Quarterly Bulletin

September 2003

South African Reserve Bank

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Quarterly Economic Review

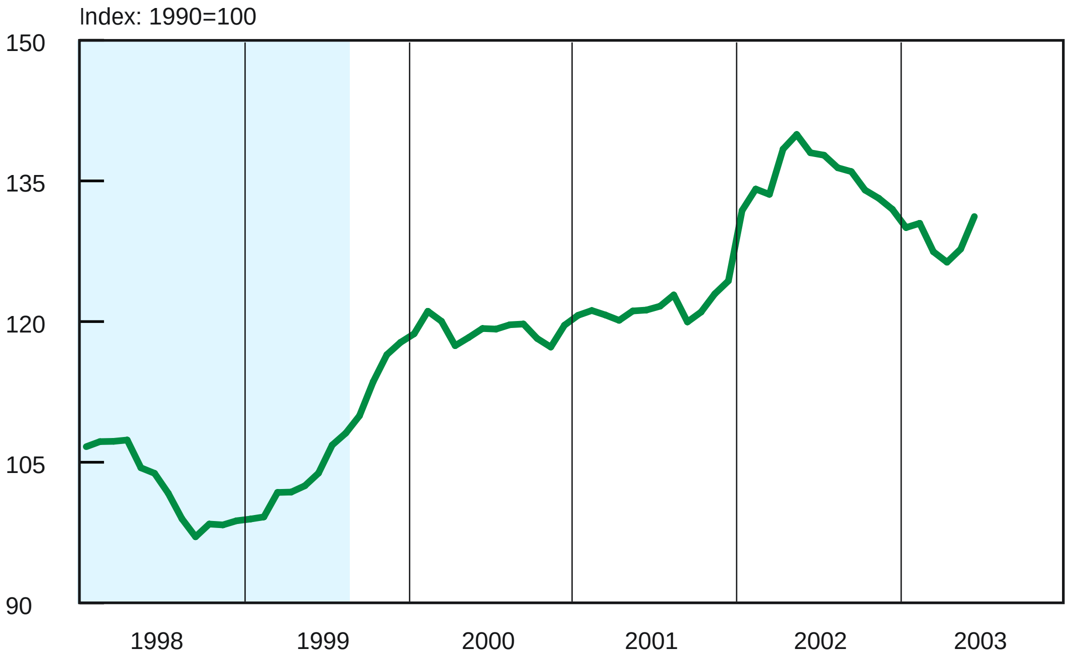
Introduction

While economic activity remained lacklustre in many parts of the world, early signs of a more buoyant performance in the United States of America were confirmed by data on real growth for the second quarter of 2003. The United States economy, which is considered by many as the growth engine of the world, expanded at an annualised rate of more than 3 per cent. With firmer economic growth, a rising budget deficit and an accommodative monetary policy stance, bond yields in the United States rose quite significantly in recent months from their earlier very low levels. While in Japan economic activity also appeared to start picking up, the major economies in Europe remained in the doldrums.

In South Africa the composite leading indicator of economic activity of the Reserve Bank, having trended downward over the 11 months to April 2003, picked up strongly in May and June as rising share prices, a higher rand price of gold, increases in the net gold and other foreign exchange reserves, lower short-term interest rates and favourable developments in other leading variables suggested an imminent turnaround for the better.

Promising as these developments may be, domestic economic growth was still decelerating up to the second quarter of 2003 as weakness in the world economy was reflected in sluggish demand for South African exports. Growth in South Africa's *real gross domestic product* receded from its recent peak rate of 4 per cent, reached in the second quarter of 2002, to only 1½ per cent in the first quarter and 1 per cent in the second quarter of 2003. Agricultural output contracted sharply in the second

Composite leading business cycle indicator



Shaded area: Downward phase of business cycle quarter on account of lower production of field crops. The real value added by manufacturing also fell back in the second quarter, while output growth in most other sectors of the economy remained positive but slowed down. There were clear signs of surplus capacity in the economy, with capacity utilisation in manufacturing for instance receding to 79 per cent in the second quarter of 2003, against a post-1994 average level of 80½ per cent.

While growth in real production slowed down, the already brisk growth in gross domestic expenditure picked up further in the second quarter of 2003 to reach an annualised rate of 5½ per cent. Inventory accumulation accelerated noticeably, offsetting a slower rate of increase in real fixed capital formation. In mining and manufacturing it seems likely that the inventory investment was partly involuntary and resulted from a quicker than anticipated reduction in sales, including export sales. Growth in real fixed capital formation by public corporations decelerated markedly during the second quarter of 2003, while that by general government and by the private sector gained further momentum. In the private sector the platinum mines recorded impressive fixed capital formation growth, with the agricultural sector at the other extreme reducing its fixed capital formation against the background of lower real output and prices of agricultural products.

Real consumption by households maintained its earlier growth momentum in the second quarter of 2003, supported by slightly stronger increases in households' real disposable income and consumers' willingness to raise their debt levels somewhat. Real consumption expenditure by government also continued to increase briskly. With all the main components of real domestic expenditure rising healthily, weak net exports to the rest of the world stood central in the explanation of the slowdown in domestic economic growth.

Reflecting the fragile world economy, South African export volumes remained subdued during the second half of 2002 and first half of 2003. By contrast, import volumes rose somewhat against the background of firm real domestic expenditure, and rising capital formation in particular. The current account of the balance of payments moved into deficit in the first quarter of 2003. Furthermore, the deficit rose from 0,6 per cent of gross domestic product in the first quarter to 1,4 per cent in the second quarter.

At this well-contained level, the current-account deficit in the second quarter was more than fully financed by inflows of foreign capital. The inflows were concentrated in portfolio investment. The National Treasury issued a new bond to the amount of €1,25 billion in the international market, while non-residents became net buyers of both domestic shares and bonds during the quarter.

Under these circumstances South Africa's international reserves rose significantly in the first half of 2003. The level of the country's gross reserves increased from 17½ weeks' worth of imports at the end of March 2003 to 20 weeks' worth at the end of June. The net open foreign-currency position of the Reserve Bank has also been maintained in overbought territory since mid-May 2003.

The nominal effective exchange rate of the rand recovered by 7½ per cent during the first quarter of 2003 and by a further 7½ per cent during the ensuing five months to the end of August. While curbing the international price competitiveness of South African exporters and import-competing industries, it helped to rein in inflation.

Led by reductions in the rand prices of imported goods, overall production price inflation receded from twelve-month rates in excess of 10 per cent in 2002 to rates as low as 1,2 per cent in May and 1,5 per cent in July 2003. Consumer price inflation also declined markedly; for instance, twelve-month CPIX inflation receded, on balance, from 11,3 per cent in November 2002 to 6,6 per cent in July 2003, while seasonally adjusted and annualised CPIX inflation in the second quarter of 2003 amounted to only 2,4 per cent.

The rate of increase in the monetary aggregates slowed down notably on account of the reduction in inflation and real domestic production growth from around the second half of 2002. The narrow M1A and M1 aggregates contracted in the first seven months of 2003 as depositors were attracted to somewhat longer-term deposits, probably attempting to protect their interest income at a time of strong expectations of imminent interest-rate reductions. While M3 continued to grow, its twelve-month rate of increase stayed below 10 per cent in the first seven months of 2003, contrasted to double-digit rates of increase throughout 2002.

Growth in the monetary sector's loans and advances to the domestic private sector decelerated markedly during the course of 2002 and reached twelve-month rates of increase of less than 10 per cent in late 2002 and early 2003. However, it picked up again from April 2003 and by July stood at 13,0 per cent, underpinned by firm demand for credit by businesses engaged in capital formation and by households contemplating buying real estate or consumer items.

The Reserve Bank continued to decrease its use of foreign currency swaps with deposits in its management of the domestic money market. Private-sector banks' liquidity requirement fluctuated around R11 billion during the first eight months of 2003.

Significantly improved prospects for inflation motivated the Reserve Bank's Monetary Policy Committee (MPC) to lower the repurchase rate by 150 basis points at its June 2003 meeting. At the same time it was announced that the frequency of scheduled meetings of the committee would be increased from quarterly to once every two months. In August the MPC decided to reduce the repurchase rate by a further 100 basis points to 11 per cent per annum, again prompted by encouraging prospects for lower inflation. Other money-market interest rates moved broadly in step with the repurchase rate, although the fact that some market participants may have looked for a somewhat larger cut in August might have contributed to limited increases in rates on some forward-looking money-market instruments. At a special meeting of the MPC held on 10 September it was decided to lower the repurchase rate by a further 100 basis points. This was informed by an assessment of the most recently available data and forecasts.

In the key international markets, long-term bond yields started decisively moving upward from June 2003, discounting prospects for stronger growth. In South Africa a slight increase in yields on long-term bonds was recorded, while simultaneously the June and August reductions in the Reserve Bank's repurchase rate were reflected in downward movements of yields on short-dated bonds. Accordingly, the yield curve flattened somewhat. The shape and level of the yield curve, as well as the trend in breakeven inflation (the difference between nominal and index-linked bond yields), indicate some success in the reduction of the public's inflation expectations.

Whereas non-residents were net sellers of South African bonds and shares during the first three months of 2003, favourable ratings by international ratings agencies contributed to a reversal in the second quarter when they turned into net purchasers. However, foreign investors subsequently again reduced their holdings of both bonds and shares in July and August 2003. Nevertheless, share prices on the JSE Securities Exchange SA have trended upward since April 2003 despite the further recovery in the exchange rate of the rand, supported by demand from value-seeking investors.

Residential property prices rose fairly steadily during 2002 and gained further momentum from early in 2003. Purchases, first in anticipation of and then in response to lower interest rates, supported the buoyancy in the property market.

Sluggish tax revenue in the period April to July 2003 was consistent with the lower real economic growth rate and reduced inflation. Together with budgeted higher real government expenditure, it was set to contribute to a smoother performance of the economy. With both fiscal and monetary policy operating within sound medium-term frameworks, the prospects for achieving more vibrant, sustainable growth and development have been enhanced – a valuable contribution to the goal of halving unemployment by 2014 which was adopted by government, the business sector, labour and organised community at the Growth and Development Summit in June 2003.

Domestic economic developments

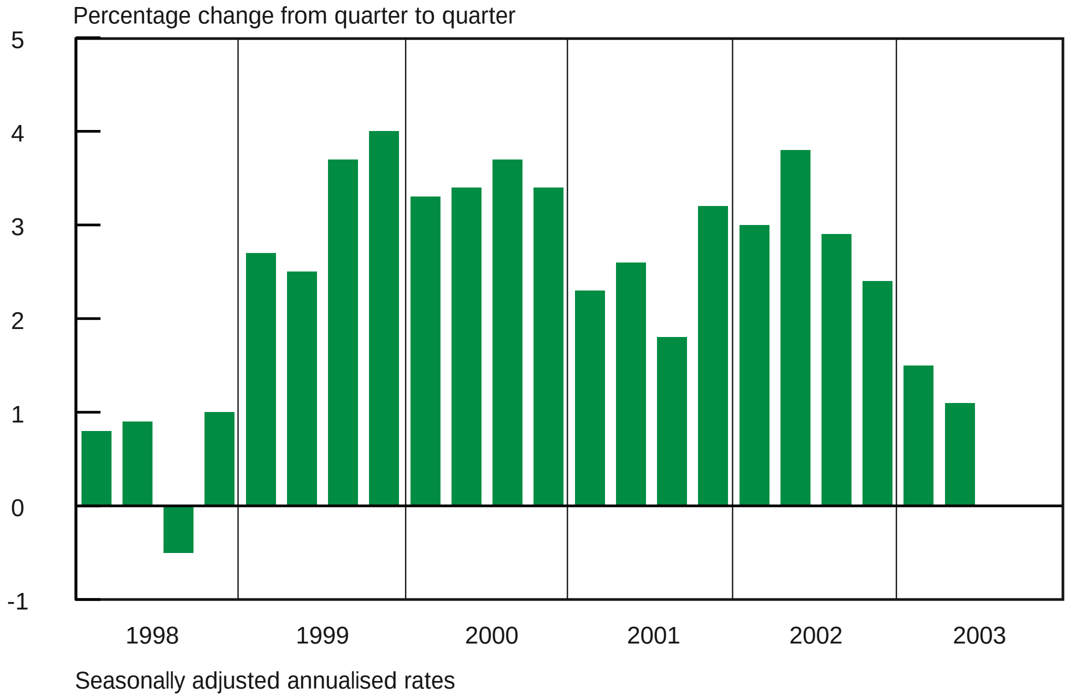
Domestic output[1]

Growth in South Africa's *real gross domestic product* slowed down from an annualised rate of 1½ per cent in the first quarter of 2003 to 1 per cent in the second quarter. This slowdown is consistent with the relatively subdued growth in the international economy in the first half of 2003. The supply side of the economy – especially the export-oriented divisions of the manufacturing sector – was adversely affected by lower demand in the country's major trading partners. This has been exacerbated by the sustained recovery in the exchange value of the rand since 2002. However, the South African economy's growth performance was supported by domestic demand which remained comparatively firm in the second quarter of 2003.

1 The growth rates referred to in this section are based on seasonally adjusted data.

The slowdown in real economic growth in the second quarter of 2003 was widespread. In the primary sector the pace of decline in real value added worsened, while in the secondary sector real value added remained broadly unchanged in the second quarter after still having increased somewhat in the first quarter. In addition, the real output growth of the tertiary sector slowed down further from the first to the second quarter of 2003. Measured over one year, total real gross domestic product in the first half of 2003 increased at a rate of 2 per cent, well below the 3 per cent growth recorded in 2002 as a whole.

Real gross domestic product



Following a decline of 2 per cent in the first quarter of 2003, the real value added by the *primary sector* contracted further at an annualised rate of 3 per cent in the second quarter. This was mainly due to a decline in the real output of the agricultural sector which more than offset the positive growth rate posted in the mining sector.

Adverse weather conditions in the 2002/03 planting season resulted in a comparatively smaller harvest of most field crops. In the case of the maize crop, this happened in spite of a relatively large area planted; at the time of planting, the price of maize was attractively high. The real value added by the *agricultural sector* declined further at an annualised rate of 8½ per cent in the second quarter of 2003 as a consequence of the unfavourable weather.

Maize crop estimates

Season	Area planted (million hectares)	Crop size (million tonnes)
2001/02	3,533	10,049
2002/03	3,567	9,405

Source: Crop Estimates Committee, 20 August 2003

The real output of the *mining sector* increased in the second quarter of 2003. Following a decline of ½ a per cent in the first quarter of 2003, growth in the real value added by the mining sector rose at an annualised rate of 2 per cent in the second quarter. This can be attributed to solid growth recorded by the diamond and platinum-mining sectors, which more than neutralised declines in output volumes of the gold and coal mines. The increase in the real output of diamond mining was underpinned by strong demand for unpolished diamonds to replenish stock levels, as consumer preferences in the overseas market shifted towards diamond jewellery. The popularity of platinum jewellery, together with consistent demand by the automotive industry for the manufacture of catalytic converters, boosted the real output of the platinum-mining sector.

Following an increase at an annualised rate of ½ a per cent in the first quarter of 2003, the real value added by the *secondary sector* stagnated in the second quarter. This was on account of a contraction in real manufacturing output which was reinforced by sharply lower growth in the real output of the construction sector. Measured over one year, growth in the real value added by the secondary sector amounted to 1½ per cent in the second quarter, compared with the 3½ per cent growth rate in the 2001 and 2002 calender years.

Real gross domestic product
Percentage change at seasonally adjusted annualised rates

	2002					2003	
Sectors	1st qr	2nd qr	3rd qr	4th qr	Year	1st qr	2nd qr
Primary sectors	3½	4½	2½	0	1½	-2	-3
Agriculture	7½	9	5	½	4	-3	-8½
Mining	½	1½	1	0	-½	-½	2
Secondary sectors	3½	5	3	2	3½	½	0
Manufacturing	4	6	3½	1½	4	-½	-1
Tertiary sectors	2½	3½	3	3	3	2½	2
Non-agricultural sectors	2½	3½	3	2½	3	1½	1½
Total	3	4	3	2½	3	1½	1

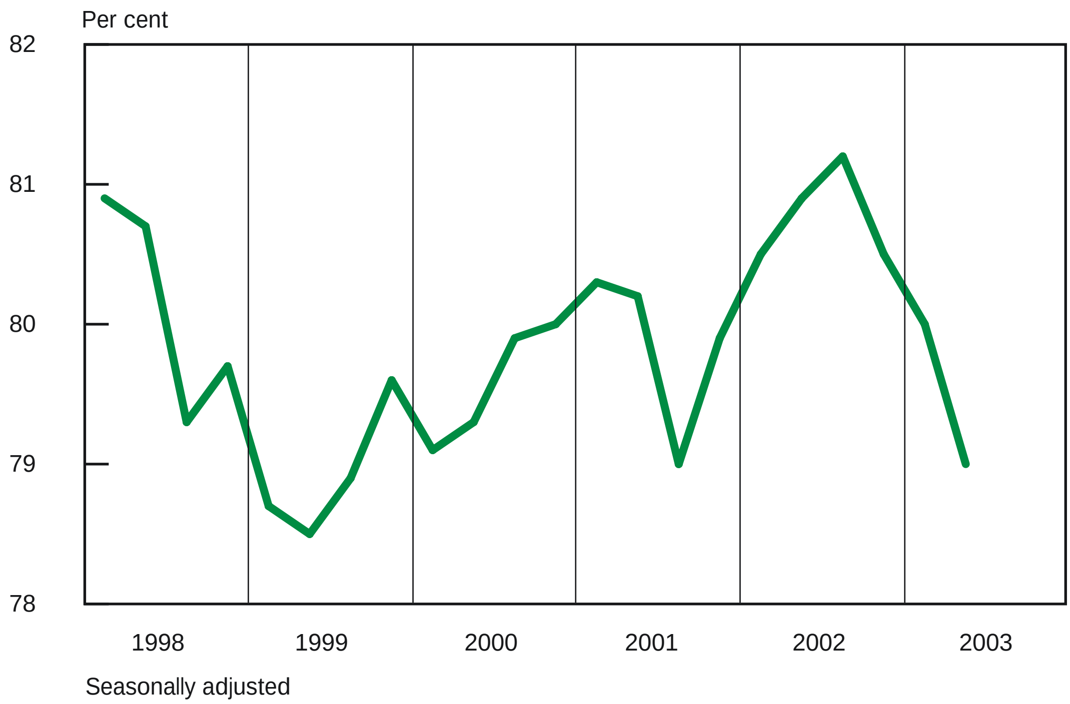
The real output of the *manufacturing sector* contracted for the second successive quarter. Following a decline of ½ a per cent in the first quarter of 2003, growth further slid to an annualised rate of contraction of 1 per cent in the second quarter. The contraction was evident in lower production volumes of almost all subsectors of the manufacturing sector. It was particularly pronounced in the export-oriented subsectors and in sectors that are vulnerable to import competition like clothing and textile products, wood and wood products, electrical machinery and apparatus as well as in radio, television and computer equipment.

The contraction in the aggregate real value added by the manufacturing sector can be attributed to, among other things:

- weaker global demand which translated into lower export volumes;
- the recovery in the exchange value of the rand which, in addition to reducing the competitiveness of South African exports, also compressed output in import-competing industries; and
- the inhibiting impact of slower real income growth and relatively high real interest rates on general business conditions.

Under these circumstances, the number of new orders for manufactured products tapered off. Capacity utilisation in manufacturing also receded to only 79 per cent in May 2003, down from 80 per cent in February and a recent high point of 81,2 per cent in August 2002.

Utilisation of manufacturing production capacity



The real value added by the *electricity, gas and water sector* increased at an annualised rate of 1½ per cent in each of the first two quarters of 2003. This can mainly be attributed to an increase in the real output of the electricity subsector on account of an increase in export demand from neighbouring countries and lower imports.

Growth in the real value added by the *construction sector* slowed down from an annualised rate of 3½ per cent in the first quarter of 2003 to 2 per cent in the second quarter. It appears as if the rising interest rates in 2002 adversely affected activity in the construction sector. Notwithstanding the declining inflation trend, increases in the building cost of new houses remain quite high, making building relatively less attractive than purchasing an existing house. As a result, growth in the demand for new residential buildings tapered off in the second quarter.

In the *tertiary sector*, growth in the real value added still held firm but at a slower rate than in the first quarter. Following an increase at an annualised rate of 2½ per cent in the first quarter of 2003, growth edged lower to 2 per cent in the second quarter. This can mainly be attributed to slower growth in the transport, storage and communication sector which outweighed the marginally better performances in the financial intermediation, insurance, real-estate and business services sector.

The real value added by the *commerce sector* increased at an annualised rate of 1½ per cent in the second quarter of 2003, thus maintaining the rather lacklustre growth recorded in the first quarter. This subdued growth can be attributed to the disappointing performance of the catering and accommodation sector. This weaker growth in catering and accommodation was partly offset by somewhat firmer growth in the retail and wholesale trade as well as the motor trade subsectors. Real output of the retail trade subsector was supported by firm demand for consumer goods.

Following an annualised increase of 5½ per cent in the first quarter of 2003, growth in the real value added by the *transport, storage and communication sector* slowed down to 4 per cent in the second quarter. This was the net effect of stagnant growth in the transport subsector, which offset robust growth in the cellular communication sector. The latter sector continued to benefit from the demand for communication services of both businesses and consumers. Anecdotal evidence suggests that cellular telephones are more readily accessible for most people than fixed line telephones.

Growth in the real value added by the *financial intermediation, insurance, real-estate and business services sector* accelerated from an annualised rate of 2 per cent in the first quarter of 2003 to 2½ per cent in the second quarter. This faster growth can mainly be attributed to an improvement in the real value added by banks and the real-estate sector. Activity in the real-estate market continued to increase firmly due to the expanding demand for housing. There was also an emerging group of market participants who acquired residential units for investment purposes. The real value added by the *general government sector* increased at an annualised rate of 1 per cent in the second quarter of 2003, broadly maintaining the growth rate recorded in the first quarter.

Domestic expenditure

In contrast to domestic production which lost considerable momentum, growth in *aggregate real gross domestic expenditure* escalated from a quarter-to-quarter and annualised rate of 3½ per cent in the first quarter of 2003 to 5½ per cent in the second quarter. This was mainly due to a rising tempo of inventory accumulation, some of which was probably involuntary. In addition, real aggregate final demand still increased strongly, albeit at a slightly slower pace than in the first quarter.

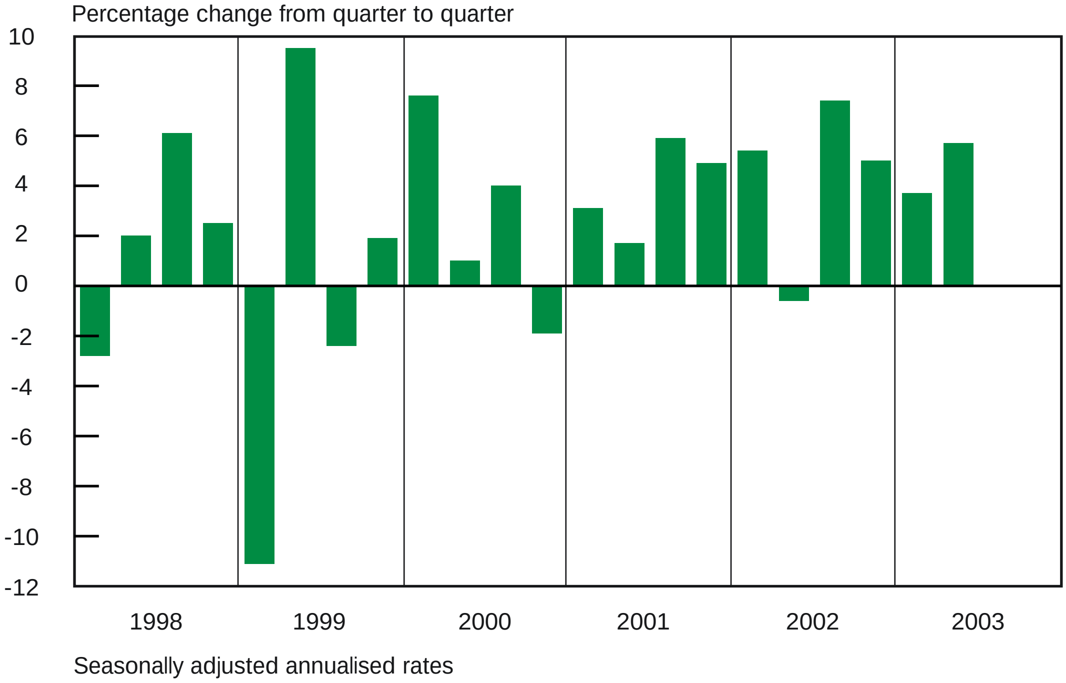
Real final consumption expenditure by households remained strong in the second quarter of 2003. Real outlays on consumer goods and services increased at a seasonally adjusted and annualised rate of 2½ per cent in the second quarter, broadly maintaining the rate attained during the fourth quarter of 2002 and the first quarter of 2003. The sustained strength in household spending was evident in all the major expenditure categories.

Real gross domestic expenditure

Percentage change at seasonally adjusted annualised rates

	2002					2003	
Components	1st qr	2nd qr	3rd qr	4th qr	Year	1st qr	2nd qr
Final consumption expenditure by households	3½	4	3	2½	3	2½	2½
Final consumption expenditure by general government	3½	3½	3½	4	3½	4	4
Gross fixed capital formation...	7	8	8½	11½	6½	8	5½
Change in inventories (R billions,1995 prices)............	6,4	0,4	4,5	6,2	4,4	4,2	6,4
Gross domestic expenditure..	5½	-½	7½	5	4	3½	5½

Real gross domestic expenditure



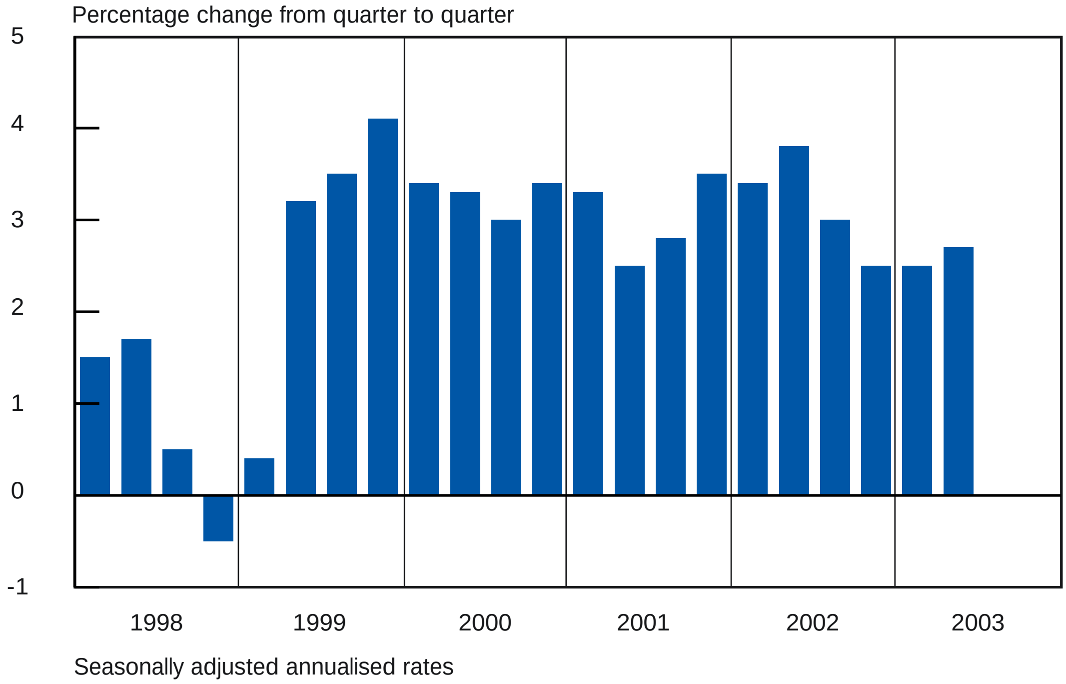
The growth in real household spending on durable goods held firm in the second quarter of 2003 at an annualised rate of 2½ per cent, the same rate recorded in the first quarter. Demand for furniture and household appliances as well as for recreational and entertainment goods was particularly robust. This was partly due to the high import content of these goods, the prices of which benefited from the appreciation of the exchange rate of the rand. Similar spending behaviour was also evident in the increase in real outlays on semi-durable goods, especially household textiles and furnishings.

Final consumption expenditure by households
Percentage change at seasonally adjusted annualised rates

Components	2002					2003	
	1st qr	2nd qr	3rd qr	4th qr	Year	1st qr	2nd qr
Durable goods	-2½	-1½	8½	-4½	1½	2½	2½
Semi-durable goods	13	17	4	2	9½	3	3
Non-durable goods	2	2	2	0	2	2	2½
Services	3	3	3	6	3½	3	3
Total	3½	4	3	2½	3	2½	2½

Real spending on the largely non-discretionary non-durable goods and services categories increased at a relatively brisk pace in the second quarter of 2003. All the spending categories showed increases, particularly household fuel and power.

Real final consumption expenditure by households

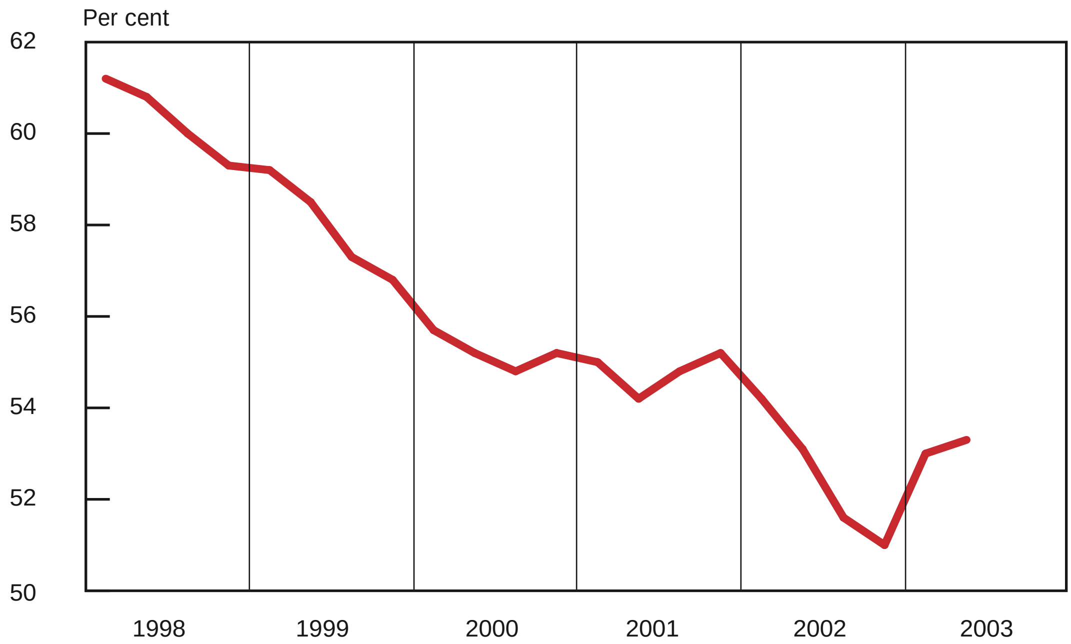


The resilience of household demand in the second quarter of 2003 was the result of an improvement in consumer finances and confidence which could be attributed to:

- tax relief to consumers announced in the 2003/04 Budget;
- the increase in size of the child grant and its extension to children in an older age group, and the increase in the disability and pension grant in the Budget;
- wage settlements which mostly matched and even exceeded the prevailing inflation rate; and
- expectations – realised in June – of a decline in debt servicing cost on account of a reduction in lending rates.

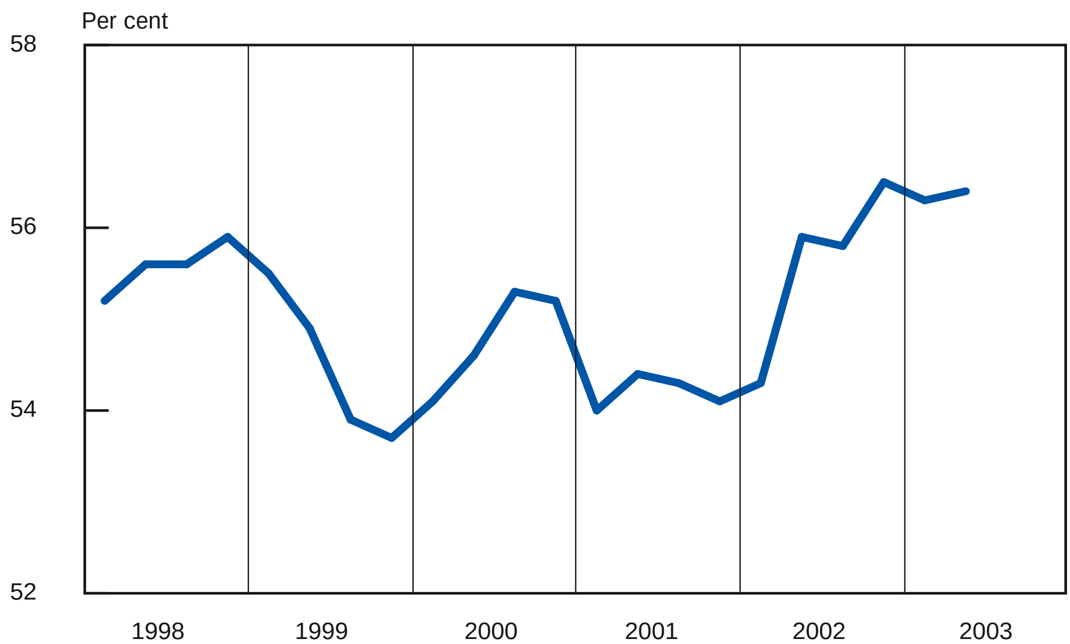
Although an increase in household disposable income partly financed higher consumption expenditure, households also incurred further debt in the second quarter of 2003. Household debt as a percentage of disposable income edged higher from 53 per cent in the first quarter to about 53½ per cent in the second quarter of 2003. While part of this additional debt was channelled to consumption expenditure, part of debt accumulation was intended for fixed property acquisitions. Mortgage advances relative to total household debt increased from 54 per cent in the fourth quarter of 2001 to 56½ per cent in both the first and second quarters of 2003.

Household debt as percentage of disposable income



Seasonally adjusted

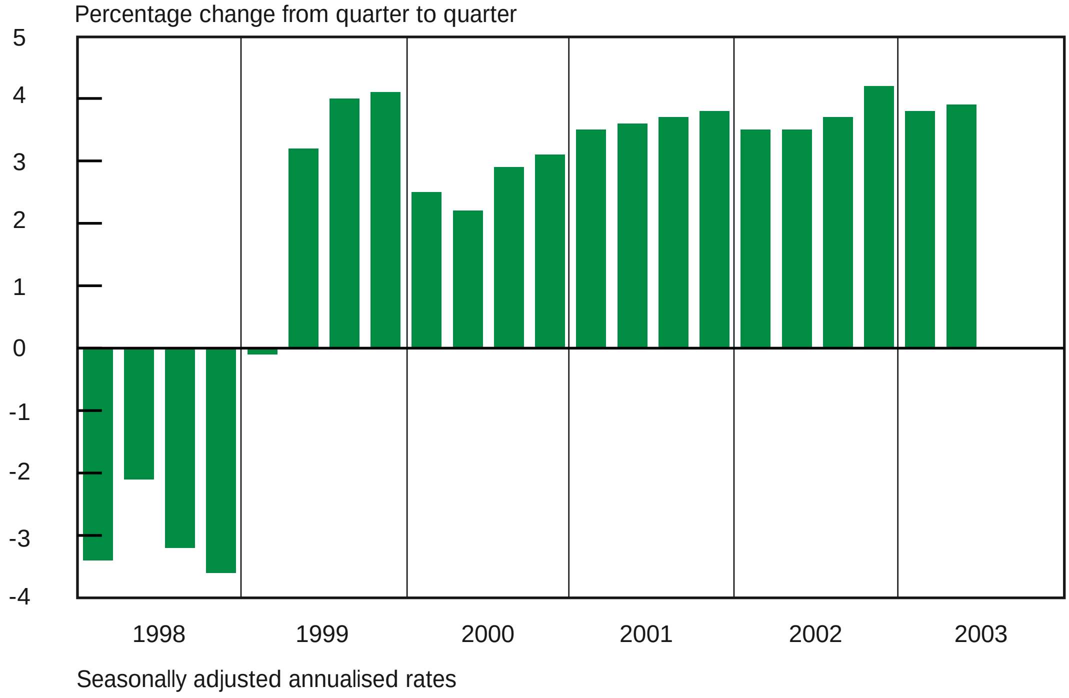
Share of mortgage advances in total household debt



Seasonally adjusted

Real *final consumption expenditure by general government* increased at an annualised rate of 4 per cent in the second quarter of 2003, thus maintaining the rate recorded in the first quarter. This can mainly be attributed to higher expenditure on non-wage goods and services. There was little growth in real compensation of employees on a quarter-to-quarter basis in the second quarter of 2003. Nevertheless, the ratio of final consumption expenditure by general government to gross domestic product increased from 19½ per cent in the first quarter of 2003 to 20 per cent in the second quarter.

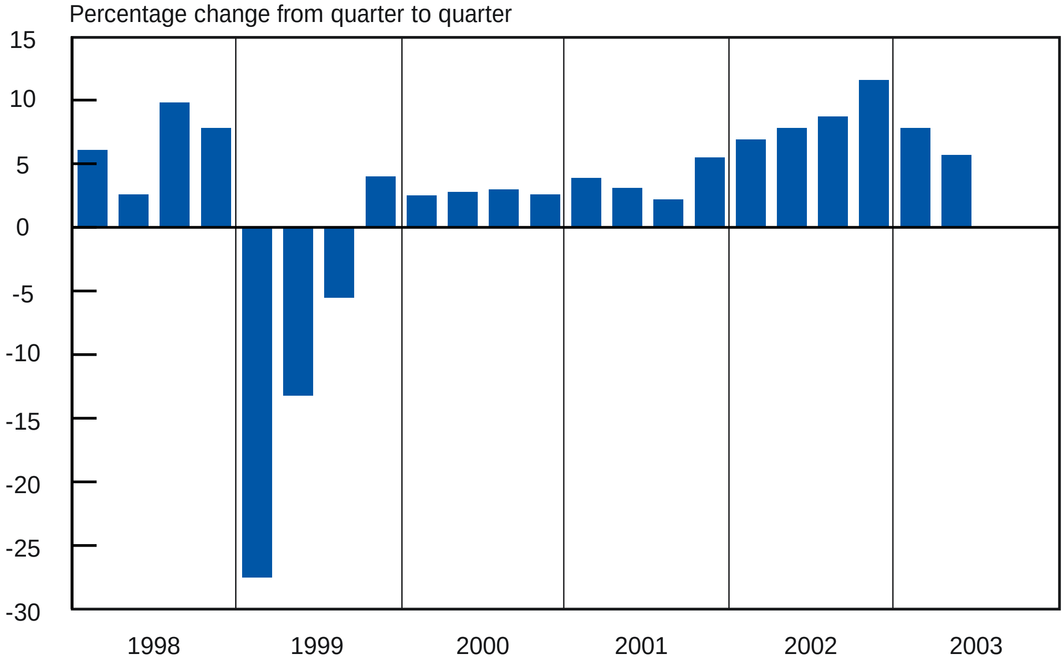
Real final consumption expenditure by general government



Growth in *real gross fixed capital formation* continued at a lively pace of 5½ per cent in the second quarter of 2003, somewhat lower than the growth rate of 8 per cent recorded in the first quarter. While rather buoyant investment activity was recorded in the private sector and general government's pace of growth in real fixed capital outlays also picked up somewhat, the tempo of growth in public corporations' real fixed capital formation decelerated sharply.

Growth in real gross fixed capital formation by the *private sector* accelerated from an annualised rate of 5½ per cent in the first quarter of 2003 to 6½ per cent in the second quarter. The bulk of new capital formation took place in the mining and quarrying sector. However, investment activity was relatively subdued in the other economic sectors compared with the first quarter. Real fixed capital expenditure by the mining sector benefited from ongoing expansion of capacity that took place mainly in the platinum-mining sector. The slowdown in real fixed capital outlays by the manufacturing sector was broadly in keeping with the reduced profitability in this sector which was adversely affected by sluggish world demand, the recovery in the exchange rate of the rand and a decline in the utilisation of production capacity. In agriculture lower real output and declining product prices resulted in a notable contraction in real fixed capital expenditure.

Real gross fixed capital formation



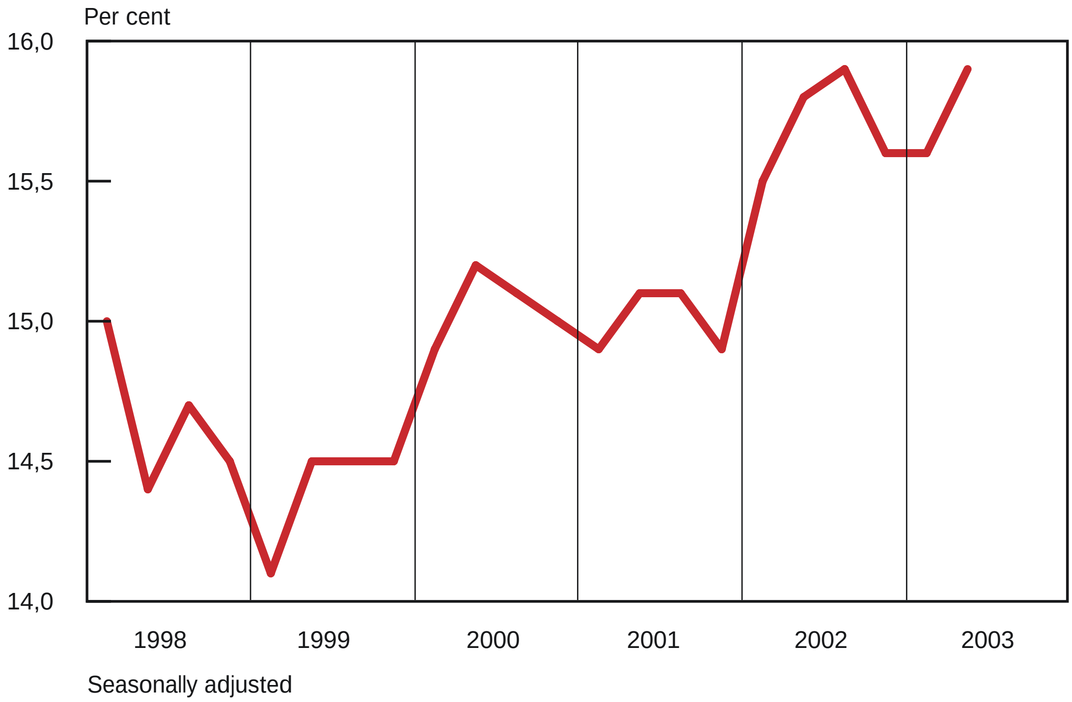
Seasonally adjusted annualised rates

Growth in real fixed capital formation by *public corporations* decelerated in the second quarter of 2003. This deceleration was the net result of a strong increase in the capital investment of Transnet which was almost neutralised by a contraction in real fixed capital expenditure of other public corporations. The replacement of rolling stock and the ongoing Coega project underpinned capital formation by public corporations.

Real gross fixed capital formation by *general government* increased at an annualised rate of 4 per cent in the second quarter of 2003 compared with 3½ per cent in the first quarter. All three levels of government were responsible for this increase in real fixed capital expenditure as government continued to expand and upgrade its capacity for service delivery.

Annualised real *inventory investment*, measured at 1995 prices, increased from R4,2 billion in the first quarter of 2003 to R6,4 billion in the second quarter. In contrast to the first quarter when inventories subtracted 1 percentage point from economic growth, inventory investment contributed 1½ percentage points to growth in real gross domestic product in the second quarter of 2003. Most of the inventory accumulation occurred in the mining and manufacturing sectors of the economy. The accumulation of inventories in these export-oriented industries was probably largely involuntary and coincided with lower export demand and, in the manufacturing sector, lower domestic sales. In addition, the cost of holding inventories was somewhat reduced with the lowering of interest rates towards the end of the second quarter. By contrast, there was a reduction in the inventories of the commerce sector as retail demand continued to increase robustly in the second quarter of 2003. As a result of these developments, the ratio of industrial and commercial inventories to non-agricultural gross domestic product increased from 15½ per cent in the first quarter of 2003 to 16 per cent in the second quarter.

Industrial and commercial inventories as percentage of non-agricultural gross domestic product



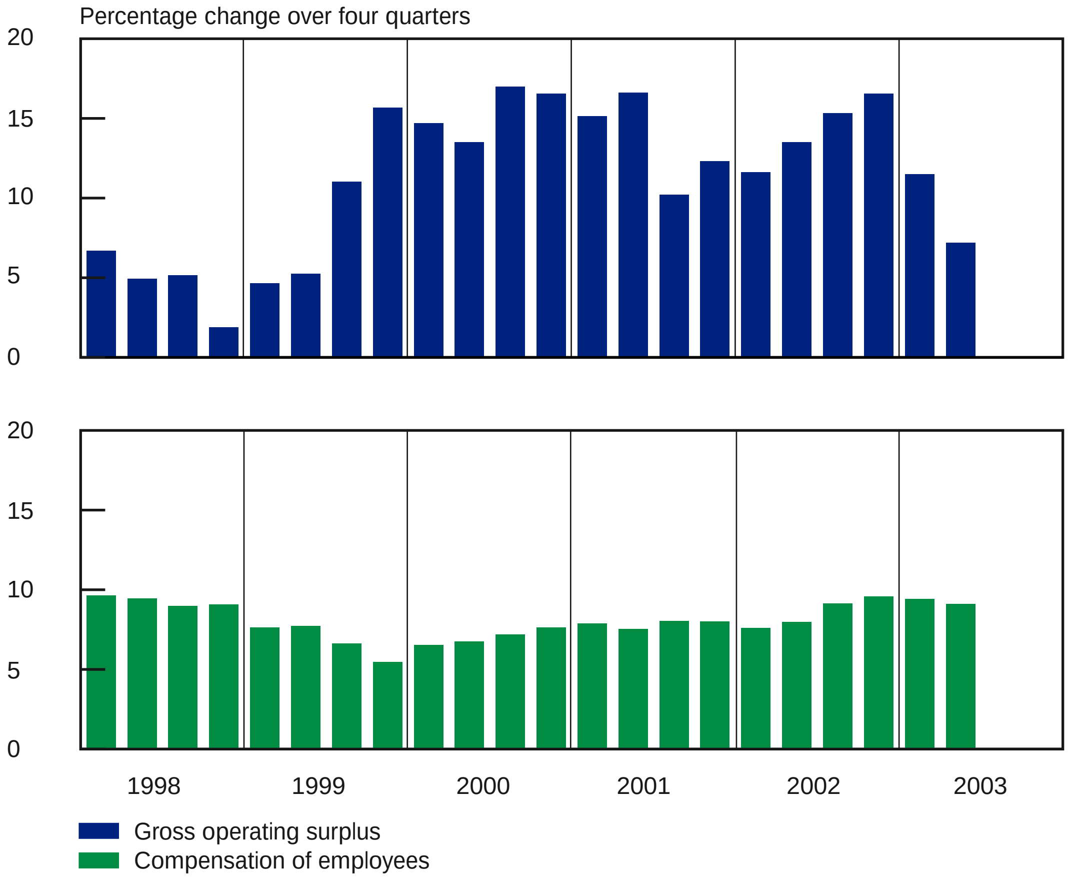
Factor income

The growth in *total nominal factor income*, measured over a year, slowed down from 10½ per cent in the first quarter of 2003 to just 8 per cent in the second quarter. This could mainly be attributed to weaker growth in gross operating surpluses of business enterprises.

Growth in *compensation of employees*, measured over four quarters, slowed down slightly from 9½ per cent in the first quarter of 2003 to 9 per cent in the second quarter. The weaker growth was evident throughout all the major sectors of the economy with the exception of the mining and manufacturing sectors where growth remained the same as in the first quarter. Against the background of the recent relatively high wage settlements, businesses appear to be rationalising staff complements in order to contain the growth in the overall wage bill.

The rate of increase in *gross operating surpluses* of business enterprises over one year slowed down sharply from 11½ per cent in the first quarter of 2003 to only 7 per cent in the second quarter. Aside from the finance, insurance, real-estate and business services sector where growth accelerated somewhat, the slowdown in growth was spread throughout all the major sectors of the economy. Operating surpluses of the financial services sector benefited from a relatively healthy performance of the banking sector. The relative weakness of the economy, coupled with the recovery in the exchange rate of the rand, took its toll on operating surpluses across most sectors of the economy. Profit margins of the export-oriented mining and manufacturing sectors, in particular, remained under pressure. Consequently, the ratio of gross operating surplus to total factor income declined from 48½ per cent in the first quarter to 47½ per cent in the second quarter of 2003.

Gross operating surplus and compensation of employees



Gross saving

Gross saving as a percentage of gross domestic product weakened from 16 per cent in the first quarter of 2003 to 15½ per cent in the second quarter. Simultaneously, capital formation rose to 17 per cent of gross domestic product; the South African economy accordingly could not meet all its financing requirements from internally generated saving resources. The lower saving ratio in the second quarter of 2003 was primarily a result of lower corporate saving. The ratios of gross saving by general government and households relative to gross domestic product remained approximately the same as in the first quarter.

Gross saving by the *corporate sector* as percentage of gross domestic product declined from 11½ per cent in the first quarter of 2003 to 11 per cent in the second quarter. This can be ascribed to somewhat faster growth in dividend payments relative to operating surpluses. In addition, dividend payments to non-resident shareholders increased firmly. Dividend payments to the rest of the world as a percentage of total dividends declared by incorporated business enterprises increased from 28 per cent in the first quarter of 2003 to 29 per cent in the second quarter.

The gross saving by *households* as a percentage of gross domestic product remained at around 3 per cent in the first and the second quarters of 2003. Despite an improvement in real disposable income, the saving of households remained under pressure as final consumption expenditure by households persisted at a relatively high level. The lower profitability of companies, partly due to the erosion of pricing power as the exchange rate of the rand recovered, impacted on the tax base of general government. Growth in tax revenue slowed down, thereby increasing the shortfall between expenditure and income and weakening the gross saving by general government.

Employment

While increases in employment were registered in the second and third quarters of 2002, recently published labour market statistics by Statistics South Africa have dispelled the perception that significant gains had been made in formal non-agricultural employment towards the end of that year. According to the new expanded *Survey of Employment and Earnings* (SEE), no significant change in formal non-agricultural employment occurred between September and December 2002. When allowing for seasonal variation, employment numbers actually contracted towards the end of 2002. Preliminary evidence suggests that employment prospects continued to deteriorate in the first half of 2003.

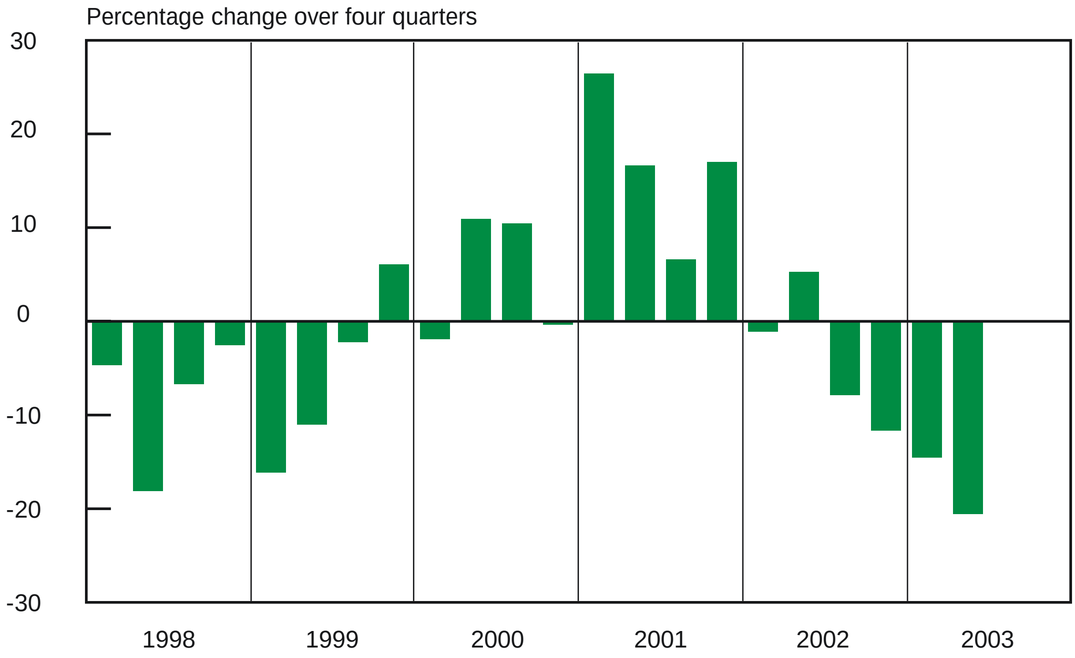
Following a process of ongoing improvements in the quality and coverage of economic statistics, Statistics South Africa has again published the SEE as an official statistical release in early August 2003. From March 2001 onwards, the SEE's precursor, the *Survey of Employment and Earnings in Selected Industries* or SEESI, was published as a discussion document to afford the agency the opportunity to expand the survey's coverage. In SEESI, industries such as restaurants and other eating and drinking places, boarding houses, caravan parks and guest farms, private air transport and private telecommunication services were excluded. Information on real-estate activities, business services, private educational services, private medical, dental and other health services, and welfare and religious organisations was also not collected. Apart from government, all *VAT-registered businesses* outside of agriculture are surveyed in terms of the new SEE. This caused the coverage of the new expanded SEE for September and December 2002, in terms of employment numbers, to rise by 35 per cent compared to the SEESI.

Although overall employment levels were fairly flat between September and December 2002, gains were made in five of the eight main sectors of the economy during this period. Over this period, approximately 20 000 new employment opportunities became available in the community, social and personal services sector. Employers in manufacturing, electricity and water supply, wholesale and retail trade, personal and household goods, hotels and restaurants also expanded their personnel complements. Unfortunately, most of these gains were of a temporary nature to satisfy once-off or seasonal labour needs around the year-end. Employment in the financial intermediation and insurance, real-estate and business services sector contracted by about 36 000 workers towards the end of 2002 and thereby nullified employment gains in other sectors.

Unfortunately, no consolidated official employment statistics have yet been released for 2003. This resulted from the comprehensive revising of labour market surveys by Statistics South Africa. Preliminary information based on indirect evidence seems to indicate that the virtually static employment numbers of the second half of 2002 turned into renewed job losses in the initial months of 2003. Factors that probably contributed to the slack in employment growth in 2003 were lacklustre world economic growth, the recovery in the exchange rate of the rand which eroded the international price competitive gains of late 2001 and early 2002, and a slowdown in domestic economic growth.

Changes in the volume of job advertisements in the print media which have historically been fairly well correlated with changes in formal non-agricultural employment, corroborate the anticipated reduction in employment totals in 2003. In fact, the volume of job advertisements in the media fell by 14,5 per cent in the year to the first quarter of 2003 and by 20,6 per cent in the year to the second quarter.

Job advertisements in print media



According to *Andrew Levy Employment Publications,* a private-sector labour publication, the number of workdays lost due to strikes and work stoppages rose from 130 000 in the first half of 2002 to 240 000 in the first half of 2003. It is stated that although the number of workdays lost almost doubled over this period, the increase was largely due to issues pertaining to company-specific rules. Changes to funeral benefits and shift allocation procedures and a dispute regarding the provision of free anti-retroviral drugs for employees living with Aids triggered labour action in the first half of 2003. A significant factor which contributed to heightened tension in the labour market was the fact that a number of long-term agreements were negotiated this year, primarily in the mining and metal and engineering sectors. Most of these negotiations were concluded without any meaningful disruption to production processes.

Labour cost and productivity

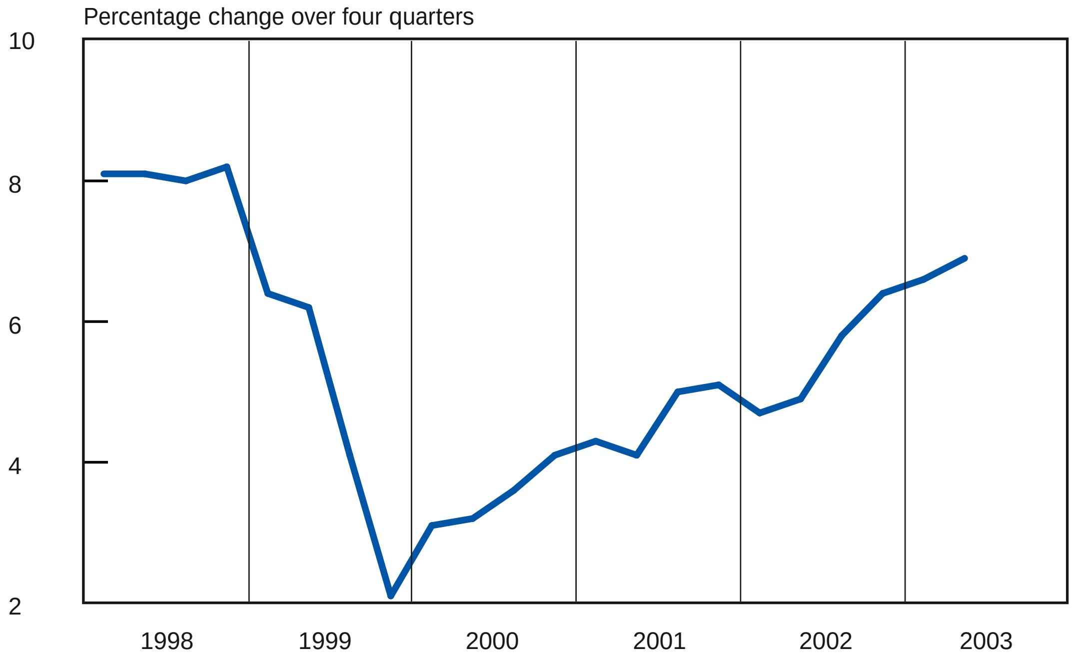
An acceleration in nominal wage growth became evident as the average settlement rate for collective bargaining agreements increased from 7,5 per cent in the first half of 2002 to 8,0 per cent for the year as a whole and to 8,9 per cent in the first half of 2003. More recent wage settlements increased further to average almost 10 per cent. It is expected that dissipating consumer price inflation may lead to a moderation in settlement rates in coming months. However, according to PE Corporate Services, a private-sector labour consultancy, wage increases are expected to remain in excess of inflation for some time to come as skills shortages continue to prevail in the labour market.

Information obtained from the Automated Clearing Bureau on salaries, wages and pensions deposited into the bank accounts of almost 5 million salaried and retired workers, suggests that nominal wage growth per worker amounted to around 9 per cent in the first half of 2003 when compared with the same period in the previous year.

Remuneration packages in both the private and public sector increasingly incorporate performance-related criteria. PE Corporate Services indicates that 75 per cent of South African organisations use some form of performance-based pay system while 60 per cent of organisations, including the public sector and parastatals, have a performance-linked component in their remuneration packages. This is likely to impact positively on future productivity trends.

As indicated in the June 2003 *Quarterly Bulletin*, year-on-year growth in labour productivity in the manufacturing sector fell back markedly to 0,6 per cent in the fourth quarter of 2002 as manufacturing production slowed down and more workers were absorbed in production processes during that period. Economy-wide labour productivity growth also diminished to 1,8 per cent in the year to the fourth quarter of 2002 from rates generally in excess of 4 per cent in preceding years. In the absence of new official labour market statistics for 2003, it is fair to accept that no meaningful turnaround in labour productivity growth had occurred in recent months as production volumes remained subdued. The possible decrease in employment numbers in recent months, though, might lead to moderate increases in labour productivity growth rates.

Compensation of employees per unit of production*



* Non-agricultural sectors

The sharp fall-back in the rate of increase in labour productivity combined with an increase in nominal wage growth propelled the pace of increase in *nominal unit labour cost in the manufacturing sector* to 9,0 per cent in the year to the fourth quarter of 2002. Preliminary indications are that this growth slowed down somewhat to 6 per cent in the year to the second quarter of 2003. The slowdown in economy-wide labour productivity and rising nominal wage growth caused nominal unit labour cost in the *overall formal non-agricultural sector of the economy* to increase at an average rate of 7,0 per cent in 2002 – almost twice as high as in 2001. Preliminary indications are that this rate remained at about 7 per cent in the year to the second quarter of 2003. The acceleration in nominal wage growth in recent months requires significant advances in labour productivity to contain further increases in nominal unit labour cost and to ensure increases consistent with the inflation target range.

Prices

Price inflation receded meaningfully in recent months, following an abrupt rise to rates in excess of 10 per cent in 2002. The recent waning in inflationary pressures was mainly a consequence of the recovery in the international exchange value of the rand since about the second half of 2002. Prudent monetary and fiscal policies further assisted the reduction in inflation. The deceleration in inflation was especially pronounced in the prices of tradeable goods, although services price inflation also slowed down.

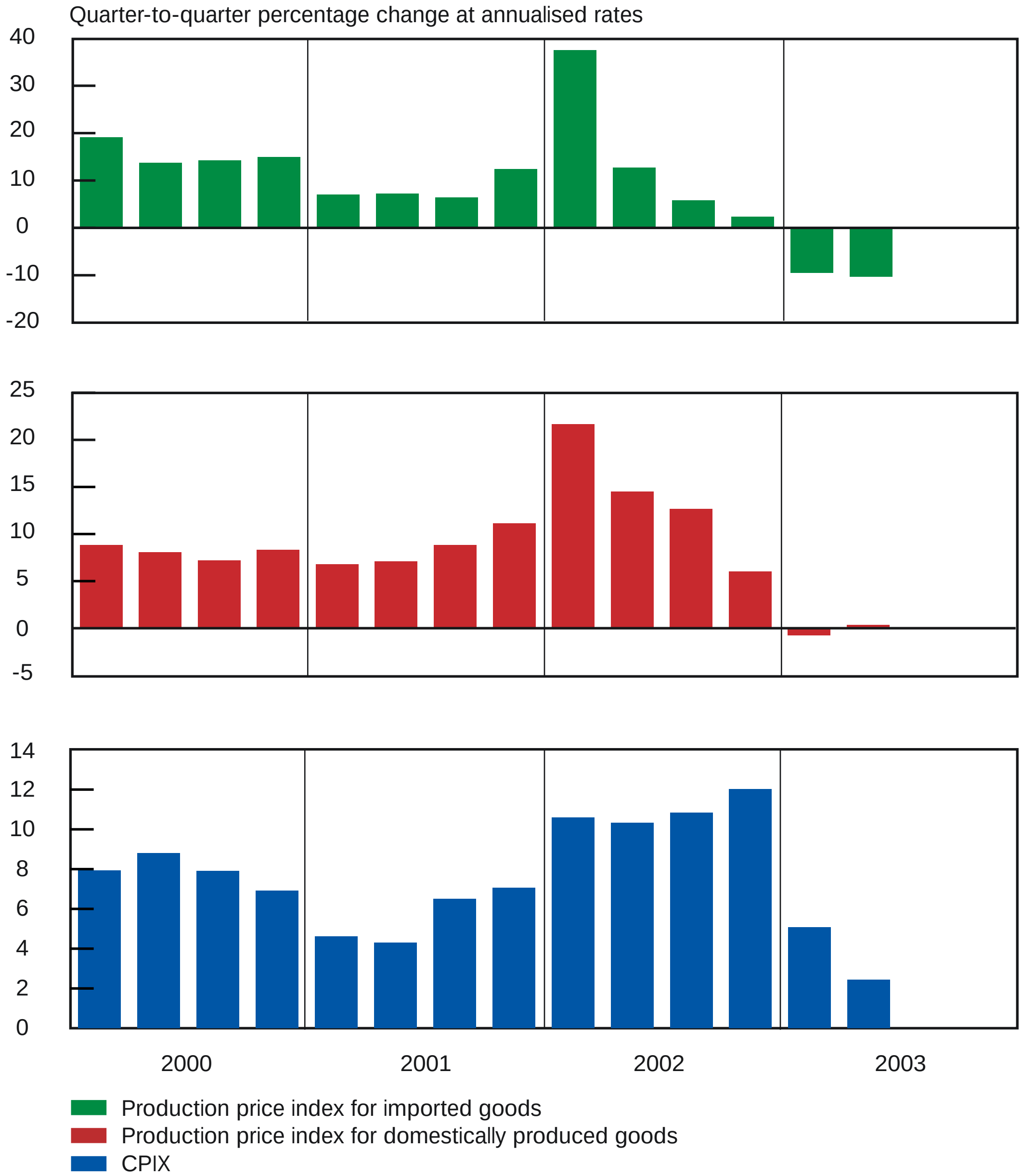
In some instances, declining price pressures even developed into absolute declines in the prices of goods and services. In fact, from quarter to quarter the production prices of goods have been declining since the first quarter of 2003 and consumer goods prices also declined in the second quarter of 2003, lagging slightly behind production prices.

As could be expected, *imported goods inflation* benefited most from the strong recovery of the rand, which on a trade-weighted monthly average basis rebounded by more than 35 per cent in the nineteen months to July 2003. The year-on-year rate of change in the prices of imported goods moved from an inflation rate of 4,6 per cent in January 2003 to a *deflation rate* of 3,4 per cent in June. Subsequently, the pace of deflation accelerated to 6,4 per cent in July 2003, mainly on account of lower prices of imported crude petroleum and the renewed recovery in the exchange rate of the rand in July 2003. When measured over periods of twelve months, declines were recorded in the prices of goods in most of the imported categories during July 2003.

The short-term pace of change in the prices of imported goods slowed down for five consecutive quarters from an annualised inflation rate of 37,5 per cent in the first quarter of 2002 to prices *falling* at a rate of 10,3 per cent in the second quarter of 2003.

As the cost of imported goods declined, the year-on-year rate of increase in the prices of *domestically produced goods* decelerated from 15,3 per cent in August 2002 to a tame 3,5 per cent in May 2003 and 4,4 per cent in both June and July. The pick-up in domestically produced goods inflation in June 2003 resulted mainly from a sharp increase in the electricity tariffs charged by Eskom, the state-owned electricity utility. Electricity tariffs increased by 45 per cent in June 2003, linked to the introduction of greater variation between summer and winter tariffs from July 2002. This increase contributed as much as 1,8 percentage points to the month-on-month increase in the prices of domestically produced goods in June 2003. In July 2003, higher electricity prices were again the main driver of domestically produced goods inflation, followed by increases in the prices of transport equipment and paper products and printing. These increases were partially offset by declines in the prices of agricultural products and products of petroleum and coal.

Price indices

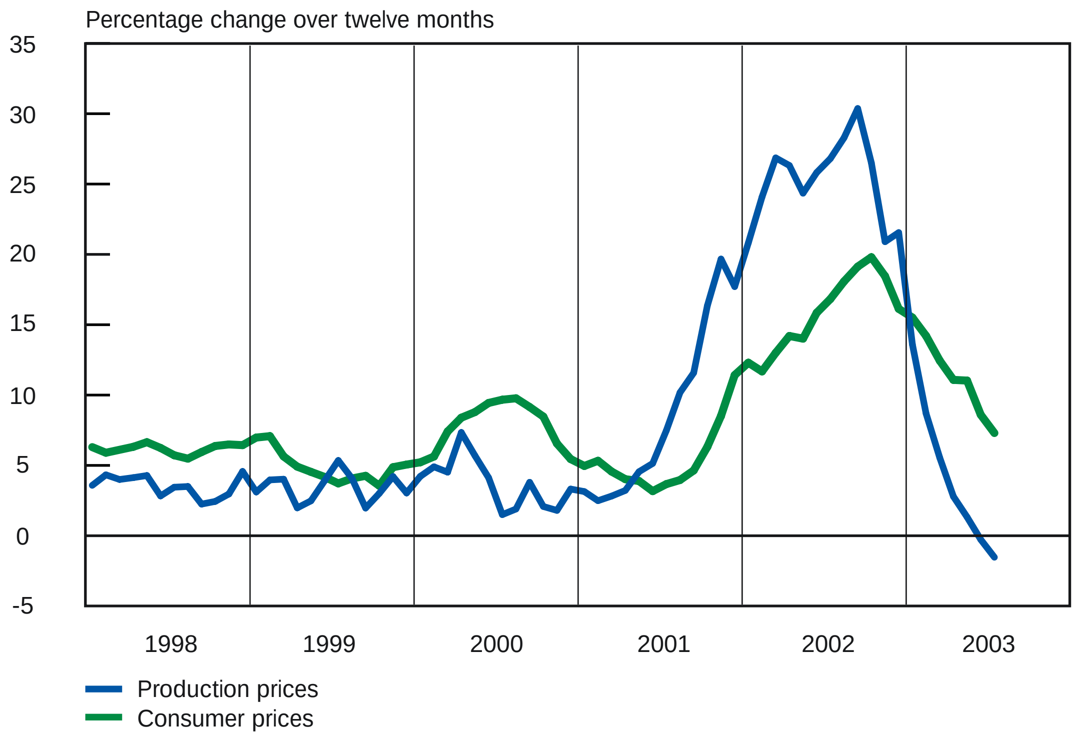


Concerning food prices, *agricultural* food prices fell by 7,3 per cent in the year to July 2003, as the prices of grain, fruit, meat and some other agricultural products declined. At the *manufactured* level, year-on-year food price increases also decelerated to 2,8 per cent in July 2003, from 30,1 per cent ten months earlier. The decline in the production prices of food bodes well for a further slowdown in food price inflation at the consumer level in coming months.

The quarter-to-quarter pace of change in the prices of domestically produced goods reverted from an annualised rate of increase of 6,0 per cent in the fourth quarter of

2002 to a *decrease* at a rate of 0,7 per cent in the first quarter of 2003. As inflationary pressures remained muted, the average price level of domestically produced goods picked up only slightly in the second quarter of 2003.

Food prices



Following a slowdown in the pace of increase in the prices of both imported and domestically produced goods in recent months, the year-on-year rate of increase in the *all-goods production price index* fell back from 8,1 per cent in January 2003 to a mere 1,2 per cent in May. As higher electricity prices pushed the index higher, the year-on-year rate of increase in the production prices of goods rose marginally to 2,3 per cent in June 2003, but fell back to 1,5 per cent in July. From quarter to quarter, production prices fell back at annualised rates of around 3 per cent in both the first and second quarters of 2003.

Production prices

Quarter-to-quarter percentage changes at seasonally adjusted annualised rates

Period		Domestically produced goods	Imported goods	Overall production prices
2001:	Year.......................................	7,8	10,0	8,4
2002:	1st qr.....................................	21,6	37,5	26,0
	2nd qr	14,5	12,7	13,4
	3rd qr	12,7	5,8	11,0
	4th qr	6,0	2,3	5,2
	Year.......................................	13,5	15,5	14,2
2003:	1st qr.....................................	-0,7	-9,5	-3,0
	2nd qr	0,3	-10,3	-3,1

Diminishing price pressures at the production level contributed significantly to the waning of consumer price inflation in the first half of 2003. Inflation in the prices of *consumer goods* declined from a year-on-year rate of 10,7 per cent in January 2003 to 4,6 per cent in June. Following an increase in the prices of petrol and diesel, water, electricity and cigarettes and tobacco products, year-on-year inflation in the prices of consumer goods rose to 5,2 per cent in July 2003. The driving force behind the general deceleration in consumer goods price inflation in recent months came from declining food price inflation. Food price inflation fell from a year-on-year rate of 15,5 per cent in January 2003 to 7,3 per cent in July. Falling transport costs, when compared over periods of twelve months, further assisted the deceleration in consumer goods inflation. A relatively stable price environment for new motor vehicles, occasioned by the recovery of the rand, also contributed to easing inflationary pressures in the first half of 2003.

Not only was price decreases being experienced at the production level in recent months, but when measured from quarter to quarter and expressed at an annualised rate, consumer goods prices also declined at a rate of 0,9 per cent in the second quarter of 2003. Declining goods prices were evident in the categories furniture and equipment, clothing and footwear, as well as transport goods.

Unlike goods price inflation, *services price inflation* remained relatively high. Year-on-year services price inflation was still at around 11 per cent during the opening months of 2003. More recently though, services price inflation declined somewhat to 9,5 per cent in June 2003. Following the decline in mortgage interest rates, services price inflation fell to 5,5 per cent in the year to July 2003. The quarter-to-quarter pace of increase in the prices of consumer services slowed down more meaningfully from 6,4 per cent in the first quarter of 2003 to 3,1 per cent in the second quarter. A deceleration in the pace of increase in home ownership costs was the main contributor to the waning of services price inflation in the second quarter of 2003.

Consumer prices

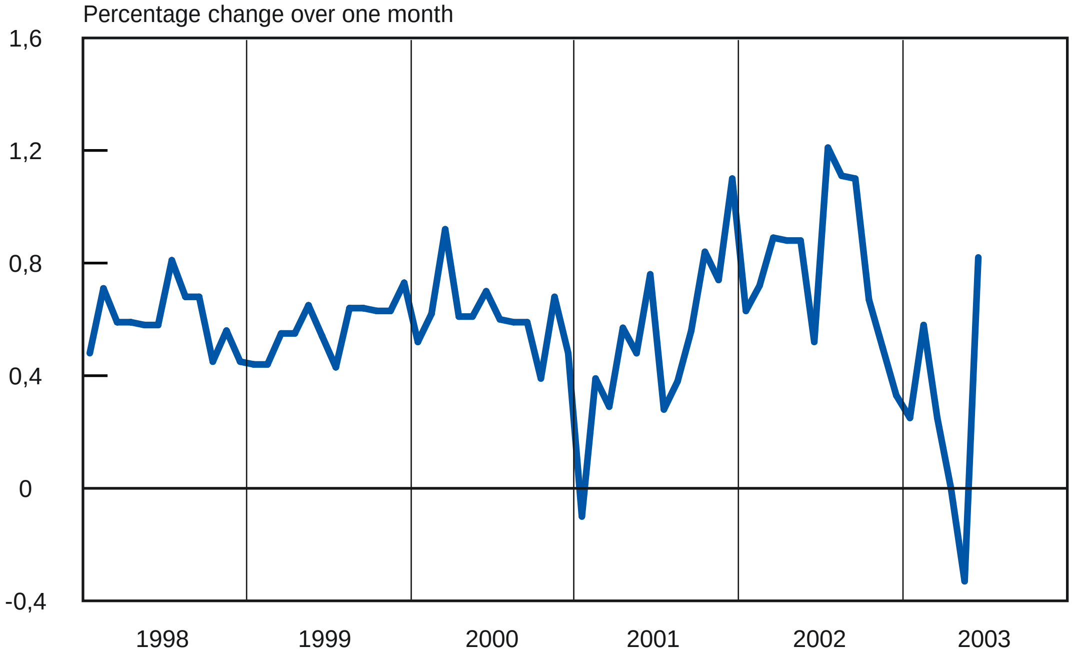
Quarter-to-quarter percentage changes at annualised rates

Period		Goods	Services	Headline inflation	CPIX inflation
2001:	Year	5,6	5,5	5,7	6,6
2002:	1st qr	12,8	10,6	11,2	10,6
	2nd qr	13,1	10,0	12,4	10,3
	3rd qr	10,9	15,6	12,7	10,8
	4th qr	13,3	15,0	13,9	12,0
	Year	10,2	7,8	9,2	9,3
2003:	1st qr	3,0	6,4	4,2	5,1
	2nd qr	-0,9	3,1	1,6	2,4

Overall consumer price inflation decelerated from a recent high point of 13,0 per cent in the year to October 2002 to 5,2 per cent in the year to July 2003. The slowdown in the year-on-year measure of overall consumer price inflation in 2003 not only resulted from high base values in the preceding year, but also from falling short-term inflation in the prices of high-weight categories. Amongst these categories are those for transport goods and food which contributed significantly to the waning of price inflation. Whereas food price inflation slowed down to an annualised rate of 1,1 per cent in the second quarter of 2003, the prices of transport goods fell back at an annualised rate of 12,6 per cent. Combined with declining prices of furniture and equipment, quarter-to-quarter and annualised consumer price inflation fell from 13,9 per cent in the fourth quarter of 2002 to 1,6 per cent in the second quarter of 2003.

Twelve-month CPIX inflation (i.e. changes in the overall consumer price index for metropolitan and other urban areas, excluding the interest cost of mortgage bonds) fell from a recent peak value of 11,3 per cent in October 2002 to a low of 6,4 per cent in June 2003 – the lowest rate of increase in nineteen months. Subsequently this rate picked up marginally to 6,6 per cent in July 2003. The general deceleration in CPIX inflation was also mainly due to the moderation in food price inflation and the decline in transport costs. Price declines were also registered across a wide range of smaller categories, resulting in the short-term pace of increase in CPIX moderating considerably from an annualised rate of 12,0 per cent in the fourth quarter of 2002 to 2,4 per cent in the second quarter of 2003. This rate of increase is the lowest since the establishment of the CPIX indicator in 1997.

CPIX



Seasonally adjusted

Consumer and production prices

Percentage changes over twelve months

Period		Production price index	Overall consumer price index	CPIX
2002:	Oct	14,6	13,0	11,3
	Nov	13,9	12,9	11,3
	Dec	12,4	12,4	10,8
	Year	14,2	9,2	9,3
2003:	Jan	8,1	11,6	10,0
	Feb	6,2	10,3	9,3
	Mar	5,1	10,2	9,3
	Apr	3,3	8,8	8,5
	May	1,2	7,8	7,7
	Jun	2,3	6,7	6,4
	Jul	1,5	5,2	6,6

Foreign trade and payments

Current account[2]

2 The current-account flows referred to in this section are all seasonally adjusted and annualised.

The most recently available data on the composite leading indicator of the Organisation for Economic Cooperation and Development (OECD) signal that growth prospects have improved in the OECD area. However, this follows a fairly lacklustre global economic performance in the first half of 2003, partly due to the uncertainties created by the US-led war in Iraq, high oil prices and concerns over the spread of the *Severe Acute Respiratory Syndrome* (SARS). Oil prices in US dollar terms reached a 12-year high in mid-February 2003, but receded following the invasion in Iraq, largely because the disruption to the oil supply from the region was expected to be less serious than previously feared. The spot price of Brent crude oil, however, rose again to reach levels of around $30 per barrel by August 2003 as a result of low OECD crude oil inventories (especially in the United States), uncertainties over Iraq's oil production and anticipation of seasonally strong winter demand in the Northern Hemisphere.

The apparent sluggish recovery in global economic activity together with the recovery in the exchange value of the rand adversely affected the total export earnings of South African producers in the second quarter of 2003. After having regressed strongly in the first quarter of 2003, the decrease in the value of merchandise exports continued in the second quarter of 2003 albeit at a slower pace than before. At the same time, the value of merchandise imports contracted only marginally, underpinned by the relatively strong growth in real gross domestic expenditure. These developments led to the narrowing of the trade surplus from R32,0 billion in the first quarter of 2003 to R23,5 billion in the second quarter.

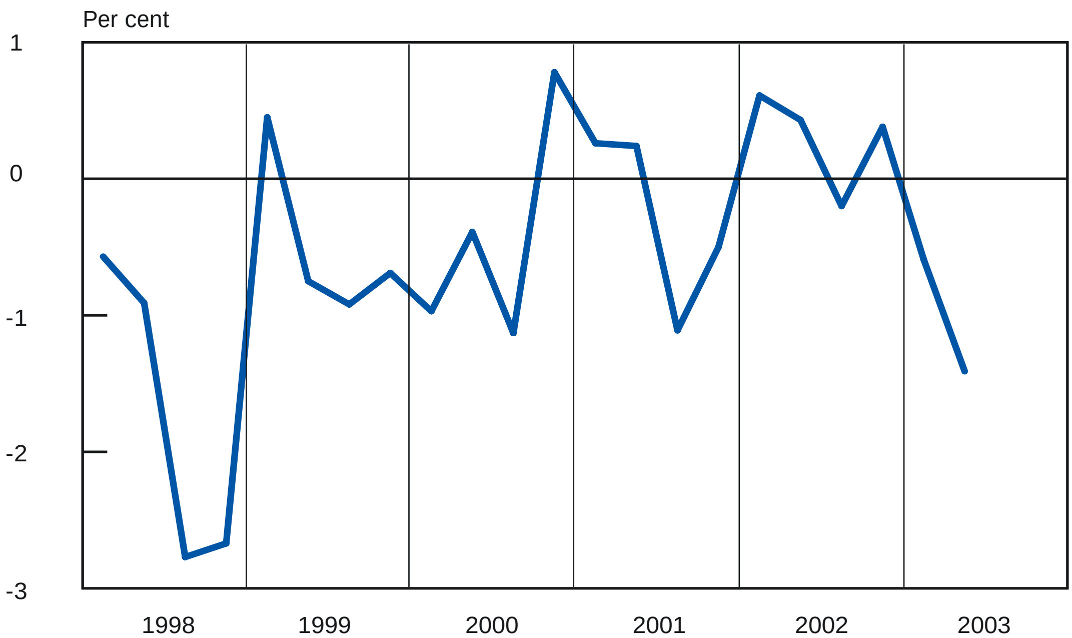
Balance of payments on current account
Seasonally adjusted and annualised
R billions

	2002				2003	
	2nd qr	3rd qr	4th qr	Year	1st qr	2nd qr
Merchandise exports	288,5	272,1	295,9	283,4	257,8	248,9
Net gold exports	43,5	46,9	40,2	42,6	35,6	33,7
Merchandise imports	-276,0	-276,8	-293,0	-279,8	-261,4	-259,1
Trade account	56,0	42,2	43,1	46,2	32,0	23,5
Net service, income and transfer payments	-51,4	-44,4	-38,8	-42,9	-38,8	-39,9
Balance on current account	4,6	-2,2	4,3	3,3	-6,8	-16,4

The trade surplus probably suffered from the realignment of relative prices following the recovery in the exchange rate of the rand from the second half of 2002 to the first half of 2003, which diminished the price competitiveness of South African exporters and import-competing producers.

The combined effect of a contraction in the trade surplus and a slightly larger shortfall on the net service and income account with the rest of the world, was a significant widening of the current-account deficit from R6,8 billion in the first quarter of 2003 to R16,4 billion in the second quarter. The second-quarter deficit amounted to 1,4 per cent of gross domestic product – a magnitude that could easily be financed through capital inflows.

Ratio of current-account balance to gross domestic product



Following the improvement in the external value of the rand and the accompanying decline in the rand prices of exported goods, the *value of merchandise exports* decreased by 3,5 per cent from the first to the second quarter of 2003. Declines were recorded in all the main categories of exports. Lower export proceeds from base metals and the platinum metals group contributed to a decline in mining exports, whereas an increase in the subcategory for vehicle and transport equipment was countered by a decrease in the subcategories for textiles and textile equipment and machinery and electrical equipment.

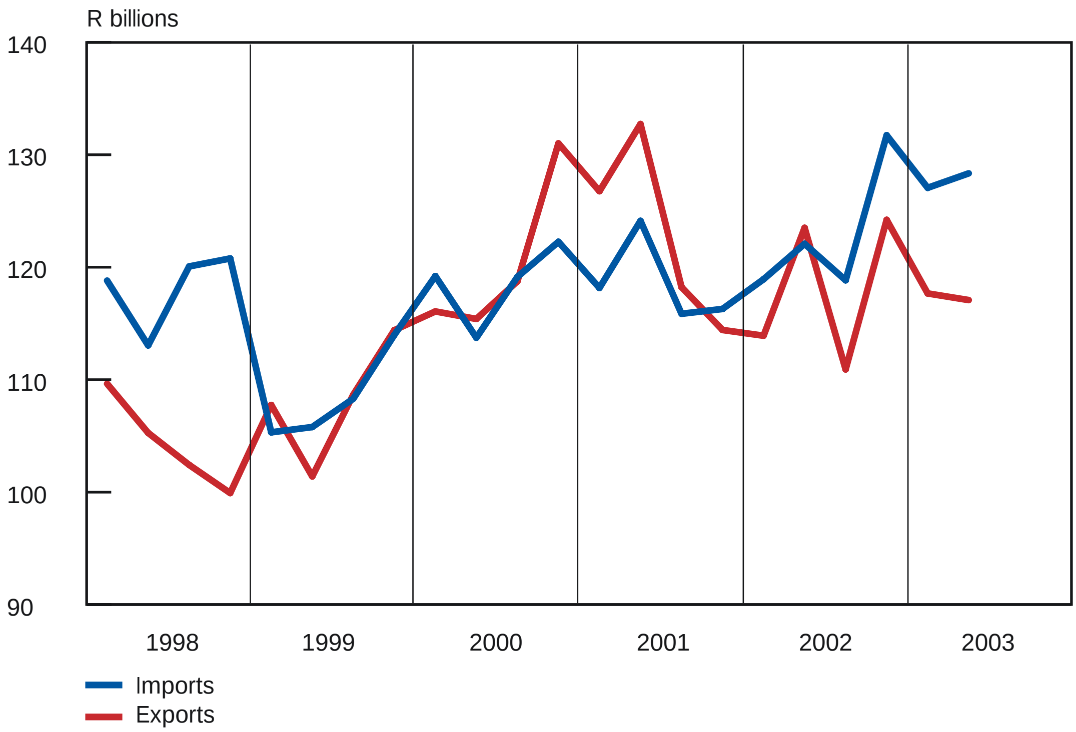
Subdued international commodity prices coupled with a moderate recovery in the external value of the rand brought about a further decline in the *unit value* of exported goods in the second quarter of 2003. The decline in the average rand prices of merchandise exports came to only 3,0 per cent in the second quarter of 2003, compared with a decline of 8,0 per cent in the first quarter. Against the background of lacklustre world demand, the physical *quantity* of merchandise exports declined by 0,5 per cent in the second quarter of 2003, having contracted by 5,3 per cent in the first quarter.

The value of *net gold exports* continued to decline in the second quarter of 2003, despite an increase of almost 1,5 per cent in the physical *quantity* of exported gold. While the average fixing price of gold on the London market dropped slightly from US$352 per fine ounce in the first quarter to US$347 per fine ounce in the second quarter of 2003, in rand terms the average realised price of gold recorded a more pronounced decline from R3 026 per fine ounce to R2 778 per fine ounce over the same period. The value of net gold exports accordingly fell by 5,3 per cent in the second quarter of 2003, having already declined by 11,3 per cent in the first quarter.

The *value of merchandise imports*, which had decreased by 10,8 per cent in the first quarter of 2003, marginally declined further by 0,9 per cent in the second quarter. The lower value of imported goods could mainly be ascribed to decreases in the imports of mining products – particularly the subcategory pearls, precious and semi-precious stones – and agricultural products. These declines barely countered the increase of almost the same magnitude in imports of manufactured goods.

The physical *volume* of imported goods rose by 1,0 per cent in the second quarter of 2003 after declining by 3,5 per cent in the first quarter. This increase came as a result of an increase in the volume of oil imports, while the volume of non-oil imports remained virtually unchanged from the first to the second quarter of 2003.

Real merchandise imports and exports



Constant 1995 prices. Seasonally adjusted annualised rates

A deceleration in wholesale price inflation in South Africa's most important trading-partner countries, together with an appreciation of the rand and lower international oil prices, pushed down the *rand prices of imported goods by* about 2,0 per cent in the second quarter of 2003, following a 7,5 per cent decline in the first quarter.

The prices of gold, non-gold commodities, other merchandise and non-factor services exported receded somewhat more than the prices of imported goods and services, resulting in a slight deterioration in South Africa's terms of trade in the second quarter of 2003.

An increase in payments for services rendered by non-residents as well as higher interest payments on government's foreign debt in the second quarter of 2003, were almost offset by a higher level of service and income receipts from the rest of the world. Larger income receipts, particularly dividend receipts from non-residents, weighed positively on the overall balance of the net service, income and current transfer account, which only widened by R1 billion from R38,8 billion in the first quarter of 2003 to R39,9 billion in the second quarter. The shortfall on the services account has been fluctuating around these levels since the fourth quarter of 2002.

Financial account

During the second quarter of 2003, net financial inflows into the economy substantially exceeded net outflows to record the highest quarterly surplus ever registered on the financial account of the balance of payments. In the second quarter of 2003 the surplus on the *financial account of the balance of payments* amounted to R28,3 billion, after a deficit of R4,2 billion had been recorded in the first quarter. Relative to gross domestic product, net capital flows changed from a deficit of about 0,4 per cent to a surplus of 2,4 per cent over the same period. The abrupt turnaround in net capital flows from the first quarter to the second quarter of 2003 can mainly be ascribed to a reversal of portfolio investment flows. While portfolio investment inflows usually have positive effects on the economy, the volatility of this type of investment holds inherent dangers if this should become the principal source of funding of current-account deficits.

Net financial transactions not related to reserves
R billions

	2002				2003	
	2nd qr	3rd qr	4th qr	Year	1st qr	2nd qr
Change in liabilities						
Direct investment	4,8	2,1	-0,7	7,9	0,2	0,6
Portfolio investment	15,7	-12,9	-1,8	5,4	-6,5	22,4
Other investment	-3,6	-3,9	-7,7	-1,1	-5,8	3,3
Change in assets						
Direct investment	5,3	2,3	-2,2	4,2	-0,1	0,7
Portfolio investment	-1,6	-0,8	-1,2	-9,7	-0,4	0,2
Other investment	-1,0	3,2	10,3	12,0	2,4	-2,3
Total financial transactions*......	21,5	-0,2	0,6	33,5	-4,2	28,3

* Including unrecorded transactions

Foreign-owned assets in South Africa

Foreign direct investment flows into South Africa recorded an inflow of R0,6 billion in the second quarter of 2003 compared to an inflow of R0,2 billion in the first quarter of 2003. While during the second quarter a domestic technology company acquired the foreign interest in another resident company, this reduction in foreign liabilities was overshadowed by an increase in foreign direct investment liabilities.

Portfolio investment flows into South Africa changed from an outflow of R6,5 billion in the first quarter of 2003 to an inflow of no less than R22,4 billion in the second quarter. Foreign portfolio investors became net buyers of both domestic shares and bonds during the quarter, and the National Treasury issued a new international bond to the value of €1,25 billion in the international capital markets.

Other foreign investment into South Africa amounted to R3,3 billion in the second quarter of 2003, compared to an outflow of R5,8 billion in the first quarter. During the second quarter of 2003 non-residents increased both their rand and foreign-currency denominated deposits with domestic banks.

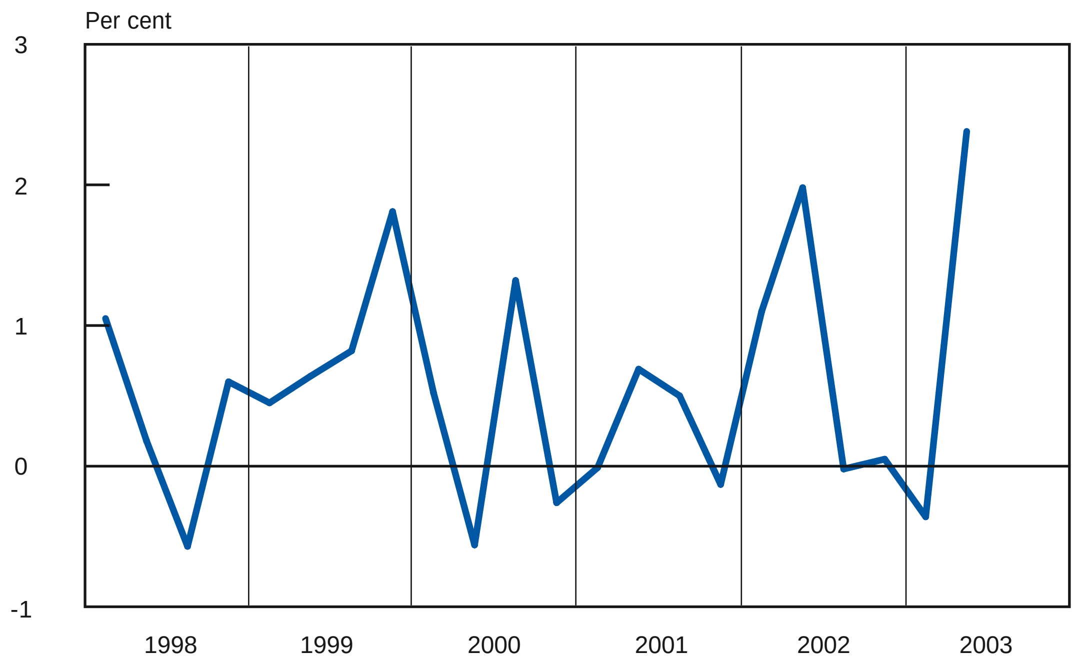
South African-owned assets abroad

Outward direct investment was reversed from an outflow of R0,1 billion during the first quarter of 2003 to an inflow of R0,7 billion during the second quarter. South African companies continued to expand abroad, but in the second quarter the repatriation of profits from affiliated companies more than neutralised this outflow.

Portfolio investment by South African entities abroad changed to an inflow of R0,2 billion during the second quarter of 2003, compared to an outflow of R0,4 billion in the first quarter. While South African individuals continued to diversify their portfolios, one institutional investor repatriated funds previously invested abroad. This could be a symptom of the lacklustre performance of foreign investment markets, as well as expectations that the exchange value of the rand would appreciate further.

Other outward investment from South Africa changed from an inflow of R2,4 billion in the first quarter of 2003 to an outflow of R2,3 billion in the second quarter. The largest contributing factor to this outflow in the second quarter of 2003 was an increase in rand-denominated deposits of domestically domiciled banks with foreign banks.

Net financial transactions not related to reserves as percentage of gross domestic product*



* Including unrecorded transactions

Foreign debt

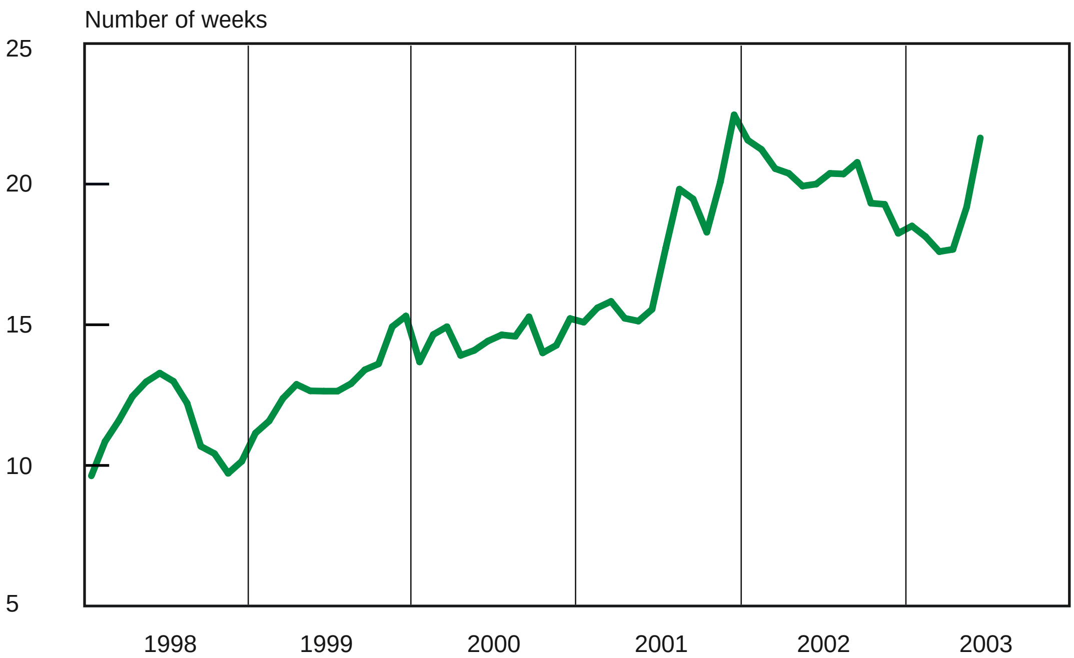
South Africa's total outstanding foreign debt decreased from US$32,7 billion at the end of December 2002 to US$31,7 billion at the end of March 2003. This decrease could be ascribed to a decline in foreign-currency denominated debt while rand-denominated debt remained unchanged.

Foreign reserves

The surplus on the financial account during the second quarter of 2003 more than compensated for the deficit on the current account of the balance of payments. Accordingly, South Africa's net international reserve position rose by R22,5 billion during the second quarter of 2003, following a decrease of R5,4 billion in the first quarter.

The value of the country's gross gold and other foreign reserves increased from US$14,9 billion at the end of March 2003 to US$18,5 billion at the end of June. The level of import cover (i.e. the value of gross international reserves expressed in relation to the value of imports of goods and services) increased from 17½ weeks' worth at the end of March 2003 to 20 weeks' worth at the end of June. Expressed in US dollars, the Reserve Bank's gross international reserves remained broadly unchanged at around US$7,7 billion from the end of March to the end of July 2003.

Imports covered by reserves



The Reserve Bank's net open foreign-currency position (i.e. the Bank's oversold forward position in foreign currency reduced by its net holdings of spot international reserves) changed from an oversold position of US$1,2 billion at the end of March 2003 to a positive position of US$0,9 billion at the end of July. On 9 May 2003 the

National Treasury announced the launch of a €1,25 billion 10-year global bond. The proceeds of this bond were utilised to close the net open foreign-currency position of the Reserve Bank, which at its earlier high oversold levels has been regarded by many analysts as a sign of weakness and vulnerability to exchange rate shocks.

Exchange rates

Despite a brief depreciation in January 2003, the nominal effective exchange rate of the rand appreciated by 7,5 per cent from the end of December 2002 to the end of March 2003. This positive trend continued in the second quarter of 2003 with the nominal effective exchange rate on balance appreciating by 4,4 per cent from the end of March to the end of June 2003. During April alone the nominal effective exchange rate appreciated by 10,2 per cent, coinciding with aggressive buying of South African fixed-interest and equity securities by non-residents. This recovery in the rand was underpinned by the continued weakness of the US dollar against various international currencies. South Africa further distinguished itself from other emerging-market countries when Standard & Poor's and Fitch Ratings upgraded South Africa's foreign and local currency sovereign debt ratings in early May 2003 and assigned a stable outlook to the country.

The consistent reduction in the Reserve Bank's net oversold forward position from the beginning of 2003 also supported the rand. From the end of June to the end of August 2003 the nominal effective exchange rate strengthened by 3,3 per cent. Over the same period the rand appreciated by 5,6 per cent, 4,9 per cent and 0,7 per cent against the euro, British pound and the US dollar respectively, while depreciating by 1,8 per cent against the Japanese yen.

Exchange rates of the rand

Percentage change

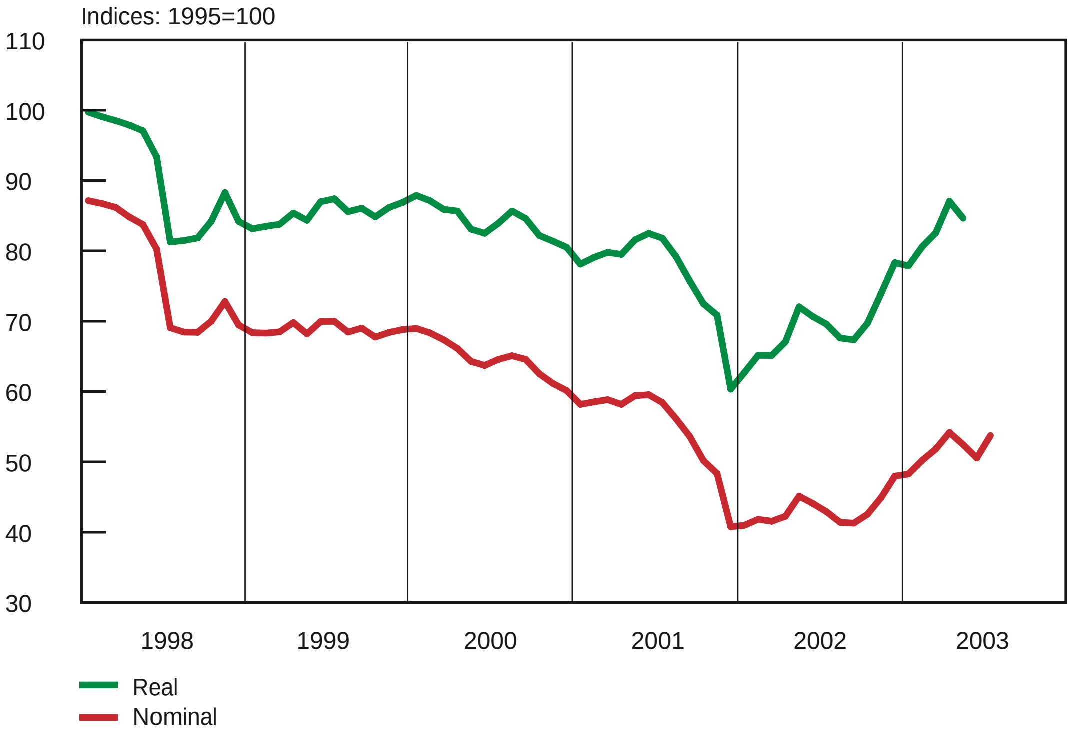
	31 Dec 2002 to 31 Mar 2003	31 Mar 2003 to 30 Jun 2003	30 Jun 2003 to 29 Aug 2003
Weighted average*	7,5	4,4	3,3
Euro	4,8	2,3	5,6
US dollar	8,9	7,6	0,7
British pound	11,0	2,9	4,9
Japanese yen	9,0	8,6	-1,8

* The weighted exchange rate is calculated with reference to a basket of 13 currencies consistently excluding Zimbabwe

The net average daily turnover in the domestic market for foreign exchange rose from US$8,1 billion in the second quarter of 2002 to US$8,4 billion in the first quarter of 2003 before increasing to a buoyant level of US$9,9 billion in the second quarter of 2003. Foreign exchange swap transactions constituted 69 per cent of total turnover in the second quarter. Non-resident participation in this market increased from US$4,6 billion per day in the second quarter of 2002 to US$5,2 billion and US$6,2 billion in the first and second quarters of 2003, respectively.

The inflation-adjusted effective exchange rate of the rand appreciated by 8,1 per cent from December 2002 to May 2003, after recovering by 29,8 per cent from December 2001 to December 2002.

Effective exchange rates of the rand*



* Consistently excluding Zimbabwe dollar

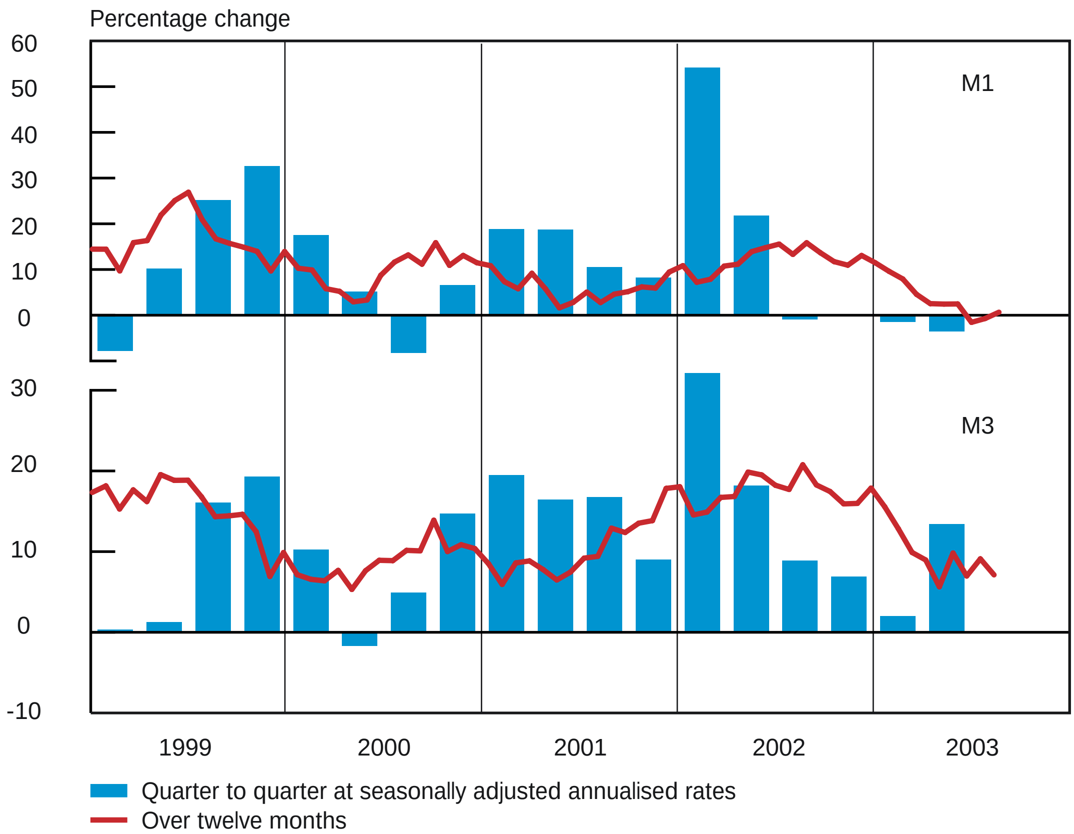
Monetary developments, interest rates and financial markets

Money supply

Having receded to a very low level during the first quarter of 2003, growth in the broadly defined money supply rebounded during the second quarter. The quarter-to-quarter seasonally adjusted and annualised growth rate in M3 accelerated from 2,3 per cent in the first quarter of 2003 to 13,1 per cent in the second quarter. An unseasonally low value of M3 at the end of March and an exceptionally high value at the end of April were largely responsible for the divergence between these successive quarterly growth rates.

Having decelerated from 20,6 per cent in May 2002 to single-digit levels from January 2003, twelve-month growth in M3 lacked clear direction in the ensuing months but remained below the 10 per cent level, as illustrated in the accompanying graph. In July 2003 it amounted to 7,2 per cent. The subdued twelve-month growth in M3 was related to the marked reduction in inflation and slowdown in growth in real production and income. In turn, these reflected the effects of the recovery in the exchange rate, weak global demand and the relatively tight monetary policy stance. As a short-term factor, a build-up in government deposits also compressed the growth in M3 during May and June 2003.

Monetary aggregates



During the first two quarters of 2003, fixed and notice deposits with maturities of six months or less rose fairly briskly. Accordingly, the quarter-to-quarter seasonally adjusted and annualised growth rate in M2 accelerated from 7,3 per cent in the first quarter of 2003 to 16,5 per cent in the second quarter. Considerable uncertainty in the financial markets, and relatively attractive interest returns on the holdings of these types of deposits probably supported the precautionary and speculative demand for such deposits.

Conversely, the growth trend displayed by the narrow monetary aggregates – M1A and M1 – largely reflected the lacklustre conditions in the real economy. The quarter-to-quarter and seasonally adjusted and annualised growth rate in M1A amounted to a negative 0,4 per cent in the first quarter of 2003 and a very low positive growth rate of 0,8 per cent in the second quarter. M1 contracted at annualised rates of 1,5 per cent in the first quarter of 2003 and 3,6 per cent in the second quarter. Growth trends in these aggregates were aligned to the deceleration in price inflation and slower growth in domestic production and income. Furthermore, the expectation of imminent reductions in short-term interest rates probably encouraged investors to shift funds from call and overnight accounts to somewhat longer maturities in order to protect their interest returns.

Growth in M3 during the second quarter of 2003 was concentrated in the bank deposits of the private corporate sector, in particular non-financial companies. The household sector contributed approximately one third to the total increase in M3 during the second quarter of 2003 – equivalent to an increase of R11 billion in household deposits. The increase in household deposits could partly be attributed to individuals' rising income on account of tax relief and higher salaries and wages. This probably spilled over into the demand for money.

The quarter-to-quarter annualised growth in nominal gross domestic product exceeded the growth in M3 by 1,1 percentage points in the first quarter of 2003. This was reversed in the second quarter when the growth in M3 exceeded the growth in nominal gross domestic product by 11,0 percentage points. The income velocity of circulation of M3 accordingly decreased from 1,75 in the first quarter of 2003 to 1,71 in the second quarter. With the income velocity of circulation of M3 at low levels there seemed to be more than sufficient liquidity to finance expenditure in the economy.

The M3 money supply increased by R33,0 billion from the end of the first quarter of 2003 to the end of the second quarter. Accounting counterparts to the change in M3 were increases of R26,4 billion in net foreign assets, R13,4 billion in banks' claims on the private sector and R0,4 billion in banks' net claims on the government sector. These increases in the counterparts of the change in M3 were partly offset by a contraction of R7,2 billion in "net other assets and liabilities".

Counterparts of change in M3

R billions

	1st qr 2003		2nd qr 2003	
Net foreign assets		-3,7		26,4
Net claims on the government sector		-18,8		0,4
Gross claims	-7,7		16,6	
Government deposits (+decrease; -increase)	-11,1		-16,2	
Claims on the private sector		77,3		13,4
Net other assets and liabilities		-62,2		-7,2
Total change in M3		-7,4		33,0

Net foreign assets were positively affected by the inflows recorded on the financial account of the balance of payments during the second quarter and by the relaxation of the endowment capital definition which came into effect on 1 May 2003. The new dispensation allows South African branches of foreign banks to invest offshore up to 40 per cent of deposits raised domestically.

During the second quarter of 2003, net claims on government were distorted to some extent by the requirement to report on a gross basis and mark-to-market assets and liabilities arising from repurchase agreements. In light of the fact that such agreements normally involve government securities, this resulted in an increase in claims on the government sector, thus giving an impression of increased funding needs by government when it was not actually the case. Conversely, government deposits increased substantially mainly on account of the proceeds from a successful bond issue abroad and a build-up in deposits in preparation for repayment of a foreign loan in July and high coupon interest payments in August.

Credit extension

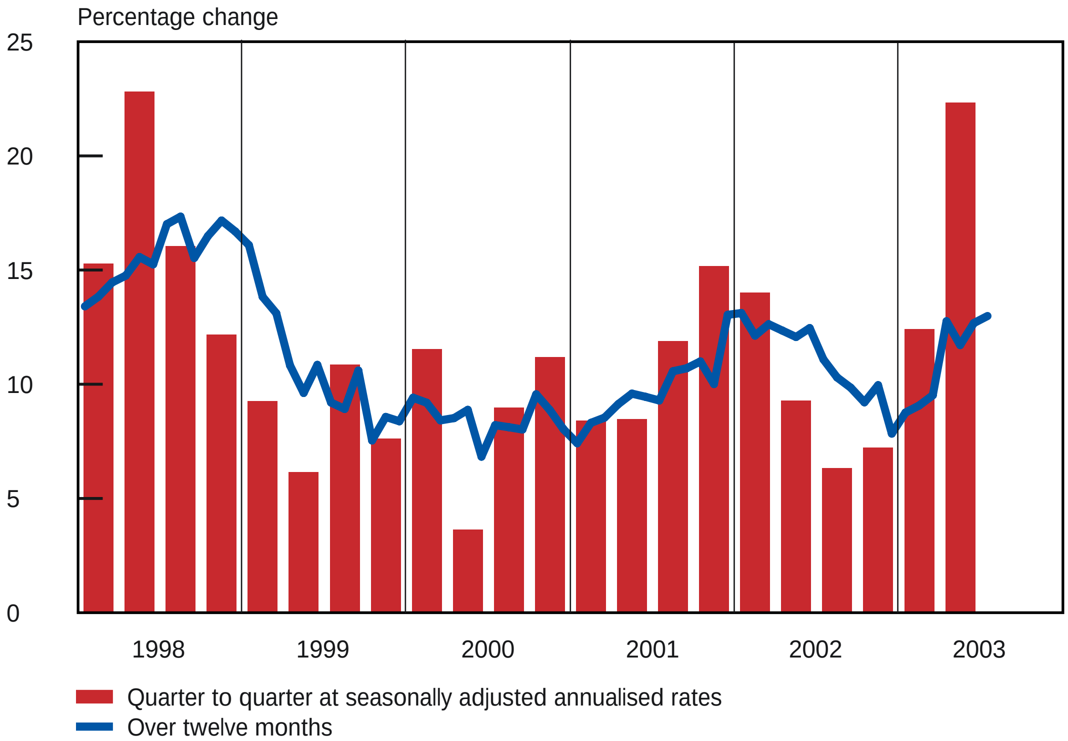
Twelve-month growth in the monetary sector's claims on the domestic private sector accelerated from 4,4 per cent in December 2002 to 18,1 per cent in July 2003, with a large part of the acceleration occurring in the *investments* category of claims on the private sector. New accounting rules caused this increase in *investments*. The analysis in the following paragraphs is focused on banks' *total loans and advances* – i.e. mortgage advances, instalment sale credit, leasing finance, overdrafts, credit card and general advances (with the last three categories together known as *other loans and advances* in the Reserve Bank's analyses). In this way the statistical aberration introduced through the *investments* category is avoided.

Growth in banks' *total loans and advances* to the private sector decelerated during 2002 responding to, amongst other things, the higher level of short-term interest rates. However, quarter-to-quarter growth turned around and started accelerating as early as the fourth quarter of 2002 – well ahead of the first reduction in the Reserve Bank's repurchase rate. Quarter-to-quarter growth in loans and advances accelerated from annualised rates below 10 per cent during the last three quarters of 2002 to 12,4 per cent in the first quarter of 2003 and further to 22,3 per cent in the second quarter – a growth rate comparable to the recent peak value of 22,8 per cent recorded in the second quarter of 1998. The *other loans and advances* category in particular registered high growth rates in both these episodes.

Measured over twelve months, growth in banks' *total loans and advances* also picked up, accelerating from low growth rates of around 9 per cent in the first three months of 2003 to levels around 12 per cent in subsequent months. It amounted to 13,0 per cent in July 2003. These firm growth rates in credit extended to the private sector suggest a more favourable environment for bank lending. This was partly a reflection of improved creditworthiness amongst economic participants on account of their relatively strong balance sheets. This was underpinned by well-contained debt levels and the prolonged bull market in real estate and associated positive wealth effects. Purchases inspired by salary and wage increases and expectations of lower short-term interest rates could also have encouraged the demand for credit.

A disaggregated analysis of banks' claims on the private sector by type of credit indicates that a large share of credit extension during the second quarter of 2003 was in the form of other loans and advances to the corporate sector. This is consistent with the continued growth in fixed capital formation and increased tempo of inventory accumulation.

Total loans and advances to the private sector



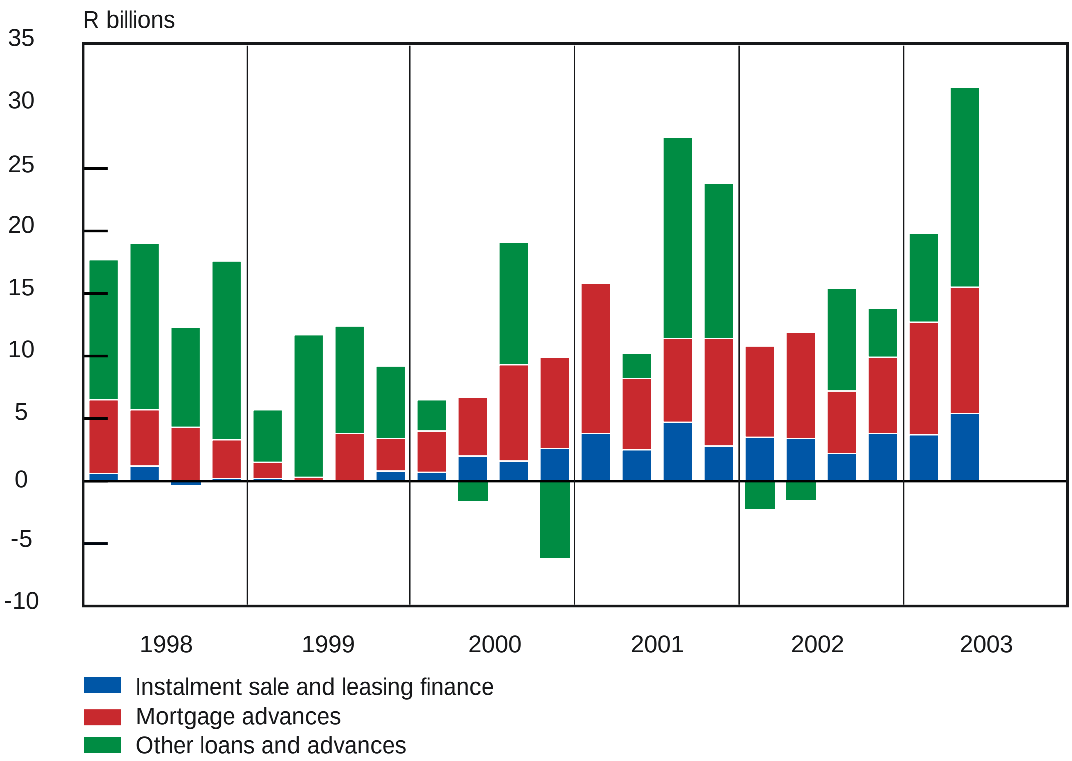
Growth in *mortgage advances* held up well during the second quarter of 2003, contributing R10,1 billion to the overall increase in total loans and advances to the private sector compared to a contribution of R9 billion in the first quarter. These strong growth rates in mortgage advances reflect, amongst other things,
- re-advances based on the accrual of homeowners' equity arising from the increases in house prices since late 1999; and
- strong demand for new home loans, as mirrored by the brisk pace of transactions in real estate evidenced by the growth in transfer duty paid.

Funds accessed through the *instalment sale* and *leasing finance* credit categories are normally directed at financing expenditure on durable goods. Reflecting reasonably strong consumer demand and brisk capital formation, the twelve-month growth in *instalment sale* and *leasing finance* credit fluctuated between 13,4 per cent and 15,4 per cent during the first seven months of 2003. This line of business was still skewed towards financing the acquisition of used cars. The contributions of used and new motor vehicle financing during the second quarter of 2003 amounted to 31 per cent and 22 per cent, respectively. Financing of trucks, buses and pickups contributed a further 21 per cent to total instalment sale and leasing finance outstanding. New business payouts of such credit increased from R16,9 billion in the first quarter of 2003 to a record high R19,3 billion in the second quarter.

The *other loans and advances* category is composed of overdrafts on current accounts, credit card advances and general advances to the private sector.

Companies in particular make use of overdrafts on current-account and general advances. Historical data indicate that *other loans and advances* tend to increase more rapidly during periods of high exchange rate volatility, probably as companies borrow for hedging or speculative purposes.

Contributions to quarter-to-quarter changes in total loans and advances to the private sector



Contributions to total loans and advances to the private sector by type of credit
Per cent of total

		30 June 2003
Mortgage advances..		42,7
Instalment sale credit and leasing finance..		16,4
Other loans and advances..		40,9
Overdrafts	*14,6*	
General advances..	*24,1*	
Credit card advances	*2,2*	
Total..		100,0

The recent acceleration in the twelve-month growth rate of *other loans and advances* from 3,2 per cent in December 2002 to 13,8 per cent in July 2003 could be on account of a combination of:

- importers taking advantage of the strong recovery in the exchange rate of the rand and the lower level of interest rates, speeding up payment for their import commitments;

- the financing requirements associated with the further build-up in inventories and expansion of gross fixed capital formation; and
- exporters resorting to the use of credit as working capital, following pressure exerted on their profit margins by reduced price competitiveness and a slowdown in global demand.

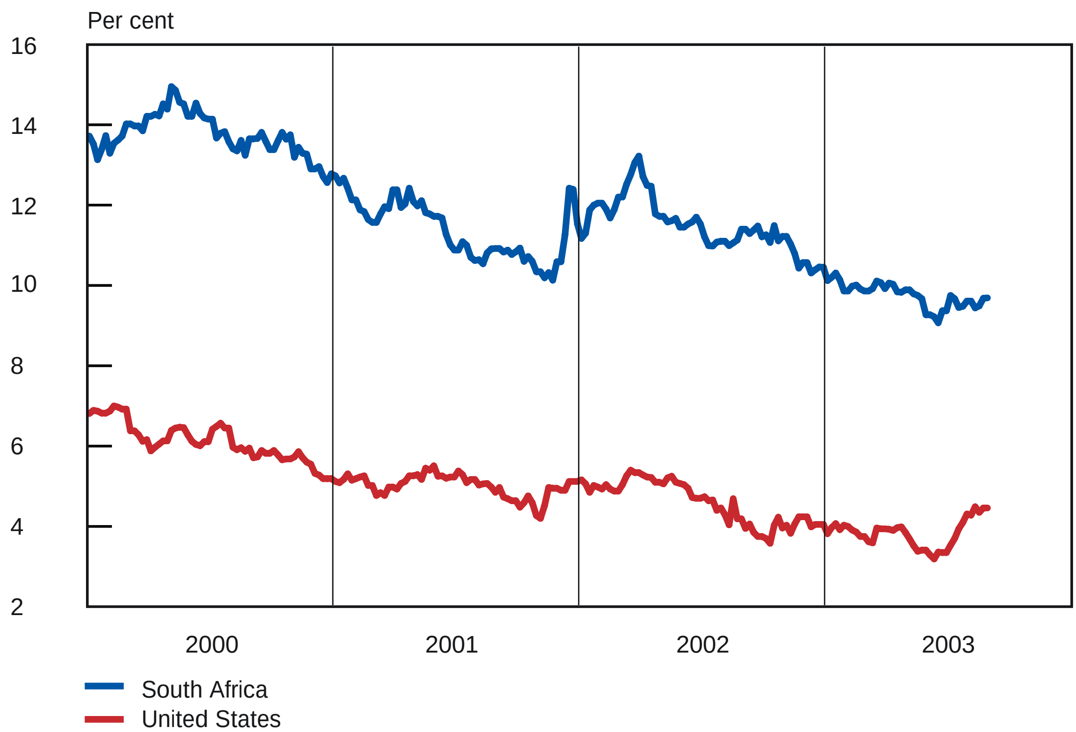
The monetary sector's *total loans and advances* to the private sector increased by R31,4 billion in the second quarter of 2003 compared with R19,7 billion in the first quarter. In contrast with the first quarter, when households absorbed the largest part of the increase, the corporate sector absorbed almost 80 per cent of the total increase in the second quarter.

Interest rates and yields

The downward movement in bond yields, which started in March 2002 in the wake of the sustained appreciation in the exchange value of the rand, started bottoming out soon after the first lowering of the Reserve Bank's repurchase rate in June 2003. Despite further monetary policy easing in August, domestic bond yields edged gently upward to the end of August as bond yields in some of the major economies also started picking up from their very low levels.

The *monthly average yield on long-term government bonds* declined from 12,6 per cent in March 2002 to 9,3 per cent in June 2003 as it followed in the footsteps of the appreciating rand and improved near-term inflation prospects, supported by the release by Statistics South Africa of significantly lower revised inflation numbers on 30 May. Such low yields were previously experienced in 1980. The reduction of 150 basis points in the repurchase rate to 12,0 per cent on 13 June 2003 contributed to a further small decline in long-term bond yields.

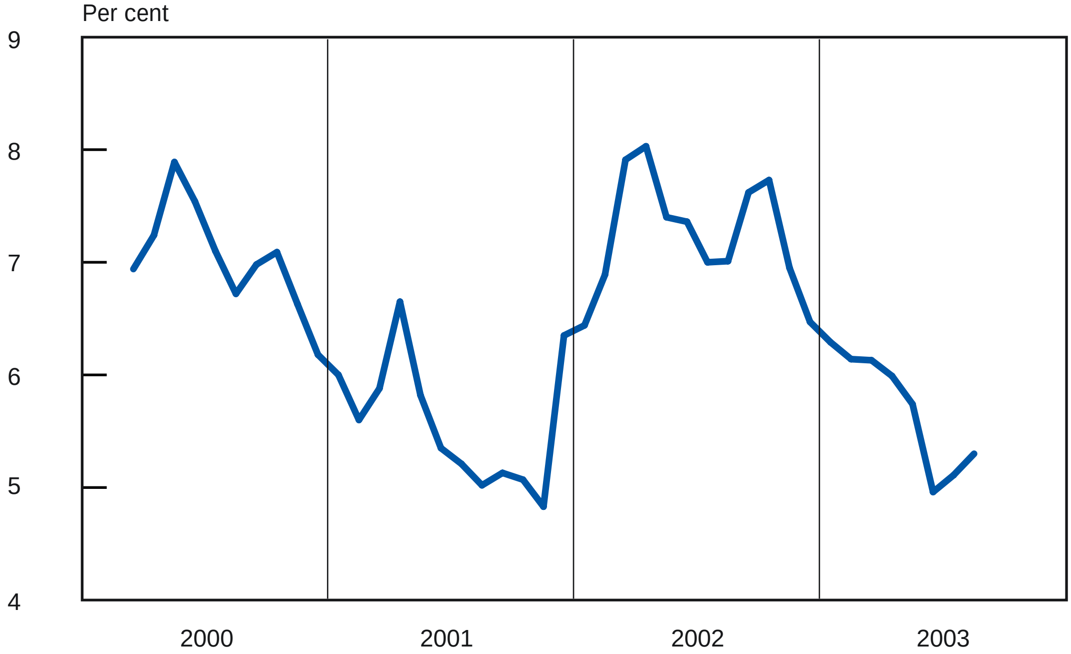
Yields on long-term government bonds



Discounting the improved outlook for inflation and associated near-term reduction in the repurchase rate, the *daily average yield* on R157 government bonds (with redemption dates ranging from 2014 to 2016) declined by 51 basis points from 9,58 per cent at the end of May 2003 to 9,07 per cent on 17 June. The daily bond yield then retraced upwards to 9,75 per cent on 16 July 2003 on account of a weaker exchange rate, before again declining to 9,43 per cent on 11 August. Following the lowering of the repurchase rate on 15 August the daily bond yield on balance increased to 9,69 per cent at the end of August. The monthly average yield on long-term government bonds reached 9,6 per cent in both July and August. The bottoming out in the bond market rally from June to August could be ascribed to, amongst other things, the sensitivity of the bond market to:

- views that the previous vigour of the rally would not be sustainable;
- national government's increased recourse to funding in the domestic bond market for fiscal 2003/04, following two years of net redemptions;
- unease surrounding inflation prospects, following the announcements in July and August of higher-than-expected production and consumer (CPIX) price inflation, respectively;
- fluctuations in the value of the rand;
- net sales of bonds by non-residents during July and August; and
- possible spill-over effects of bond rate increases and portfolio adjustments in the rest of the world as these markets reacted to tentative optimism regarding global growth.

Inflation expectations in the bond market*



* Break-even inflation rate, or difference between the nominal yield on conventional and real yield on inflation-linked bonds. Monthly averages

The interruption in the bond market rally from June 2003 is also evidenced by a bottoming out in the rate of decline in the *break-even inflation rate*. This proxy for expected long-term inflation, calculated as the difference between the nominal yield on conventional bonds and the real yield on inflation-linked bonds within the six-to-ten-year maturity range, initially decreased by 316 basis points from 7 October 2002 to 26 June 2003, shortly after the first lowering of the repurchase rate on 13 June. Inflation expectations subsequently levelled out and the break-even inflation rate increased by 64 basis points to the end of August, notwithstanding a further lowering of the repurchase rate. The level of the break-even inflation rate nevertheless stood at 5,40 per cent at the end of August, indicating expectations consistent with the inflation target range of 3 to 6 per cent.

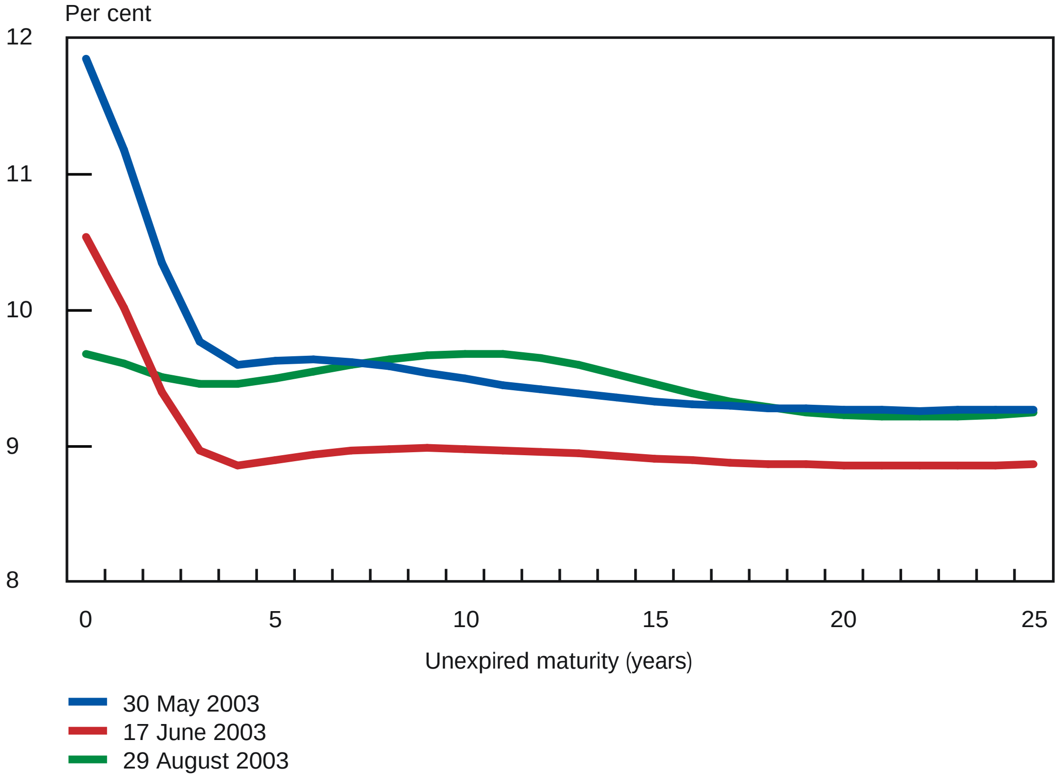
Notwithstanding the subdued sentiment most recently encountered in the bond market, the real returns on fixed-interest securities improved during the first seven months of 2003. The *real* or *inflation-adjusted yield on long-term government bonds* (using historical year-on-year increases in CPIX as an indicator of future price changes) improved from a negative value of 0,4 per cent in November 2002 to positive values from January 2003 and reached 2,8 per cent in July as the deceleration in CPIX inflation exceeded the decline in nominal bond yields. The upward trend in domestic real yields until recently contrasted with the low real yields in the United States of America and the United Kingdom, currently experiencing low inflation.

However, the yield differential in favour of South African domestic government debt became less pronounced in recent months, especially towards the shorter side of the maturity spectrum. This is reflected in a decline in the differential between nominal yields on South African government bonds in the one-to-three-year maturity range in the domestic market and in the United States market. The differential, referred to as the *currency risk premium*, narrowed by 211 basis points from May 2003 to August as short-term bond yields in the domestic market followed the reduction in the repurchase rate downwards.

The *country risk premium* on South African bonds levelled out during July and August 2003 after declining by 134 basis points from September 2002 to June 2003. At the same time the yield spread of emerging markets' sovereign debt over benchmark United States Treasury Bonds (as measured by the JP Morgan Emerging Markets Bond Index or EMBI+) continued to narrow, declining significantly by 537 basis points from September 2002 to August 2003. This was its lowest level since the emerging-markets financial crisis in 1998, despite benchmark long bond yields in the United States and United Kingdom declining to record lows. In absolute terms, the sovereign risk premium of foreign-currency denominated debt of the South African government is, however, far less than that of typical emerging-market debt.

The downward sloping *yield curve*, which persisted from April 2002 into the first half of 2003 flattened out and began to normalise following the reductions in the repurchase rate in June and August. The level of the inverted yield curve at first shifted downwards across the full maturity spectrum from the end of May to 17 June in anticipation of and in the wake of the reduction of the repurchase rate on 13 June. By the end of August, following the Reserve Bank's decision on 14 August to again lower the repurchase rate, short-term yields declined further, while long-term yields increased markedly to their levels of three months earlier. Consequently, the yield curve flattened out at the short end and became upward sloping for maturities between three and eleven years, although remaining somewhat inverted beyond eleven years. The *inverse yield gap*, i.e. the difference between bond yields at the extreme long and short ends of the yield curve, declined from 234 basis points on 10 June 2003, shortly before the first lowering of the repurchase rate, to 43 basis points at the end of August 2003, subsequent to the second reduction in the repurchase rate.

Yield curves



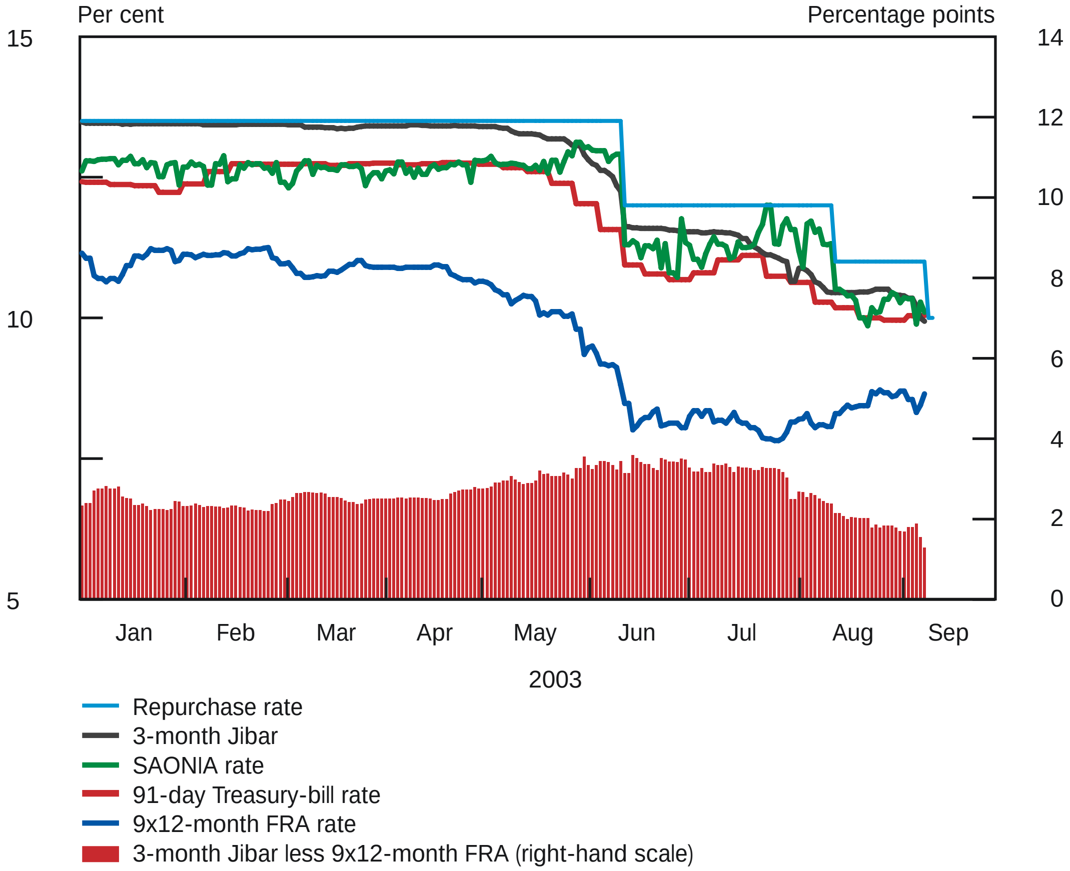
The MPC left the Reserve Bank's repurchase rate unchanged at 13,5 per cent at its March 2003 meeting. In the build-up to the June MPC meeting, lower consumer price inflation outcomes materialised, while at the production level prices actually fell back from late 2002. CPIX inflation was also driven lower by a 1,9 percentage-point downward revision following the correction of the erroneously estimated rental component of the index. Inflation expectations were favourably affected by the end of the war in Iraq with minimal damage to the oil infrastructure, and by the strong recovery of the rand.

In light of these and other factors pointing to a favourable inflation outlook, the committee lowered the repurchase rate by 150 basis points to 12 per cent on 14 June 2003 – the biggest cut since the formal targeting of inflation started in 2000. Simultaneously, the MPC announced that it had decided to increase the number of MPC meetings from four to six per annum, allowing the committee more frequent scheduled opportunities to consider the impact of new developments and, if necessary, to respond with appropriate monetary policy steps.

The 1,5 percentage-point reduction in the repurchase rate was more than the average expectation in the market and this was reflected in the movements in money-market rates. Prior to the announcement of the interest rate decision, money-market rates had generally discounted a 100-basis-point decrease in the repurchase rate. After the bigger-than-expected cut, short-term market rates declined further: For instance, the rate on 9x12-month forward rate agreements declined by 87 basis points from 9,35 per cent on 2 June 2003 to 8,48 per cent on 13 June. It declined by a further 47 basis points to 8,01 per cent on 17 June.

The increased number of MPC meetings and boldness of the repurchase rate reduction had a noticeable effect on market expectations and thus the evolution of money-market rates. Once the market had fully adjusted to the reduction in June, focus and attention turned to the August meeting. In the build-up to the meeting, movements in money-market interest rates at times suggested expectations of another reduction in the repurchase rate in excess of 100 basis points, although most market commentators and analysts assigned the highest probability to a 100-basis-point reduction.

Money-market interest rates



On 13 and 14 August the MPC met and announced a further 100-basis-point cut in the repurchase rate to 11 per cent on the basis of the committee's favourable assessment of the inflation outlook. (The MPC's statement is reproduced in full elsewhere in this *Quarterly Bulletin*.) Short-term money-market interest rates showed a very limited reaction to the 100-basis-point decline in the repurchase rate, as the rate cut was widely discounted.

Nevertheless, shortly after the August reduction in the repurchase rate, the rates on forward rate agreements rose slightly. For instance, the rate on 9x12-month forward rate agreements increased from 8,07 per cent on 14 August 2003 to 8,30 per cent on 15 August. This could possibly be seen as a correction following the repurchase rate reduction, which was slightly less than the average expectation in the market.

At a special meeting of the MPC held on 10 September it was decided to lower the repurchase rate by a further 100 basis points. This was informed by an assessment of the most recently available economic data, forecasts and surveys of expectations.

In the interbank market, the South African Overnight Interbank Average (SAONIA) rate responded to the movements in the repurchase rate and also to factors affecting interbank funding such as month-end liquidity pressures, the availability of overnight funding and changes in the required reserve balances at the beginning of each maintenance period. In response to the reduction in the repurchase rate on 13 June 2003, the SAONIA rate declined by 161 basis points to 11,30 per cent. It receded further during the remainder of June, but fluctuated upward as liquidity conditions became somewhat tighter in July. It declined by 81 basis points immediately following the decline in the repurchase rate in August – from 11,32 per cent on 14 August to 10,51 per cent on 15 August.

The 3-month Johannesburg interbank agreed rate (Jibar) declined from 12,25 per cent on 12 June to 11,62 per cent on 13 June and further to 11,60 per cent on 17 June – a total of 65 basis points. In response to the repurchase rate cut in August, it declined by 16 basis points from 10,61 per cent on 11 August to 10,45 per cent on 15 August.

Other money-market interest rates broadly followed the movements in the repurchase rate but also responded to peculiarities in their respective sub-markets. The tender rate on 91-day Treasury bills already started moving lower about five weeks before the June MPC meeting, and again about four weeks before the August meeting. The increase in the amount on offer at the weekly tender from 1 August, from R1,0 billion to R1,25 billion, had virtually no impact on the downward trend in the Treasury bill rate.

The private banks followed the reduction in the Reserve Bank's repurchase rate in June by lowering their prime overdraft rates by 150 basis points to 15,5 per cent. After the MPC’s decision in August their prime rates were reduced by a further 100 basis points to 14,5 per cent. Interest rates on mortgage loans were lowered by a similar magnitude.

Likewise, the *predominant rate on twelve-month fixed deposits with banks* was reduced from 12,0 per cent in September 2002 to 8,0 per cent in August 2003. Notwithstanding the lower nominal interest rates, real lending rates, using historical year-on-year increases in CPIX as an indicator of expected price changes, remained at high levels as inflation decelerated. The *real prime overdraft rate* of banks increased from 5,1 per cent in November 2002 to a three-year high of 8,6 per cent in June 2003, before decreasing moderately to 8,4 per cent in July. Real deposit rates initially improved as banks’ *real 12-month deposit rate* increased from 0,6 per cent in November 2002 to 3,2 per cent in April 2003, before declining to 2,0 per cent in July.

The *official rate of interest* applicable to fringe benefit taxation, as defined by the Income Tax Act, was reduced from 14,5 per cent to 13 per cent, effective from 1 July 2003. On 7July 2003 the *maximum annual finance charge rates* on money loans and credit and leasing transactions, as laid down by the Usury Act, were lowered by two percentage points to 27 per cent for amounts less than R10 000 and to 24 per cent for amounts above R10 000, but not exceeding R500 000.

The 3-month Jibar amounted to 10,51 per cent on 29 August 2003 whilst the rate on 9x12-month FRAs was 8,67 per cent. The spread between these rates of 184 basis points implied market expectations of a further decline of approximately 2 full percentage points in three-month money-market interest rates by May 2004.

Money market

Money-market conditions remained fairly stable during the second quarter of 2003 and the first two months of the third quarter. The average daily liquidity requirement of the private banks decreased slightly from R11,1 billion in May 2003 to R10,3 billion in July, but rose again to R11,1 billion in August.

The Reserve Bank participated actively in the money market and adjusted the amount of its liquidity-draining operations in such a way that it broadly offset other forces impacting on money-market liquidity. The total outstanding amount of liquidity-draining operations at the end of August amounted to R34 billion – R14,4 billion lower than at the end of April.

The breakdown by type of instrument and maturity of the outstanding amount of liquidity-draining instruments provided in the table below shows further reductions in the use of *foreign-currency swap transactions. Reverse repurchase transactions* with private-sector parties declined briefly to R9,0 billion at the end of June 2003, but quickly returned to their previous level of R10,3 billion. During July and August the Reserve Bank increased its reverse repurchase transactions with a maturity of 91 days and reduced those of 28 days. Although the total outstanding amount of *Reserve Bank debentures* was maintained at R8,0 billion since April 2003, in July and August there was also a shift from 28-day to 91-day debentures.

Outstanding balances of selected money-market intervention instruments
R billion

End of		Foreign-currency swaps with deposits	Reserve Bank debentures			Reverse repurchase agreements			Total instruments outstanding
			Total	28 days	91 days	Total	28 days	91 days	
2002:	Aug	54,8	7,2	5,4	1,8	7,0	5,3	1,7	69,0
	Sep	53,4	7,2	3,9	3,3	6,8	6,3	0,6	67,5
	Oct	51,6	7,5	4,2	3,3	8,0	7,1	0,9	67,1
	Nov	49,6	7,5	5,6	1,9	8,6	6,8	1,7	65,7
	Dec	45,3	7,7	4,7	3,0	7,6	5,1	2,5	63,6
2003:	Jan	45,3	7,6	3,9	3,7	10,5	6,4	4,1	63,3
	Feb	42,9	8,0	3,4	4,6	10,0	6,4	3,6	60,9
	Mar	34,9	7,9	4,7	3,2	10,3	5,8	4,5	53,1
	Apr	30,1	8,0	4,4	3,6	10,3	6,3	4,0	48,3
	May	27,3	8,0	5,2	2,8	10,3	7,0	3,3	45,5
	June	20,6	8,0	5,0	3,0	9,0	5,0	4,0	37,8
	July	17,6	8,0	2,4	5,6	10,3	0,5	9,8	35,9
	Aug	15,3	8,0	2,8	5,2	10,3	0,6	9,7	33,6

Several factors have influenced market liquidity in recent months in such a way as to reduce the need for liquidity-draining operations by the Reserve Bank:

- Profits realised on foreign exchange forward cover provided by the Reserve Bank helped to drain liquidity.

- On balance, changes in notes and coin in circulation outside the Reserve Bank contracted the money market by R0,6 billion during the second quarter of 2003 and a further R1,2 billion in July and August.

- The Bank in June 2003 repaid US$500 million on a syndicated gold loan facility. The Bank drew down US$1 billion on a syndicated loan facility, and delivered the net proceeds of US$500 million against the forward book, causing counter-parties to pay in rand for the foreign currency delivered and thereby draining rand liquidity.

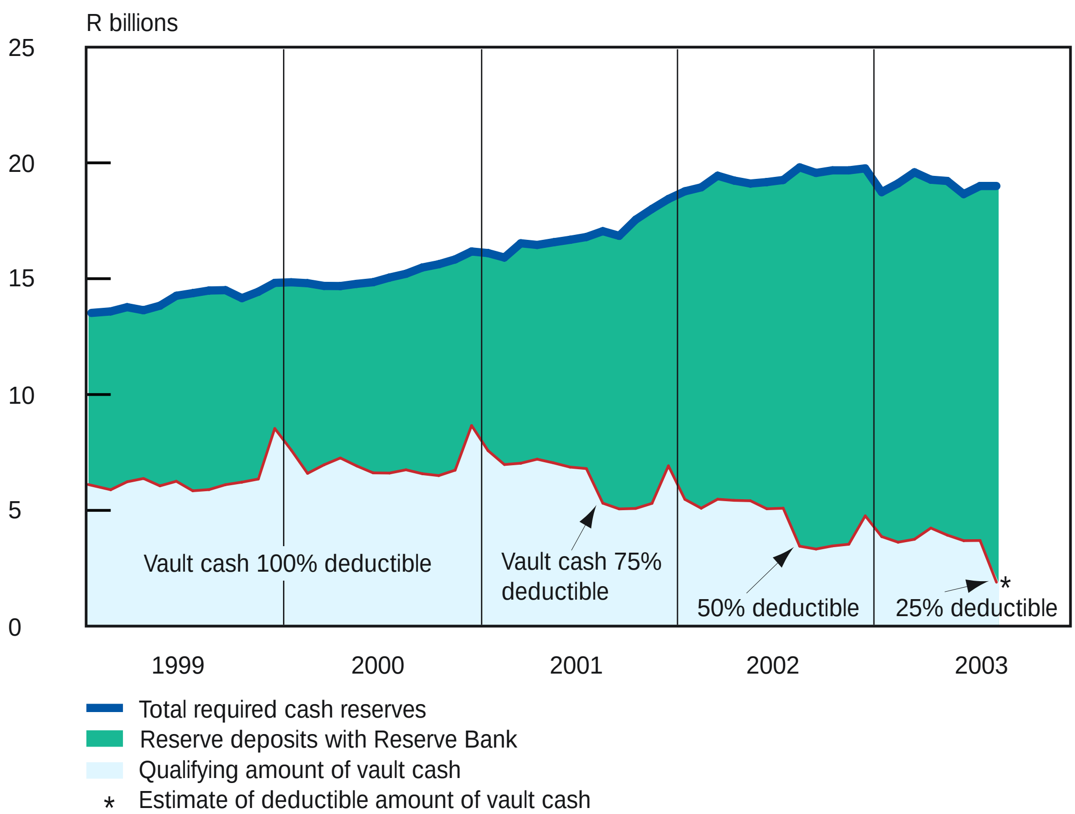
- Repayments of lender-of-last-resort assistance provided to certain banks early in 2002 also helped in draining liquidity from the market.

- In July 2003 government repaid a US$750 million foreign loan. In purchasing foreign exchange from the Reserve Bank to effect the repayment, rand liquidity was also drained.

- From the reserve maintenance period based on the August 2003 balance sheets, banks are only allowed to deduct 25 per cent of their vault cash holdings when calculating their required reserve balances with the Reserve Bank, rather than 50 per cent as before. This is set to contract money-market liquidity by approximately R1,8 billion.

As shown in the accompanying graph, banks' total required cash reserves and their cash reserve deposits with the Reserve Bank have receded slightly over most of the past year. This happened despite a sizeable increase in banks' liabilities, and was brought about because a greater proportion of their liabilities fell in the reserve-exempt category.

Banks' required holdings of cash reserves



By the end of July 2003 the stock of interest-bearing active liquidity-draining instruments issued by the Reserve Bank, at R35,9 billion, had finally fallen below the Bank's note and coin liability. The latter liability, amounting to R38,0 billion at the end of July, is not interest-bearing and is instrumental in tightening liquidity over time on account of the upward trend in the public's demand for cash.

Bond market

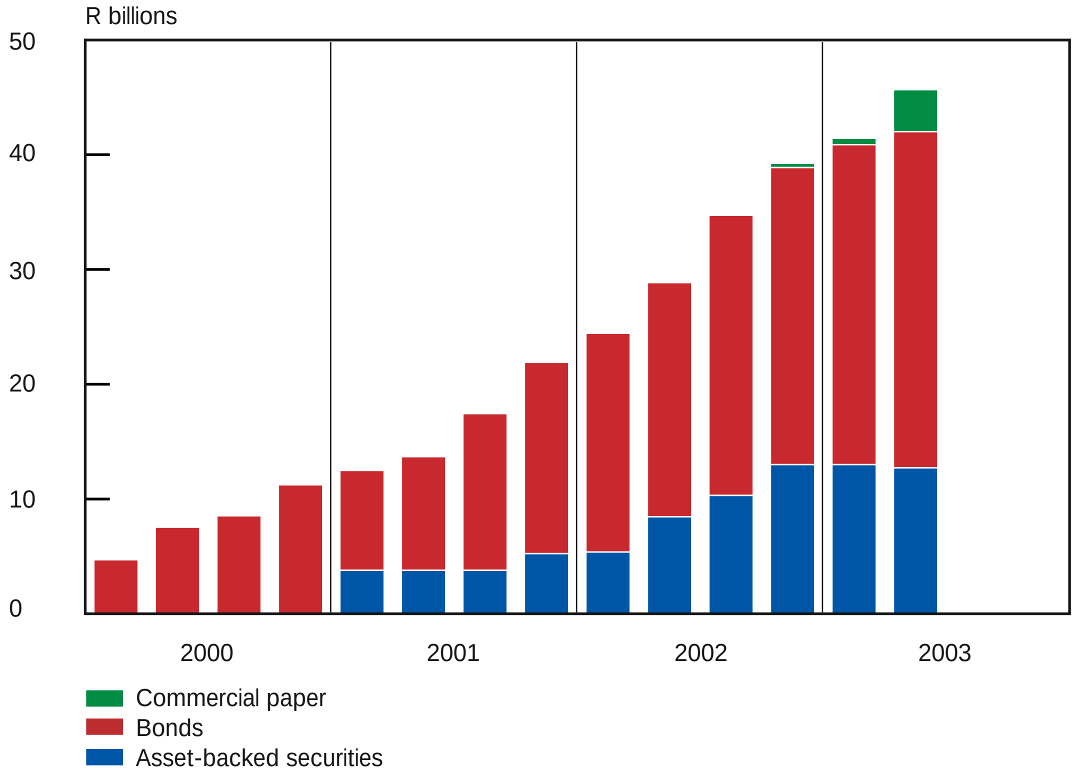
Public-sector borrowers' demand for funds in the *domestic primary bond market* increased strongly in the first months of fiscal 2003/04. Following two years of net redemptions, *national government* raised R16,9 billion from April 2003 to July, compared to a budgeted domestic funding requirement of R9,3 billion in fiscal 2003/04. Redemptions to the amount of R26,4 billion, however, fall due towards the end of the current fiscal year. National Treasury issued a new ultra-long dated inflation-linked bond, the R202, with a real coupon rate of 3,45 per cent and a maturity of 30 years, on 15 August. The new issue is in accordance with National Treasury's objective of developing an inflation-linked bond yield curve; inflation-linked bonds now cover the five, ten, twenty, and thirty-year intervals of the yield curve. The auction for R400 million, of which R220 million was allotted, followed soon after a R1 billion nominal value auction of the existing inflation-linked R197 bond on 1 August 2003. Since the introduction of inflation-linked bonds in March 2000, the nominal value of the amount in issue has increased to R23 billion at the end of August 2003, comprising approximately 5 per cent of total outstanding marketable domestic government bonds.

National government raised R10,6 billion through a foreign-currency denominated debt issue in the *international bond market* during May 2003. The issuance of the ten-year €1,25 billion global bond fulfilled the bulk of the government's foreign financing needs for fiscal 2003/04. Public corporations have refrained from foreign funding since the public utility company, Eskom, raised R2 billion through the issuance of a three-year eurobond in October 2002, replacing a maturing bond.

In the international bond market interest in rand-denominated bonds remained limited and the scheduled redemptions of rand-denominated bonds issued by non-residents in the *European bond markets* exceeded new issues by R2,0 billion during the first eight months of 2003, substantially exceeding the net redemptions of R1,4 billion for the whole of 2002. South African borrowers similarly abstained from the eurorand bond market since June 2002 when liabilities were reduced to the net amount of R0,2 billion.

After rapid growth in 2002, the issuance of fixed-interest securities in the *primary corporate bond market* slowed down during the course of 2003 as companies utilised alternative sources of financing. The outstanding nominal value of private-sector loan stock listed on the Bond Exchange of South Africa increased modestly from R38,9 billion in December 2002 to R43,8 billion in August 2003. A preference for short-term funding through the issuance of commercial paper counteracted the slowdown in private-sector corporate bond issuance from the beginning of 2003. After the first commercial paper listing of asset-backed notes on the Bond Exchange of South Africa in December 2002, the outstanding nominal value of commercial paper has increased to R4,2 billion in August 2003. Currently, the commercial paper listings comprise entirely of asset-backed notes.

Private-sector funding in the interest-bearing securities markets

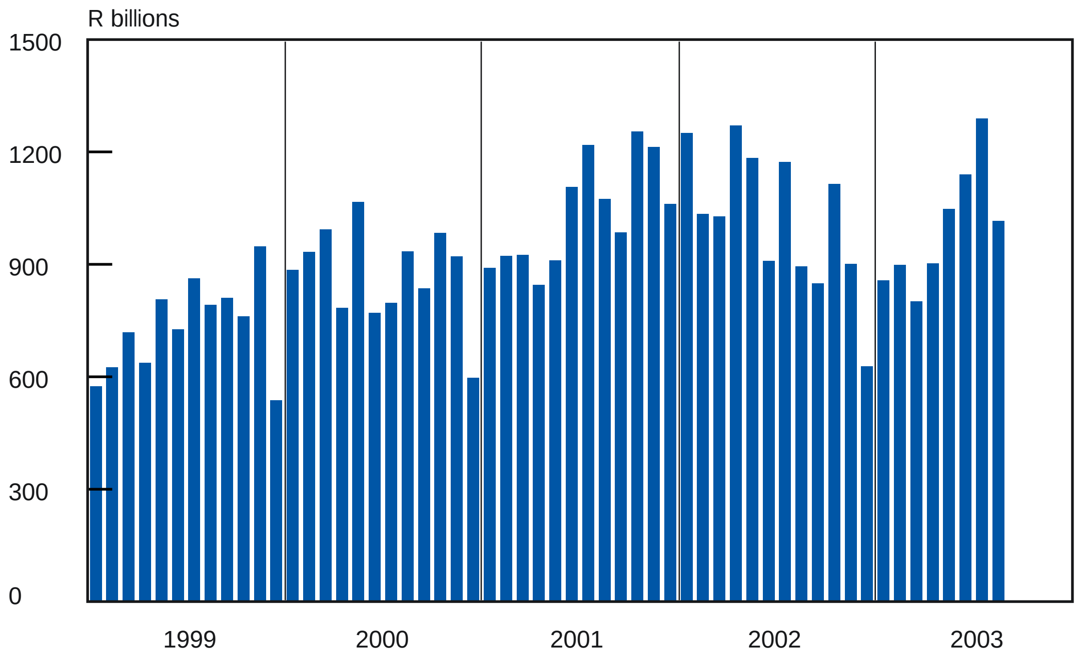


The rapid growth in asset-backed securitisation and collateral debt obligations was aided by the amended banking regulations for asset securitisation published in December 2001. This market effectively transforms non-marketable assets into tradeable securities. The outstanding nominal value of these securities increased from R5,3 billion at the end of 2001 to R13,4 billion at the end of 2002 and further to R17,7 billion at the end of August 2003, and includes a diverse range of assets, such as mortgage-backed securities, collateralised debt obligations and the already mentioned commercial paper.

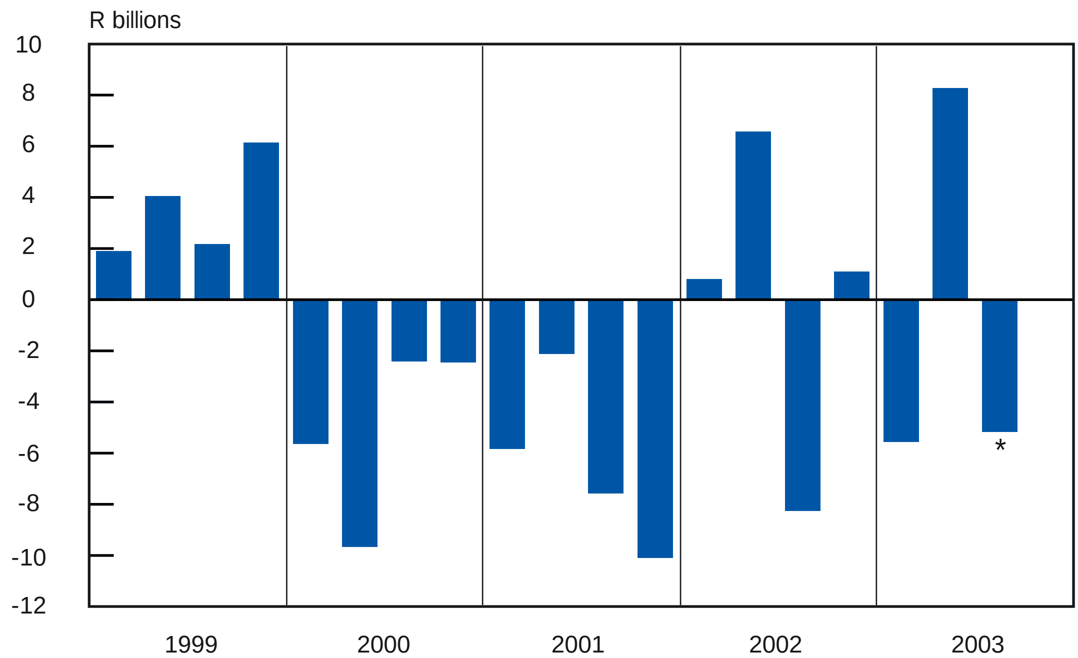
Trading activity in the *secondary bond market* improved markedly from April 2003 as investors started to anticipate a relaxation in monetary conditions. This followed the slowdown in trade during 2002 as bond prices gradually rose in an environment of declining yields and an appreciating exchange value of the rand. Turnover declined from a record R3,5 trillion in the last quarter of 2001, at the height of the exchange rate depreciation, to R2,6 trillion in the first quarter of 2003. Turnover on the Bond Exchange of South Africa subsequently improved to R3,1 trillion in the second quarter of 2003, boosted by increased trade in short-dated bonds preceding the repurchase rate reduction in June. In anticipation of further monetary policy easing, the value of bonds traded reached a monthly record of R1,3 trillion in July, before slowing to R1,0 trillion in August 2003.

Supported by improvements in South Africa’s foreign credit ratings by international ratings agencies, *non-resident investors*’ appetite for South African bonds was stimulated in the second quarter of 2003, turning them into net purchasers of bonds to the amount of R8,3 billion. This was reversed in July and August and net sales of R5,2 billion by non-residents during this period contributed to cumulative net sales of bonds amounting to R2,5 billion for the year to date. The recent selling of bonds by non-residents coincided with a global increase in bond yields in anticipation of continued sizeable fiscal deficits and an improvement in global growth.

Turnover in the secondary bond market



Net purchases by non-residents in the secondary bond market



* July and August 2003

Share market

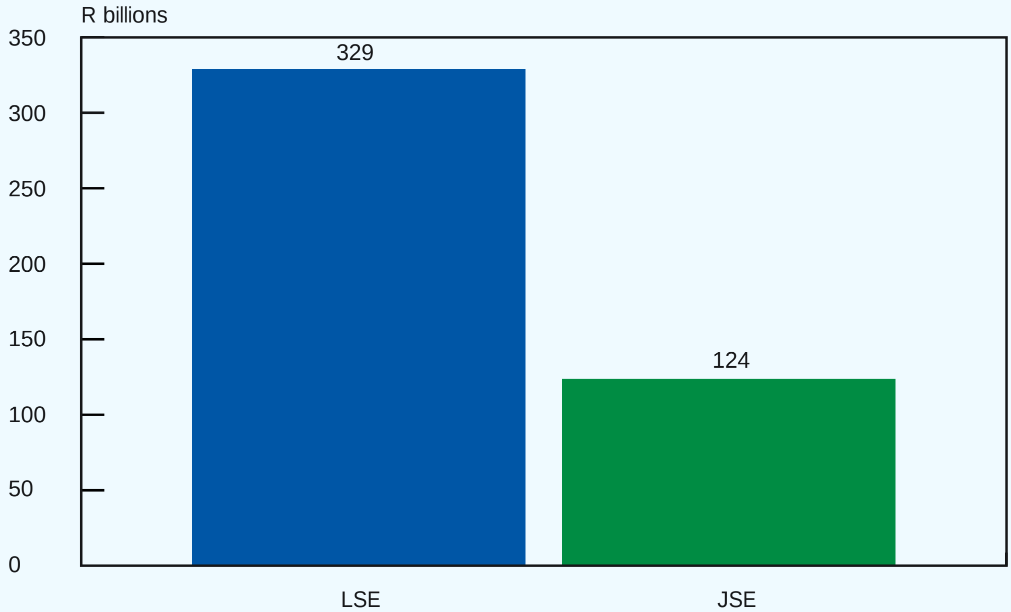
After increasing strongly in 2002, the total value of equity capital raised in the domestic and international *primary share markets* by companies listed on the JSE Securities Exchange SA declined sharply from R28,1 billion in the third quarter of 2002 to only R2,2 billion in the second quarter of 2003. Geopolitical risks and disappointing domestic and international share market returns discouraged equity financing. Optimism improved moderately from May 2003 as the outlook for the global economy improved and the war in Iraq ended with less damage than feared. Capital raised in the first eight months of 2003 of R12,8 billion was, however, still less than a third of the R47,6 billion raised during the same period in 2002.

Where are dual-listed companies' shares traded?

Several large companies which were established in South Africa currently have dual listings of their shares, with primary listings abroad and secondary listings in South Africa. The six dual-listed companies with primary listings on the London Stock Exchange are Anglo American plc, BHP Billiton plc, Dimension Data Holdings plc, Old Mutual plc, SABMiller plc and Investec plc. The volume of trading on the London Stock Exchange of these companies' shares overwhelmed trade in their shares on the JSE Securities Exchange SA. During the first eight months of 2003 trading in these shares in London was on average two and a half times as high as in Johannesburg. Previously, the ratio of trade in these shares on the London Stock Exchange, compared to their trade on the JSE Securities Exchange SA, increased from an average of 1,9 in 2000 to 2,6 in 2001 and 2,5 in 2002.

The higher liquidity of these shares on the London Stock Exchange is to the detriment of turnover on the JSE Securities Exchange SA and non-resident portfolio investment in the South African market. International investors are attracted to markets with higher liquidity, which tends to reinforce the turnover advantage of the London market.

Dual-listed companies: Value of shares traded by exchange, January to August 2003



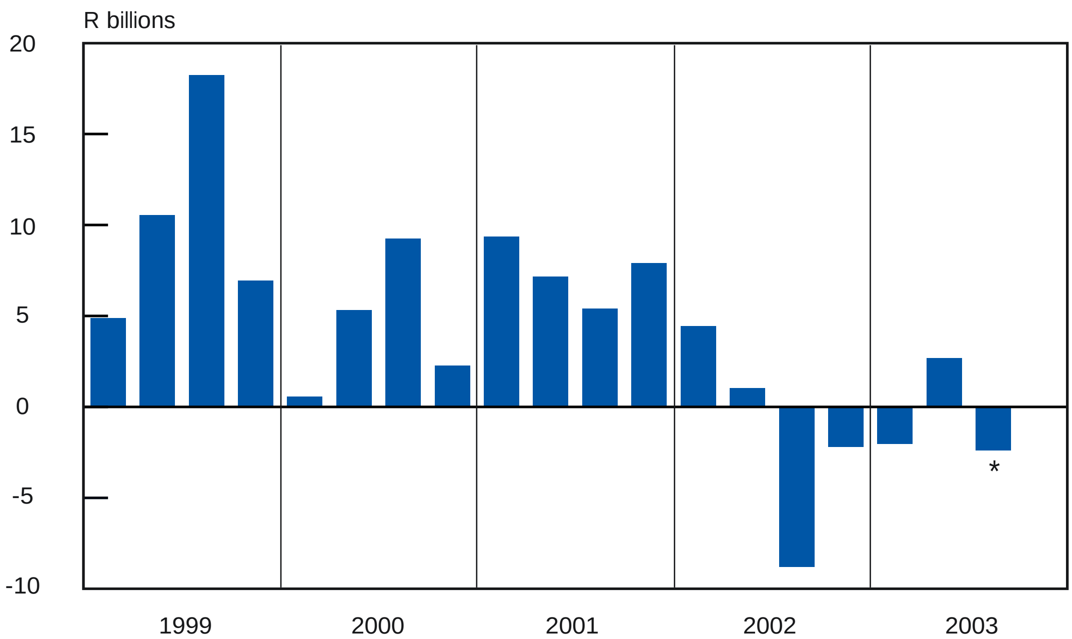
Source: London Stock Exchange and JSE Securities Exchange SA

On 23 June 2003 the JSE Securities Exchange SA announced the first alternative exchange in Africa, named AltX, that will list small and medium companies, specifically targeting black empowerment and junior mining companies. The new market is set to open in October 2003 and will run parallel to the Main Board, with reduced fees and separate listing requirements, such as a pre-tax profit of no more than R8 million and a minimum share capital of R2 million. These companies will get support from the JSE through public forums and directors' education courses subsidised by the Department of Trade and Industry. AltX will ultimately replace the venture capital market and the development capital market established by the JSE in the late eighties.

Turnover in the *secondary share market* contracted from a record high R236 billion in the second quarter of 2002 to R176 billion in the second quarter of 2003 as the appreciation of the exchange value of the rand and the concomitant decline in share prices dampened trading activity. From an eighteen-month low of R47 billion in April 2003, turnover improved by 38 per cent to R65 billion in June as the share market recovered, before slowing to R57 billion in August. Market liquidity (turnover expressed as a percentage of market capitalisation), however, improved from 46 per cent in 2002 to an annualised 50 per cent over the first eight months of 2003, but this was partly due to the lower level of share prices and a reduction in the number of listed companies. The market capitalisation of the JSE Securities Exchange SA decreased from R1 913 billion in May 2002 to R1 568 billion in August 2003. Over the same period the number of listed companies shrank by 89. Takeovers, mergers and stringent listings requirements, together with prevailing bear market conditions, amongst others, contributed to the spate of delistings.

Non-resident investor interest in shares listed on the JSE Securities Exchange SA changed noticeably during the second half of 2002 when share prices worldwide declined in response to the worsening global economic outlook. Non-residents' net transactions in the *secondary share market* switched from net purchases of R5,4 billion in the first half of 2002 to net sales of R11,0 billion in the second half of the year, resulting

Net purchases by non-residents in the secondary share market

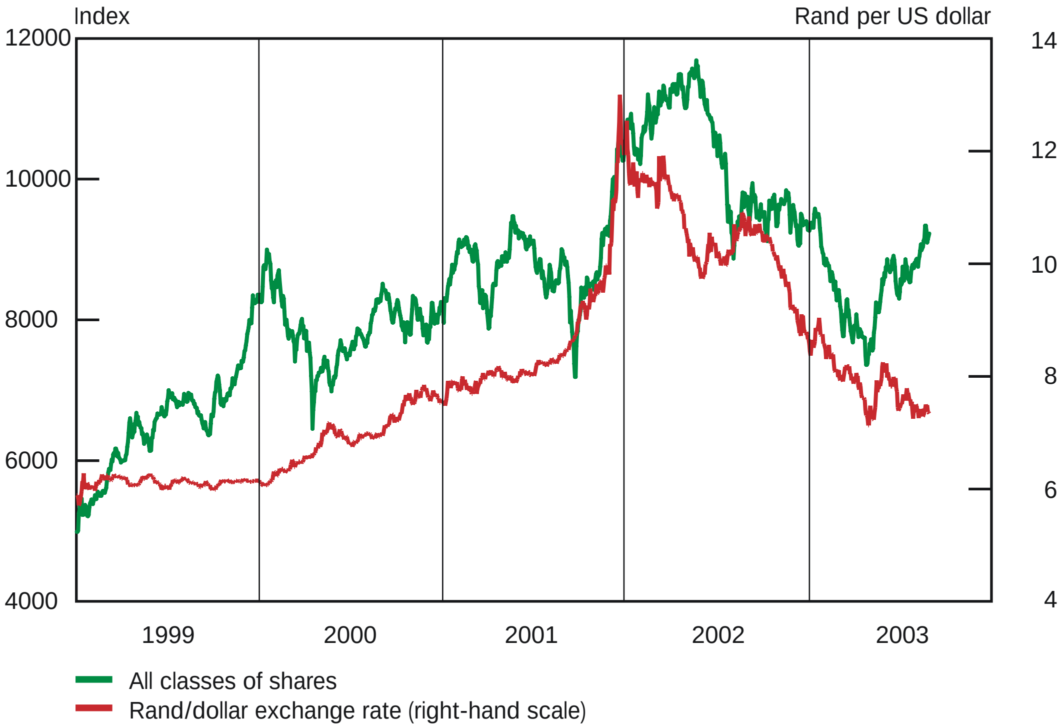


* July and August 2003

in the first annual net sales since 1992. This pattern continued in the first quarter of 2003 when non-residents recorded net sales of R2,0 billion. An improvement in sentiment resulted in net purchases of R2,7 billion in the second quarter, but net sales of R2,4 billion in July and August contributed to net cumulative sales of shares amounting to R1,7 billion from the beginning of 2003 to the end of August.

The decline in domestic share prices, from record highs in May 2002 to consecutive lows thereafter, was largely in response to the worsening global economic outlook, the recovery in the exchange value of the rand and the associated deterioration in expected profits. Share prices reached a lower turning point in April 2003 when share markets worldwide started to recover. The *monthly average price level of all classes of shares* listed on the JSE Securities Exchange SA fell by 31 per cent from May 2002 to April 2003, before recovering by 15 per cent to August 2003. Indications of improved growth prospects in the United States and cautious optimism in several other major economies contributed to improved sentiment in global share markets. The S&P 500 composite index of the United States share market already showed signs of recovery from February 2003 and increased by 18 per cent to the end of August.

Share prices and the exchange rate



The *daily closing level of the all-share price index* continued to decline to 25 April 2003 before improving by 25 per cent to the end of August. The increase in share prices became more pronounced from the end of June 2003, in the wake of domestic monetary policy easing and the improved performance of international bourses. These forces dominated the impact of further increases in the exchange value of the rand.

The prices of *resources shares* recovered by 10,3 per cent from April to June 2003 as the exchange value of the rand weakened moderately, the outlook for the global economy improved, the war in Iraq ended and the SARS virus and its risk on growth appeared to be under control. These share prices then declined by 4,7 per cent in July before increasing by 8,5 per cent in August on account of increases in the dollar price of gold and platinum.

The recovery in the share market was furthermore underpinned by improvements in the prices of *financial shares*. The stronger rand ultimately benefited the sector as inflation declined and expectations of lower interest rates led to the prospect of increased credit extension and fewer bad debts. The prices of financial shares improved by 9,3 per cent from April 2003 to August, supported by strong improvements in the share prices of investment companies, while real-estate and banking shares also improved in the wake of monetary easing.

Mirroring the decline in share prices, the *dividend yield* on all classes of shares increased from 3,0 per cent in May 2002 to 4,6 per cent in April 2003, the highest level since 1990 – before receding to 3,5 per cent in August. At the same time the *price-earnings ratio* of all classes of shares increased to 11,5 in August 2003 after falling from 13,7 in May 2002 to 9,7 in April 2003 – its lowest level since September 2001. The current price-earnings ratio is still substantially below the monthly average of 12,5 in 2002 and also well below a ten-year average of about 14, hinting that shares on the JSE Securities Exchange SA may still be relatively cheap, notwithstanding the recent gains in share prices.

Market for derivatives

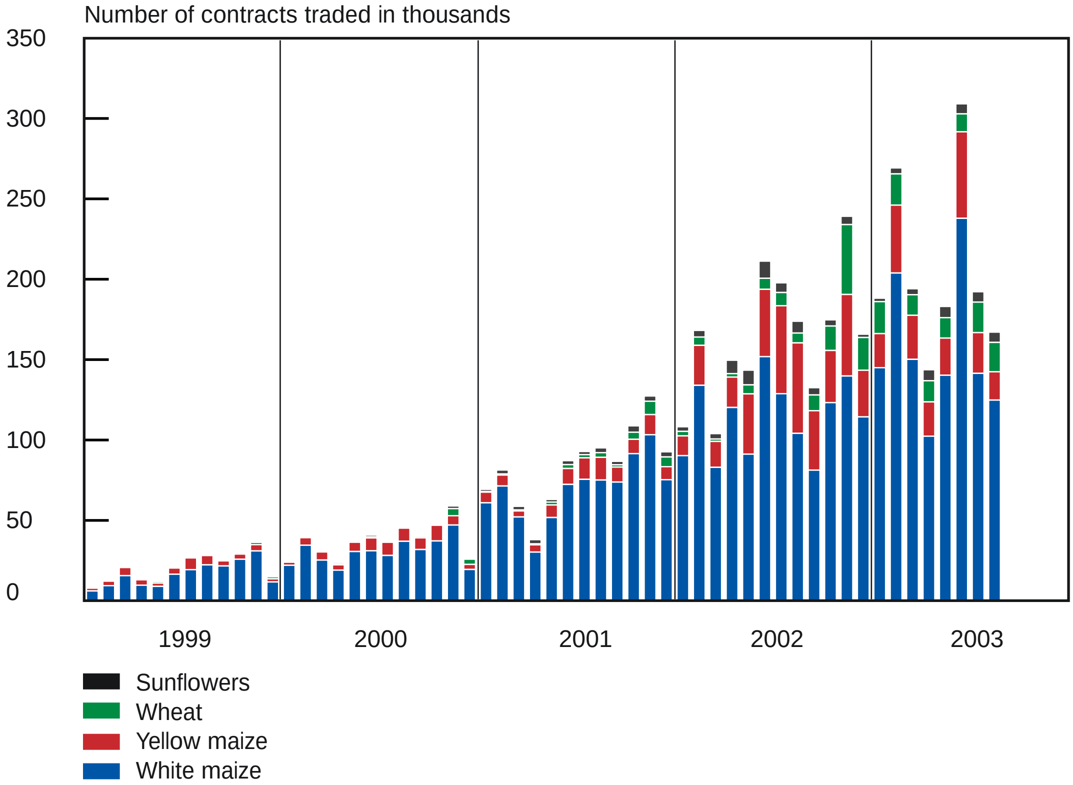
The stronger exchange value of the rand and fluctuating share prices during the first eight months of 2003 coincided with sluggishness in the formal market for equity derivative products. Trade in warrants fell back significantly from the high levels recorded in 2002, while trade in individual equity futures and options on futures stayed more or less on par with the activity recorded in 2002.

The total number of *futures and options contracts* traded on the JSE Securities Exchange SA decreased moderately from 20,4 million contracts in the first eight months of 2002 to 19,4 million in the corresponding period of 2003. The number of contracts based on individual equity futures increased from 6,8 million in the first eight months of 2002 to over 7,2 million during the same period in 2003 while trade in warrants declined from 14,9 billion to 3,8 billion over the same period, reflecting a change in market sentiment towards these derivative products. The number of warrants listed subsequently declined from 662 at the end of February 2002 to 269 in August 2003.

Non-resident participation in the derivatives market, as measured by the number of open interest contracts, declined markedly during the current year from an average of about 45 per cent during the first eight months of 2002 to about 36 per cent in the corresponding period for 2003. Despite a slight upsurge in December 2002 and June 2003, non-residents' participation has dwindled downwards ever since April 2002 when equity prices were high, and the current trend follows suit with that of non-resident participation in shares.

The movements in the rand price of maize, which generally followed the changes in the exchange rate of the rand, boosted trading in commodity derivative instruments during the first eight months of 2003. The *number of commodity futures and options contracts*, dominated by white maize contracts, increased by about 19 per cent from the second half of 2002 to the first half of 2003, having reached a record high of 652 000 in the first quarter of 2003 followed by a still high 636 000 contracts in the second quarter. Subsequently, the monthly average number of 212 000 contracts in the second quarter of 2003 declined to 180 000 contracts in July and August.

Agricultural futures and options



The spot price of *yellow maize* as quoted by the JSE Agricultural Products Division reached a two-year low on 30 April 2003 before increasing strongly to the end of May as the rand weakened. Subsequently, the spot price of yellow maize decreased to the end of August as estimates of supply increased and the rand improved. The spot price of yellow maize in August 2003 was on average R252 per ton below import parity, the breakeven price for the import of maize. By contrast, the spot price of *wheat* increased strongly to the end of August as supply shortages due to drought conditions in the supply areas became evident. Subsequently, the spot price of wheat increased to above import parity from the middle of June 2003 onwards. The number of wheat contracts traded on the JSE Agricultural Products Division subsequently rose by 64 per cent from June 2003 to August. Trade in wheat contracts, however, accounts for less than 10 per cent of all commodity related contracts, while maize contracts account for more than three quarters thereof.

Real-estate market

The *real-estate market* remained buoyant in the first seven months of 2003, aided by the prospect of and subsequent lowering of the cost of mortgage finance in June and August 2003. The overall seasonally adjusted value of turnover, measured by *transfer duty paid*, increased by 19 per cent in the first seven months of 2003 when compared with the same period of 2002, even though transfer duty rates were lowered and the exempt level increased from March 2003.

The buoyancy in the property market was supported by brisk growth in mortgage advances in the first seven months of 2003. Banks' outstanding stock of *home loans* increased by R26,8 billion in 2002, and by a further R23,2 billion in the first seven months of 2003.

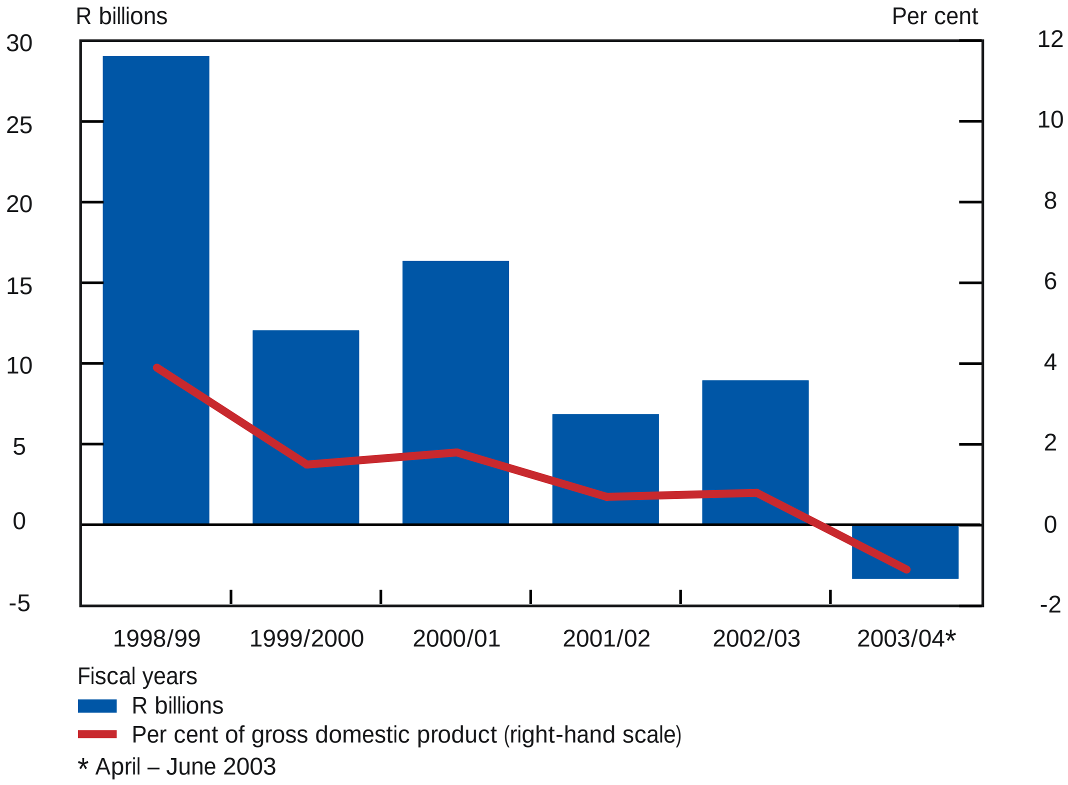
The buoyancy in the property market is also confirmed by the acceleration in *residential property prices* during 2003. Calculated over twelve months, the rate of increase in residential property prices, as measured by Absa Bank, increased from 14,1 per cent in December 2002 to a high of 19,0 per cent in June 2003 before declining to a still high 18,6 per cent in July. Purchases in anticipation of lower interest rates, the growing demand from the emerging black middle class and the relative attractiveness of property as an investment, given the poor performance of many other asset classes in both the domestic and global markets, contributed to the resilience in the property market.

Public finance

Non-financial public-sector borrowing requirement

The *borrowing requirement of the non-financial public sector* (calculated as the cash surplus/deficit of the consolidated central government, provincial governments, local governments and non-financial public enterprises and corporations) for the April-June quarter of fiscal 2003/04 resulted in net investment in non-financial assets of R3,4 billion, compared with an investment of R2,5 billion in the corresponding quarter of the previous fiscal year. As a ratio of gross domestic product, the non-financial public-sector surplus in the April-June quarter of 2003 amounted to 1,1 per cent, compared with a surplus of 0,9 per cent recorded in the corresponding quarter of the previous fiscal year. Although the borrowing requirement of national government increased, it was negated by the improvement in the finances of provincial governments and the non-financial public enterprises and corporations.

Non-financial public-sector borrowing requirement

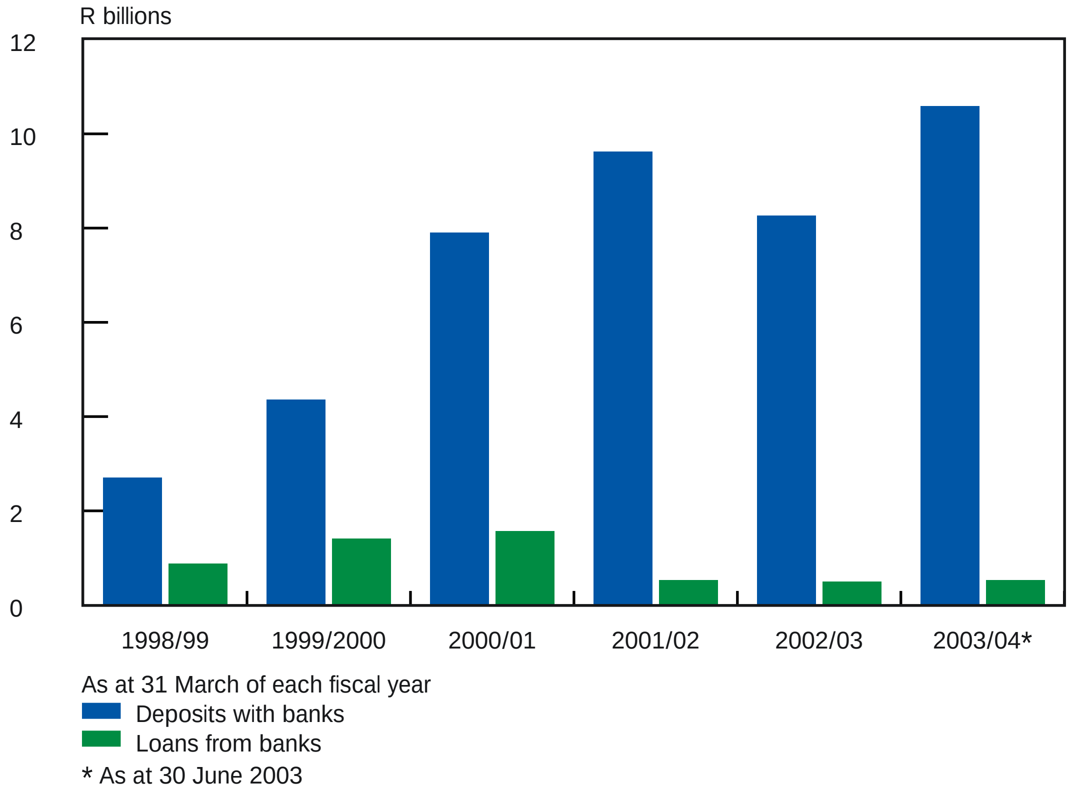


The *Budget Review 2003* projected that the non-financial public-sector borrowing requirement for fiscal 2003/04 as a whole would amount to 3,1 per cent of gross domestic product. This ratio is expected to fall back to marginally below 3 per cent in the ensuing years. However, it should be noted that the calculation of the non-financial public-sector borrowing requirement in the *Budget Review 2003* is not strictly comparable with the calculation of the data reported above. The revised methodology for the compilation of the public-sector borrowing requirement (PSBR) as introduced in this *Quarterly Bulletin* excludes net lending from the calculation of the PSBR. Net lending transactions are now included in transactions in financial assets and liabilities.

The Government Finance Statistics analysis of *national government* finances indicates that cash receipts from operating activities increased by only 3,2 per cent in April – June 2003 compared with the same period in the previous fiscal year. Cash payments for operating activities of national government increased by 6,7 per cent. Including the cash outflow due to investment in non-financial assets, the result was a cash deficit of R3,9 billion in April – June 2003 compared with a cash deficit of R1,6 billion recorded in the same period of the previous fiscal year. The cash deficit was mainly financed from the issuance of long-term bonds in the international and domestic capital markets and a change in the stock of cash.

The cash surplus of *provincial governments* amounted to R4,5 billion in the April-June quarter of 2003 compared with R6,2 billion recorded in the same quarter of the previous fiscal year. The reduction in the surplus of provincial governments can mainly be attributed to increases in both the outflows of cash payments for operating activities and an increase in investment in non-financial assets, as envisaged in the *Budget Review 2003*.

Provincial governments' deposits and loans



Provincial governments, being at the forefront of service delivery to the public, received substantial transfers from the national revenue pool in recent budget allocations. The cash surplus of the provincial governments was partly reflected in an increase in their bank deposits from R8,3 billion at the end of March 2003 to R10,6 billion at the end of June 2003, while their overall indebtedness to banks remained unchanged at R0,5 billion on both these dates.

The cash deficit of *local governments* in the April-June quarter of 2003 was estimated at R1,3 billion, which was well below the R4,6 billion recorded in the same quarter of the previous fiscal year.

Preliminary data on the finances of the *extra-budgetary institutions* and *social security funds* indicate that they both recorded cash surpluses for the April-June quarter of 2003. The surplus of the social security funds increased from R0,6 billion in the said quarter of the previous fiscal year to R1,4 billion in the current fiscal year, which can mainly be attributed to increases in social contributions resulting from workers at all remuneration levels and their employers contributing to the Unemployment Insurance Fund, and from the extension of coverage to include farm and domestic workers.

At the level of consolidated general government, the cash surplus amounted to R0,8 billion compared with R0,9 billion in the same period of the previous fiscal year.

Budget comparable analysis of national government finance

National government expenditure in the April-June quarter of 2003 amounted to R73,8 billion, which was 8,1 per cent more than in the corresponding quarter of 2002. In the Budget proposals for fiscal 2003/04, national government expenditure was estimated to amount to R334,0 billion for the full fiscal year, representing an increase of 14,7 per cent on the actual expenditure in fiscal 2002/03.

An amount of R3,5 billion of national government spending was recorded as capital outlays in the April-June quarter of 2003. This represents 15,5 per cent of the R22,7 billion envisaged in the original Budget for the current fiscal year as a whole. It was expected that capital expenditure would grow at a rate of 19,2 per cent in fiscal 2003/04 and that this would be supplemented by the investment spending of partnerships formed between government and private-sector parties. These partnerships have gained momentum and now form a significant share of investment spending. To date, some 50 projects have been registered. Interest payments declined by 11,2 per cent compared with the same period in fiscal 2002/03, mainly due to the shrinking borrowing requirement and the decline in interest rates. Interest payments as a share of government expenditure are expected to decline and are projected to amount to 15,2 per cent of total expenditure for the full fiscal year 2003/04 compared with 16,0 per cent in the previous fiscal year.

National government expenditure as a ratio of gross domestic product amounted to 25,3 per cent in the April-June quarter of 2003, virtually the same as in the corresponding quarter of the previous fiscal year. After allowing for cash-flow adjustments (i.e. accounting adjustments for timing differences between the recording of transactions and bank clearances, and late departmental requests for funds), national government's cash expenditure increased by 6,1 per cent to amount to R73,6 billion in the April-June quarter of 2003 compared with R69,3 billion in the corresponding period of the previous year.

National government revenue amounted to R68,7 billion in the April-June quarter of 2003, representing a year-on-year rate of growth of 3,0 per cent. This growth rate was significantly lower than the growth rate of 25,8 per cent recorded in the same period of the previous fiscal year and also much lower than the average growth rate of 12,2 per cent recorded in the same period of the preceding five years. It also fell short of the increase of 9,4 per cent that was budgeted for the full fiscal year in February 2003. For the current period under review, almost all categories of revenue displayed a weak performance (see accompanying table). Taxes on income and profits decreased by 3,6 per cent, which can mainly be ascribed to lower corporate tax collections as company profits declined due to, amongst other things, the recovery of the exchange value of the rand and the associated reduction in export receipts. Domestic taxes on goods and services decreased appreciably, mainly because of lower collections of value-added tax in an environment of declining sales volumes and low inflation.

National government revenue in fiscal 2003/04

Revenue source	R billions		
	Budgeted full fiscal year	Actual April – June	Percentage change*
Taxes on income and profits	177,9	38,7	-3,6
Payroll taxes	3,6	0,9	12,9
Taxes on property	5,9	1,4	2,6
Domestic taxes on goods and services	109,6	22,1	-1,2
Taxes on international trade and transactions	11,3	2,7	8,3
Other revenue	5,9	5,4	232,0**
Less: SACU*** payments	9,7	2,4	17,7
Total revenue	304,5	68,7	3,0

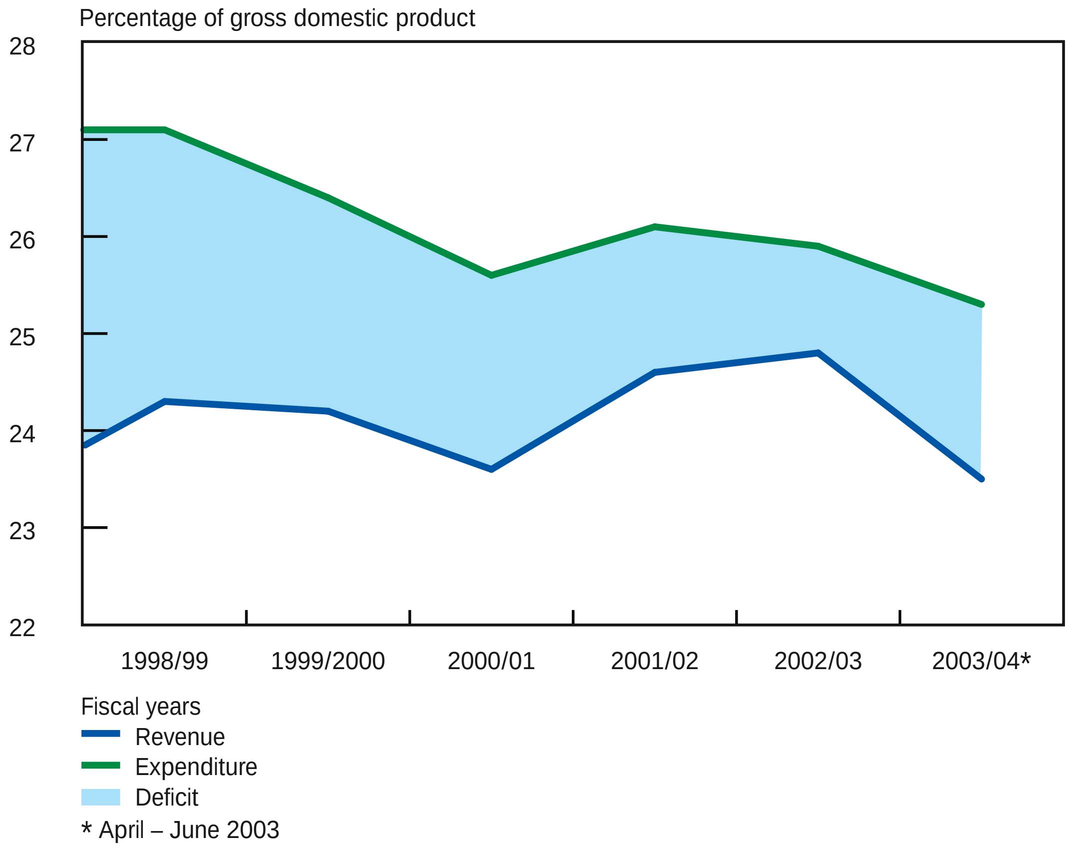
* April – June 2002 to April – June 2003
** High values are due to unallocated revenue which is not allocated to a specific revenue source
*** Southern African Customs Union

National government revenue as a ratio of gross domestic product decreased from 24,6 per cent in the April-June quarter of 2002 to 23,5 per cent in the April-June quarter of the current fiscal year. After allowing for cash-flow adjustments due to timing differences between the recording of transactions and bank clearances, national government's cash revenue amounted to R68,9 billion in the April-June quarter of 2003. This represents an increase of 3,4 per cent compared with the same period in the previous fiscal year.

The net result of the revenue and expenditure of national government in the April-June quarter of 2003 was a *deficit before borrowing and debt repayment* of R5,1 billion, which was substantially higher than the deficit of R1,6 billion recorded in the same period of the previous fiscal year. As a ratio of gross domestic product, the deficit ratio amounted to 1,8 per cent in the April-June quarter of 2003 compared with 0,6 per cent in the corresponding quarter of the previous fiscal year. The cash-flow adjusted deficit amounted to R4,7 billion in the April-June quarter of 2003.

Although an amount of R6,0 billion was projected to be received from the restructuring of government assets in fiscal 2003/04 and provision was made for an extraordinary payment, virtually no extraordinary receipts or payments were reported for April – June 2003. The net borrowing requirement amounted to R4,7 billion. An extraordinary payment of R7 billion provided for in the Budget for fiscal 2003/04 will be made to the South African Reserve Bank to defray part of the realised losses on the Gold and Foreign Exchange Contingency Reserve Account. In addition, an amount of R1,9 billion is expected to be paid on the revaluation of maturing foreign loans in fiscal 2003/04.

National government revenue and expenditure



As indicated in the table on the following page, the net borrowing requirement in the April-June quarter of 2003 was financed mainly through the issuance of long-term bonds in the international and domestic capital markets. In May 2003 the National Treasury issued a new €1,25 billion global benchmark bond with an annual coupon rate of 5,250 per cent and a maturity of 10 years. It yielded R10,6 billion to the National Revenue Fund. The proceeds of this issue were used to bring the net open foreign-currency position (NOFP) of the Reserve Bank close to zero. This net position, which measures the Bank's uncovered exposure in the foreign currency market, stood at an oversold US$1,2 billion at the end of March 2003, but swung around to an overbought dollar position in the subsequent quarter. The foreign bond issue concluded government's budgeted funding programme in the international market for fiscal 2003/04 as envisaged in the *Budget Review 2003*. It resulted in the average outstanding maturity of government's foreign bonds lengthening from 85 months at the end of March 2003 to 88 months at the end of June 2003. An amount of R5,3 billion will also be drawn on the foreign export credit facilities for the financing of the strategic defence procurement programme in fiscal 2003/04. During July 2003 the national government redeemed US$750 million of the dual currency loan originally drawn down in April 2002.

Financing of the deficit of national government
R billions

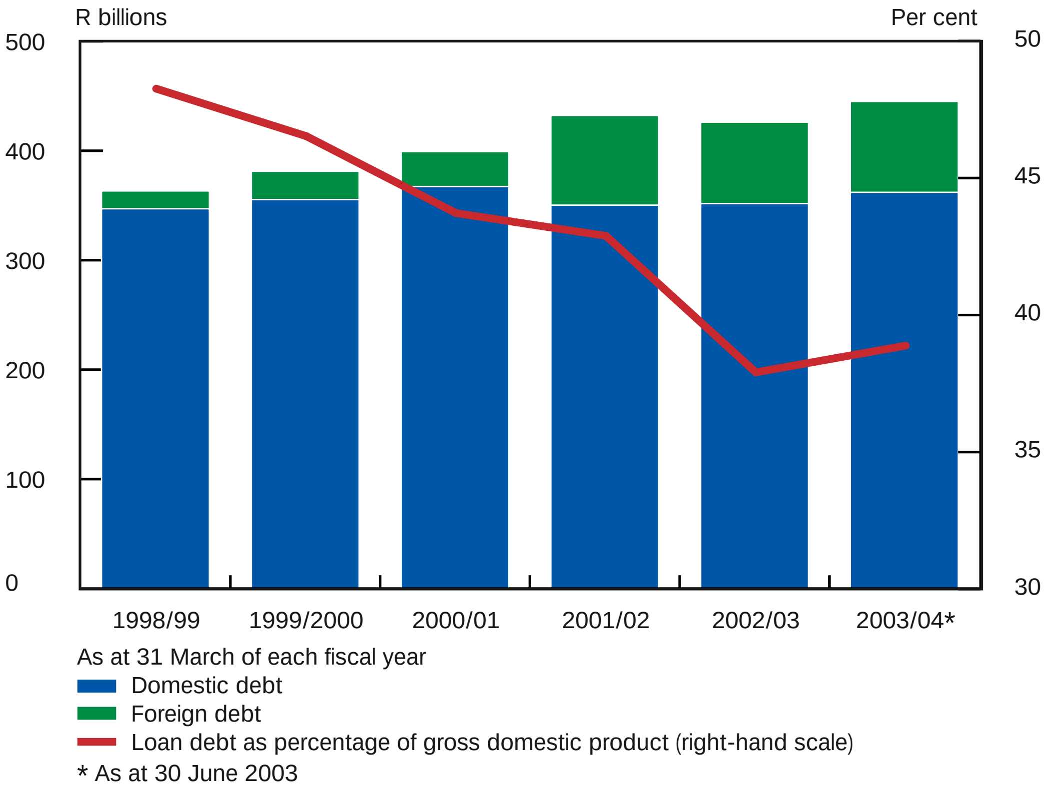
Instrument	Fiscal 2003/04 Originally budgeted	April – June 2003 Actual
Domestic government bonds	9,3	13,4
Treasury bills	6,0	-3,5
Foreign loans	13,6	11,8
Change in available cash balances*	3,1	-16,9
Total net financing	32,0	4,7

* Increase -, decrease +

Net receipts from government bonds issued in the domestic market amounted to R13,4 billion during the April-June quarter of 2003. Long-term fixed-interest bonds were obtained at an average rate of 11,3 per cent, compared with the Budget assumption of 10,2 per cent. The issuance of long-term bonds in the international and domestic capital markets placed national government in a position to redeem net Treasury bills to the amount of R3,5 billion. These bills were originally issued at an average rate of 12,0 per cent compared with the Budget assumption of 12,1 per cent. These funding activities resulted in an increase of R16,9 billion in government balances in the April-June quarter of 2003, bringing the balances to R26,7 billion at the end of June 2003. National government deposits are being accumulated partly in preparation for large interest payments due at the end of August 2003.

Total national government debt rose from R462,6 billion at the end of March 2003 to R481,6 billion at the end of June 2003 mainly due to the global benchmark bond

Loan debt of national government



issued in May. Total foreign debt amounted to 18,7 per cent of the total national government loan debt at the end of June 2003 compared with 17,4 per cent at the end of March 2003 and 19,0 per cent at the end of the previous fiscal year. As a ratio of gross domestic product, national government loan debt amounted to 38,9 per cent at the end of June 2003 compared with 37,9 per cent at the end of March 2003. This increase should, however, be seen in the context of the simultaneous increase in government deposits.

National government finance in July 2003

National government expenditure in July 2003 amounted to R25,5 billion, bringing the cumulative expenditure in the first four months of fiscal 2003/04 to R99,3 billion which was 10,1 per cent more than in the same period of the previous fiscal year. The cash-flow adjusted expenditure for the first four months of fiscal 2003/04 amounted to R98,4 billion which was 8,2 per cent more than in the corresponding period of 2002.

National government revenue amounted to R20,8 billion in July 2003 and to R89,5 billion in the first four months of fiscal 2003/04, representing a year-on-year rate of increase of 3,7 per cent. After the usual adjustment for cash flows, revenue amounted to R89,6 billion in the first four months of fiscal 2003/04, which was 3,8 per cent more than in the corresponding period of 2002.

The net result of the national government's revenue and expenditure in the first four months of fiscal 2003/04 was a deficit of R9,8 billion compared with R3,9 billion in the same period of the previous fiscal year. The deficit before borrowing and debt repayment, adjusted for cash flows, amounted to R8,8 billion. During July 2003 national government redeemed US$750 million of the dual currency loan originally drawn down in April 2002 and made a profit of R3,0 billion on the revaluation at redemption, as indicated in the accompanying table. This resulted in a net borrowing requirement of R5,8 billion.

National government finance
R billions

Instrument	Fiscal 2003/04 Originally budgeted	April – July 2003 Actual
Deficit	29,5	8,8*
Plus: Extraordinary payments	7,0	0,0
Cost/profit on revaluation of foreign loans**	1,9	-3,0
Less: Extraordinary receipts	6,4	0,0
Net borrowing requirement	32,0	5,8
Domestic government bonds	9,3	16,8
Treasury bills	6,0	-4,0
Foreign loans	13,6	4,5
Change in available cash balances***	3,1	-11,5
Total net financing	32,0	5,8

* Cash-flow deficit
** Cost +, profit -
*** Increase -, decrease +

National government funding activities in July led to a decrease in total national government debt to R479,7 billion at the end of that month.

Statement of the Monetary Policy Committee

14 August 2003

Issued by Mr T T Mboweni, Governor of the South African Reserve Bank, at a meeting of the Monetary Policy Committee in Pretoria

Introduction

Since the last meeting of the Monetary Policy Committee the rate of inflation has slowed down further to a level just above the upper limit of the inflation target range. The sharp decline in inflation in the first half of 2003 has been a major accomplishment of the prudent monetary policy stance adopted during 2002 combined with the recovery in the external value of the rand. The increase in short-term interest rates in 2002 served to contain inflation and inflationary expectations. Aggregate production began to grow at a slower rate from the middle of 2002. Although aggregate domestic demand continued to increase strongly, supported by government spending, sections of the business sector have experienced some pressure on their earnings and profitability largely as a consequence of a reduction in exports.

The inflation outcome

The rate of increase in the consumer price index for metropolitan and other urban areas excluding the interest cost of mortgage bonds (the CPIX), slowed down further in May and June 2003. The year-on-year rate of increase in the CPIX, which had decelerated from a peak of 11,3 per cent in November 2002 to 8,5 per cent in April 2003, came down to 6,4 per cent in June. Although this slower growth was largely a result of a lower rate of increase in food prices and an actual decline in fuel prices, the prices of other consumer goods and services also increased at a slower pace. The twelve-month rate of increase in the CPIX excluding food and energy prices amounted to 6,8 per cent in June 2003, compared to 8,0 per cent in November 2002.

Measured from quarter to quarter at seasonally adjusted and annualised rates, there was an even more significant decline in CPIX inflation from 11,9 per cent in the fourth quarter of 2002 to 2,1 per cent in the second quarter of 2003. In fact, the prices of a number of categories of consumer goods and services, such as grain products, meat, clothing, footwear, transport goods and reading matter, actually declined in the second quarter of 2003.

Despite the stickiness in the prices of services when inflation began to subside, the quarter-to-quarter seasonally adjusted and annualised rate of increase in the prices of all services slowed down from 13,2 per cent in the fourth quarter of 2002 to 3,8 per cent in the second quarter of 2003. Measured on a year-on-year basis, the inflation in services amounted to 9,5 per cent in June 2003. This still high rate of inflation was mainly due to the low level of the base for year-on-year growth calculations in the preceding year.

Changes in the all-goods production price index fell back considerably from a peak year-on-year rate of 15,4 per cent in September 2002 to 1,2 per cent in May 2003, but then rose slightly to 2,3 per cent in June. However, the latter rise in production prices could mainly be attributed to an increase in electricity tariffs for the high-demand winter months, and probably will have only a temporary effect on domestic inflation.

Measured from quarter to quarter, the overall production price index has declined in both the first and second quarters of 2003. This decline was to a large extent related to the recovery in the external value of the rand and low inflation rates in South Africa's main trading-partner countries, which brought about a decrease in the prices of imported goods throughout the first half of 2003. The prices of domestically produced food products also declined in the first two quarters of 2003. Despite this actual decline in production prices of food, the consumer prices of most types of food are still rising, albeit at low rates. The full advantage of the lower food prices has therefore not as yet been passed on to the consumer.

The inflation outlook

Not only did the inflation outcome improve over the past two months, but the inflation outlook generally remains promising. Most commentators and economists expect inflation to come down over the short term and to remain at this lower level over the long term. The expected further improvement in long-term inflation is confirmed by the decrease in the break-even inflation rate, measured as the difference between the nominal yield on conventional bonds and the real yield on inflation-linked bonds. Expected inflation derived in this way has decreased from 8,0 per cent in February 2002 to 5,9 per cent in April 2003 and 5,1 per cent in July.

A number of other developments also favour a further decline in consumer price inflation. First, the fiscal discipline applied by government has materially contributed to the lowering of inflation in the immediate past and will continue to be supportive of monetary policy in the future.

Second, the recovery in the external value of the rand favours future moderate price increases in South Africa. The nominal effective exchange rate of the rand has increased by approximately 13 per cent in the first seven months of 2003. Even after this increase, the level of the real effective exchange rate of the rand was still below the index values in early 2000, leaving domestic producers in a more competitive situation in export markets than at the turn of the century.

Third, the generally low inflation in the rest of the world is assisting South Africa in combating domestic inflation. In addition, international oil markets are somewhat more stable.

Fourth, the slowdown in aggregate production has led to a decline in the utilisation of production capacity in manufacturing from 81,1 per cent in the third quarter of 2002 to 80,3 per cent in the first quarter of 2003. It seems unlikely that capacity constraints will arise in the near future taking the international and domestic economic conditions into consideration.

Although the inflation outlook generally still seems to be favourable, there are certain developments in the domestic economy which require the Monetary Policy Committee to remain vigilant. Of particular concern were the recent wage settlement rates of around 10 per cent. Nearly all the salary and wage increases in 2003 have been above the current inflation rate and have been negotiated in an environment of declining productivity. High nominal unit labour costs will therefore inevitably put pressure on price increases. In addition, high rates of increase in some administered prices are also a cause for concern.

Another development in the domestic economy which could lead to increasing inflation pressures has been the continued strong aggregate domestic demand for goods and services. National accounts statistics are not yet available for the second quarter of 2003. However, many indicators, such as wholesale and retail trade at constant prices, new and used vehicle sales, real value of buildings completed and electricity consumed, signal that domestic final demand was sustained at a relatively high level in the first half of 2003.

The strong performance of domestic demand combined with a slowdown in total domestic production, have led to a reversal in the balance on the current account of the balance of payments from a surplus to a deficit of about ½ per cent of gross domestic product in the first quarter of 2003. In the second quarter of 2003, a moderate decline in merchandise imports could not neutralise a much larger fall in exports. This caused the trade balance to shrink from a seasonally adjusted and annualised value of R32 billion in the first quarter of 2003 to R23,5 billion in the second quarter. However, the consequent larger current-account deficit was financed by inflows on the financial account without putting any significant pressure on the exchange rate of the rand. Going forward if the current account continues to behave in the same fashion it could lead to pressure on domestic inflation.

The high domestic demand in the first half of 2003 has been financed to some extent by means of bank credit. The year-on-year growth in underlying bank credit extension to the private sector (i.e. private-sector credit extension excluding investments and bills discounted) amounted to 12,7 per cent in June 2003, compared with 7,8 per cent in December 2002. The quarter-to-quarter growth rate in underlying bank credit extension to the private sector rose even more sharply from 12,4 per cent in the first quarter of 2003 to 22,4 per cent in the second quarter. Money supply has also recently accelerated. Although the twelve-month growth rate of the broadly defined money supply (M3) has remained at single-digit levels in the first six months of 2003, the momentum of growth in M3 has accelerated considerably over the past three months. This is clearly reflected in the quarter-to-quarter annualised growth rate in M3 which rose from 2,0 per cent in the first quarter of 2003 to 13,5 per cent in the second quarter.

Monetary policy stance

These developments clearly demonstrate that a careful balance needs to be struck in the determination of monetary policy. The welcome fall in inflation, and the prospect going forward that inflation will remain in line with the target range of 3 – 6 per cent, gives scope for an easing of the monetary policy stance. But against that there needs to be balanced the continuing buoyancy of final domestic demand, and the risks to inflation from the specific sources of cost pressures identified above. Taking all this into account the Monetary Policy Committee has decided to reduce the repo rate by 100 basis points to a level of 11 per cent effective from 15 August 2003. The course of any future movements in the repo rate, in either direction, will continue to be judged by the committee in the light of the outlook for inflation against the inflation target.

Statement of the Monetary Policy Committee

10 September 2003

Issued by Mr T T Mboweni, Governor of the South African Reserve Bank, at a meeting of the Monetary Policy Committee in Pretoria

Introduction

The Monetary Policy Committee (MPC) of the South African Reserve Bank has held a special meeting on Wednesday, 10 September. The impetus for this meeting came from the regular Governors' Committee meeting where, amongst other things, recent economic developments are reviewed as part of the Bank's continuous assessment of economic and financial conditions. Although the monetary policy stance is generally set at the MPC meetings that are scheduled on alternate months, there is in fact a continuous process of keeping the monetary stance under review, taking account of any new information or developments.

In the interest of transparency and to keep the market informed, the decision to hold an extra MPC meeting today (10 September) was announced last Friday (5 September).

Recent economic developments

There are signs that the international economy is beginning to recover from its extended period of low growth, although the process is proving to be slow and protracted. Second quarter growth in the United States was revised to above 3 per cent, and the prospects for the Asian economies, including Japan, have improved. The outlook for the major European economies however remains less certain. Despite the nascent recovery, its sustainability is not yet assured and there remain significant downside risks. Against this background, world inflation is not expected to be a cause for concern in the near future.

Domestically, growth performance has been weak during the first half of the year. Growth in gross domestic product moderated from 1½ per cent in the first quarter to 1 per cent in the second quarter. Although there are signs of a revival of output growth following the 3 per cent increase in manufacturing production and the 11½ per cent increase in mining production in July 2003, manufacturing production over the 3 months to July declined by 0,9 per cent compared to the previous 3 months. On a year-on-year basis, manufacturing output declined by 1½ per cent. The increasing gap between actual output growth and potential growth was further illustrated by the decline in capacity utilisation in manufacturing to 79 per cent in the second quarter of 2003. Domestic expenditure, on the other hand, appears to have held up well so far: for example, the demand for new motor vehicles recorded month-on-month increases of 8½ per cent in July and 5½ per cent in August.

Statistics on South Africa's international trade indicate an improvement in merchandise export earnings, probably reflecting the improved international environment, whereas merchandise imports remained broadly unchanged from June to July. The seasonally adjusted trade surplus improved significantly in July. South Africa's total gold and other foreign exchange reserves rose further from US$18,5 billion (R138,9 billion) at the end of June 2003 to US$19,0 billion (R141,6 billion) at the end of July.

The exchange rate of the rand has continued to display greater stability, despite the recent variability in the major currencies. The nominal effective exchange rate stood at 55,1 on 14 August and rose to 57,4 on 4 September, before receding to 54,5 on 9 September 2003.

Year-on-year growth in M3 money supply remained below 10 per cent in July 2003. In fact, the seasonally adjusted level of money supply declined by 0,6 per cent from the end of June to the end of July. Bank loans and advances to the domestic private sector recorded a seasonally adjusted increase of only 0,1 per cent in July, bringing the twelve-month growth rate to 13 per cent.

During the second quarter of 2003 non-residents were net purchasers of both bonds and shares on the South African exchanges. But in July and August they reduced their holdings by a combined total of R7,6 billion. There was also a reduction in non-residents' foreign-currency deposits with South African banks in July.

Fairly buoyant conditions continued to prevail in the real-estate market, while equity prices continued to recover. Share prices have risen by more than 6 per cent from 14 August to date. House prices increased by more than 18 per cent in the year to August 2003.

Data on national government finances during the first four months of the current fiscal year indicate an increase of 3,7 per cent in government revenue and an increase of 10,1 per cent in expenditure compared with the corresponding period of the previous year.

Inflation and inflation expectations

CPIX inflation, measured over periods of twelve months, picked up slightly from 6,4 per cent in June to 6,6 per cent in July 2003. The increase from month to month picked up from minus 0,3 per cent in June to 0,8 per cent in July, mainly on account of an increase in municipal rates and taxes. Despite this slight increase, the previous downward trend is expected to resume. Production price inflation continues to indicate further future declines in CPIX inflation with the twelve-month rate of production price inflation decelerating from 2,3 per cent in June to 1,5 per cent in July, while the month-on-month increase in July was 0,6 per cent.

In the bond market, long yields continue to reflect declining inflation expectations. Consistent with that, CPIX inflation expectations as measured by the Bureau for Economic Research quarterly survey declined across the board for the coming three years, and the levels of CPIX inflation expectations are below those of the same time last year.

The monetary policy stance

Against this background the MPC discussed underlying trends in both the international and the domestic economies.

There is growing evidence that the recovery in the international economy is proceeding. It is becoming clearer, too, that the pace of activity in the domestic economy is slowing. Helped by the recovery in the rand, prospects for lower inflation remain encouraging: there is continued evidence of declining inflationary expectations and CPIX inflation should fall within the target range of 3 – 6 per cent.

Going forward, the Bank's most recent forecasts show that, all things remaining the same, the inflation target should be achieved for the forecast period.

Taking all these factors into account the Monetary Policy Committee has decided to lower the repo rate by 100 basis points to a level of 10 per cent effective from 11 September 2003. This reduction should not be interpreted as a move to a more aggressive lowering of interest rates. Should the inflation outlook deteriorate in the near future, the Committee will not hesitate to take the appropriate action.

A note on developments in the retail-trade sector

By H Wagner[1]

Introduction

South Africa's services-providing industries have increased their share in the total economy significantly over the past fifty years or so. This reflects the increasing sophistication of the South African economy, but other factors, such as the end to economic isolation and the repeal of sanctions in the early 1990s, trade liberalisation, globalisation and the associated technological progress, also contributed to the growing importance of the services industries.

All the subsectors of the tertiary sector are not benefiting equally from these structural changes. The share in total gross domestic product of the transport, storage and communication subsector, and the financial services subsector increased during the 1990s. By contrast, the contribution of the total trade subsector initially remained broadly unchanged but declined later in that decade.

The aim of this note is to briefly review some developments in the retail-trade sector since the beginning of the 1990s. Firstly, changes in the contribution of the retail-trade sector to total gross value added are reviewed. In the section thereafter the growth in real value added by the retail-trade sector is described. This is followed by a short overview of changes in the sector's gross fixed capital formation, saving and net lending. The subsequent section analyses the composition of factor income in the retail-trade sector. This is followed by a discussion of employment changes, while concluding remarks are made in the final section.

1 The views expressed are those of the author and do not necessarily reflect the views of the South African Reserve Bank.

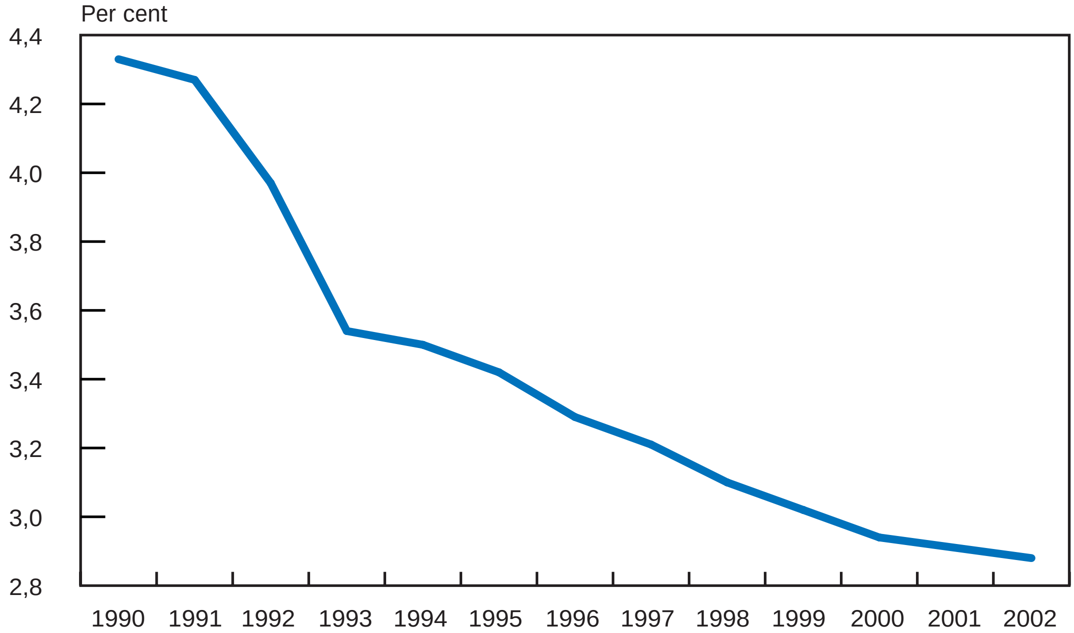
Contribution to total gross value added

The services-providing industries of South Africa increased their share in the national economy from 49½ per cent in the 1950s to 64 per cent in 2002. This can mainly be attributed to the faster growth in real value added by services-providing industries relative to the goods-producing industries and was particularly evident in the transport, storage and communication sector and the financial intermediation, insurance, real-estate and business-services sector.

The growing importance over the past decade of the transport, storage and communications sector can mainly be attributed to the expansion of the fixed-line telephone infrastructure to previously under-serviced areas and the introduction of cellular-telephone networks. Financial intermediation, insurance, real estate and business services benefited, among other things, from the liberalisation of financial markets and the growing demand for financial services brought about by globalisation. In addition, government increased its share in overall gross value added in order to improve service delivery in the years after 1994.

After the contribution of the *retail-trade* sector to the total economy had remained constant at a level of about 4 per cent from the 1950s to the 1980s, this contribution declined to 3 per cent in 1998 and remained at around that level until 2002. The share of the *overall commerce sector* (i.e. the wholesale, retail and motor-trade, and catering and accommodation sectors) in the total economy declined somewhat from the 1950s to the 1980s, before increasing during the 1990s. The increased contribution in the 1990s can partly be attributed to the increase in real value added by the motor-trade and the catering and accommodation subsector.

Contribution of gross value added by retail trade to total gross value added



The declining share of the traditional retail-trade sector relative to total gross value added reflects a change in consumers' buying behaviour in the second half of the 1990s. Among other things, this is evident in a shift away from traditional retail goods to new products and services. Also, a growing portion of final consumption expenditure by households was directed to wholesalers (establishments of which sales to final consumers constitute less than half of their turnover) and this reduced the gross value added by the retail-trade sector.

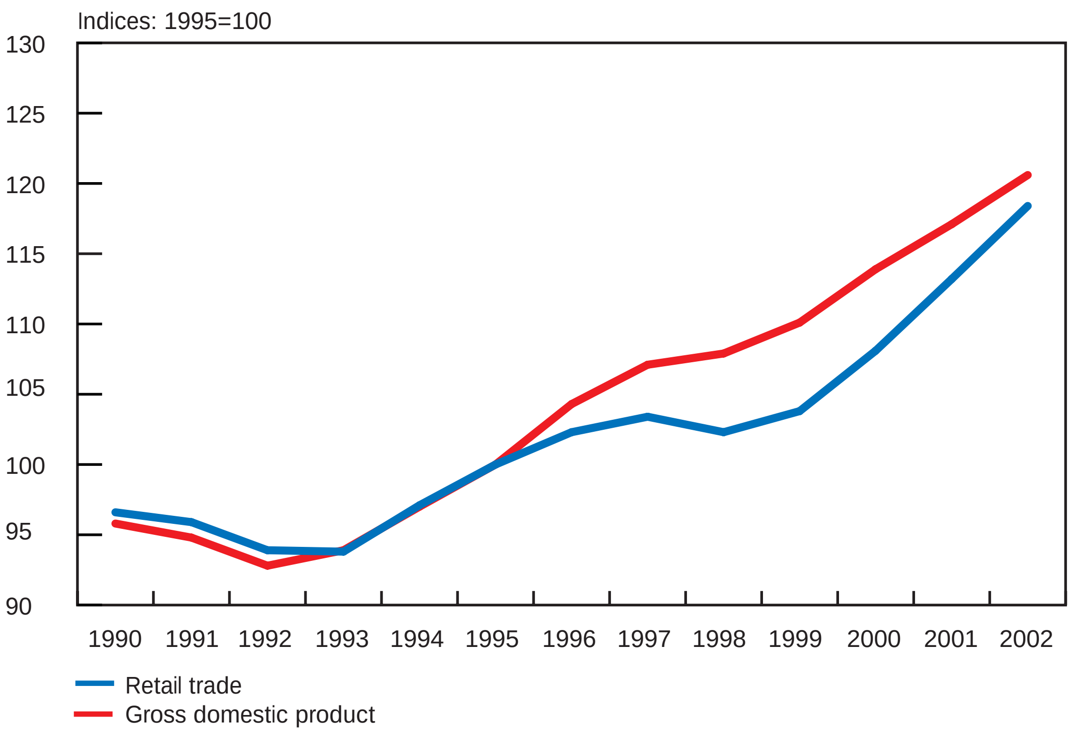
Table 1: Sectoral contributions to total gross value added

Period	Goods-producing industries	Services-providing industires	Commerce		Transport, storage and communi-cation	Financial interme-diation, insurance, real-estate and business services	Other services-providing indus-tries
			Total	Retail trade			
Decade averages							
1950s	50½	49½	14½	4	9½	9½	15½
1960s	48½	51½	14	4	9½	11½	16
1970s	47½	52½	13	4	9½	13½	16½
1980s	49	51	12	4	8½	12½	17½
1990s	39	61	14	3½	9	16½	21½
Years							
1993	39½	60½	14½	3½	8½	16	21
1994	39½	60½	14	3½	8½	16	21½
1995	38½	61½	14½	3½	9	16½	21½
1996	37½	62½	14	3½	9	16½	22½
1997	36½	63½	13½	3½	9	17½	23
1998	36	64	13½	3	9½	18½	23
1999	34½	65½	13	3	9½	19½	23
2000	34½	65½	13½	3	10	20	22½
2001	35	65	13½	3	10	20	22
2002	36	64	13½	3	10	19½	22

Growth in real value added

The growth in real value added by the retail-trade sector since the beginning of the 1990s has followed roughly the same pattern as the growth in real value added by the broad commerce sector and the economy as a whole. Following the long and severe downward phase of economic activity from 1989 to 1993, the real value added by the retail-trade sector increased at an average annualised rate of about 3 per cent from the first quarter of 1993 to the second quarter of 1997. This was lower than the annualised 3½ per cent growth recorded in the total gross domestic product over the same period.

Real gross value added of retail trade and gross domestic product



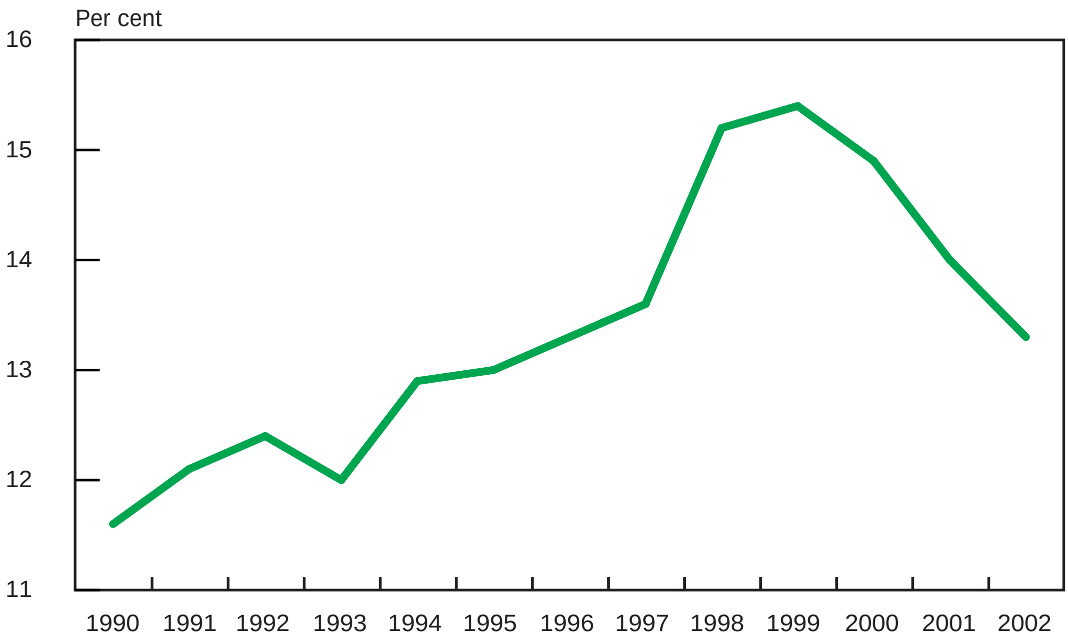
Around the middle of the 1990s the South African economy benefited materially from the repeal of trade and financial sanctions and from progress made in combating inflation. As the recovery in economic activity from June 1993 to November 1996 became more broadly based, consumers became more optimistic. Real final consumption expenditure by households increased strongly, boosting growth in the real value added by the retail-trade sector. This stronger demand for consumer goods occurred in all main spending subcategories, but expenditure on durable and semi-durable goods increased more briskly than the spending on other categories of goods and services.

An increase in the disposable income of households and a rise in the debt-financing of consumption expenditure underpinned the demand for durable goods during most of the 1990s. Households apparently made full use of the easy accessibility of debt financing facilities offered by the banking sector and by retailers themselves. In addition, the redistribution of income to households with a high propensity to consume, lifted expenditure on essential goods and services after 1993.

The real value added by the retail-trade sector *contracted* at an average annualised rate of 4 per cent from the second quarter of 1997 to the fourth quarter of 1998. Global economic conditions, particularly the financial turbulence in south-east Asia in 1997 and 1998, adversely affected South Africa and other emerging-market economies. The domestic financial securities markets experienced severe downward pressure in May 1998. The domestic monetary policy stance was tightened and the prime lending rate of banks rose from 18,25 per cent in May 1998 to 25,5 per cent in August 1998. Business and consumer confidence deteriorated quite severely in 1998.

As the slack in the economy became more pronounced, households' disposable income was adversely affected by declining employment, high debt-to-income ratios and high debt-servicing costs. There was also a sharp increase in the tax burden of households from about 11½ per cent of current income in 1990 to more than 15½ per cent in 1999. Wealth effects following the decline in equity values in the second half of 1998 also weighed on households' willingness to spend. All these factors contributed to slower growth in consumer demand, curbing the growth in the real value added by the retail-trade sector.

Income tax paid as percentage of current household income



The South African economy recovered robustly from the setbacks suffered during the financial crises of 1997 and 1998. From the beginning of 1999 to 2002 the real value added by the retail-trade sector increased at an average annualised rate of 4½ per cent, faster than the increase of 3½ per cent in the broad commerce sector and the 3 per cent in the economy as a whole. Activity in the retail-trade sector benefited from solid consumer demand, following strong growth in the real disposable income of households.

The real disposable income of households from 1999 to 2002 was boosted by, among other things,

- the consistent lowering of the tax burden of households from 15½ per cent of current income in 1999 to 13½ per cent in 2002;

- an increase in the net property income of households as the declining interest rates lowered debt-servicing costs; and
- increases in nominal labour compensation in excess of increases in the prices of consumer goods and services.

An analysis of the composition of final consumption expenditure shows a distinct shift in expenditure patterns away from those goods and services traditionally supplied by retailers. Expenditure on these goods and services (essentially consumer goods) increased at an average annualised rate of 2½ per cent during the period 1999 to 2002, compared with an increase of 3 per cent in total household consumption expenditure.

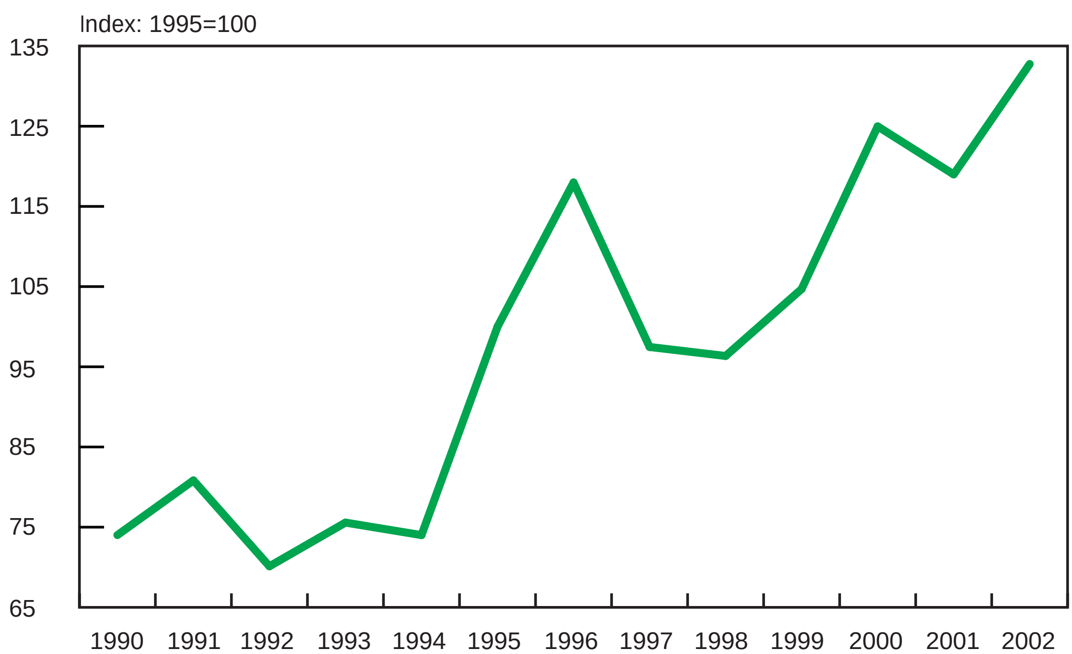
In part, this was a reflection of the faster pace of price increases in spending categories that are considered essential by households. It is estimated that increases in the prices of petrol, medical products and services, transport services, household fuel and power and educational services diverted spending of some R17 billion away from traditional retail goods in the period 1999 to 2002. The popularity of cellular telephones and Internet services, together with a strong rise in outlays by households to secure property and living conditions, contributed further to this apparent structural shift in spending habits.

Gross fixed capital formation

Gross fixed capital formation by the retail-trade sector increased rather poorly in the early part of the 1990s, but picked up in the second half of the decade, lifting the average annual growth rate of real fixed capital formation by the retail-trade sector to about 4 per cent for the decade as a whole.

The peaceful conclusion of the political transition in 1994 was followed in 1995 and 1996 by a rapid expansion of retail-trade facilities. This expansion was temporarily interrupted during the financially turbulent years of 1997 and 1998, but a fairly robust

Real gross fixed capital formation by the retail-trade sector

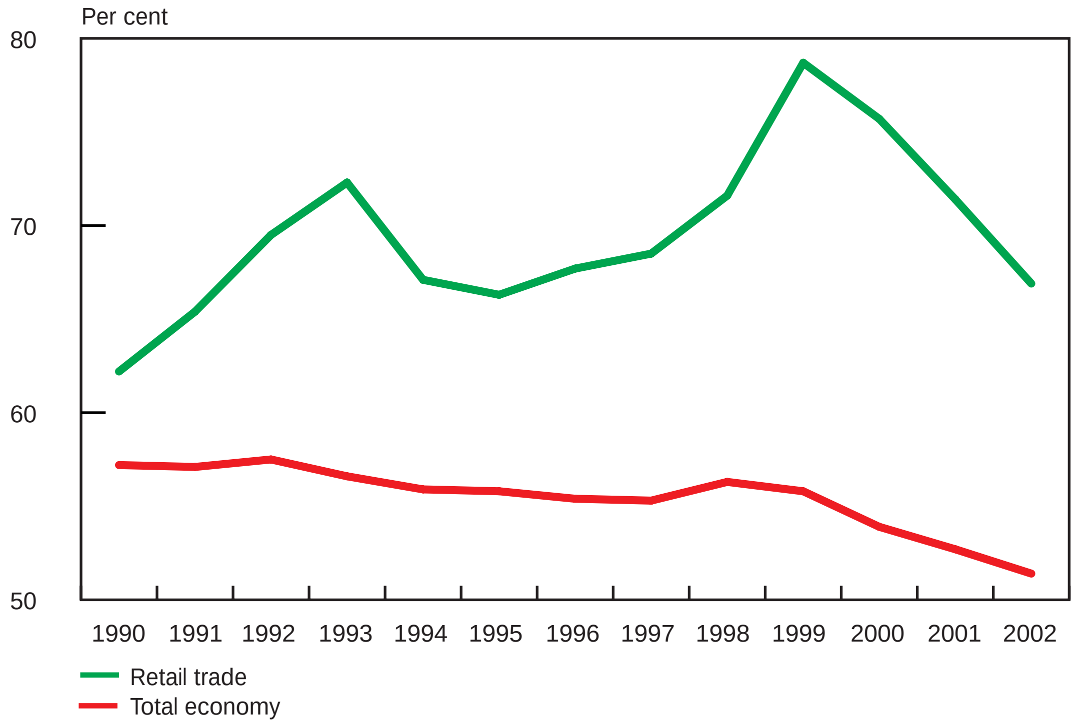


and prolonged recovery got under way in 1999. Several large shopping malls were developed during these years, and new investment in transport and other capital equipment such as barcode scanning devices was also stepped up substantially. In addition, strong growth in the demand for franchising facilities contributed to the expansion of capacity in the retail-trade sector.

Factor income

An analysis of developments in the components of factor income in the retail-trade sector shows that, on average, almost 71 per cent of total factor income was allocated to employees over the past four decades. The economy-wide ratio was 56½ per cent. During the 1990s, labour's share in the total value of output originating in the retail-trade sector drifted higher, on balance, from 62 per cent in 1990 to about 78½ per cent in 1999, before falling back to 66½ per cent in 2002. By contrast, employees' share in economy-wide factor income declined almost uninterruptedly from 57 per cent in 1990 to 51½ per cent in 2002.

Compensation of employees as percentage of total factor income in the retail-trade sector and in the total economy

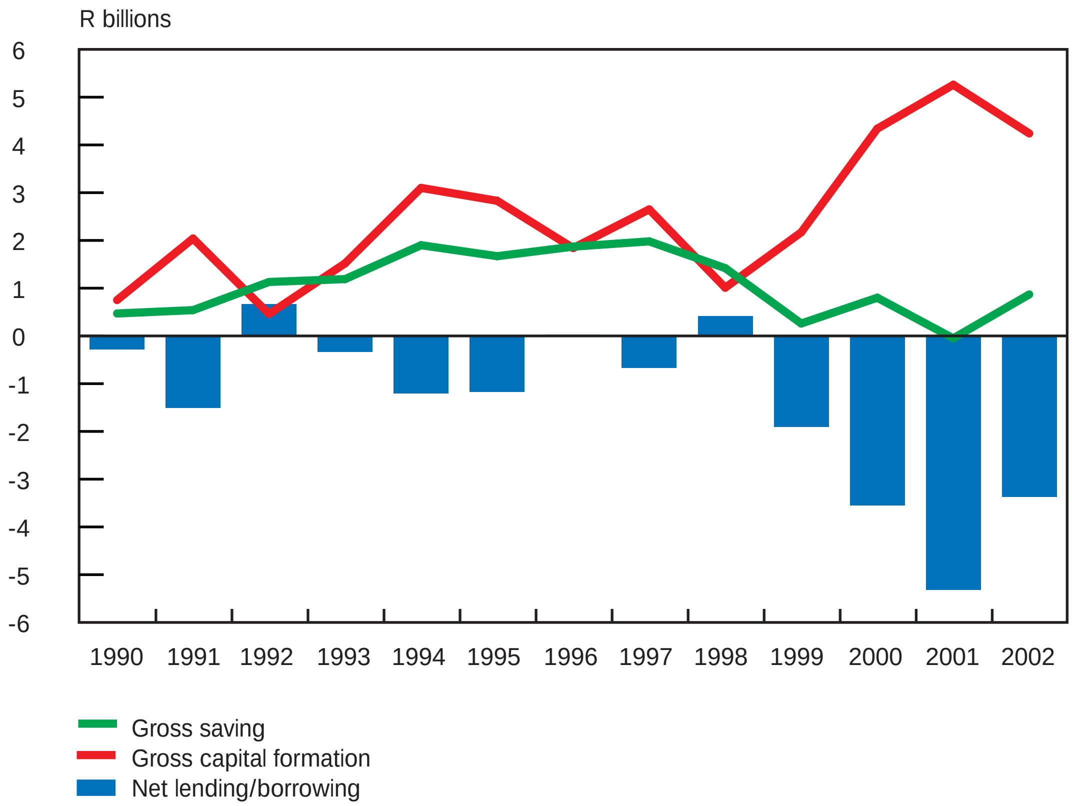


The expansion of employees' share in total factor income in the retail-trade sector from 1990 to 1999 coincided with two downward phases of the business cycle. Rising employee rewards relative to overall factor income are not uncommon in periods of economic contraction. Operating surpluses and profits in the retail-trade sector are far more severely compressed than employee compensation during times of economic slack. In fact, the number of employees in the retail-trade sector increased from 1997 to 1999 despite the slowdown in the economy. As activity picked up during 2000, retail businesses were able to restore their operating margins and spread their overhead costs over larger sales volumes, increasing the share of operating surpluses in total factor rewards and lowering the share of employee compensation.

Saving and net lending

The gross operating surpluses of the retail-trade sector grew at a comparatively modest average annual rate of 6 per cent during the 1990s. Rising dividend and tax payments caught up with the slow growth in operating surpluses, causing gross saving in the retail-trade sector to reach a peak in 1997 and to generally decline in the ensuing years. As fixed capital formation grew quite strongly in the second half of the 1990s and inventories were accumulated, gross capital formation by the retail-trade sector tended to exceed gross saving. The retail-trade sector accordingly became increasingly dependent on external sources for meeting its investment requirements. In 2001 the saving shortfall of R5,3 billion was equal to 20 per cent of the value of output originating in the retail-trade sector.

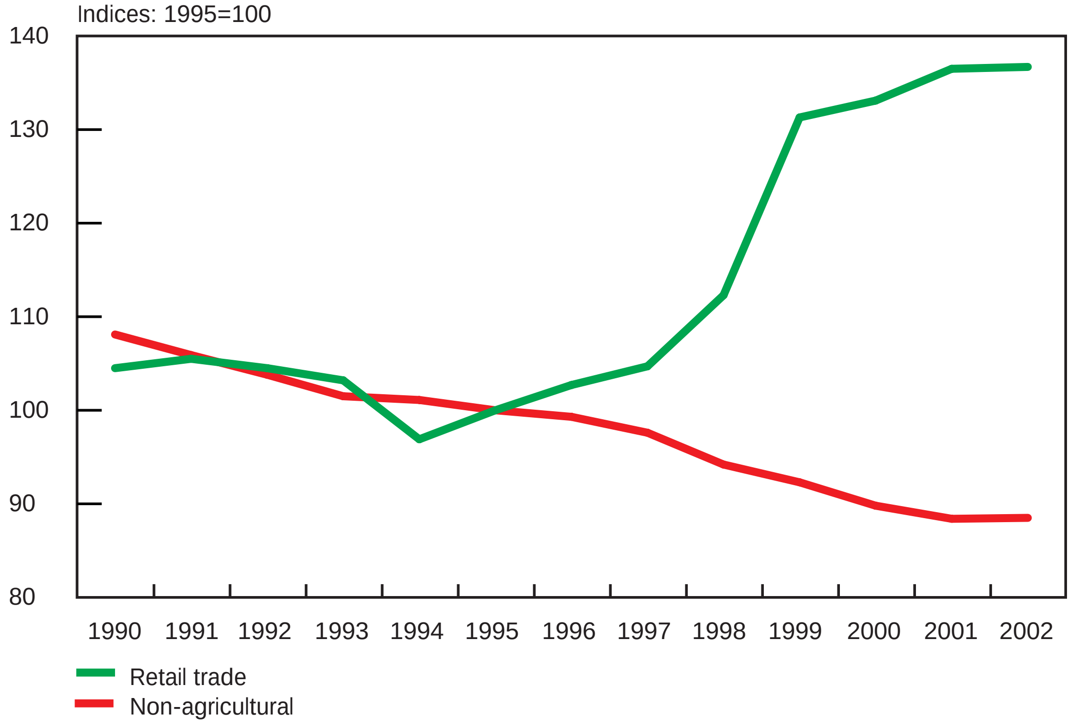
Excess of gross capital formation over gross saving in the retail-trade sector



Employment trends

Contrasting the dismal performance of employment creation in the manufacturing sector and in the total formal non-agricultural sectors of the economy, employment in the retail-trade sector has increased substantially since the middle of the 1990s. Employment in the retail-trade sector grew at an average annualised rate of 4½ per cent from 1995 to 2002. The increase in employment in the retail-trade sector can also be attributed to the expansion of retail space in a number of large shopping centres in major metropolitan areas and heightened franchise activities in the retail-trade sector over the past number of years.

Formal employment in the retail-trade and total non-agricultural sectors*



* Based on quarterly surveyed data in selected industries

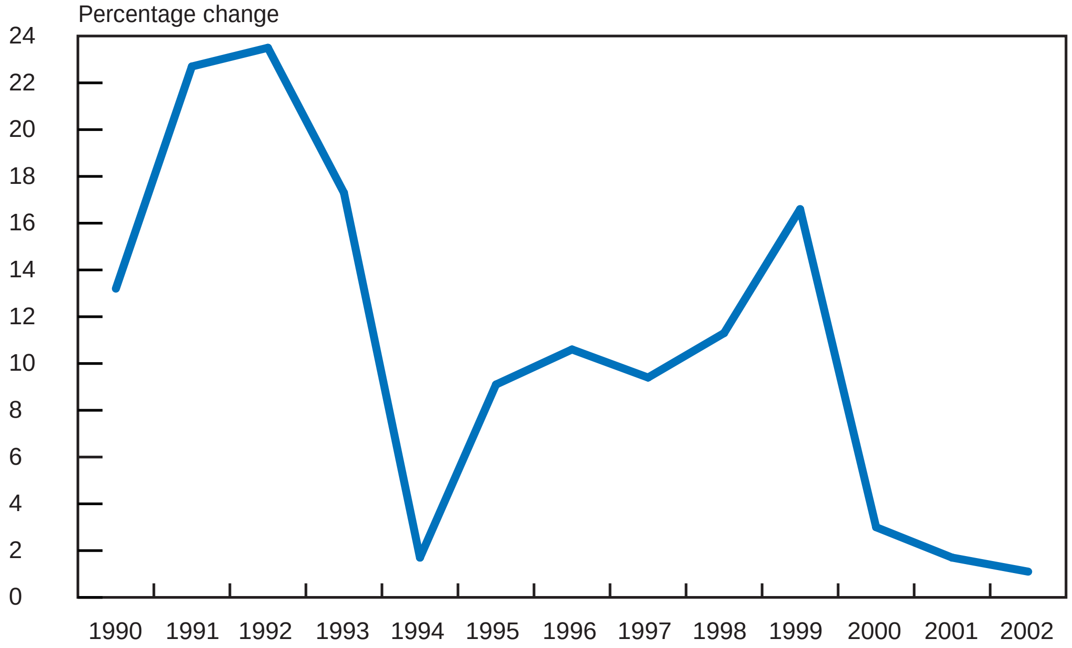
The increase in employment levels in the retail-trade sector, at an average annualised rate of 7½ per cent from 1994 to 1999, was significantly faster than the increase of 1½ per cent in real value added by this sector. Consequently, real output per employee in the retail-trade sector fell during this period and the share of employee compensation in total factor income increased. Although employment numbers increased further at an average annualised rate of 2½ per cent from 1999 to 2002, real value added increased at a rate of 4 per cent, causing real output per employee to rise. This was partly due to technological advances such as integrated barcode scanning and impovements in pricing, payment and inventory control systems. The growth in labour productivity in the retail-trade sector since 2000 compressed the growth in nominal unit labour cost to modest levels, thereby contributing to the containment of inflation in the economy.

Summary

Despite the increase in the share of the services-providing industries in the domestic economy, the share of the retail-trade sector has remained more or less unchanged since the 1950s. This followed from the fact that the growth in real value added by the retail-trade sector followed broadly a similar pattern as the growth in economy-wide real value added. Still, the real value added by the retail-trade sector was directly influenced by changes in consumer demand. This was particularly evident during 1998 and 1999 when tight monetary conditions curbed the growth in consumer spending.

An analysis of the composition of final consumption expenditure shows a distinct structural shift in expenditure away from goods traditionally sold by retailers, mainly in response to sharp price increases in some goods categories considered essential by households. The popularity of new products such as cellular telephones and other electronic devices and services also contributed to this structural shift.

Nominal unit labour cost in the retail-trade sector



A distinct characteristic of the retail-trade sector is the relatively high share of factor income allocated to employee compensation, averaging about 71 per cent in the period 1950 to 2002. Although job creation in the overall economy was very poor, the retail-trade sector has consistently increased employment opportunities since 1995. In recent years the internally generated saving of the retail-trade sector fell increasingly short of fixed capital formation in the sector, making the retail-trade sector more and more dependent on external resources to finance capital expenditure.

Despite the prominent share of labour in total factor income, the growth in nominal unit labour cost in the retail-trade sector generally slowed down during the 1990s, thereby contributing to the containment of inflation in the economy.

A note on the revision of the Government Finance Statistics framework

by Sagé de Clerck[1]

Introduction

The South African authorities recognise the importance of the timely availability of high-quality macroeconomic data. In view of the important role of government finance statistics in the assessment of the stability and sustainability of macroeconomic policies, South Africa has devoted considerable resources to ensuring that best practice is adhered to in the compilation of statistics. The quest for best practice was informed by recent initiatives of the International Monetary Fund (IMF) in developing methodologies for the compilation of statistics. The *Government Finance Statistics Manual 2001 (GFSM 2001)*, released by the IMF, was one of a series of manuals that was thoroughly revised to set a standard for the compilation and presentation of statistics. The revision was done following the identification of deficiencies in the reporting framework of traditional government reporting systems as portrayed in the IMF's *Manual on Government Finance Statistics 1986 (GFS 1986)*. *GFSM 2001* aims at providing improved flows of information that can be used to optimally guide policy decisions, and was released in December 2001 after extensive consultation.

1 The views expressed are those of the author and do not necessarily reflect the views of the South African Reserve Bank. Technical information is based on the Government Finance Statistics Manual 2001 *of the International Monetary Fund.*

The aim of this note is to briefly describe
- the background to the revision of the manual;
- major changes introduced by the new manual;
- the structure and accounts of the revised analytical framework of the *GFSM 2001*;
- the migration path needed to convert from the *GFS 1986* framework to the revised framework; and
- the adjustments made to the *Quarterly Bulletin* tables (Tables S71 – S79) as a first step in the migration process.

Background to the revised manual

In its time, *GFS 1986* provided valuable guidance regarding the compilation of government finance statistics. The compilers of this manual had drawn from other publications such as the *System of National Accounts* of 1968, the United Nations' *Classification of the Functions of Government* of 1980 and the *European System of Integrated Economic Accounts* of 1971.

Traditional reporting and analysis of government finances were not complex and were based on simple cash accounting systems. The main focus was placed on a single balancing item – the overall deficit/surplus – calculated by considering all non-repayable cash inflows as "revenue and grants" and all non-repayable cash outflows as "expenditure". Some repayable items pertaining to policy lending were included in the balancing item as "net lending". In the traditional approach the financing of this balance was the primary focus of analysts, and it can therefore be stated that liquidity considerations stood central in policy evaluation. This approach proved to be insufficient in providing information on the long-term sustainability of fiscal policies. It did not provide information needed for a realistic assessment of the effectiveness of policy decisions, and it ignored a large portion of the future obligations of the government. In addition, all future payment obligations of other units of the economy towards government were ignored.

The global dissatisfaction with cash accounting was aggravated by its focus on cash flows at the time of acquisition of capital goods and lack of attention to the subsequent management of and services arising from such goods. Similarly, the traditional cash accounting systems ignored all transactions in kind, which resulted in serious mis-calculations of the true economic value transferred to and from governments.

It can rightfully be stated that the growing complexity of the economic and financial environment in which governments operate, necessitated a more complex and integrated approach to the compilation and analysis of government operations.

The integrated approach to the compilation of economic statistics was to a large extent led by the work done which culminated in the publication of the *System of National Accounts 1993 (SNA 1993).* The revisions of statistical guidelines such as the fifth edition of the *Balance of Payments Manual, the Monetary and Financial Statistics Manual* and the *GFSM 2001* followed in due course and were harmonised as far as possible with the *SNA 1993.*

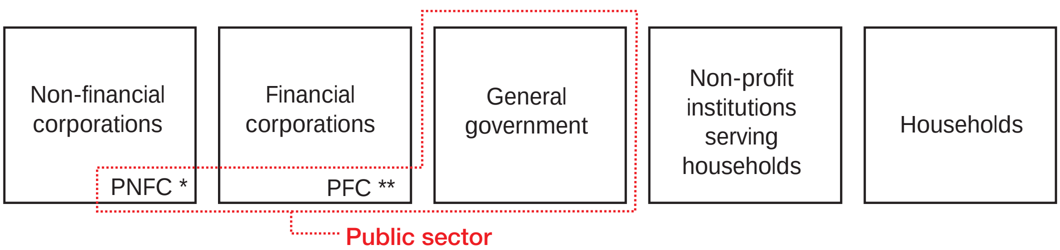
Major changes introduced by *GFSM 2001*

The methodology for the compilation and presentation of data on government operations as presented in *GFSM 2001* differs significantly from that presented in the 1986 manual. These changes can broadly be summarised as follows:

Coverage

The main focus of the coverage of the *GFSM 2001* system is the *general government sector*, including all the *institutional units* that perform the functions of government as their *primary activity*. The functions of government are considered to be providing goods and services to the whole of the community on a non-market basis, to redistribute income and wealth by means of transfer payments and to fund these activities primarily by raising taxes and other compulsory transfers. An entity is defined as an *institutional unit* when it can own assets, incur liabilities and enter into economic activities in its own right. In addition, an entity can only be considered to be an institutional unit if a complete set of accounts, including a complete balance sheet for the entity, exists or can reasonably be constructed. This approach differs from that of the *GFS 1986*, which followed a *functional* approach – all activities resulting from the execution of the functions of government were included in the statistics, irrespective of the institution performing the function.

Table 1: Coverage of *GFSM 2001*



* Public non-financial corporations
** Public financial corporations

The *GFSM 2001* also encourages extension of coverage to the *public sector*. The public sector is derived by consolidating the financial results of the general government with that of the public non-financial corporations and public financial corporations in the analysis of government finances. Close relationships usually exist between public corporations and the governments that own and/or control them. This analysis is particularly important due to the potential fiscal impact on the resources of governments that these entities, producing for the market at market-related prices, could cause.

Basis of recording

The *GFSM 2001* adheres to the *accrual basis* of recording flows. All economic flows are therefore recorded at the time when economic value is created, transformed, exchanged, transferred, or extinguished. The accrual basis also recognises all monetary and non-monetary flows of economic value. By contrast, the *GFS 1986* recommended a basis of recording as close to the cash flow stage as possible. Transactions in kind were not included in the framework but were only recognised as a memorandum item if data on these transactions existed.

Valuation

In order to reflect true economic value, all flows, assets, liabilities and net worth are valued at prices that these goods, services, assets, or liabilities could be exchanged for in cash. This approach in the *GFSM 2001* results in valuation at market value or as close to market value as possible. The *GFS 1986* measured flows according to the value of cash flows and contractual liabilities according to the value government is obligated to pay on maturity of the debt.

Balance sheets

The *GFSM 2001* introduces the compilation of a full balance sheet for all units of government operating at all levels of the public sector. It records government's position with regard to all stocks of non-financial assets, financial assets and liabilities, and net worth. The *GFS 1986* recorded only stocks of certain contractual debt liabilities.

Integrated system

The *GFSM 2001* proposes a comprehensive integrated system which records all transactions and other economic flows. The system also contains all the information to reconcile these flows with the changes in the stock of assets, liabilities and net worth as presented on the balance sheets at the end of two consecutive periods.

Analytical framework

The new analytical framework as contained in *GFSM 2001* introduces several new or revised definitions, classifications and balancing items to enhance the analytical usefulness of the statistics and to redirect attention to various policy considerations, compared with the single balancing measure contained in *GFS 1986*.

The analytical framework of *GFSM 2001*

The system created by the *GFSM 2001* provides an analytical framework that caters for the data needs of a wide range of users. These users include compilers of macroeconomic information, analysts of government's performance, policymakers and government financial managers and auditors. It not only allows for the assessment of financial and economic performance, but also of fiscal soundness and long-term sustainability.

The structure of the integrated framework as presented in *GFSM 2001* comprises primarily four interrelated statements:
- *Statement of government operations;*
- *Statement of other economic flows;*
- *Balance sheet;* and
- *Statement of sources and uses of cash.*

All information previously recorded according to the cash basis of accounting is retained and presented in a reorganised format in the *Statement of sources and uses of cash* – still serving the analysis of liquidity management. In addition, the other statements serve to provide an integrated presentation of the economic operations and position of government.

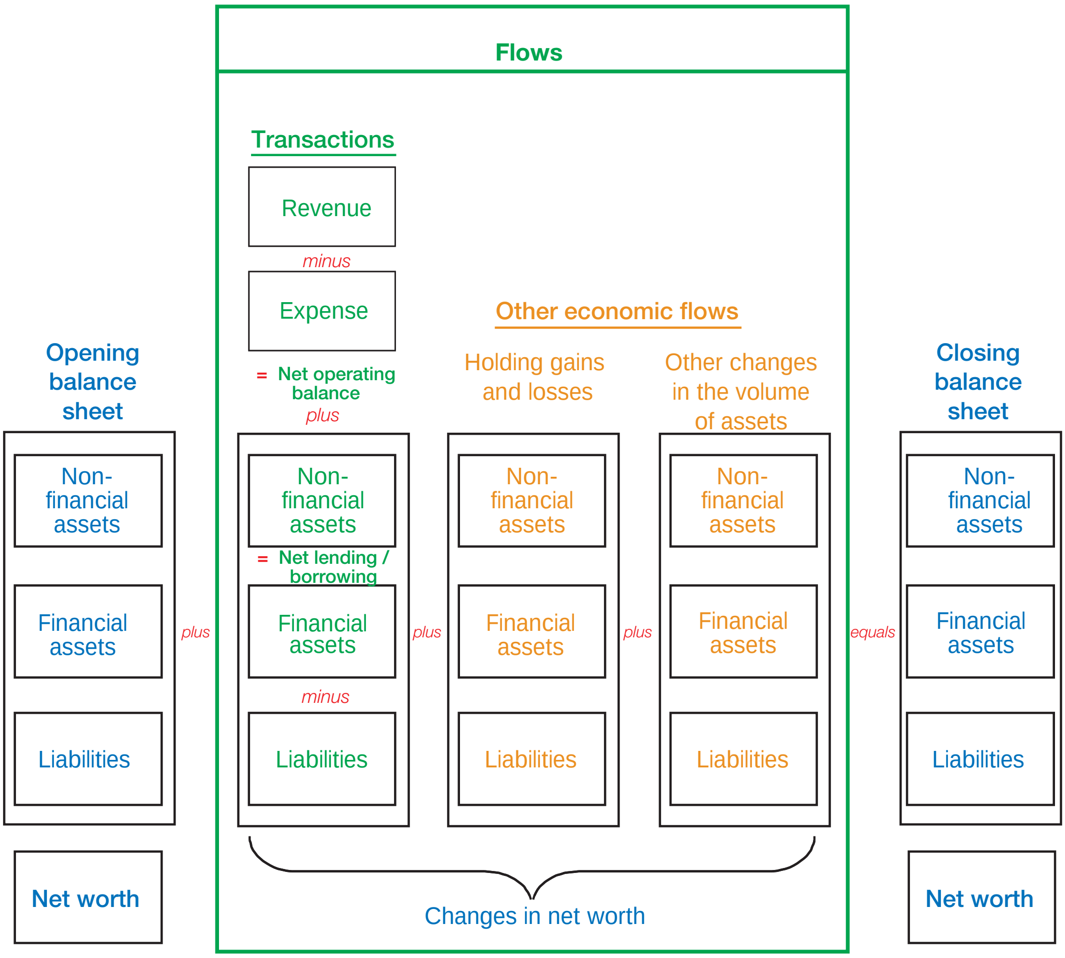
As indicated in Table 2, the system integrates stocks and flows in a double-entry system, which ensures an integral balance in the system at all times. The integrated approach ensures that changes to the stock of net worth, financial and non-financial assets, and liabilities of government, as presented in the opening balance sheet, are explained by flows during the reporting period, to derive the closing balance sheet values of the stocks. These flows represent the creation, transformation, exchange, transfer, or extinction of economic values. In addition, the *GFSM 2001* classifies all flows as either a *transaction* or an *other economic flow* where:
- *transactions* are defined as flows resulting from interaction between two economic units by mutual agreement and include flows due to exchanges and transfers; and
- *other economic flows* are defined as changes in the volume or value of stocks of assets and liabilities not resulting from transactions.

As indicated earlier, the structure of the integrated framework as presented in *GFSM 2001* consists of four integrated statements. The concepts and balancing items underlying each of these statements differ in order to serve a variety of purposes.

Statement of government operations

This statement summarises all the *transactions* (as defined earlier) of government and largely gives an indication of the impact of fiscal policies on the economy. The statement is organised to firstly calculate the *net operating balance* of government. As indicated in Table 2, this balance is calculated by subtracting expense from revenue. The concepts introduced by the *GFSM 2001* analytical framework for *revenue* and *expense* comprise all transactions increasing or decreasing net worth, respectively. As such, the *net operating balance* represents the change in net worth due to transactions. The *GFSM 2001* classification system also introduces sub-categories of revenue and expense according to the economic nature underlying the transactions.

Table 2: Integrated analytical framework of *GFSM 2001*



Revenue is broadly classified according to four main types of revenue, with provision made for further sub-classifications. The broad categories of revenue comprise the following:

Taxes are defined as compulsory transfers levied by general government institutional units. Taxes also include fees levied for services that are clearly out of proportion to the costs of providing the services, but exclude compulsory transfers in respect of social security contributions, fines and penalties.

Social contributions are defined as all receipts of contributions to general government social security schemes and employer social insurance schemes, other than retirement benefit schemes.

Grants are defined as all non-compulsory transfers received from foreign governments, international organisations and other general government units.

Other revenue is defined as all revenue other than taxes, social contributions and grants and comprises primarily:
- property income such as interest, dividends and rent;
- the sales of goods and services;

- fines, penalties and forfeits;
- voluntary transfers other than grants; and
- miscellaneous and unidentified revenue.

The *GFSM 2001* also classifies expense in eight categories and provides for further sub-classifications. The broad categories of expense comprise the following:

Compensation of employees, defined as the remuneration in cash and in kind paid to employees in exchange for work done.

Use of goods and services, defined as the value of goods purchased by governments to be used in the production process or goods acquired for resale, less the net change in inventory of those goods.

Consumption of fixed capital defined as the decline in the value of the stock of fixed assets during an accounting period as the result of physical deterioration, normal obsolescence and normal accidental damage.

Interest, defined as the expense incurred by a debtor for the use of another unit's funds.

Subsidies, defined as current transfers that government units pay to market enterprises in support of the price of their products or in support of their production processes.

Grants, defined as non-compulsory current and capital transfers in cash and in kind to foreign governments, international organisations and other general government units.

Social benefits, defined as current transfers to households to provide for needs arising from events such as sickness, unemployment, retirement, etc.

Other expense, defined as all expense transactions not classified elsewhere and comprising primarily of
- property expense other than interest;
- rent of non-produced assets; and
- miscellaneous other expenses related to transfers, other than grants and social benefit payments.

The second balancing item calculated in the *Statement of government operations* is *net lending/borrowing* – calculated by adding the net acquisition of non-financial assets to the net operating balance. The transactions resulting in the acquisition or disposal of non-financial assets do not affect net worth but change the composition of assets or liabilities. These transactions often lead to exchanges of a financial asset, such as cash for a non-financial asset such as a vehicle. Alternatively, an asset can be exchanged for a liability when acquired on credit – also not affecting net worth of government. The *GFSM 2001* analytical framework distinguishes mainly between produced assets comprising fixed assets, inventories and valuables, and non-produced assets such as land. In order to serve economic analysis these categories of assets are further sub-divided to reflect their exact nature.

Net lending/borrowing as a measure of government's performance gives an indication of the financial resources that government places at the disposal of other units of the economy (government lending) or of the financial resources created by the rest of the economy that government utilises (government borrowing). Activities of government pertaining to the acquisition or disposal of financial assets and liabilities are recorded in the last part of the *Statement of government operations.*

Statement of other economic flows

The *Statement of other economic flows* records all *other economic flows*, which are defined as changes in the volume or value of stocks of assets and liabilities not resulting from transactions. Other economic flows can broadly be disaggregated into two categories. The first category pertains to all changes in the monetary value of stocks of assets and liabilities and is referred to as *holding gains and losses.* Changes in the value of assets and liabilities denominated in foreign currency resulting from exchange rate movements and adjustments to the value of securities due to interest rate movements, can be cited as examples of this type of flows. The second category of flows recorded in this statement is the result of changes in the volume of assets due to the occurrence of various events. The *GFSM 2001* refers to this type of flows as *other changes in the volume of assets.* Events resulting in recording this type of flows are quite often beyond the control of the owner, or occur naturally. Three broad categories of events are recognised in the system:

- the recognition or derecognition of an existing entity as an asset;
- changes in the quantity or quality of assets such as new discoveries;
- extinction due to disasters, or natural depletion; and
- changes due to the reclassification of assets.

Balance sheet

The *Balance sheet* introduced by the *GFSM 2001* presents the stocks of assets and liabilities at a specific point in time and could be regarded as the result of all flows recorded in periods prior to the date of the balance sheet. The value of all non-financial and financial assets owned on the balance sheet date are disclosed, as well as the value of all liabilities of the reporting unit, representing financial claims of other units against the reporting unit. The balancing item calculated from the value of total assets of government less the liabilities of government is the net worth of government as on the reporting date. For analytical purposes the use of the balance sheet as an indicator of the financial position of governments is supplemented by the usefulness of information on the changes in the balance sheet over time. This information forms the basis of the assessment of the sustainability of governments’ operations.

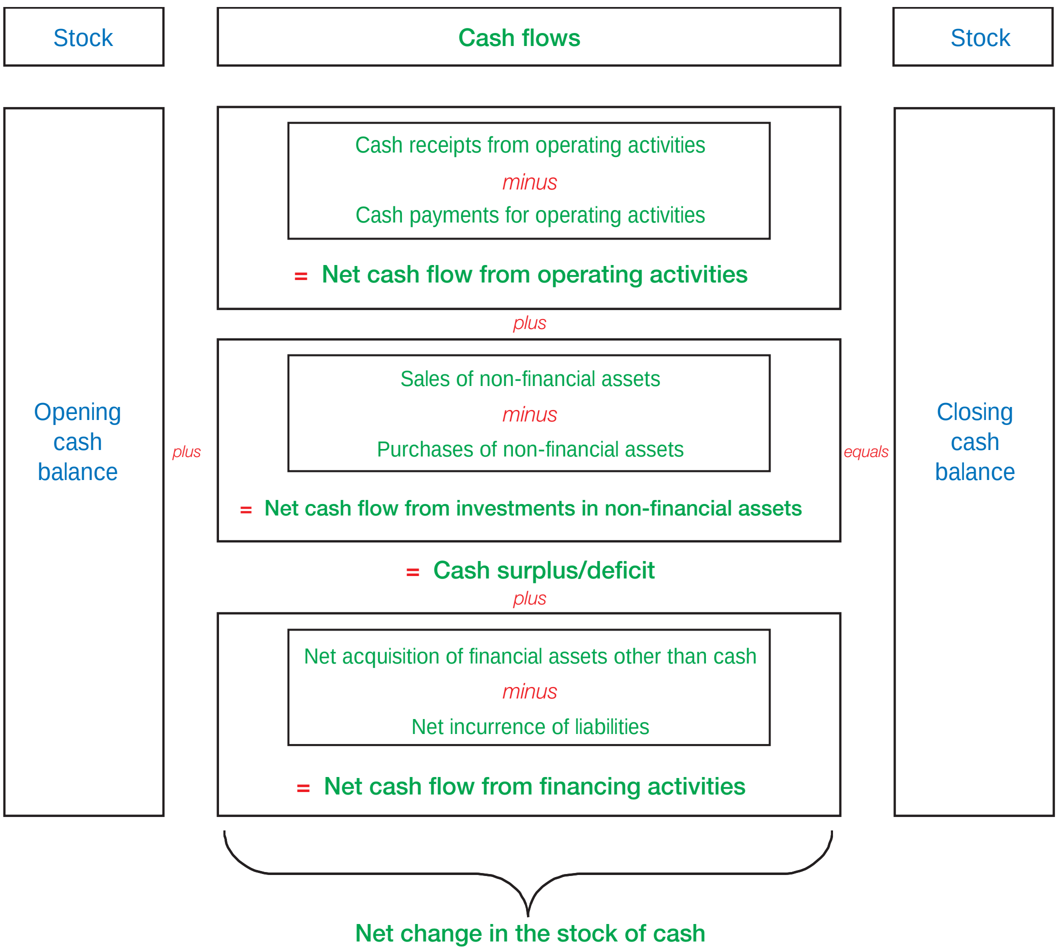
Statement of sources and uses of cash

Cash is one of the financial assets reported on the balance sheet of the integrated analytical framework of the *GFSM 2001*. Owing to the importance of assessing the liquidity of government units, this statement presents the structure according to which the changes in the stock of cash can be recorded. Cash as defined in the *Statement of sources and uses of cash* refers to cash on hand, deposits of a highly liquid nature and overdrafts considered to be entered into for cash management purposes.

The *Statement of sources and uses of cash* records all transactions of the government unit on a cash basis, which means that transactions are captured when cash is received or when cash payments are made. The statement therefore also relates to historic data on government finances that were traditionally compiled on a cash basis in the *GFS 1986* framework. The analytical usefulness of the *Statement of sources and uses of cash* is further increased when a comparison between this statement and the *Statement of government operations* is made. Such a comparison could clearly indicate potential cash inflows and outflows (or the lack thereof) which could indicate a need for policy changes.

Transactions recorded in the *Statement of sources and uses of cash* can be disaggregated according to the same economic classifications than those followed in the *Statement of government operations*. To this effect the cash receipts from operating activities are recorded as taxes, social contributions, grants or other revenue. Similarly, cash payments follow the classification of expense transactions. However, non-cash transactions such as consumption of fixed capital, imputed transactions and transactions in kind are not recorded in this statement. As indicated in Table 3, the *Statement of sources and uses of cash* introduced the balancing items *cash surplus/deficit* calculated as the sum of the net cash flow from operating activities and the net cash flow from investing in non-financial assets. The cash surplus/deficit is financed through cash flows from financing activities derived from the net result of all transactions in financial assets and liabilities. The net change in the stock of cash can therefore be explained by the total of the cash surplus/deficit and the net flow from financing activities.

Table 3: Statement of sources and uses of cash



Migration from *GFS 1986 to GFSM 2001*

The IMF rightfully noted that the full implementation of the recommendations as contained in *GFSM 2001* would be a complex and arduous process. Implementation of the revised statistical framework is also to a large extent dependent on major accounting reforms in a country – taking into consideration the capacity constraints existing in individual countries. It was therefore suggested that each country should develop its own migration path within its means. Such a migration path comprises different phases of implementation over time. These phases start with awareness of the revised framework and should translate into political conviction to change, adopting the broad analytical framework and classification system, and eventually adopting accrual accounting and implementing the complete integrated system.

In South Africa the release of the Public Finance Management Act, Act 1 of 1999 (as amended) to a large extent already laid the foundation for a number of these reforms. The Act gives effect to section 216 of the Constitution of the Republic of South Africa, which requires that the National Treasury should introduce generally recognised accounting practices. To this effect the Minister of Finance, by regulation in terms of section 91, established the Accounting Standards Board as a juristic person. This Board was established with the purpose of setting standards of generally recognised accounting practice to be adhered to by South African government entities. These accounting standards are expected to adhere to international best practice in respect of public-sector accounting and would provide the basis for compiling data according to the *GFSM 2001* framework.

The IMF published a supplement to the *GFS Yearbook* of 2002, containing government finance statistics in the revised analytical framework for a number of countries. Working with GFS compilers, the IMF published the accrual accounting data for a number of countries, but in addition, the historic cash accounting data of a number of countries, including South Africa, were converted to illustrate the use of the new analytical framework. As from the 2003 edition of the *GFS Yearbook* all the government finance statistics will only be published in the new format.

Adjustments made to the *Quarterly Bulletin* tables (Tables S71 – S79)

As a step in the migration towards publishing government finance statistics according to the revised *GFSM 2001* framework, the Government Finance Statistics, as previously presented in Tables S71 – S79 of the *Quarterly Bulletin*, were revised to reflect the conversion of the cash data to the analytical framework of the *Statement of sources and uses of cash*. These changes were specifically effected in this edition of the *Bulletin* to coincide with the start of reporting data for the new fiscal year 2003/04. Although historic data are in some instances insufficient to fully complete these new tables, broad conversion guidelines and assumptions were followed in the conversion process, as indicated in Table 4.

It should also be noted that separately identifiable data on the payments of social benefits are currently not available for all levels of government. These payments are included in the other expense categories if not shown separately.

In addition to the above-mentioned conversions, financial data on the result of the activities of the non-financial public corporations are also now presented in the same format than that of the general government. Previously, these data were sourced from less comprehensive surveys conducted by the Reserve Bank. Data for the fiscal years

2000/01 and 2001/02 were sourced directly from the published financial statements of these corporations. Past trends in their financial data were used to estimate quarterly data for this period. Data for periods prior to the analysis of the financial statements were retained and it should be noted that this could constitute a break in the time series.

Table 4: Summary of major changes effected in Tables S-71 to S-79

GFS 1986	Amendments to derive *GFS 2001*
Tax revenue	Disaggregated to reflect *taxes* and *social contributions* separately
Non-tax revenue	Recorded as *other receipts*
Capital revenue	Recorded as cash flow from investment activities – *sales of non-financial assets*
Grants	Continue to be recorded as grants
Goods and services	Disaggregated to record *compensation of employees* and *purchases of goods and services* separately
Interest	Continue to be recorded as *interest*
Subsidies and current transfers	Disaggregated to record subsidies, grants, social benefit payments and other expenses separately. In addition capital transfers were added to the respective categories, as relevant
Acquisition of capital assets	Recorded as cash flow from investment activities – *purchases of non-financial assets*
Capital transfers	Capital transfers were disaggregated to be included in: - grants if the transfer was made to another government or international organisation; or - social benefit if the transfer was made to the household sector; or - other expenses if the transfer was irregular in nature and used to recapitalise an entity or if debt was forgiven
Net lending	Recorded as part of cash flows from financing activities
Domestic and foreign financing	Disaggregated to record the incurrence or redemption of *liabilities*, the acquisition or disposal of *financial assets*, and the change in *cash and cash equivalents* separately

Local government data were revised to include the gross revenue and expense of trading accounts of local governments in accordance with the recommendations of *GFSM 2001*. Previously, only the net result of these trading activities was recorded as a source of non-tax revenue when a surplus was recorded or as a subsidy when a deficit was recorded. Following the institutional approach of *GFSM 2001*, the gross result of these market establishments is included in the statistics for local government due to the fact that they do not operate as a separate institutional unit.

Table S-79 reports the non-financial public-sector borrowing requirement (PSBR). However, it should be noted that this estimate of the non-financial PSBR differs from the estimates previously reported due to the revised reporting formats of Tables S-71 to S-78. The non-financial PSBR is now calculated as the inverse of the cash surplus/deficits of all levels of government, which differs due to the net lending amount previously included in the calculation of the deficit/surplus and the revised results of the analysis of the public corporations.

Conclusion

As with the financial results of companies in the private sector, a thorough analysis of the government's accounts requires more than just an abbreviated cash flow statement. South Africa is moving towards an integrated presentation of stocks and flows of the public sector's activities. The more comprehensive disaggregation shown in Tables S-71 to S-79 of this *Quarterly Bulletin* is an important step forward in ensuring adherence to best practice in the dissemination of government finance statistics.

Notes to tables

South African Reserve Bank assets and liabilities, and money-market accommodation – Tables S-2, S-3 and S-27

The South African Reserve Bank Act, No 90 of 1989, did not provide for the direct withdrawal and depositing of additional amounts against Cash Reserve Accounts (CRAs) when the refinancing system was implemented in March 1998. The Act was amended to reverse these arrangements and Cash Reserve Contra Accounts (CRCAs) were abolished. As from February 2003 onwards, the withdrawal and depositing of additional amounts against CRAs are applied directly to balances on these accounts. The terminology used in the above-mentioned tables has been amended accordingly.

Key information: Capital market – Table S-147

The value of transfer duties collected replaces the value and number of real-estate transactions, which have become unavailable. The sectors for which changes in share prices are shown have been adjusted in accordance with the table on page S-32. While gold mining is still shown separately, non-gold mining has been replaced by resources – the overarching sector which includes gold and non-gold mining and mining finance as well as oil and gas. Financial shares have also been added.