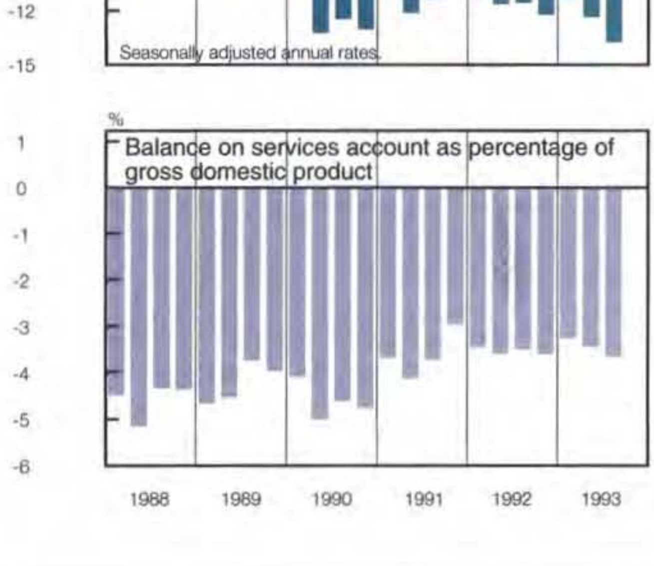
The higher and still increasing levels of the value of net gold exports could, however, also be ascribed to a rise in the volume of gold exports. The gold mines, as part of their rationalisation programmes, not only introduced cost-cutting measures, but also started mining higher-grade ore to maintain reasonable profit levels. The substantial increase of 8 per cent in the volume of gold exports in the third quarter of 1993 was, however, also related to a running-down of inventories stockpiled over the preceding quarters.

After having risen substantially from R47,2 billion in the first quarter of 1993 to R56,2 billion in the second quarter, the value of *merchandise exports* (seasonally adjusted and annualised) declined somewhat to a still high level of R54,8 billion in the third quarter of 1993. Although showing sharp quarter-to-quarter fluctuations, the volume of merchandise exports tended upwards, on balance, and in the first nine months of 1993 it was 2 per cent above its level in the corresponding period of 1992. The depreciation of the rand was mainly responsible for a sharp increase in export prices in the first three quarters of 1993. As could be expected in view of the improved weather conditions, the exports of agricultural products rose sharply in the first nine months of 1993. The exports of manufactured goods also increased steadily. As a percentage of total merchandise exports, manufacturing exports amounted to approximately 26 per cent in the third quarter of 1993; as recently as 1988, this ratio had averaged only 16 per cent.

Net gold exports



Services account



Net service and transfer payments to non-residents increased from a seasonally adjusted and annualised value of R11,2 billion in the first quarter of 1993 to R13,7 billion in the third quarter. This substantial increase resulted from higher service payments coupled with a decline in service receipts. Higher payments for freight and merchandise insurance related to the higher imports, and an increase in interest payments owing to the continued strengthening of non-residents' interest in South African securities, were largely responsible for the rise in service payments, whereas significantly lower receipts from foreign tourists' expenditure in South Africa contributed to a decline in service receipts from the rest of the world.

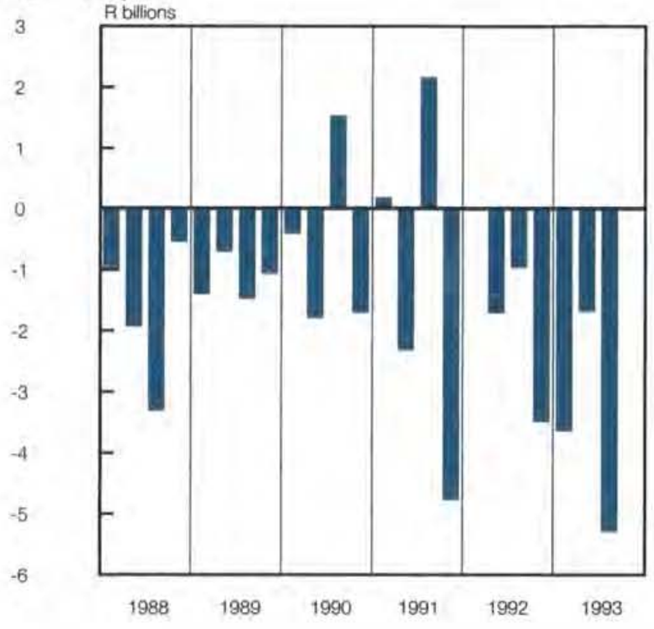
Capital movements

A further and substantially larger *total net outflow of capital* not related to reserves was recorded on the capital account of South Africa's balance of payments during the first nine months of 1993. The net outflow of capital, which had at first fallen from R3,5 billion in the fourth quarter of 1992 and R3,7 billion in the first quarter of 1993 to R1,7 billion in the second quarter, rose again to R5,3 billion in the third quarter of 1993. In the first nine months of 1993 the total net outflow of capital accordingly amounted to R10,7 billion, compared with an outflow of R6,2 billion for 1992 as a whole.

The large outflow of capital during the first nine months of 1993 mainly took the form of *short-term capital* (excluding reserve-related liabilities but including errors and unrecorded transactions), which amounted to no less than R9,4 billion. The large net outflow of short-term funds from South Africa could be ascribed to continued unfavourable leads and lags in foreign payments and receipts, which were fostered by the strength of the US dollar on international foreign exchange markets and sustained downward pressure on the value of the rand. The ongoing internal unrest, political and social uncertainty, the ready availability of domestic trade financing, and the relatively favourable cost of domestic finance, also contributed to the persistent outflow of short-term capital.

After having amounted to only R0,2 billion in the first six months of 1993, the net outflow of *long-term capital* in the third quarter came to R1,1 billion. The third-quarter outflow was mainly due to the repayment of R570 million to foreign creditors in terms of the Third Interim Debt Arrangements on 15 August 1993, the redemption of bearer bonds and notes of R445 million, and repayments of Government-guaranteed loans to an amount of R420 million. Affected debt amounting to R460 million, which had been converted in terms of the Second and Third Interim Debt Arrangements into long-term loans outside the so-called standstill net, also fell due for repayment in the third quarter of 1993. These outflows were, however, neutralised to some extent by net purchases of securities to an amount of almost R500 million by non-residents on the Johannesburg Stock Exchange. Although these purchases were reported as a net inflow of long-term capital to the private sector, they were, of course, offset by corresponding outflows in other items on the balance of payments because they were made through the financial-rand mechanism.

Total net capital movements (not related to reserves)

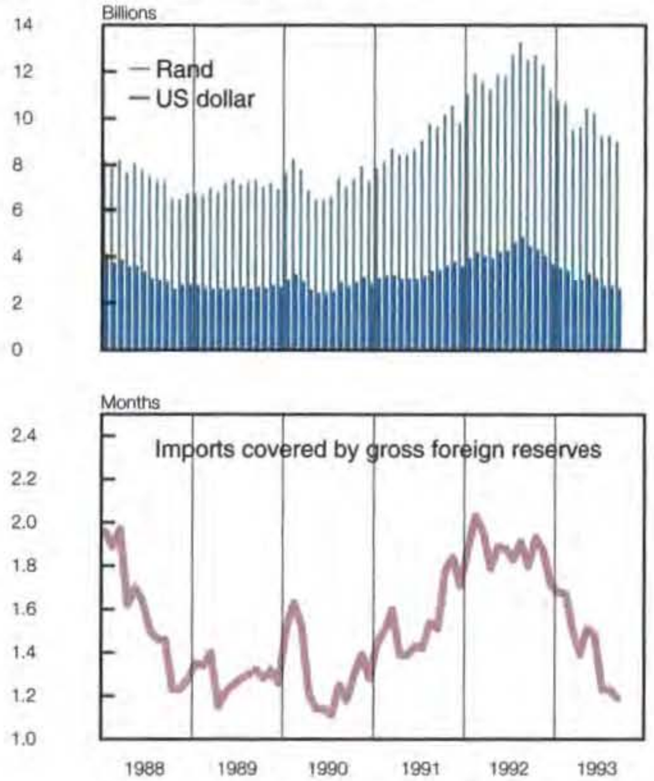


Foreign reserves

The substantial further net outflow of capital in the first nine months of 1993 exceeded the surplus on the current account, with the result that the country's *net gold and other foreign reserves* declined by R5,6 billion; in 1992 as a whole the net foreign reserves had contracted by R2,3 billion, while an increase of R1,4 billion had still been recorded in 1991. Having decreased by about R2,0 billion in the first half of 1993, the net gold and other foreign reserves fell by a further R3,6 billion in the third quarter.

In view of this decline in the net foreign reserves, the level of the *gross gold and other foreign reserves* had to be supported by reserve-related borrowing, especially in the first and third quarter of 1993. In the first nine months of 1993 the liabilities related to reserves of the country therefore increased by R1,2 billion. Taking into account positive valuation adjustments of R2,2 billion arising mainly from the higher level of the gold price and a depreciation of the rand against the dollar, South Africa's gross gold and other foreign reserves declined by R2,2 billion in the

Total gross gold and other foreign reserves

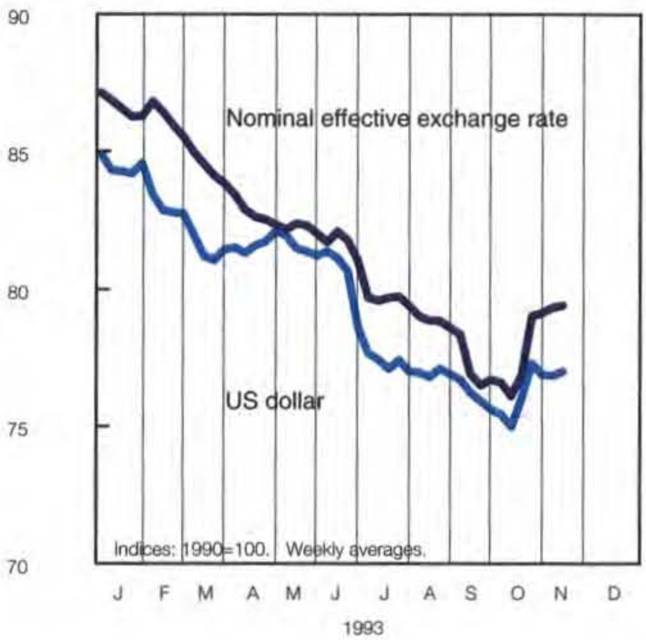


first nine months of 1993. This brought the level of the gross foreign reserves to R9,0 billion at the end of September, which was about one-third lower than its peak of R13,2 billion at the end of August 1992. The level of the total gross foreign reserves accordingly contracted sharply from about eight weeks' imports of goods and services in August 1992 to only five weeks' imports in September 1993. In October 1993, however, the gross foreign reserves of the South African Reserve Bank increased by R283 million to R7,1 billion at the end of the month.

Exchange rates

The *nominal effective exchange rate* of the rand declined by 12,9 per cent from the end of 1992 up to 12 October 1993. Owing to substantial intervention by the Reserve Bank during the second week of October and an improvement in the level of the gross foreign reserves, the monetary authorities managed to stem and reverse the downward trend in the weighted average exchange rate of the rand: the nominal

Exchange rates of the rand



Changes in exchange rates of the rand
%

	31 Dec '92 to 31 Mar '93	31 Mar '93 to 30 Jun '93	30 Jun '93 to 6 Oct '93	6 Oct '93 to 18 Nov '93	31 Dec '92 to 18 Nov '93
Weighted average	–3,8	–4,8	–4,6	4,6	–8,7
US dollar	–3,9	–4,4	–3,9	2,7	–9,3
British pound	–2,6	–5,3	–4,3	5,4	–6,9
German mark	–3,4	–0,1	–7,5	7,9	–4,0
Japanese yen	–10,0	–11,9	–4,6	4,0	–22,1
Netherlands guilder	–3,3	–0,4	–7,3	7,7	–4,2
Italian lira	5,3	–8,4	–0,5	7,7	2,6

effective exchange rate of the rand increased by 4,6 per cent from 6 October 1993 to 18 November. This brought the net decline in the nominal effective exchange rate of the rand to 8,7 per cent from the beginning of the year until 18 November 1993. During the first eight months of 1993 the *real effective exchange rate* of the rand declined by 6,6 per cent.

From the end of December 1992 to 18 November 1993 the rand depreciated against all the currencies of its major trading-partner countries, with the notable exception of the Italian lira. Against the Japanese yen the rand depreciated by no less than 22,1 per cent over this period. The exchange rate of the rand against the US dollar also reached a record low of R3,46 per US dollar on 6 October 1993 before stabilising again at a level of between R3,34 and R3,38 per dollar until 18 November 1993.

The continuing strong demand for South African securities, the progress made with the political negotiation process, and the lifting of many of the remaining sanctions against South Africa by various countries and international organisations, resulted in an appreciation of the *financial rand* of nearly 15 per cent in the first ten months of 1993. On 15 October 1993 the financial rand reached a high of R4,0950 per dollar before depreciating again to R4,2653 per dollar on 18 November 1993. On balance, the financial rand discount narrowed substantially from 37,2 per cent at the end of December 1992 to 16,5 per cent on 8 October 1993; it then rose again to 21,1 per cent on 18 November 1993.

Financial markets

Money supply

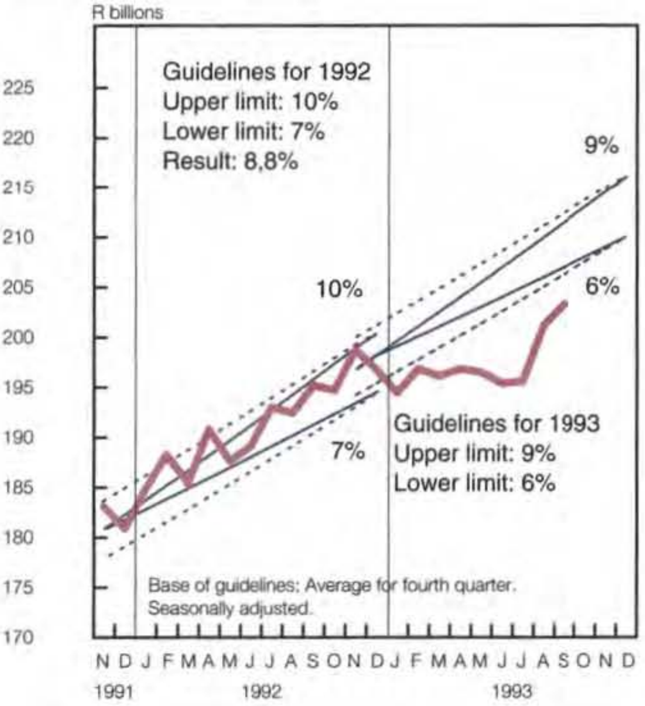
The change to positive and rising real economic growth rates during 1993 was at first accompanied by a continued decline in the growth of the *broadly defined money supply* (M3). Measured over periods of twelve months, the rate of increase in M3 slowed down from an already low 8,0 per cent in December 1992 to only 1,6 per cent in July 1993; only then did it start to rise moderately to 4,3 per cent in September. The quarter-to-quarter rate of increase in the average value of M3 (seasonally adjusted and annualised) receded likewise from 8,5 per cent in the fourth quarter of 1992 to 0,9 per cent in the second quarter of 1993, and accelerated to 5,0 per cent in the third quarter.

As could be expected under these circumstances, the lower growth in money supply was accompanied by an increase in the income velocity of M3: the velocity of circulation rose by about 10 per cent from the fourth quarter of 1992 to the third quarter of 1993. Various factors contributed to this sharp increase in the income velocity and the low rate of increase in M3, including:

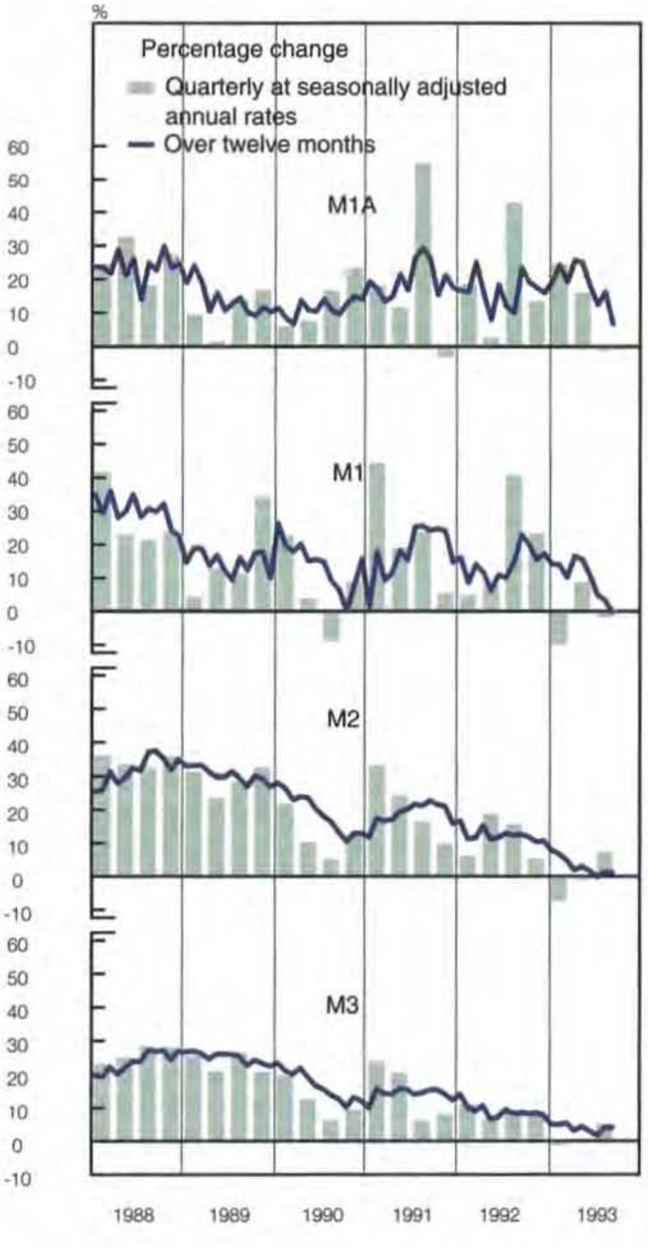
- The improvement in economic activity, led mainly by a substantial increase in agricultural output. Owing to the already very high and rising level of farm debt, this recovery in the income of farmers did not bring about a proportionate increase in the demand for money.
- The notable overfunding of the government deficit, which resulted in a shift in the deposits with banks from the private sector (included in M3) to the government sector (not part of M3).
- The increased flexibility in the use of mortgage facilities of banks and the associated tax advantages of making use of these facilities, which encouraged many depositors to shift funds from current and savings deposits to their mortgage accounts.
- The large margins between lending and deposit rates, which brought about some further disintermediation and therefore led to a rise in the income velocity of M3 and a complementary decline in money supply.
- Regulatory changes to the liquid asset and the cash reserve requirements, which instigated the selling of certain bank assets to the non-bank private sector.

As a result of this low growth in M3, the broadly defined money supply, which had remained well within the *money supply guidelines* of 7-10 per cent during 1992, receded to levels significantly below the lower boundary of the new guidelines of 6-9 per cent for 1993 in the first nine months of this year. The seasonally adjusted value of M3 came to R203,9 billion at the end of September 1993, R2,9 billion or 1,4 per cent below the corresponding lower limit of the money

Guidelines for growth in M3



Monetary aggregates



supply guideline range for 1993. The growth in M3 from the base of the current guideline year (the average value of M3 in the fourth quarter of 1992) amounted to an annual rate of only 4,3 per cent in September 1993.

Despite the low growth in money supply, the Reserve Bank continued to pursue a fairly restrictive monetary policy and did not take active steps to force the growth in money supply back into the guideline range for the year. The Bank adhered to its approach of applying monetary targeting in a discretionary manner and not accepting a rigid and overriding "money rule". Accordingly, the Governor of the Reserve Bank stated recently that after taking the underlying conditions into consideration and because of the priority given to the protection of the foreign reserves of the country, the Bank accepted this low rate of growth in M3.

The growth rate of the *narrower monetary aggregates* also slowed down significantly during the first seven months of 1993. The rate of increase in M2 over periods of twelve months contracted from 10,8 per cent in December 1992 to –0,3 per cent in July 1993, and then rose again somewhat to 1,3 per cent in September. The corresponding growth rate in M1 also decreased from 17,5 per cent at the end of 1992 to 4,1 per cent in July 1993 and further to 3,6 per cent in August; it then became negligibly small in September. The growth rate over twelve months in M1A fluctuated considerably in 1993 but decreased, on balance, from 16,2 per cent in December 1992 to 12,7 per cent in July 1993; it then rose again to 16,5 per cent in August and receded to 6,9 per cent in September. These relatively high rates of increase in M1A could be ascribed to a shift from longer-term deposits to cheque and transmission deposits, reflecting a greater preference for more liquid investments by the private sector against a background of political and economic uncertainty as well as lower opportunity costs associated with these deposits in conditions of declining interest rates.

The main *counterparts* (in a statistical or accounting sense) of the R5,8 billion increase in M3 from the end of December 1992 to the end of September 1993 were increases in these institutions' net claims on the private sector of R12,0 billion and in their "net other assets" of R0,9 billion. This more than counteracted decreases in the monetary sector's net gold and other foreign reserves and net claims on the government sector of R5,7 billion and R1,4 billion, respectively.

Credit extension

The higher real economic growth and concomitant rise in real domestic demand in the first nine months of 1993 were not financed by an increase in real credit extension by the monetary sector. In fact, the increase in *total nominal domestic credit extension* by monetary institutions receded from 10,4 per cent in December 1992 to 6,7 per cent in May 1993 before rising to 9,6 per cent in September.

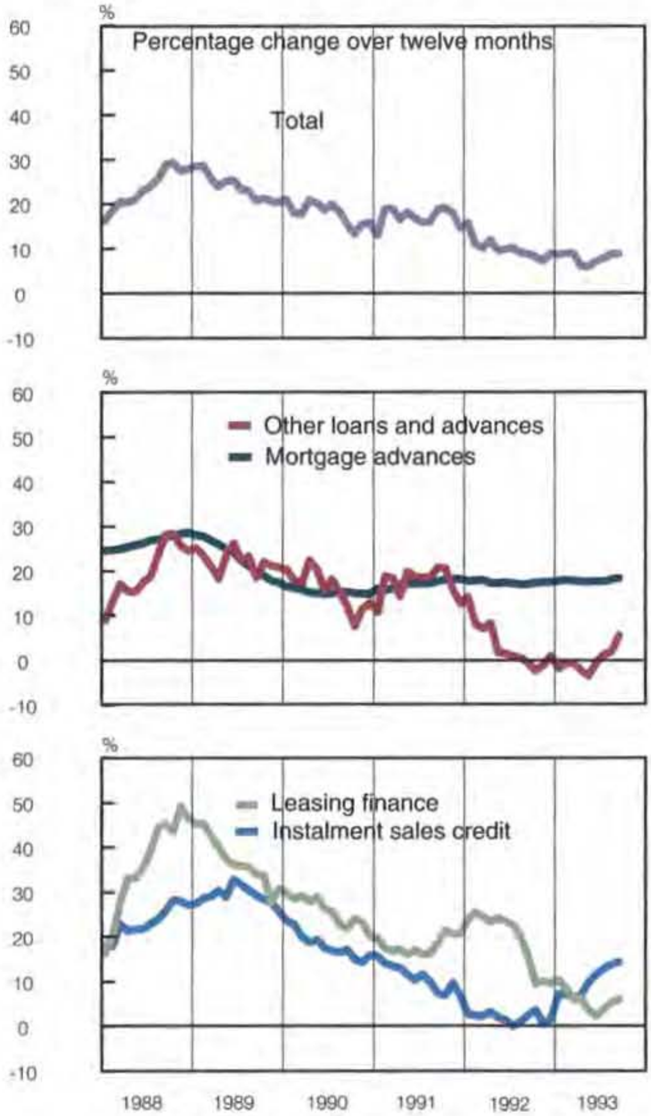
The twelve-month growth rate in *credit extension to the domestic non-bank private sector* by monetary institutions also declined from 8,7 per cent in December 1992 to 5,7 per cent in May 1993 and then accelerated somewhat to 8,6 per cent in September; it therefore remained well below the rate of consumer price inflation. This relatively low growth in claims on the private sector was mainly due to the still low level of economic activity in the country, the relatively high cost of borrowing, regulatory changes and disintermediation practices.

An analysis by *type of credit* of the monetary institutions' claims on the domestic private sector reveals that the low growth in such credit extended during the first nine months of 1993 was mainly due to the relatively low rates of increase in leasing finance and in "other loans and advances" (including overdrafts). The growth rate over twelve months in leasing finance contracted markedly from 9,6 per cent in December 1992 to only 2,2 per cent in June 1993; it then rose again to 6,0 per cent in September. The corresponding growth rate in "other loans and advances" also decreased further from an already low level of 0,9 per cent in December 1992 to negative levels throughout the first six months of 1993, but increased again to a positive 5,4 per cent in September.

In contrast to these developments, the growth rate over twelve months in instalment sales credit increased significantly from only 1,5 per cent in December 1992 to 11,4 per cent in June and even further to 14,3 per cent in September. This sharp acceleration in instalment sales credit was related to pre-emptive purchases in anticipation of an increase in the value-added tax rate, a rise in the purchases of new motor vehicles and an increase in retail sales in the third quarter of 1993.

Owing to the advantages of the flexibility of some mortgage schemes already referred to and the banks' active promotion of this credit facility on account of the lower capital requirements applicable to such advances, the demand for mortgage advances

Credit extension to the private sector



remained buoyant in the first nine months of 1993. The rate of increase over twelve months in mortgage advances namely increased from a relatively high level of 17,3 per cent in December 1992 to 17,5 per cent in June 1993 and to 18,2 per cent in September.

Money market conditions and Reserve Bank operations in the money market

Money market conditions remained relatively tight during the first nine months of 1993, but eased considerably in October. *The average daily level of accommodation* at the discount window increased from R3,2 billion in December 1992 to R5,6 billion in April 1993. Although the level of accommodation then receded to R2,8 billion in July 1993, this did not reflect an easing of money market conditions; the money market shortage simply moved to a lower but still restrictive level under the new system of accommodation provided by the Reserve Bank as from 1 May 1993. In August and September the average daily level of accommodation increased to slightly more than R3 billion, but then contracted to R2,6 billion in October 1993.

The relatively tight money market conditions that prevailed in the first nine months of 1993 were also reflected in the *amount of accommodation at month-ends*, which increased from R3,8 billion at the end of December 1992 to R5,4 billion at the end of April 1993; after the implementation of the new system of accommodation it declined and amounted to R4,2 billion at the end of October 1993.

These tight money market conditions during the first nine months of 1993 were mainly due to a decrease in the net gold and other foreign reserves of the Reserve Bank and a substantial increase in government deposits with the Reserve Bank. These influences were counteracted to some extent by the reduction in the reserve balances of banks with the Reserve Bank from May 1993.

The *actions of the Reserve Bank* in the money market during the first nine months of 1993 were aimed mainly at easing money market conditions. This was achieved by reducing the minimum cash reserve requirement that banks have to comply with, by means of buy-back arrangements and by the transfer of funds from the Exchequer and Paymaster-General Account at the Reserve Bank to the banks as an interim measure in anticipation of the proposed introduction of a system of Tax and Loan Accounts. At the end of September 1993 the government funds placed with the banks amounted to R6,0 billion. Despite these movements of government funds, the government deposits with the Reserve Bank still increased by R1,1 billion in the first nine months of 1993.

In addition to relieving relatively tight money market conditions, the monetary authorities also neutralised short-term fluctuations by adjusting the asset portfolio of the Corporation for Public Deposits. From the end of December 1992 to September 1993 these adjustments also had, on balance, an easing effect of about R2,3 billion on money market conditions.

In a further attempt to solve structural problems of banks heavily involved in security trading and to relieve tight money market conditions somewhat, the Reserve Bank announced a further reduction in the minimum cash reserve requirements of banks on 4 August 1993 and allowed the banks to reduce their liabilities for purposes of calculating their cash reserve requirements by subtracting interbank deposits and certain repurchase agreements. These changes reduced the total minimum cash reserve requirement for all banks by about R1,2 billion, but the effect on the money market shortage was considerably smaller because of the relatively large holdings of vault cash by certain banks, which did not record a proportionate decline.

The easing in money market conditions in October 1993 could mainly be ascribed to a decrease in government deposits with the Reserve Bank, an increase in the net gold and other foreign reserves of the Reserve Bank, and a decrease in banknotes in circulation. During this month the Reserve Bank tightened money market conditions by means of a reverse buy-back agreement of R580 million, and by requesting the Treasury to switch R500 million of the government's deposits with private banks back to the Reserve Bank. However, the Reserve Bank transferred R300 million of these government funds back to the banks towards the end of October.

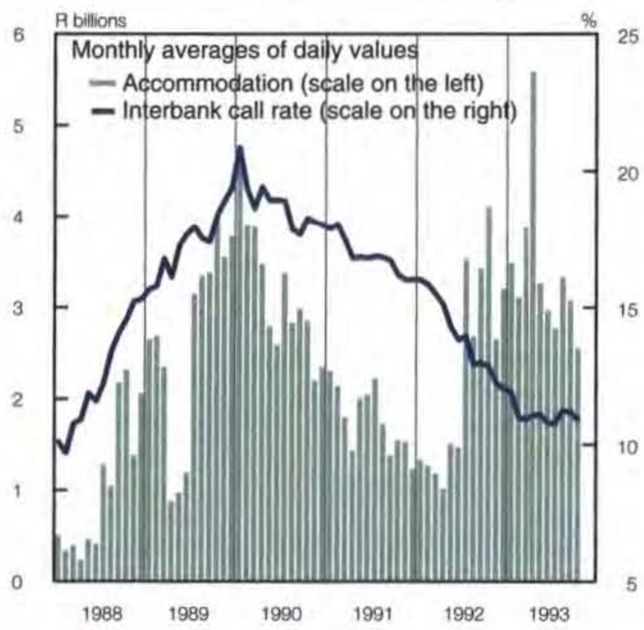
Gross *sales of government stock* by the Reserve Bank amounted to R151 billion in the first ten months of 1993, compared with R95 billion in the corresponding period in 1992 and R112 billion during 1992 as a whole. *Net* sales of government stock by the Reserve Bank amounted to R11,9 billion during the first ten months of 1993; in the corresponding period of 1992 such net sales had come to R13,7 billion. The Reserve Bank's trading of government stock options, which had increased from a monthly average of R2,0 billion in 1991 to R5,2 billion in 1992, remained at this level during the first ten months of 1993.

Money market interest rates

The general downward trend in money market interest rates, which had already started at the beginning of 1990, continued in the first ten months of 1993, but at a considerably slower pace than in 1992. The declining trend in money market rates from the middle of 1992 was based mainly on expected downward adjustments in Bank rate in an environment characterised by a low demand for funds. This is clearly illustrated by the relationship between the *inter-bank call rate* and the level of accommodation at the discount window. As shown in the accompanying graph, changes in the inter-bank call rates have often been correlated positively with changes in the level of accommodation. However, this relationship changed from the second half of 1992, when the level of accommodation began to rise sharply but the monthly average inter-bank call rate decreased further. Under the circumstances the higher level of accommodation at that stage was probably regarded by the banks as only a temporary development, and they still expected Bank rate to be lowered.

The market's perceptions of further imminent decreases in Bank rate changed after Bank rate had been lowered in February 1993 and it became apparent that the net foreign reserves had declined again to uncomfortably low levels. In the subsequent months the inter-bank deposit rate therefore became more stable and fluctuated around 11 per cent. Only after the lowering of Bank rate by one percentage point from 13 to 12 per cent on 28 October 1993 in an environment of easier money market conditions, did

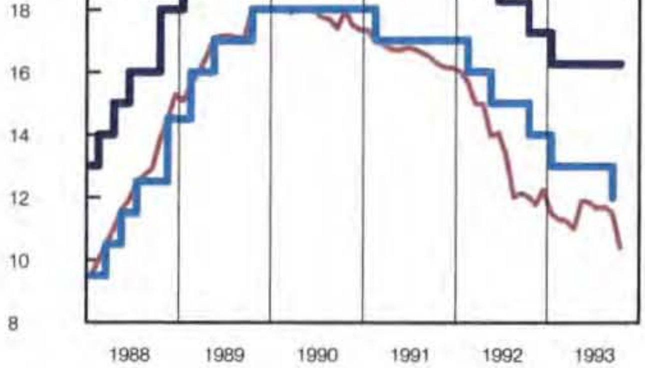
Accommodation and interbank call rate



the inter-bank call rate decline to 9,80 per cent at the end of October.

Most *other money market interest rates* followed a more or less similar course during 1993. The rate on

Short-term interest rates



three-month bankers' acceptances, for instance, rose from 11,80 per cent at the end of February 1993 to 12,30 per cent at the end of April, before receding to 11,50 per cent at the end of September 1993; it then dropped to 10,50 per cent at the end of October. The three-month Treasury bill tender rate decreased from 11,32 per cent at the end of February 1993 to 11,02 per cent at the end of April before rising to 11,90 per cent at the end of May; it then declined to 10,42 per cent at the end of October 1993.

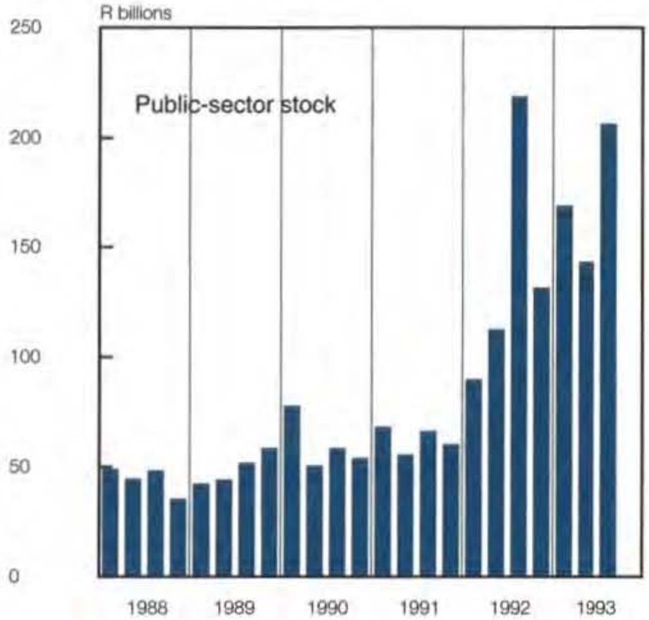
The *prime lending rate* of the banks was reduced (following the reductions in Bank rate) from 17,25 to 16,25 per cent with effective dates ranging from 15 February to 2 March 1993 at the various banks and further to 15,25 per cent from 1 November 1993. The inflation-adjusted or real prime lending rate decreased from 7,0 per cent in December 1992 to 4,7 per cent in April 1993 because of the lowering of the nominal rate and a slight increase in the inflation rate as measured by changes in the consumer price index over this period. The real prime lending rate then increased again to 6,6 per cent in September 1993 when the recorded rate of inflation came down.

Capital market developments

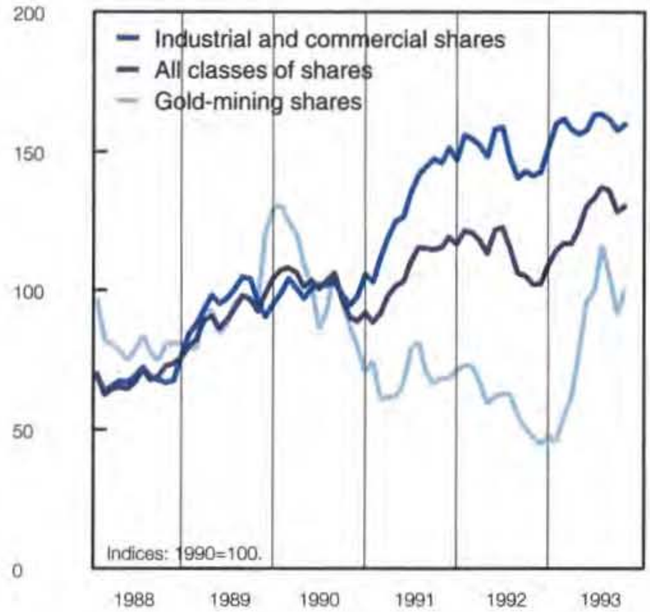
Buoyant activity prevailed in the *secondary capital markets* throughout the first ten months of 1993. The value of *public-sector stock* traded on the Johannesburg Stock Exchange decreased from R168 billion in the first quarter of 1993 to a still high level of R143 billion in the second quarter of 1993, owing to the large number of public holidays during which no trading took place and a firming of yields. The resumed decline in long-term interest rates stemming from sluggish economic growth, lower inflationary expectations and increased net purchases of stock by non-residents, raised the value of public-sector stock traded sharply to R206 billion in the third quarter of 1993. The further decline of the yield on long-term stock in October caused trading activity to increase to an all-time high of R90,6 billion from R85,3 billion in September 1993.

Sharp increases in the value of *shares traded* on the Johannesburg Stock Exchange in the first two quarters of 1993 were followed by a slight further improvement in the third quarter. The higher level of the gold price and the downward movement in short-term interest rates provided considerable support for the share market. The turnover of shares, which had increased from R5,4 billion in the fourth quarter of 1992 to R10,8 billion in the second quarter of 1993, rose further to R11,3 billion in the third quarter. This increase was mainly the result of the sharply higher gold price in the earlier part of the third quarter and the accompanying high volume of gold shares traded, as well as an amendment to the Stock Exchanges Control Act in July 1993 allowing trading in derivative instruments by members of the Johannesburg Stock

Stock exchange transactions



Share prices

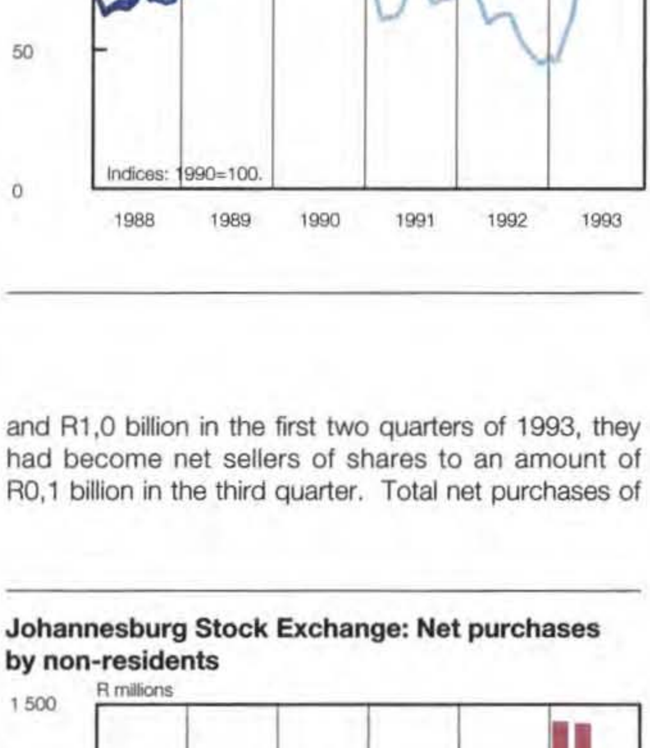


Exchange so that they can hedge their positions in the spot market for equities. The subsequent decline in the gold price contributed to a slight decline in the value of shares traded to R3,6 billion in October from the average monthly value of R3,8 billion in the preceding three months.

Share prices reached a record monthly average peak in July 1993, but then fell back in the following two months before recovering somewhat in October. Following an increase of 34,6 per cent from November 1992 to July 1993, the average monthly price level of all classes of shares declined by 6,7 per cent up to September 1993. The sharp turn-about in the gold price on the world markets in August, weaker international commodity prices in dollar terms related to the sluggish international economic recovery, and uncertainty on the local equity market attributable to worse-than-expected financial results, brought about a sharp decline in the prices of mining shares and industrial and commercial shares. However, the improvement in the gold price towards the end of October 1993 and a renewed interest in gold and industrial shares, led to a small increase of 1,5 per cent in the average monthly price level of all classes of shares.

Non-residents' net purchases of public-sector stock amounted to R1,2 billion in the first nine months of 1993, of which approximately 50 per cent took place in the third quarter of the year. Although non-residents were also net purchasers of shares amounting to R1,2 and R1,0 billion in the first two quarters of 1993, they had become net sellers of shares to an amount of R0,1 billion in the third quarter. Total net purchases of

Johannesburg Stock Exchange: Net purchases by non-residents



securities by non-residents consequently declined from R1,4 billion in both the first and second quarter of 1993 to only R0,5 billion in the third quarter. The call for the lifting of the remaining sanctions against South Africa caused a renewed interest in stocks and shares by non-residents in October. Non-residents' net purchases of securities in this month rose accordingly to R0,5 billion, compared with an average monthly value of R0,2 billion in the preceding three months.

In the *primary capital markets* net new borrowing by the *public sector* through issues of fixed-interest securities fell back sharply to R4,7 billion in the third quarter of 1993 after R11,3 billion of the estimated public-sector borrowing requirement had been raised in the first fiscal quarter. This brought the net new issues of public-sector stock to R16,0 billion in the first half of the fiscal year, against R8,7 billion in the corresponding period of the previous fiscal year.

No new issues of *fixed-interest securities* (including convertible preference shares, debentures and corporate bonds) by listed private-sector companies were made in the third quarter of 1993. However, the value of rights issues of ordinary shares by listed companies increased from R0,3 billion in the second quarter of 1993 to R2,0 billion in the third quarter. Companies raised equity funds through rights issues mainly to reduce debt and in certain cases to facilitate unbundling. The relatively high share prices and strong demand for good quality scrip made share capital issues attractive to both issuers and investors.

In the *mortgage market* the promotion of flexible bond facilities gave rise to an average monthly amount of mortgages paid out by banks of R3,2 billion in the first nine months of 1993. Lack of demand for credit induced banks to offer various incentives to attract home loan applications. These incentives and fierce competition in the home loan market affected profitability of mortgage advances adversely. In September certain banks therefore announced that they would no longer carry bond registration costs and valuation fees.

The value of *real estate transactions* recovered slightly from a low of R5,6 billion in the second quarter of 1993 to R5,9 billion in the third quarter. The real estate market was none the less characterised by an oversupply of commercial property and a relatively stagnant housing market.

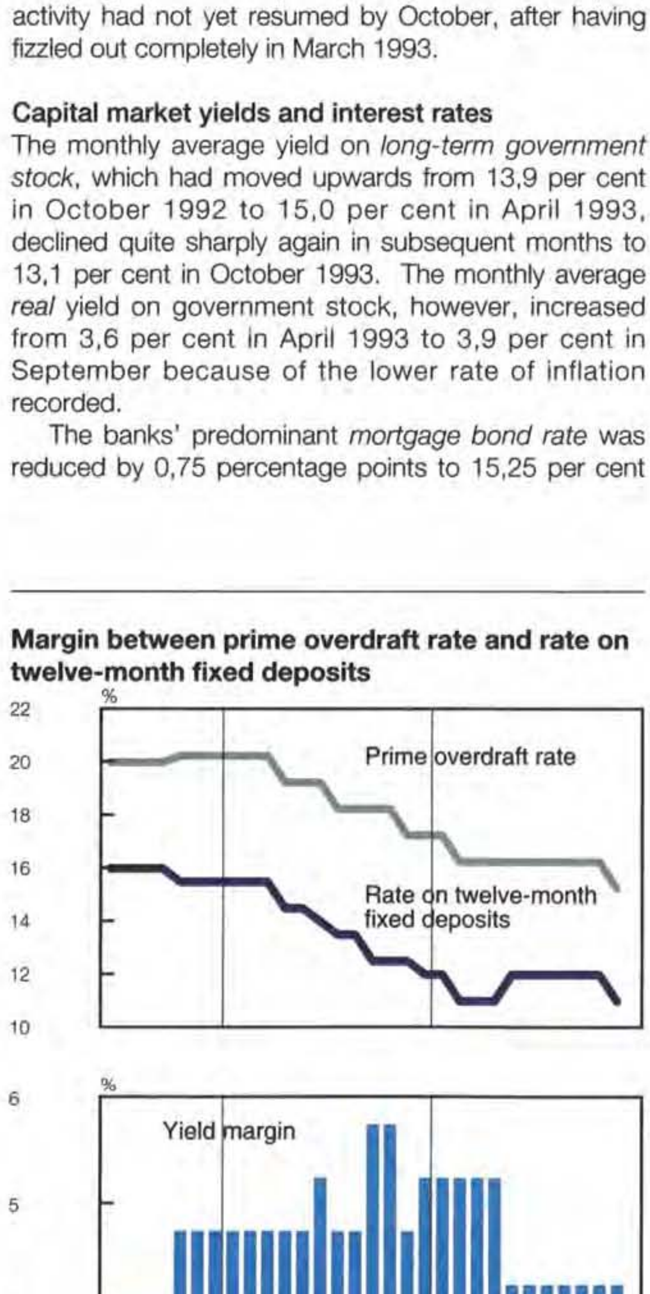
Activity in the *derivative market* increased considerably in the first three quarters of 1993. Trade in share indices, representing overwhelmingly the largest part of the value of futures contracts, was affected favourably by the volatile gold price, reduced trading fees on the South African Futures Exchange and increased uncertainty about the future direction of share prices. The underlying value of transactions in futures contracts rose to a quarterly average of R22,1 billion in the first nine months of 1993, compared with R11,8 billion in the corresponding period of 1992. The high average monthly transactions in futures contracts of R8,3 billion in the third quarter of 1993 then contracted moderately to R6,9 billion in October. The value of trade in options on index futures contracts increased from a monthly average of R103 million and R305 million in the first two quarters of 1993 to R343 million in the third quarter. In October the value of trade in options on index futures declined to R206 million. Although the Johannesburg Stock Exchange's Traded Options Market remained open, activity had not yet resumed by October, after having fizzled out completely in March 1993.

Capital market yields and interest rates

The monthly average yield on *long-term government stock*, which had moved upwards from 13,9 per cent in October 1992 to 15,0 per cent in April 1993, declined quite sharply again in subsequent months to 13,1 per cent in October 1993. The monthly average *real* yield on government stock, however, increased from 3,6 per cent in April 1993 to 3,9 per cent in September because of the lower rate of inflation recorded.

The banks' predominant *mortgage bond rate* was reduced by 0,75 percentage points to 15,25 per cent

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

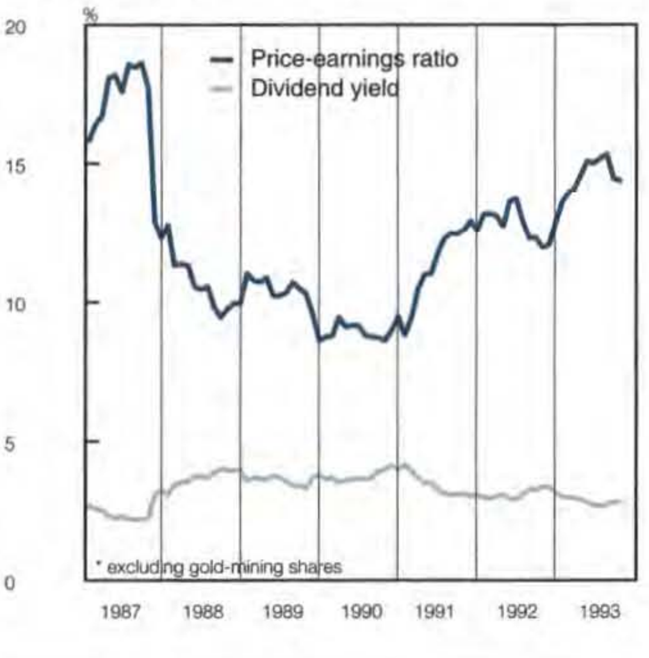


from 1 November 1993, following the reduction in Bank rate on 28 October 1993. The mortgage bond rate has therefore now been lowered by 1,5 percentage points since the beginning of 1993 and by 4,75 percentage points since the beginning of 1992.

The *twelve-month deposit rate* was lowered from 15,5 per cent at the beginning of 1992 to 12,0 per cent in December and further to 11,0 per cent in February 1993. Without an accompanying increase in the mortgage bond rate, some banks increased the twelve-month deposit rate again to 12,0 per cent in April, while others followed suit towards the middle of May. The twelve-month deposit rate was again lowered to 11,0 per cent in November 1993. In view of the fact that the prime overdraft rate of clearing banks declined to the same extent in November, the margin between the twelve-month deposit rate and the predominant prime overdraft rate of banks remained at 4,25 percentage points.

The significant decline in the average level of share prices from August to October 1993 resulted in a firming of the *dividend yield* from 2,75 per cent in July to 2,95 per cent in October. Reflecting a weakening of financial results of listed companies, the *earnings yield* on shares (excluding gold-mining shares) decreased slightly in August 1993 before firming to 6,95 per cent in October. Although the *price-earnings ratio* of non-gold-mining shares decreased slightly to 14,4 in October 1993, it was still indicative of a high level of share prices when compared with its all-time high of 18,6 in September 1987.

Yield and ratio on company shares*



Most of the *officially determined longer-term interest rates* were decreased during the first ten months of 1993. The standard and the prescribed interest rate were only lowered more recently. The standard interest rate applicable to loans by the State out of the State Revenue Fund (Exchequer Act, Act No. 66 of 1975) was reduced from 15,5 to 15,0 per cent on 1 July 1993, to 14,75 per cent on 1 August 1993, and to 13,5 per cent on 1 November 1993. After having remained unchanged since 1 July 1989, the prescribed rate of interest for the payment of interest on certain judgement debts, was lowered by 3 percentage points to 15,5 per cent with effect from 1 October 1993.

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 public enterprises) amounted to R5,8 billion (6,1 per cent of gross domestic product) in the second quarter of fiscal 1993/94. In the corresponding quarter of fiscal 1992/93 the public sector had a borrowing requirement of R10,3 billion. The second-quarter deficit brought the borrowing requirement in the first half of fiscal 1993/94 to R13,3 billion (7,3 per cent of gross domestic product); this was substantially less than the public-sector borrowing requirement of R16,7 billion, or 10,3 per cent of gross domestic product, in the first half of fiscal 1992/93.

This improvement in the public-sector borrowing requirement was partly due to an increase in the surplus on the accounts of the *non-financial public enterprises:* the small surplus of R0,1 billion in the first half of fiscal 1992/93 rose to R0,4 billion in the first half of fiscal 1993/94 owing to cutbacks in costs and other rationalisation programmes of these enterprises. More importantly, however, the borrowing requirement of *general government* contracted from R16,8 billion to R13,7 billion over the same period. As a ratio of gross domestic product, the borrowing requirement of general government of 7,5 per cent in the first half of fiscal 1993/94 was also substantially lower than the 10,4 per cent in the corresponding period of the preceding year.

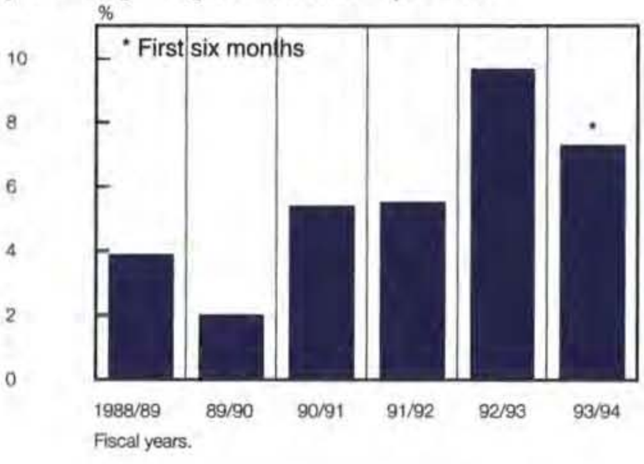
A substantial reduction in transfers was, in turn, responsible for the lower borrowing requirement of the general government in the first half of fiscal 1993/94; in the corresponding period of the preceding year, large extraordinary transfers of R3,8 billion to the Gold and Foreign Exchange Contingency Reserve Account and of R2,0 billion to the civil service pension funds had been made. If these two transfers are not taken into account, the borrowing requirement of the general government in the first half of fiscal 1993/94 would be 23,9 per cent higher than in the first half of fiscal 1992/93.

The further rise was recorded in the borrowing requirement of general government (excluding large extraordinary transfers), despite a sharp increase in the current income of general government. The more favourable developments in government revenue, however, were neutralised by a continued sharp increase in expenditure on goods and services and particularly by a substantial rise in interest payments on government debt. Interest paid on public debt rose from R8,8 billion in the first half of fiscal 1992/93 to R11,2 billion in the first half of fiscal 1993/94, or by no less than 27,3 per cent.

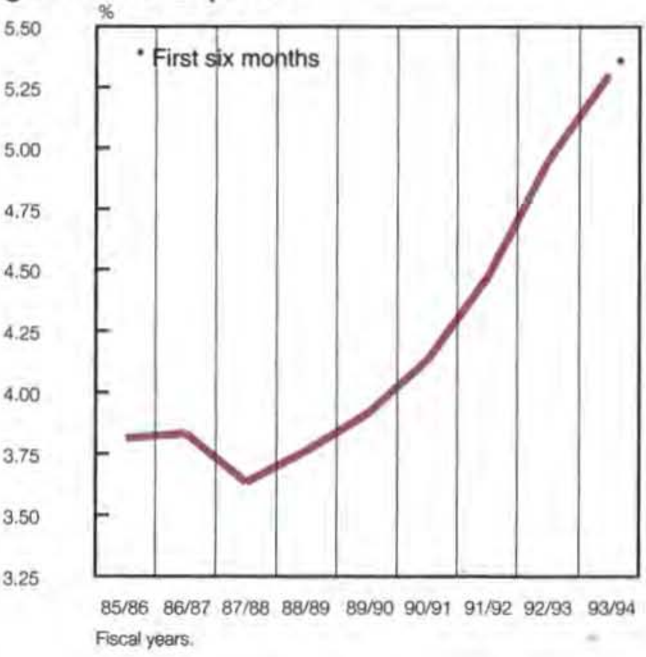
Exchequer account

The increase in interest payments was responsible for an acceleration in the year-on-year rate of increase in *Exchequer issues* to government departments (after the usual adjustment for changes in the balance on the Paymaster-General Account) from 12,7 per cent in the first quarter of fiscal 1993/94 to 17,1 per cent in the second quarter. Measured over a period of twelve

Public-sector borrowing requirement as percentage of gross domestic product



Interest on government debt as percentage of gross domestic product



months, the rate of increase in Exchequer issues in the first half of fiscal 1993/94 came to 15,0 per cent, which was well in excess of the budgetary provision of 8,8 per cent for the year as a whole.

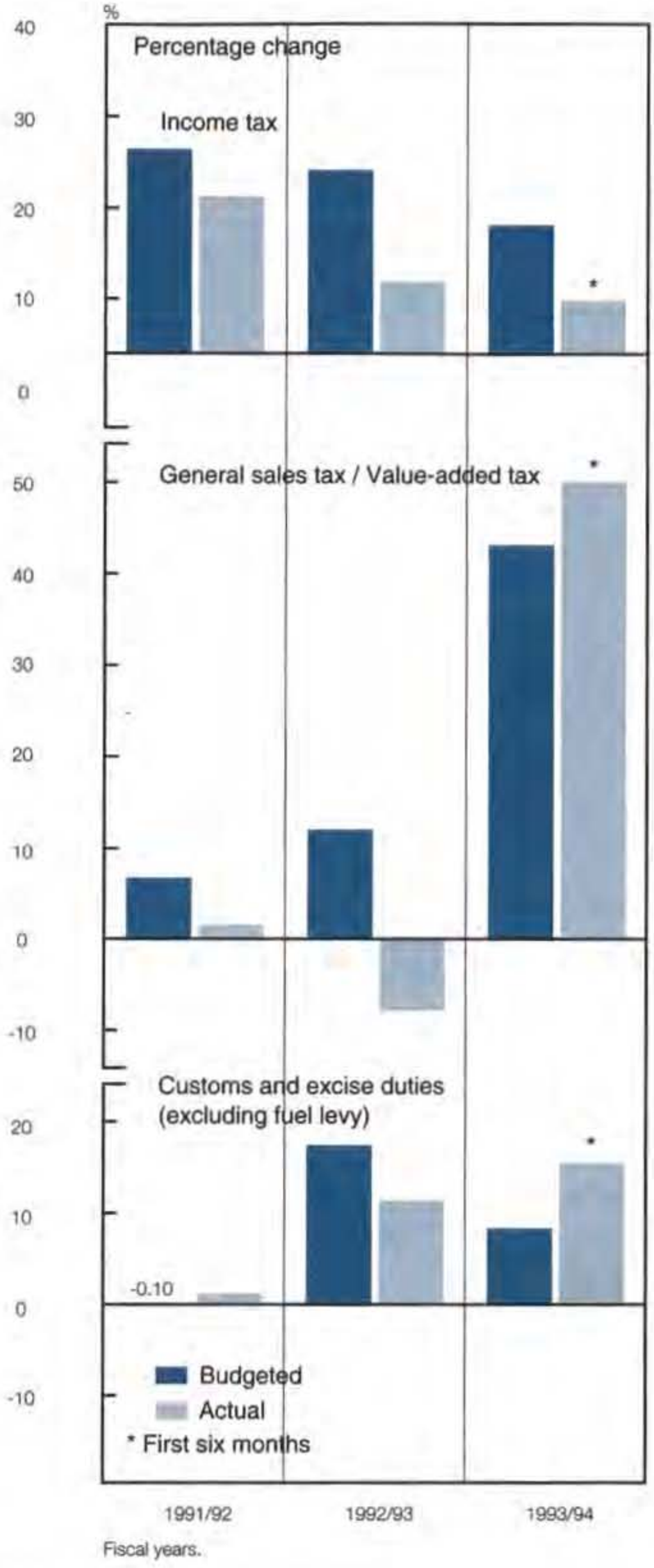
This year-on-year rate of increase in Exchequer issues to government departments during the first half of fiscal 1993/94 nevertheless was below the average year-on-year rate of increase of 16,9 per cent in the corresponding period of the preceding five fiscal years. As a ratio of gross domestic product, Exchequer issues to government departments in the first half of fiscal 1993/94 amounted to 31,5 per cent, compared with an average of 28,3 per cent in the first half of the preceding five fiscal years. If Exchequer issues in October 1993 are also taken into consideration, the year-on-year rate of increase for the first seven months of fiscal 1993/94 came to 12,8 per cent.

The year-on-year rate of increase in *Exchequer receipts* (excluding proceeds from privatisation) increased from 13,0 per cent in the first quarter of fiscal 1993/94 to 17,1 per cent in the second quarter. This brought the increase in the first half of the year to 15,3 per cent above the level in the first half of fiscal 1992/93; in the Budget an increase of 17,3 per cent had been envisaged for the year as a whole. The rate of increase in the first half of fiscal 1993/94 can also be compared with an average year-on-year rate of increase of 15,9 per cent for the corresponding period in the preceding five fiscal years.

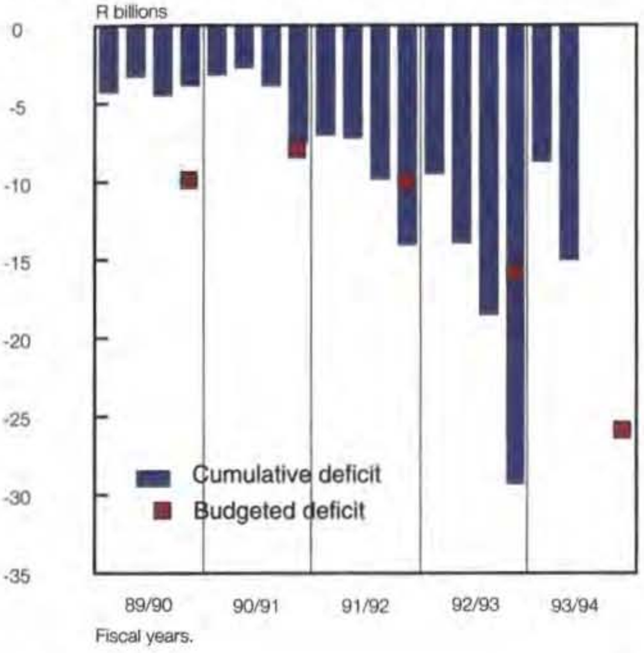
If Exchequer receipts in October are also taken into consideration, the year-on-year rate of increase in the first seven months of fiscal 1993/94 amounted to 16,2 per cent. The less favourable performance of Exchequer receipts was entirely due to the low rate of increase in income tax receipts: in the first six months of fiscal 1993/94 these receipts were only 4,9 per cent above their level in the corresponding period of the preceding year, whereas an increase of 11,6 per cent had been budgeted for the year as a whole. In particular, income tax receipts from companies declined in the first six months of fiscal 1993/94 compared with the first six months of fiscal 1992/93, as opposed to a small increase provided for in the Budget. This disappointing behaviour of income tax receipts from companies was probably related to the lower profits under generally depressed economic circumstances and the lag in the collection of the newly introduced tax on distributed profits. The income tax proceeds from individuals in the first six months were also lower than envisaged in the Budget, probably because of lower-than-expected salary and wage increases and continued labour retrenchments.

The year-on-year growth rates of nearly all the other main categories of government revenue in the first six months of fiscal 1993/94 performed better than the budgeted growth projected for the year as a whole. Large increases were recorded particularly in receipts from customs duties and from the surcharge on imports owing to a sharp rise in the value of merchandise imports, following the devaluation of the rand against most of the major currencies. Excise

Budgeted and actual revenue



Deficit before borrowing



duties also performed better than expected, largely as a result of the higher-than-expected value and volume of motorcar sales. After a relatively poor performance in the first quarter of the fiscal year, the receipts from value-added tax rose sharply in the second quarter; a year-on-year rate of increase of 50,1 per cent was recorded in the first half of fiscal 1993/94, compared with a rate of increase of 43,1 per cent budgeted for the year as a whole.

Financing of the Exchequer deficit in the first six months of fiscal 1993/94 according to type of sector

	R millions
Public Investment Commissioners	7 508
Non-monetary private sector	13 655
Monetary institutions	–3 542
Corporation for Public Deposits	–784
Other monetary institutions	–2 758
Foreign sector	–207
Total gross financing	17 414
Less: Discount on new issues of government stock	2 366
Total net financing	**15 048**

The *deficit on the Exchequer Account* before borrowing and debt repayment for the first half of 1993/94 added up to R15 048 million, or to 58 per cent of the deficit budgeted for the year as a whole. As a ratio of gross domestic product, the Exchequer deficit before borrowing amounted to 8,2 per cent, i.e. exactly equal to the ratio in the corresponding period of the preceding year and higher than the projected ratio of 7,0 per cent for the year as a whole.

This deficit of R15 048 million plus the discount on new issues of government stock of R2 366 million were *financed* entirely by means of funds obtained from the Public Investment Commissioners and the non-monetary private sector. As shown in the accompanying table, large net repayments were made on the government debt due to monetary institutions and the foreign sector during the first six months of fiscal 1993/94.

The following *borrowing instruments* were utilised to finance the Exchequer deficit of R16 063 million for the first seven months of fiscal 1993/94:

	R millions
Government stock (including discount)	26 811
Treasury bills	–206
Foreign loans	–120
Non-marketable securities	–127
Increase in available cash balances	–7 867
Total financing	18 491
Less: Discount on new government stock	2 428
Total net financing	**16 063**

The deficit on the Exchequer Account before borrowing and debt repayment, plus the discount on new government stock and some overfunding, led to an increase in government debt from R154,7 billion at the end of fiscal 1992/93 to R181,0 billion at the end of October 1993. As a ratio of gross domestic product, government debt now is approximately 51 per cent.