Quarterly Bulletin

September 2008

South African Reserve Bank

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Statements issued by Mr T T Mboweni, Governor of the South African Reserve Bank

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Introduction

The slowdown in global economic growth continued during the second quarter of 2008. This moderation in growth was largely due to a contraction in economic activity experienced in Japan and the euro area, and stagnant production volumes in the United Kingdom. Output growth accelerated in the United States (US), partly in response to temporary fiscal stimulation. Although growth in some emerging-market and developing countries also moderated during the quarter, it remained firm and continued to be underpinned by the strong performance of the Chinese economy.

Despite the moderation in growth, global output volumes continued to reach new heights in each quarter and capacity constraints continued to limit the supply of key commodities. Against this background the price of Brent crude oil, for example, rose to levels of around US$146 per barrel in early July 2008, while the prices of wheat, maize, platinum and gold were also exceptionally buoyant in the first half of 2008. Under these circumstances, inflationary pressures intensified further in both advanced and emerging-market economies. In many countries this resulted in a further tightening of the monetary policy stance. However, in a few instances concerns about decelerating economic growth and continued dislocations in the credit markets prompted central banks to reduce policy interest rates.

On the African continent real growth is expected to exceed 5 per cent for the seventh consecutive year in 2008. Net oil exporter countries have been experiencing more favourable growth than the oil importers. As elsewhere in the world, food price inflation worsened considerably in most parts of Africa during the past year.

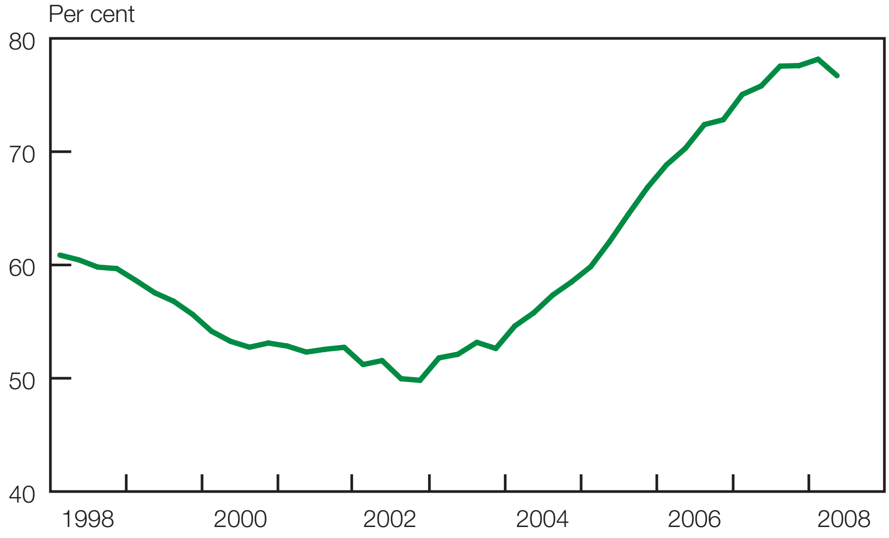
In South Africa real gross domestic production rebounded in the second quarter of 2008 and expanded at an annualised rate of 4,9 per cent. This improvement in growth in the second quarter of 2008 reflected strong increases in real value added by the primary and secondary sectors. The expansion was concentrated in mining and manufacturing, and could partly be attributed to base effects as electricity supply improved considerably in the second quarter, following severe disruptions, which weighed on production in the preceding quarter. The pace of growth in real value added by the tertiary sector slowed as tighter economic and credit conditions resulted in the first contraction registered by the trade sector since the third quarter of 2001.

In contrast to the rebound in real gross domestic production, aggregate real gross domestic expenditure contracted in the second quarter due to negative inventory investment, a decline in government consumption expenditure and slower growth in the other two components of domestic final demand.

Real final consumption expenditure by general government declined in the second quarter of 2008, reflecting the statistical effect of a high base set in the first quarter when expenditure was boosted by government's acquisition of a submarine.

Growth in real final consumption expenditure by households lost further momentum in the second quarter of 2008, led by a sharp decline in the demand for durable goods. In addition, real outlays on semi-durable and non-durable goods and services moderated over the period. Consumption responded to the rising interest rates and cost of servicing

Household debt as percentage of disposable income



Seasonally adjusted

household debt. This simultaneously contributed to greater caution among households in their use of credit: in the second quarter a reduction in the ratio of household debt to disposable income was registered, signalling the end of a four-year upswing in the household sector's debt ratio as households slowed their pace of debt accumulation.

Real gross fixed capital formation remained buoyant, although its pace of growth slowed on account of a moderation in capital investment by all institutional sectors over the period. With the exception of the construction and commerce subsectors, capital investment moderated throughout the private sector in the second quarter of 2008. Real fixed capital expenditure by public corporations remained quite strong, supported by capital outlays to address some of the electricity-supply constraints. The slowdown in investment spending was evident among all three tiers of government.

Export volumes benefited considerably from the recovery in mining and manufacturing production in the second quarter of 2008, while simultaneously the international prices of key export commodities were favourable to South African producers. Consequently, the trade deficit narrowed significantly in the second quarter. Net service, income and current transfer payments to the rest of the world remained at high levels. Together, these developments brought about a significantly smaller deficit on the current account of the balance of payments in the second quarter of 2008.

Whereas in the first quarter of 2008 foreign direct investment inflows featured prominently in the financial account of the balance of payments, capital inflows in the second quarter mainly comprised net portfolio and other investment capital. The net capital inflows on the financial account were sufficient to finance the deficit on the current account and allow for a further increase in the net official holdings of international reserve assets. At the same time, the external value of the rand against a basket of currencies recovered moderately, having depreciated by some 20 per cent during the previous quarter. The exchange value of the rand continued to appreciate in July.

In the first half of 2008 inflation gained further momentum. As in many other parts of the world, it was driven by the rising global prices of energy and food. Of concern was not only that CPIX inflation rose further above the inflation-target range, but also that indicators of second-round inflationary forces, such as wage settlements and the rate of increase in CPIX excluding food and petrol, continued to accelerate while significant increases in electricity prices were also in the pipeline.

The deterioration in the outlook for inflation motivated the South African Reserve Bank (the Bank) to raise the repurchase rate in April and June 2008, by 50 basis points on each occasion. With the economy seeming to be responding to the tighter monetary policies, and given the signs of moderation in some of the largely exogenous drivers of inflation such as the prices of crude oil and agricultural foodstuffs, the Bank did not raise interest rates further at the August 2008 meeting of its Monetary Policy Committee (MPC). Other money-market interest rates broadly kept pace with the repurchase rate.

The yields on conventional South African government bonds as well as break-even inflation rates rose significantly from mid-January 2008 to early July in response to deteriorating inflation expectations and widening risk premiums, but subsequently receded somewhat as market participants adopted more sanguine views on future inflation. The all-share price index reached a record high on 22 May 2008, bolstered by resources shares that benefited from high commodity prices. In the two months that followed commodity prices receded and resources share prices declined, dragging the all-share price index lower, notwithstanding a recovery in the prices of financial shares. House prices performed poorly in the first seven months of 2008 and recorded the lowest rates of increase since 1999.

Turnover in the bond, share and derivatives markets remained lively in the first seven months of 2008, while nominal income and expenditure also increased apace given the relatively high rate of inflation. These developments, higher interest returns on holdings of monetary deposits, as well as speculative and precautionary motives rendered support to growth in the M3 money supply. While growth in M3 moderated somewhat over the past year, it continued to exceed that of nominal gross domestic product, resulting in an all-time low income velocity of circulation of M3 in the second quarter of 2008.

The tighter credit conditions started to manifest in slower growth in loans and advances extended by banks. In the second quarter of 2008 advances to the household sector recorded sluggish increases, in tandem with the less buoyant property and vehicle markets. However, credit extension to the corporate sector retained considerable momentum.

Government's finances continued to be disciplined, as demonstrated by the virtually balanced fiscal position recorded in the first three months of fiscal 2008/09. Sound fiscal policy continued to nurture long-term growth prospects, building in a measure of protection against cyclical and external risks.

Domestic economic developments

Domestic output[1]

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

South Africa's *real gross domestic product* rebounded in the second quarter of 2008 and expanded at an annualised rate of 4,9 per cent, following sluggish growth at a rate of only 2,1 per cent in the first quarter. This improvement in growth in the second quarter of 2008 reflected strong increases in the real value added by the primary and secondary sectors, which comfortably offset a further moderation in real output growth of the tertiary sector over the period.

Real gross domestic product
Percentage change at seasonally adjusted annualised rates

	2007					2008	
Sectors	1st qr	2nd qr	3rd qr	4th qr	Year	1st qr	2nd qr
Primary sector	-1,1	-4,5	1,9	-1,1	-0,6	-13,9	16,9
Agriculture	7,4	8,3	4,4	11,2	0,9	17,2	19,6
Mining	-4,1	-9,1	0,9	-5,8	-1,2	-25,1	15,6
Secondary sector	7,8	2,0	0,6	8,1	5,8	1,0	12,3
Manufacturing	4,5	-0,1	-2,5	8,2	3,9	-1,0	14,5
Tertiary sector	5,6	5,9	6,8	5,1	5,7	4,2	1,4
Non-agricultural sector	*5,5*	*3,9*	*4,9*	*5,1*	*5,3*	*1,5*	*4,7*
Total	**5,5**	**4,0**	**4,6**	**5,1**	**5,1**	**2,1**	**4,9**

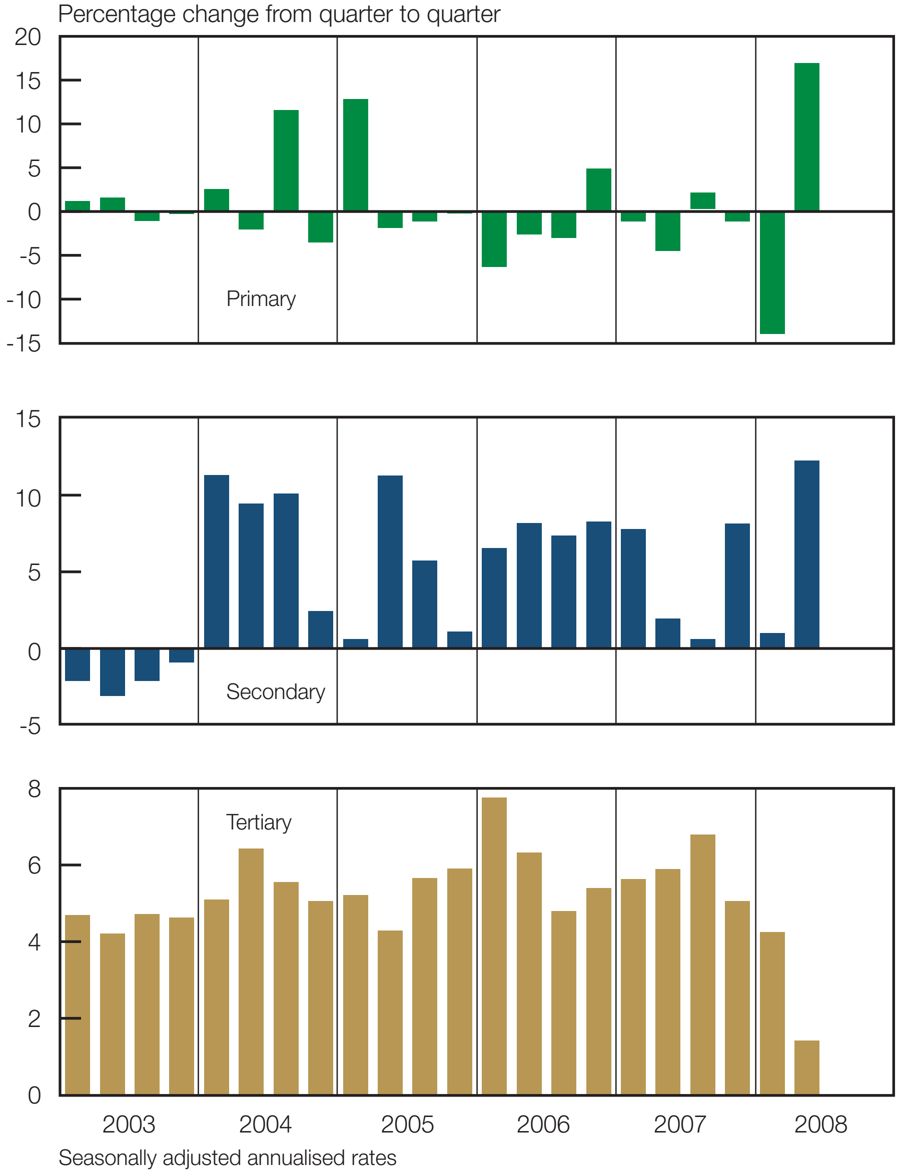
The quarter-to-quarter change in the real value added by the *primary sector* rebounded from an annualised rate of decline of 13,9 per cent in the first quarter of 2008 to a rate of increase of 16,9 per cent in the second quarter. Real output of the mining sector, in particular, recovered in the second quarter of 2008, following a sharp contraction in the preceding quarter.

Real output growth in the *agricultural sector* edged higher from the first to the second quarter of 2008. Favourable weather conditions for field crop production, combined with a marked increase in the acreage planted, resulted in higher output volumes over the period. The size of the commercial maize crop was expected to increase from 7,1 million tons in the 2006/07 production season to 11,6 million tons in the 2007/08 season.

The real value added by the *mining sector* recovered some of its earlier losses in the second quarter of 2008 and rose at an annualised rate of 15,6 per cent, following a contraction of 25,1 per cent in the first quarter. On a year-on-year basis, however, real output of the mining sector still contracted in the second quarter. Production of gold, diamonds, coal and platinum increased in the second quarter of 2008, notwithstanding the fact that the mines had to operate at power levels fluctuating between 90 and 95 per cent of their earlier electricity requirements. The more stable supply of electricity and favourable commodity prices more than offset the loss of production due to continuing, but fewer, safety-related shutdowns over the period.

Having increased at an annualised rate of only 1 per cent in the first quarter of 2008, the real value added by the *secondary sector* expanded at a rate of 12,3 per cent in the second quarter, primarily due to the improved performance of the manufacturing sector.

Real gross domestic product by sector



Subsequent to a decline of 1,0 per cent in the first quarter of 2008, output in the *manufacturing sector* expanded at an annualised rate of 14,5 per cent in the second quarter – the improved performance of the sector could partly be attributed to base effects, following the subdued level of production in the preceding quarter. The increase in production was especially pronounced in the subsectors for food and beverages, and petroleum and petroleum-related products.

While production in the manufacturing sector recovered in the second quarter of 2008, it coincided with a further drop in business confidence levels. The utilisation of production capacity in the manufacturing sector receded from 85,4 per cent in the first quarter of 2008 to 85,1 per cent in the second quarter – slightly below the recent peak of 86,5 per cent registered in the second quarter of 2007.

The real value added by the *sector supplying electricity, gas and water* contracted marginally to a negative rate of 1,3 per cent in the second quarter of 2008, compared with a strong decline at an annualised rate of 6,2 per cent in the preceding quarter.

Exports of electricity to neighbouring countries were lower in the second quarter of 2008 than during the first quarter, while the volume of imported electricity increased during this period. Even though the average coal stockpiles at power stations still fell short of the targeted 20 days of supply, the supply of coal to Eskom and the availability of electricity improved considerably. However, a mild winter contributed to lower electricity demand in the second quarter.

Activity in the *construction sector* remained extremely buoyant considering that the real value added by the sector increased at an annualised rate of 10,6 per cent in the second quarter of 2008, lower than the rate of 14,9 per cent recorded in the first quarter. This moderation in growth reflected deteriorating conditions in the residential and non-residential building sectors, as developers increasingly felt the strain of higher interest rates and mounting inflationary pressures. The activity of the civil construction sector held up well in both quarters.

The pace of growth in the real value added by the *tertiary sector* slowed from 4,2 per cent in the first quarter of 2008 to 1,4 per cent in the second quarter, mainly reflecting notably slower growth registered in the trade sector.

The real value added by the *trade sector*, which increased at an annualised rate of 3,6 per cent in the first quarter of 2008, declined at a rate of 2,2 per cent in the second quarter – the first contraction since the third quarter of 2001. Slower output growth in the retail and motor trade subsectors mainly contributed to the weaker growth. Tighter credit conditions and inflationary pressures negatively affected consumer spending and consumer confidence levels in the second quarter of 2008.

Real output growth in the *transport, storage and communication sector* increased from an annualised rate of 3,5 per cent in the first quarter of 2008 to 4,1 per cent in the second quarter. Increased activity in both the transport and communication subsectors boosted performance in the sector.

Growth in the real value added by the *finance, insurance, real-estate and business services sector* decelerated from 4,9 per cent in the first quarter of 2008 to 2,3 per cent in the second quarter, following weaker growth in the subsector for finance. Likewise, activity in the real-estate sector tapered off somewhat.

The real value added by the *general government sector* decelerated noticeably from growth at an annualised rate of 4,6 per cent in the first quarter of 2008 to 1,1 per cent in the second quarter.

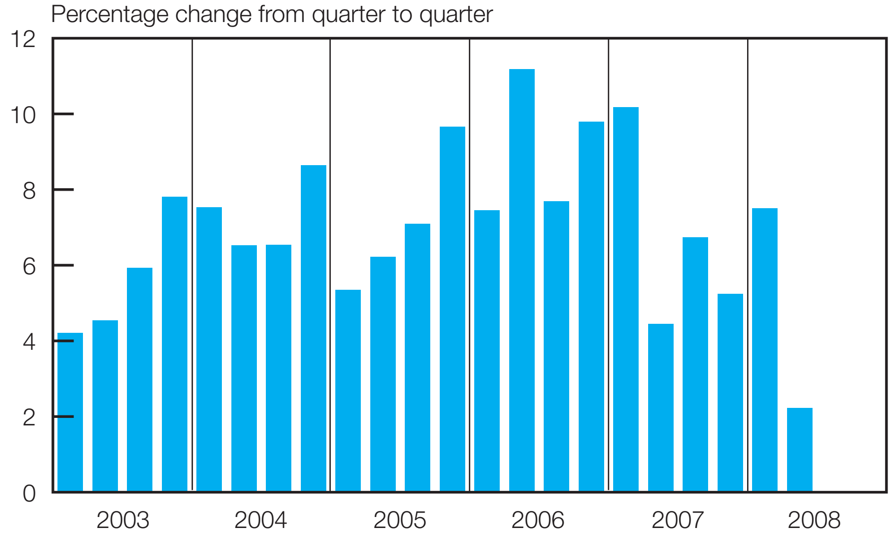
Domestic expenditure

In contrast to the rebound in growth in real domestic production in the second quarter of 2008, aggregate *real gross domestic expenditure* contracted at a rate of 4,2 per cent over the same period. This reversal in growth was brought about by substantially slower growth in all components of domestic final demand. In addition, real inventories were depleted over the period.

Growth in *final consumption expenditure by households* continued on a downward trend from its most recent quarter-to-quarter peak registered in the first quarter of 2007. Having increased at an annualised rate of 3,3 per cent in the first quarter of 2008, growth in household spending slowed to 1,2 per cent in the second quarter, led by a sharp decline in the demand for durable goods. In addition, real outlays on semi-durable and non-durable goods abated over the period.

Real gross domestic final demand

Percentage change from quarter to quarter



Seasonally adjusted annualised rates

Real gross domestic expenditure

Percentage change at seasonally adjusted annualised rates

	2007					2008	
Components	1st qr	2nd qr	3rd qr	4th qr	Year	1st qr	2nd qr
Final consumption expenditure:							
Households	7,2	4,9	4,4	3,8	7,0	3,3	1,2
General government	14,0	-3,8	8,7	1,2	5,0	12,8	-1,4
Gross fixed capital formation	17,2	11,2	12,9	14,1	14,8	16,9	9,1
Domestic final demand	**10,2**	**4,4**	**6,7**	**5,3**	**8,0**	**7,5**	**2,2**
Change in inventories (R billions)*	12,9	9,1	6,5	-8,7	4,9	9,8	-6,8
Gross domestic expenditure	**6,8**	**2,9**	**5,2**	**0,0**	**6,0**	**14,2**	**-4,2**

* At constant 2000 prices

A contraction in demand for personal transport equipment – mainly new motor vehicles – restricted growth in total spending on *durable goods* in the second quarter of 2008. Spending on furniture and household appliances and on medical equipment also lost considerable momentum over the period. This moderation in spending was, however, partly countered by an increase in spending on durable recreational and entertainment goods. As a result, real expenditure on durable goods contracted at a rate of 14,9 per cent in the second quarter of 2008, compared with a decline of 8,1 per cent in the preceding quarter.

The declining demand for new motor vehicles reflected the confluence of overall slower economic activity, reduced income growth, high household debt levels, tighter credit conditions and rising fuel prices.

Real final consumption expenditure by households
Percentage change at seasonally adjusted annualised rates

	2007					2008	
Components	1st qr	2nd qr	3rd qr	4th qr	Year	1st qr	2nd qr
Durable goods	10,7	-15,7	8,9	2,5	5,2	-8,1	-14,9
Semi-durable goods	11,9	22,7	3,5	8,4	16,0	10,5	2,4
Non-durable goods	6,4	3,9	5,2	1,9	5,5	3,0	0,2
Services	5,0	6,0	2,9	4,0	5,4	4,3	6,5
Total	**7,2**	**4,9**	**4,4**	**3,8**	**7,0**	**3,3**	**1,2**

A contraction in spending on motor car tyres, parts and accessories, together with subdued demand for clothing and footwear, resulted in slower growth in real expenditure on *semi-durable goods* in the second quarter of 2008. Real spending on the other subcategories of semi-durable goods also either slowed or contracted, causing growth in overall household expenditure on semi-durable goods to slow to a rate of 2,4 per cent in the second quarter, compared with an increase of 10,5 per cent in the first quarter of 2008.

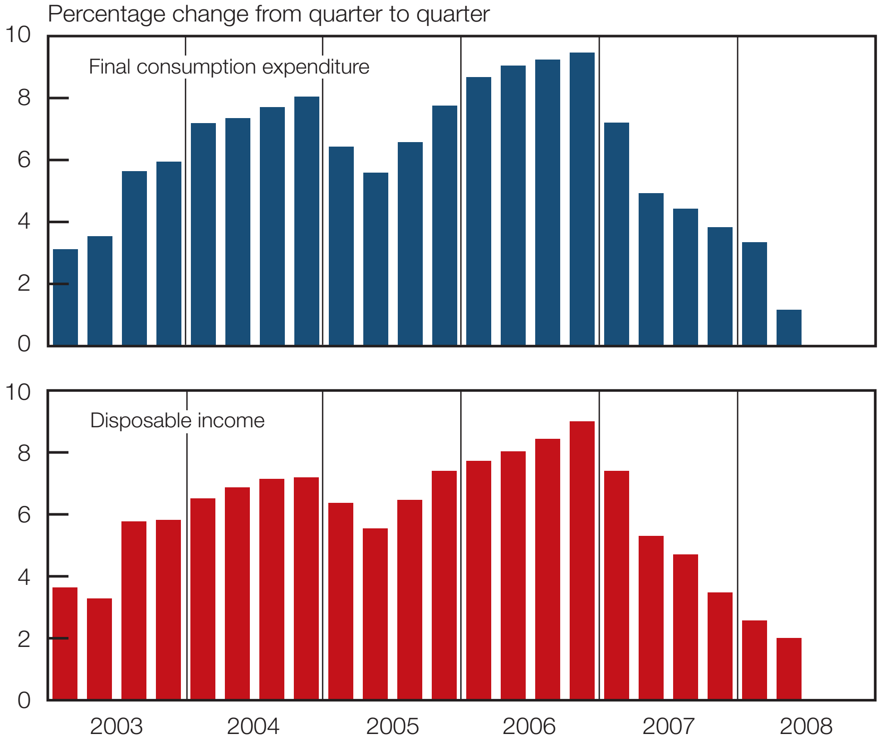
Growth in real expenditure on *non-durable goods* slowed from an annualised rate of 3,0 per cent in the first quarter of 2008 to less than half a per cent in the second quarter. Private consumer demand for household fuel and power, medical and pharmaceutical products, and petroleum products contracted over the period. In addition, demand for all other categories of non-durable goods decreased. Increased prices of most of these components were particularly responsible for declining trends in real outlays on these items.

Quarter-to-quarter growth in real household expenditure on *services* increased from an annualised rate of 4,3 per cent in the first quarter of 2008 to 6,5 per cent in the second quarter. Spending on household services and transport and communication services more than offset decreased spending in the other categories over the period.

Growth in *real disposable income of households* eased from 2,6 per cent in the first quarter of 2008 to an annualised rate of 2,0 per cent in the second quarter. This moderation in growth was reflected in sustained growth in compensation of employees and slower growth in net income from property. Consistent with the slower pace of growth in consumer spending and the prevailing tighter credit conditions, growth in credit extended to households lost momentum in the second quarter of 2008. As the pace of debt accumulation by households tapered off in the second quarter of 2008, the ratio of household debt to disposable income slowed notably to 76,7 per cent during the second quarter of 2008 from 78,2 per cent in the first quarter. However, the ratio of debt-service cost to disposable income of households rose from 11,3 per cent in the first quarter of 2008 to 11,6 per cent in the subsequent quarter.

After increasing at a buoyant rate of 12,8 per cent in the first quarter of 2008, real final *consumption expenditure by general government* turned around and declined at a rate of 1,4 per cent in the second quarter. This contraction partly reflected the statistical effect of the high base set in the first quarter, when growth was boosted by the acquisition of a submarine in terms of government's Defence Procurement Programme.

Real final consumption expenditure and disposable income of households

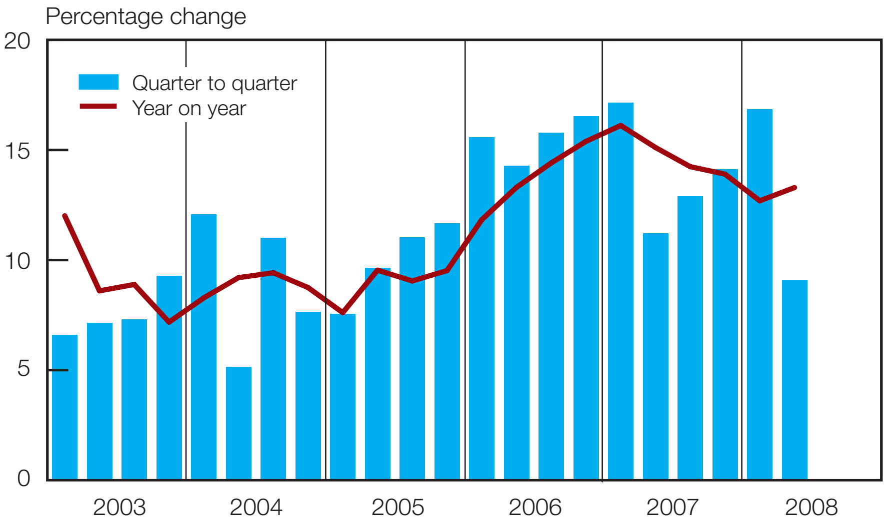


Seasonally adjusted annualised rates

Real gross fixed capital formation remained buoyant, although the pace of growth slowed from an annualised rate of 16,9 per cent in the first quarter of 2008 to 9,1 per cent in the second quarter. Capital investment by all institutional sectors moderated over the period.

Having increased at an annualised rate of 11,2 per cent in the first quarter of 2008, growth in real fixed capital outlays by *private business enterprises* slowed to 9,9 per cent in the second quarter. With the exception of the construction and commerce sectors,

Real gross fixed capital formation



Seasonally adjusted annualised rates

capital investment moderated in all other subsectors of the private sector over the period. The upgrading of freeway networks provided further impetus to investment by contractors. Consumer demand, although subdued, continued to provide an incentive for the further expansion of retail space and, accordingly, gave rise to further growth in real fixed outlays by the commerce sector. In the agricultural sector the acquisition of agricultural machinery proceeded briskly against the background of favourable product prices, increased production volumes and late summer rains.

Real fixed capital expenditure by *public corporations* remained quite strong and increased to an annualised rate of 9,9 per cent in the second quarter of 2008. While investment expenditure in the sector supplying electricity, gas and water maintained its upward momentum in order to address electricity supply constraints, the transport sector also advanced real capital investment in the second quarter of 2008. The refurbishment of coaches to improve rail services in particular contributed to increased investment in rail infrastructure.

Growth in gross fixed capital formation by *general government* decelerated in the second quarter of 2008. This slowdown in investment spending was evident among all three tiers of government. Provincial governments have broadly maintained their capital investment in addressing provincial infrastructural backlogs. Although real capital spending on transport equipment tapered off in the second quarter of 2008, the demand for trucks was supported by various infrastructural projects.

Real inventory investment reversed from an accumulation of R9,8 billion in the first quarter of 2008 to an inventory depletion of R6,8 billion in the second quarter. In part, the slower pace of inventory accumulation could be attributed to a reduction in inventories in the mining and manufacturing sectors. Since the maize-harvesting season started, the delivery of maize to silos has been giving rise to real inventory accumulation in the trade sector by increasing the agricultural stocks-in-trade. Real inventory investment subtracted 4,7 percentage points from growth in real gross domestic expenditure in the second quarter of 2008, compared with a positive contribution of 5,8 percentage points in the first quarter.

Factor income

Growth over four quarters in *total nominal factor income* accelerated from 14,7 per cent in the first quarter of 2008 to 17,7 per cent in the second quarter. The increase in total nominal factor income resulted from higher growth in the operating surpluses of business enterprises and compensation of employees.

Growth over four quarters in *compensation of employees* increased marginally from 10,9 per cent in the first quarter of 2008 to 11,3 per cent in the second quarter. This development was particularly evident in the government sector, with pronounced increases in the wage bill of provincial government over this period.

The *nominal gross operating surplus* of business enterprises, measured over four quarters, increased from 18,3 per cent in the first quarter of 2008 to 23,6 per cent in the second quarter. This increased growth mainly occurred in the agricultural, manufacturing and mining sectors where high international trade volumes and a positive exchange rate boosted income earnings.

Gross saving

The country's *saving ratio* (gross saving as a percentage of gross domestic product) increased markedly from 13,9 per cent in the first quarter of 2008 to 14,9 per cent in the second quarter. Gross saving by the corporate sector and by households increased, offsetting a slightly weaker saving performance by general government. The level of gross saving increased by an annualised R32,0 billion in the second quarter of 2008, thereby lowering South Africa's dependency on foreign capital to finance investment from a recent peak of 39,0 per cent in the first quarter of 2008 to 32,8 per cent in the second quarter.

Gross saving by the *corporate sector* as a percentage of gross domestic product advanced from 9,8 per cent in 2007 and 10,0 per cent in the first quarter of 2008 to 11,1 per cent in the second quarter. Strong performances by the agricultural, mining and manufacturing sectors boosted the operating surpluses of business enterprises. This increase comfortably neutralised the marginally higher interest and dividend payments recorded in the second quarter of 2008.

The gross saving ratio of the *general government* increased steadily from 2,4 per cent in the third quarter of 2007 to 2,7 per cent in the first quarter of 2008, before declining to 2,3 per cent in the second quarter. The saving level of general government continued to benefit from tax revenue, although growth in total tax revenue moderated during the second quarter of 2008. The growth in total tax revenue slowed from 19,6 per cent in 2005 to 13,4 per cent in 2007 and to only 9,1 per cent in the second quarter of 2008.

The gross saving rate of the *household sector* edged up from 1,3 per cent in the first quarter of 2008 to 1,4 per cent in the second quarter. The slower pace of growth in final consumption expenditure and marginally higher year-on-year growth rates in current income contributed to the increased saving performance.

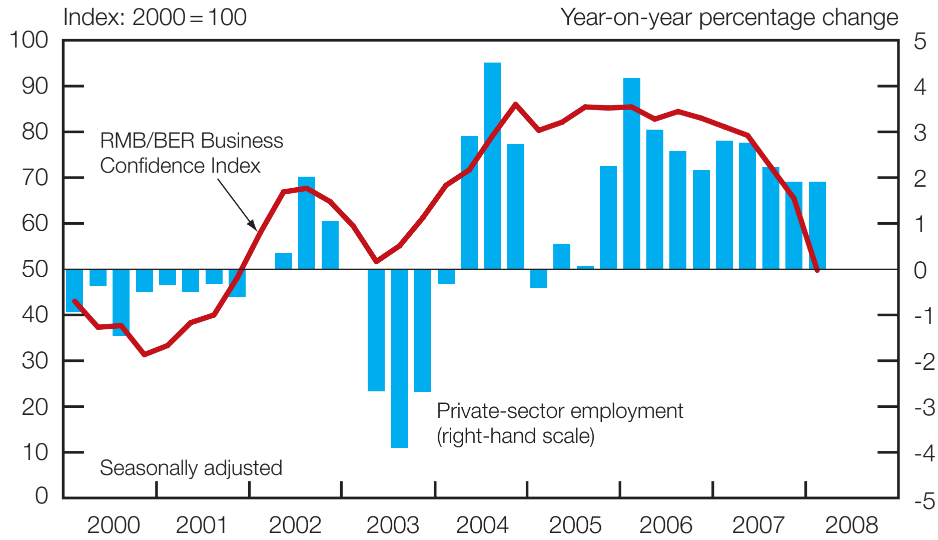
Employment

Despite the slowdown in real growth in the first quarter of 2008, the level of formal non-agricultural employment increased at a firm seasonally adjusted and annualised rate of 3,9 per cent during the quarter. According to the *Quarterly Employment Statistics (QES)* survey conducted by Statistics South Africa (Stats SA), the number of employed advanced to 8,4 million over the period. This somewhat puzzling pickup in employment numbers within an environment of slackening output growth was probably related to the temporary nature of the setback to production arising from the interruptions in electricity supply; employers preferred to maintain their workforce under the circumstances. Furthermore, a meaningful increase in employment in the finance, insurance, real-estate and business services sector was recorded in the opening months of 2008. Private-sector employment, constituting roughly 79 per cent of formal non-agricultural employment, increased at a quarter-to-quarter and annualised rate of 4 per cent during this period, while public-sector employment numbers expanded at a rate of 3,4 per cent.

Within the private sector, quarterly employment gains were evident in the construction; non-gold mining; financial; and trade, catering and accommodation services sectors. The quarter-to-quarter rate of increase in employment in these sectors ranged from 4 per cent to 9,2 per cent in the first quarter of 2008. In the public sector, employment growth during this period was most pronounced at provincial level, followed by public enterprises.

The Rand Merchant Bank/Bureau for Economic Research (RMB/BER) Business Confidence Index decreased substantially between the fourth quarter of 2007 and the second quarter of 2008, pointing to sluggish employment growth in coming months. Despite the quarterly increase in formal non-agricultural private-sector employment in the first quarter of 2008, the year-on-year rate of increase slowed appreciably from 2,8 per cent in the second quarter of 2007 to 1,9 per cent in the first quarter.

Business confidence and private-sector employment



Source: Rand Merchant Bank/Bureau for Economic Research (RMB/BER) and Stats SA

Since the second half of 2006 the manufacturing sector has experienced significant job losses. This trend persisted throughout most of 2007 and into the first quarter of 2008. This weakness in manufacturing employment is corroborated by recent readings of the employment sub-index of the Investec Purchasing Managers Index, which has mostly fallen below the neutral level of 50 since February 2008, indicating possible employment losses.

Enterprise-surveyed formal non-agricultural employment: Changes during the first quarter of 2008

Quarter-to-quarter seasonally adjusted changes

Sector	Number	Annualised percentage change
Mining	40	0,0
Gold mining	-5 330	-11,8
Non-gold mining	5 370	6,6
Manufacturing	-700	-0,2
Electricity supply	-690	-4,9
Construction	5 120	4,4
Trade, catering and accommodation	18 940	4,4
Transport, storage and communication	1 340	2,1
Financial intermediation and insurance	41 280	9,2
Community, social and personal services	340	0,3
Total private sector	**65 710**	**4,0**
National, provincial and local government	13 720	3,6
Public-sector enterprises	1 150	2,0
Total public sector	**14 870**	**3,4**
Grand total	**80 580**	**3,9**

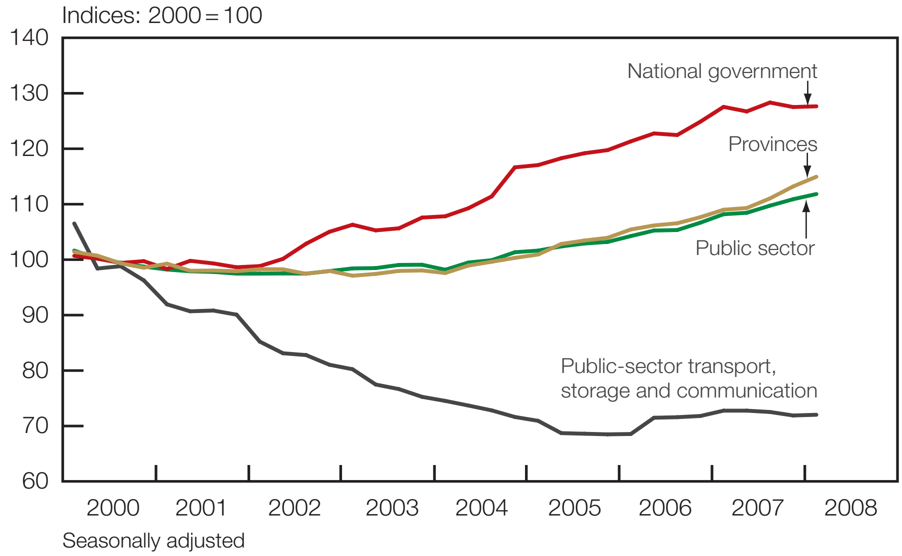
Construction activity in the domestic economy has been buoyed by increased investment expenditure in recent quarters, spurring employment growth to an annualised rate of 4,4 per cent in the first quarter of 2008. Measured over four quarters, employment growth moderated from 2,7 per cent in the final quarter of 2007 to 0,7 per cent in the first quarter of 2008. Continued optimism in the civil construction industry relates to major construction projects, such as the building of the 2010 World Cup stadiums, water schemes, roads, bridges and the Gautrain rapid rail link. However, residential building contractors are facing tight conditions due to weaker consumer demand and, as such, expect job pruning during the second quarter of 2008. The confidence levels of non-residential building contractors remained positive, but moderated somewhat as tendering competition intensified and profit margins came under pressure. Weaker demand conditions and lower profit margins were the main reasons cited for the moderation in confidence levels.

Mining employment benefited from the boom in commodity prices during the past few years. The gold-mining sector generated significant employment opportunities in response to the rising gold price, recording a consistent increase in employment numbers since the first quarter of 2006. However, employment numbers in this sector fell back in the first quarter of 2008. Job creation in the non-gold mining sector has been increasing, following continued strong global demand for mining commodities in recent years. Insufficient electricity supply, safety concerns at mines and high fuel prices have recently constrained mining production and were probably also reflected in employment in this sector.

As already mentioned, meaningful gains in employment were recorded in the finance, insurance, real-estate and business services sector in the first quarter of 2008, when job opportunities rose at an annualised quarter-to-quarter rate of 9,2 per cent. Employment in the trade, catering and accommodation services sector also remained robust, rising at a seasonally adjusted and annualised rate of 4,4 per cent during this quarter.

Employment growth in the public sector in recent years has primarily been driven by steady increases at national and provincial government levels. Since 2000, considerable employment losses have, however, occurred in the public-sector transport, storage and communication sector. The public sector, which is generally less sensitive to austere economic conditions, further expanded its job complement at an annualised rate of

Public-sector employment



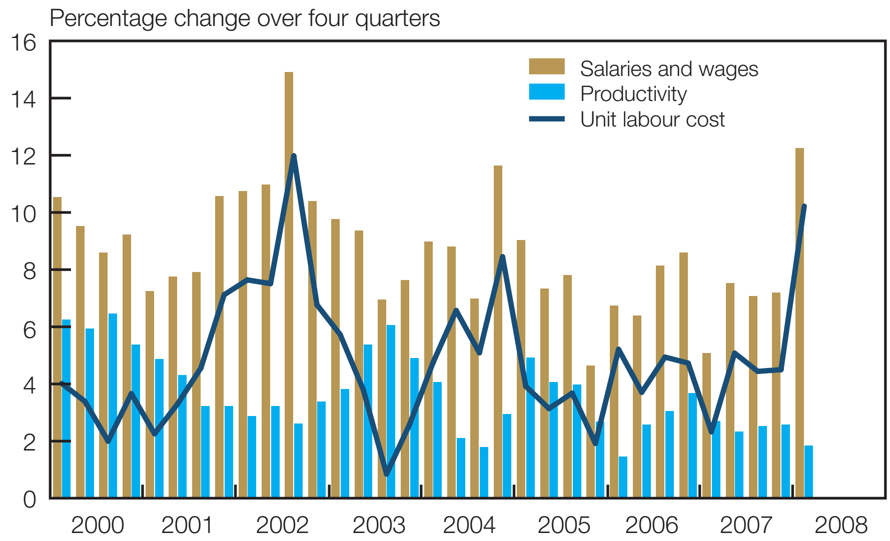
3,4 per cent in the first quarter of 2008 when compared with the previous quarter. Job creation progressed across all tiers of the public sector in this quarter, except in the transport, storage and communication sector.

Labour cost and productivity

When measured over a four-quarter period, nominal remuneration per worker in the formal non-agricultural sector of the economy increased at a rate of 12,3 per cent in the first quarter of 2008. This came off a low base, but was the highest rate of increase in almost six years. Remuneration growth in the private sector more than doubled from 6,1 per cent in the fourth quarter of 2007 to 12,6 per cent in the first quarter of 2008, while that in the public sector amounted to 11 per cent in the first quarter of 2008. Given the increases in the cost of living in South Africa, some acceleration in wage inflation could be expected. Increases in average nominal salaries and wages per worker in the private sector were, with the exception of the gold-mining and transport, storage and communication sub-sectors, in excess of 10 per cent in the year to the first quarter of 2008. In the public sector, marked increases over four quarters of 14,7 per cent and 12,8 per cent were recorded in national departments and provinces respectively in the first quarter of 2008.

According to the private-sector labour consultancy Andrew Levy Employment Publications, the average rate of wage settlements amounted to 8,3 per cent in the first half of 2008, compared with 6,8 per cent in the same period of the preceding year. Following the more pronounced deceleration in economy-wide output growth in the non-agricultural sectors of the economy relative to employment growth, labour productivity growth moderated from a year-on-year rate of 2,6 per cent in the fourth quarter of 2007 to 1,8 per cent in the first quarter of 2008. Growth in nominal unit labour cost (the cost of labour per unit of gross domestic output) in the formal non-agricultural sector of the economy accelerated significantly to 10,2 per cent in the first quarter of 2008. The rate of increase in nominal unit labour cost in the manufacturing sector also accelerated markedly from 1,4 per cent in the year to the fourth quarter of 2007 to 6,6 per cent in the year to the first quarter of 2008, following the substantial increase in salaries and wages during this period.

Salaries and wages, productivity and unit labour cost in the formal non-agricultural sector

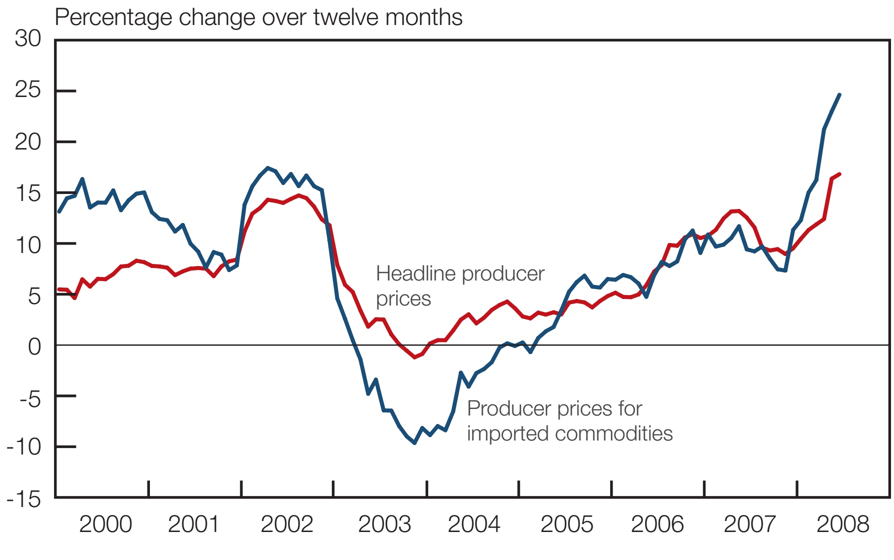


Prices

Consumer and producer price inflation moved to a higher plane in most parts of the world during the past year, fuelled by the rising prices of food, oil and commodities in general. Most inflation-targeting economies overshot their inflation targets and South Africa was no exception to this phenomenon. Domestic price pressures intensified at both the producer and consumer level, compounded by supply-side constraints. Producer price inflation scaled new heights and reached a year-on-year rate of 16,8 per cent in June 2008, while the gap between actual CPIX inflation and the upper band of the inflation target range of 6 per cent also continued to widen and tallied to 5,6 percentage points. Twelve-month CPIX inflation measured 11,6 per cent in June 2008 and 13,0 per cent in July.

Year-on-year *producer price inflation* accelerated from 9 per cent in November 2007 to 16,8 per cent in June 2008, driven by sharply rising prices of basic steel, other metals and crude oil, combined with a depreciation in the exchange value of the rand. Producer price inflation of domestic output in the mining and quarrying sector increased from 3,7 per cent in the year to October 2007 to 17,7 per cent in the year to June 2008. Inflation in the producer prices of petroleum and coal products accelerated for nine consecutive months to a twelve-month rate of 40,4 per cent in June 2008. The prices of basic metal and steel products also increased markedly, recording a year-on-year rate of 36,4 per cent in June 2008. By contrast, year-on-year producer price inflation at the agricultural level decelerated considerably from 29,5 per cent in October 2007 to 6,0 per cent in June 2008 as the production of grain and vegetables, among other things, increased.

Producer prices

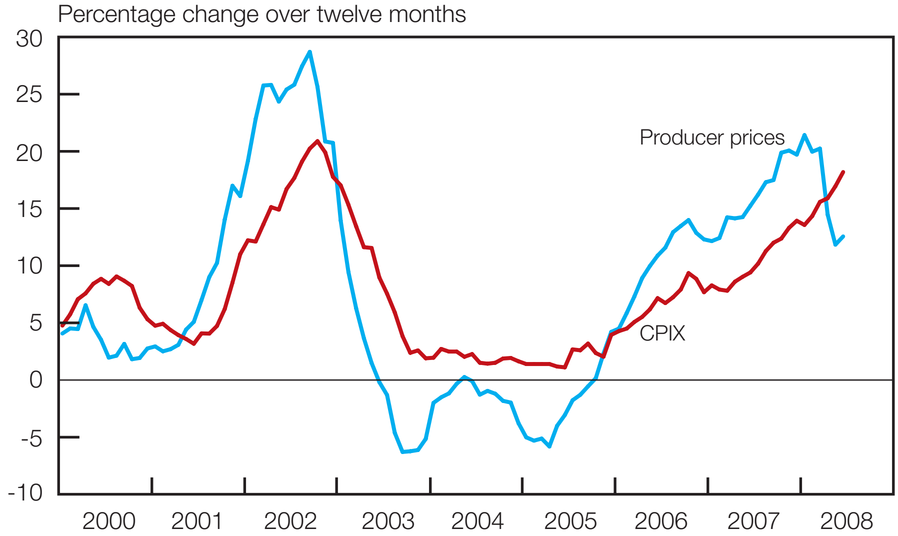


Imported commodity price inflation amounted to a year-on-year rate of 24,6 per cent in June 2008, compared with a substantially lower rate of 7,3 per cent in November 2007. This substantial acceleration could primarily be attributed to significant increases in the prices of mining and agricultural commodities, manufactured food products, products of petroleum and coal, and chemicals and chemical products.

Twelve-month inflation in the producer prices of food products accelerated markedly from the end of 2006 to reach a high of 21,4 per cent in January 2008. This acceleration was brought about by the steep increase in domestic food prices, primarily at the agricultural level, but also at the manufactured level. In fact, when measured over twelve months, the rate of increase in the prices of food at the agricultural level accelerated from 15,6 per cent in January 2007 to 27,7 per cent in October, mainly due to increases in the prices of grain products, particularly wheat. However, in subsequent months it decelerated substantially and amounted to 2,0 per cent in June 2008. The twelve-month rate of increase in the prices of food at the manufactured level accelerated from 9,8 per cent in February 2007 to as much as 20,4 per cent in March 2008, before decelerating to 19,4 per cent in June.

Food prices

Percentage change over twelve months



CPIX consumer food price inflation consequently accelerated significantly from 7,9 per cent in February 2007 to 17,6 per cent in June 2008. The most pronounced increases occurred in the price of fats and oils, which rose at a year-on-year rate of 65,0 per cent in June. Grain product prices, especially bread and pasta prices, and the prices of milk, milk products and eggs also recorded year-on-year rates of increase of more than 20 per cent in June 2008.

By June 2008 headline producer price inflation exceeded CPIX inflation by as much as 5,2 percentage points, indicating sustained cost–push pressures from the producer level, which may possibly affect consumer price outcomes in coming months.

Twelve-month CPIX *goods price inflation* more than doubled from 6,6 per cent in August 2007 to 14,4 per cent in June 2008. Besides the impact of food and petrol on CPIX goods price inflation, price increases in excess of the 6-per-cent level were fairly widespread, such as for transport goods, household consumables, medical goods and personal care goods.

Lagging somewhat behind the acceleration in CPIX goods price inflation, *CPIX services price inflation* accelerated from a year-on-year rate of 4,6 per cent in January 2007 to 6 per cent in January 2008, breaching the upper limit of the inflation target range in April 2008, before accelerating to 6,7 per cent in June. Higher rates of increase in CPIX services prices were fairly pervasive, led by increases in homeowners' cost, domestic workers' wages and education costs.

The relative price of food

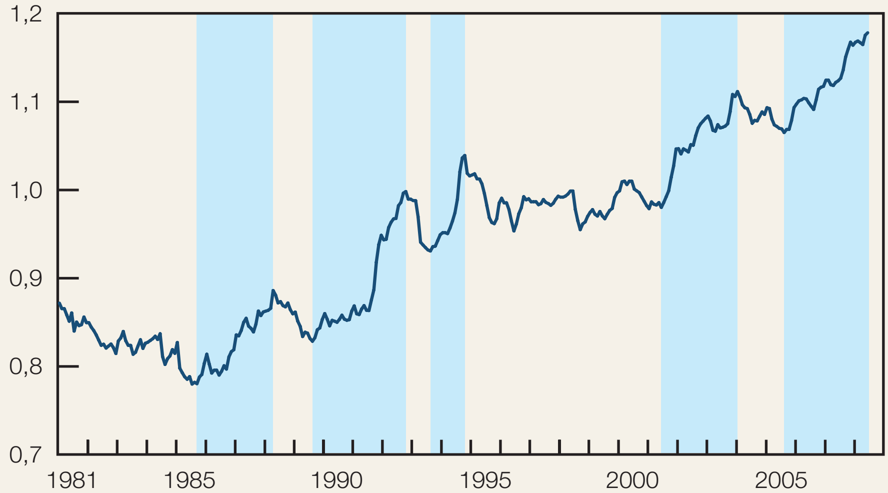
The accompanying graph depicts the relative price of food, calculated as the ratio of consumer prices of food to the headline consumer price index. Not surprisingly, this ratio displays an upward trend over the longer term. However, the focus in this box is on the duration of shorter-term cycles in food prices. Periods of cyclically rising relative food prices have been identified, using as a guideline that the relative price of food should rise cumulatively by 10 per cent or more in a broadly continuous fashion, followed by a significant decline in the relative price series. In reviewing the period since 1981, five episodes of cyclically rising food prices were identified:

Trough	Peak	Duration
September 1985	April 1988	31 months
September 1989	October 1992	37 months
August 1993	October 1994	14 months
June 2001	January 2004	31 months
August 2005	June 2008 or later	34 months plus

The current rising phase, which started in August 2005, has so far continued for 34 months. Three of the preceding upward phases had a broadly similar duration. The longest of them – and therefore the most protracted episode of rising relative food prices in the past quarter of a century – had a duration of 37 months.

Numerous factors may play a role in generating food price cycles. However, conventional supply and demand responses tend to limit the amplitude of food price swings. For instance, rising relative prices of food prompt producers to raise food output. While fairly long lags are involved, this eventually moderates food price increases.

Ratio of food prices to total headline consumer prices



Shaded areas indicate periods of rising relative food prices

Substantiating the view that inflationary pressures became more broad-based in recent months, six of the ten main components, constituting roughly 71 per cent of the overall CPIX index, increased at year-on-year rates in excess of 6 per cent in June 2008. As indicated in the accompanying table on page 18, year-on-year inflation in the prices of only two components, with a combined weight of almost 9 per cent, fell below the lower boundary of the inflation target range in June 2008, while only two components, constituting approximately 20 per cent of the basket, remained within the inflation target range. Food prices, one of the two main drivers of inflation, increased at a year-on-year rate of 18,2 per cent in June 2008, substantially in excess of the 7,8 per cent recorded 15 months earlier.

Inflation in CPIX components

Percentage change over twelve months

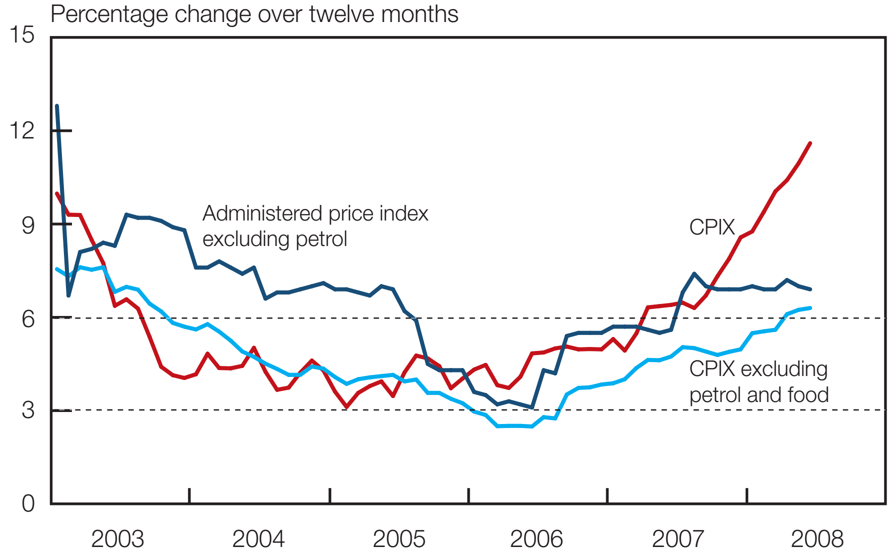
	Weights	June 2008
Transport running cost	5,7	33,6
Food and soft drinks	26,9	17,8
Clothing and footwear	4,1	10,2
Alcoholic beverages and tobacco	3,1	6,6
Total housing services	13,4	8,4
Total other goods (not included elsewhere)	17,5	7,6
Services excluding housing and transport	16,5	*5,7*
Total transport services	*3,9*	*4,8*
Vehicles	5,7	0,5
Furniture and equipment	3,2	0,2
Total CPIX	100,0	11,6

Italics denote values inside the inflation target range of between 3 and 6 per cent in June 2008

Inflation in the prices of administered goods and services accelerated from a year-on-year rate of 4,6 per cent in February 2007 to 16,0 per cent in June 2008. However, if petrol prices were to be excluded from the calculation, administered prices would have increased at a far lower rate of 6,9 per cent in the year to June 2008. Price increases in excess of 6 per cent were pervasive in the components for housing, education, fuel, power and communication.

Measures of underlying CPIX inflation

Percentage change over twelve months



At the beginning of July 2008 Stats SA announced its intention to release various reweighted and rebased consumer price inflation measures in February 2009. The consumer price index will undergo reweighting with the introduction of new expenditure weights, based largely on the *Household Income and Expenditure Survey* of 2005/06. The Classification of Individual Consumption by Purpose (COICOP) will replace the current International Trade Classification (ITC). The consumer price index will also be rebased so that 2008 equals 100. However, consumer price indices published for 2008 are, and will remain, the official consumer price indices for 2008.

Foreign trade and payments

International economic developments

Most recent projections by the International Monetary Fund (IMF) indicate that global output growth is expected to moderate from 5 per cent in 2007 to 4,1 per cent in 2008 and 3,9 per cent in 2009. Global consumer and investment sentiment continues to be negatively affected by the ongoing financial market turmoil following the sub-prime mortgage market problems in the United States (US). Commodity prices, and more specifically food and energy prices, continued to surge in the first half of 2008, adding to mounting global inflationary pressures.

Real economic growth in the US accelerated further in the second quarter of 2008, whereas real output in the euro area contracted due to technical reasons related to the rapid growth in the previous quarter, slower global growth, and the adverse impact of high food and energy prices. Economic activity in Japan also contracted in the second quarter of 2008 as a result of negative contributions from exports, private consumption expenditure and public investment.

Tentative signs indicate that real output growth in emerging economies moderated somewhat in the second quarter of 2008. The pace of economic expansion remained robust in China as real growth progressed at a rate of 11,5 per cent in the second quarter of 2008. According to IMF projections, the solid growth momentum in Africa is expected to persist with real gross domestic product projected to increase at a rate of 6,4 per cent in both 2008 and 2009.

Mounting inflationary pressures due to rising food and energy prices continue to be a concern for many policy-makers in an environment of slowing economic growth. Having increased notably towards the end of 2007, annual headline consumer price inflation in the US surged to a 17-year record high in July 2008. However, excluding food and energy, inflation remained fairly stable. Inflationary pressures in the euro area continued to intensify in the second quarter of 2008 and annual headline inflation accelerated to a record-high rate of 4 per cent during the period. After returning to positive territory, the annual rate of change in Japan's core consumer price index (consumer prices excluding fresh food) reached its highest level in almost eleven years in June 2008. The rise in inflation could mainly be attributed to higher fuel prices.

Annual consumer price inflation also continued to accelerate in most emerging-market countries in the second quarter of 2008, driven by strong domestic demand growth, supply constraints and rising commodity prices. The reduction in fuel subsidies in many Asian countries also added to recent inflationary pressures. Countries such as Indonesia, the Philippines, Russia, Turkey and Venezuela registered double-digit inflation rates in July 2008, while countries such as Chile and Ecuador also approached such a threshold with rates of 9,5 per cent and 9,9 per cent respectively.

Since April 2008, monetary policy has been tightened in countries such as Brazil, Chile, Denmark, the euro area, Hungary, India, Indonesia, Israel, Mexico, Poland, Russia, South Korea, Sweden, Taiwan, Thailand and Turkey. By contrast, Canada, the Czech Republic, Hong Kong, New Zealand, the United Kingdom and the US have lowered policy rates. The US Federal Open Market Committee reduced the target for the federal funds rate further by 25 basis points to 2 per cent in April 2008, thereby effecting a cumulative 325-basis-point reduction since September 2007.

Current account

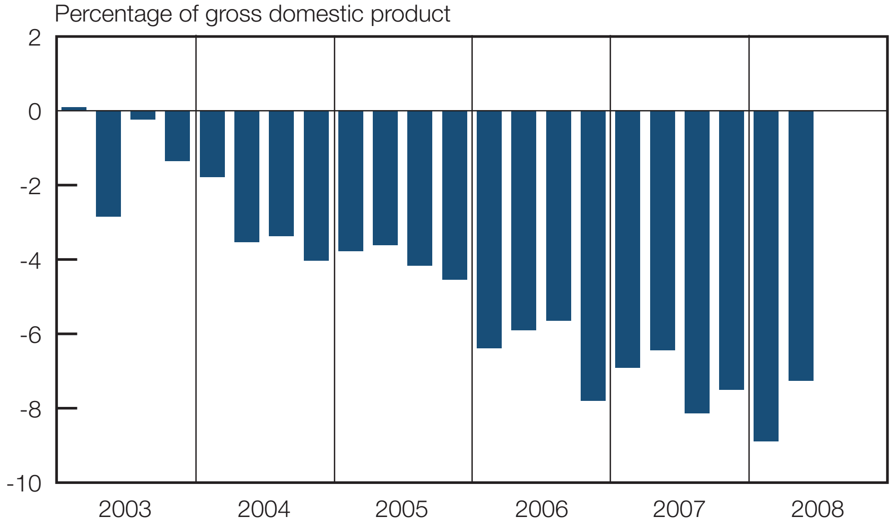
The recovery in output in the aftermath of the electricity-induced lapse in production in the first quarter of 2008, coupled with high international commodity prices and a more competitive exchange value of the rand, resulted in significant increases in both the volume and average price of South African exports in the second quarter. The improved export performance of local suppliers operating in the primary and secondary sectors of the economy coincided with more subdued domestic demand, and resulted in the substantial narrowing of the deficit on the trade account of the balance of payments from R61,4 billion in the first quarter of 2008 to R31,3 billion in the second quarter.

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

	2007				2008	
	2nd qr	3rd qr	4th qr	Year	1st qr	2nd qr
Merchandise exports	494,6	494,3	527,9	495,8	568,3	682,1
Net gold exports	36,3	41,0	45,1	39,9	46,1	47,5
Merchandise imports	-562,3	-587,3	-599,7	-576,0	-675,8	-760,9
Trade balance	-31,4	-52,0	-26,7	-40,3	-61,4	-31,3
Net service, income and current transfer payments	-94,7	-111,3	-131,0	-104,7	-133,2	-133,1
Balance on current account	-126,1	-163,3	-157,7	-145,0	-194,6	-164,4
As percentage of gross domestic product	*-6,4*	*-8,1*	*-7,5*	*-7,3*	*-8,9*	*-7,3*

Concurrently, the deficit on the country's net services, income and current transfer account with the rest of the world remained broadly unchanged. The deficit on the current account of the balance of payments consequently shrank to R164,4 billion or 7,3 per cent of gross domestic product in the second quarter of 2008. This same ratio amounted to 8,9 per cent in the first quarter of 2008.

Current-account balance



The value of merchandise exports advanced from R568,3 billion in the first quarter of 2008 to R682,1 billion in the second quarter or by 20 per cent. Higher export earnings largely emanated from a firm recovery in the volume of exported goods, but to a lesser extent also reflected an increase in the rand price of such goods.

Having contracted by 7,2 per cent in the first quarter of 2008, the volume of merchandise exports increased by 12,2 per cent in the second quarter. The substantial rebound in the volume of exported goods over the period could largely be attributed to South African producers, especially in the mining industry, stepping up their production levels in an effort to compensate for the loss of output caused by electricity supply disruptions in the opening months of 2008. A 10-per-cent increase in the volume of mining exports was, furthermore, augmented by a rise in the volume of manufactured exports. As a ratio of gross domestic product, the volume of merchandise exports amounted to almost 22 per cent in the second quarter of 2008 – a level previously recorded in the final quarter of 2006.

A slowdown in the rate of increase in international commodity prices, alongside the depreciation in the exchange value of the rand, resulted in a 7-per-cent increase in the rand price of merchandise exports in the second quarter of 2008 – export prices advanced by 16 per cent in the preceding quarter.

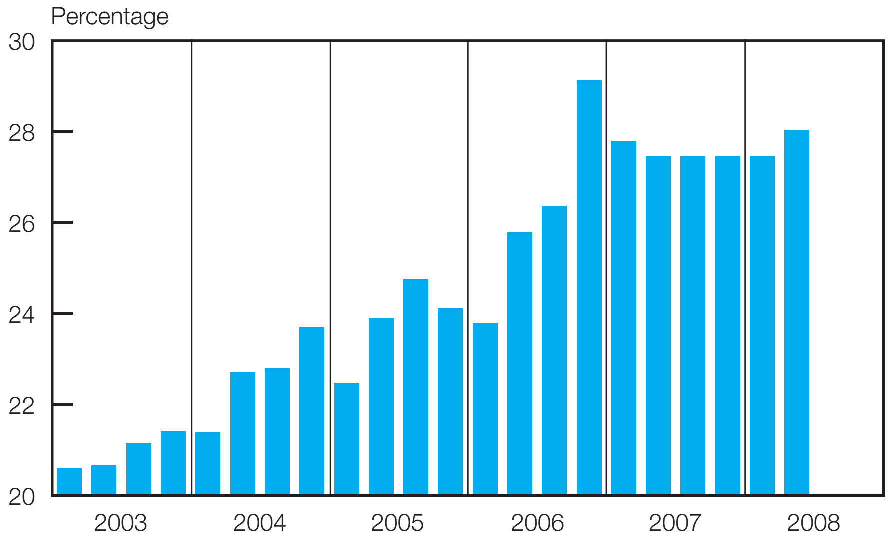
Similarly, the physical quantity of gold exports increased by 4,8 per cent in the second quarter of 2008 following a contraction of 22,9 per cent in the first quarter. The realised rand price of gold, however, declined by 1,5 per cent in the second quarter, notwithstanding the depreciation in the average exchange value of the rand during the period. As a result of the combined effect of a decline in the price of gold exports and an increase in their volume, the value of gold exports escalated further in the second quarter of 2008. On the London market the fixing price of gold declined by 3,3 per cent from US$927 per fine ounce in the first quarter of 2008 to US$897 per fine ounce in the second quarter. In July the fixing price of gold averaged US$941 per fine ounce.

Volume of merchandise exports

A further sharp increase in the international price of crude oil, together with the decline in the nominal effective exchange rate of the rand, raised the rand price of imported goods by 11,5 per cent in the second quarter of 2008. Despite only a marginal increase in the quantity of crude oil imports, the higher price of oil lifted the value of crude oil imports by 40,4 per cent in the second quarter of 2008, compared with a decrease of 4,6 per cent in the preceding quarter. The value of non-oil merchandise imports advanced by 8,1 per cent over the period due to noticeable increases in most of the subcategories of imports associated with fixed capital formation in the domestic economy.

Having previously increased at a much faster pace than the volume of merchandise exports, the volume of merchandise imports increased only marginally in the second quarter, consistent with the deceleration in domestic demand. Minor increases were recorded in the volume of crude oil as well as non-oil imports over the period. Notwithstanding the broadly unchanged import volumes, the country's import penetration ratio remained high at 28 per cent in the second quarter of 2008, signalling that a fairly large portion of aggregate domestic demand continues to be satisfied by foreign suppliers.

Import penetration ratio



The deficit on the net services, income and current transfer account moved sideways in the second quarter of 2008 as higher net service payments to the rest of the world were more than neutralised by a reduction in net dividend payments to non-resident investors. Increased net service payments in the second quarter of 2008 primarily reflected higher payments for freight-related services rendered by foreign carriers alongside escalating fuel prices. In addition, tourism expenditure by South African residents travelling abroad also increased.

A firm increase in the international price of crude oil, which surpassed that of other international commodity prices, had a dampening effect on South Africa's terms of trade during the second quarter of 2008. The country's terms of trade accordingly weakened by 4,7 per cent following an improvement of 5,6 per cent in the previous quarter. During July and the first half of August 2008 the prices of many commodities fell sharply, including the prices of platinum, gold and crude oil.

Financial account

Despite the ongoing turmoil in world financial markets, the South African economy continued to demonstrate its resilience by attracting net capital inflows to the value of R44,7 billion on the financial account of the balance of payments in the second quarter of

2008. Contrary to the first quarter of 2008, capital inflows in the second quarter largely comprised net portfolio and other investment capital. As a ratio of gross domestic product, the balance on the financial account, including unrecorded transactions, declined from 8,9 per cent in the first quarter of 2008 to 7,9 per cent in the second quarter.

Net financial transactions not related to reserves
R billions

	2007				2008	
	2nd qr	3rd qr	4th qr	Year	1st qr	2nd qr
Change in liabilities						
Direct investment	11,2	13,1	13,4	40,3	41,5	6,5
Portfolio investment	42,0	33,7	2,9	107,4	-19,1	27,3
Other investment	19,8	30,5	5,1	58,2	33,4	3,8
Change in assets						
Direct investment	-14,4	-2,2	-7,8	-26,2	-6,4	-5,5
Portfolio investment	-6,4	-4,5	-8,9	-24,2	-1,5	-4,7
Other investment	-7,4	-14,5	29,8	7,5	-3,7	15,4
Total financial transactions*	47,8	58,0	54,1	192,6	47,8	44,7

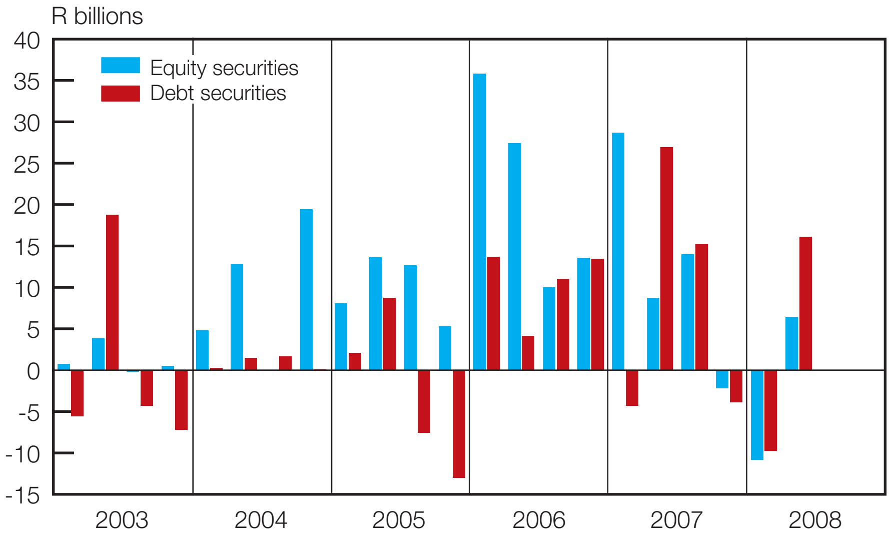
* Including unrecorded transactions

Foreign-owned assets in South Africa

Foreign direct investment into South Africa shrank from an inflow of R41,5 billion in the first quarter of 2008 to R6,5 billion in the second quarter. The further increase in direct investment liabilities mostly reflected loans extended by foreign parent companies to their domestic subsidiaries.

Portfolio investment liabilities rose by R27,3 billion in the second quarter of 2008 as non-resident investors increased their holdings of South African equity and fixed-interest securities. The inward movement of portfolio capital was, however, partially countered by the redemption of euro-denominated bonds in international capital markets by the National Treasury and private-sector entities. Foreign investor confidence in the country was most probably positively affected by the government's commitment to addressing structural shortages in the economy and persisting with sound macroeconomic policies.

Net portfolio investment flows



Other investment flows into the country decreased substantially from R33,4 billion in the first quarter of 2008 to R3,8 billion in the second quarter. In view of the decline in non-resident rand and foreign-currency deposits with the domestic banking sector, South African banks increasingly embarked on utilising foreign credit facilities in the second quarter of 2008.

South African-owned assets abroad

The acquisition of foreign direct investment assets by domestic entities increased by R5,5 billion in the second quarter of 2008 as South African companies extended loans to their foreign direct investment affiliates.

The acquisition of foreign portfolio assets by South African investors escalated by R4,7 billion in the second quarter of 2008 due to the further diversification of institutional and individual investors' investment portfolios. The outflow of capital was possibly partly encouraged by the further relaxation of exchange control regulations on outward portfolio investment earlier this year.

Other outward investment capital turned around from an outflow of R3,7 billion in the first quarter of 2008 to an inflow of R15,4 billion in the second quarter. The inward movement of capital in the second quarter mainly reflected a reduction in the foreign-currency deposits of domestic banks abroad, which was only partly offset by loan and trade finance extended to unrelated non-resident parties.

Foreign debt

South Africa's total outstanding foreign debt showed a distinct upward trend during the past two years, but decreased from US$75,3 billion in the fourth quarter of 2007 to US$74 billion in the first quarter of 2008. A further increase in foreign-currency-denominated debt was more than neutralised by a decline in the rand-denominated debt over the period.

Foreign debt of South Africa
US$ billions at end of period

	2007				2008
	1st qr	2nd qr	3rd qr	4rd qr	1st qr
Foreign-currency-denominated debt	**34,9**	**39,6**	**42,8**	**43,6**	**44,7**
Bearer bonds	10,3	13,9	14,8	15,2	16,0
Public sector	5,2	5,5	5,6	5,6	5,9
Monetary sector	10,7	11,2	13,2	12,7	12,5
Non-monetary private sector	8,7	9,0	9,2	10,1	10,3
Rand-denominated debt	**22,7**	**26,6**	**29,2**	**31,7**	**29,3**
Bonds	6,1	7,1	6,8	7,9	6,0
Other	16,6	19,5	22,4	23,8	23,3
Total foreign debt	**57,6**	**66,2**	**72,0**	**75,3**	**74,0**

Owing mainly to the depreciation of the US dollar against the euro and the subsequent revaluation of South Africa's debt, the level of foreign-currency-denominated debt expressed in US dollar terms rose by about US$1 billion from the end of December 2007 to the end of March 2008. While depreciating against the euro, the US dollar displayed some strength against the domestic currency, lowering the level of the country's rand-denominated debt by US$2,4 billion over the period. This decline occurred despite an increase in non-resident rand-denominated deposits with, and loans drawn upon by, the private-banking sector in South Africa.

Measured in rand terms, South Africa's total outstanding foreign debt increased from R511 billion at the end of the fourth quarter of 2007 to R601 billion at the end of the first quarter of 2008.

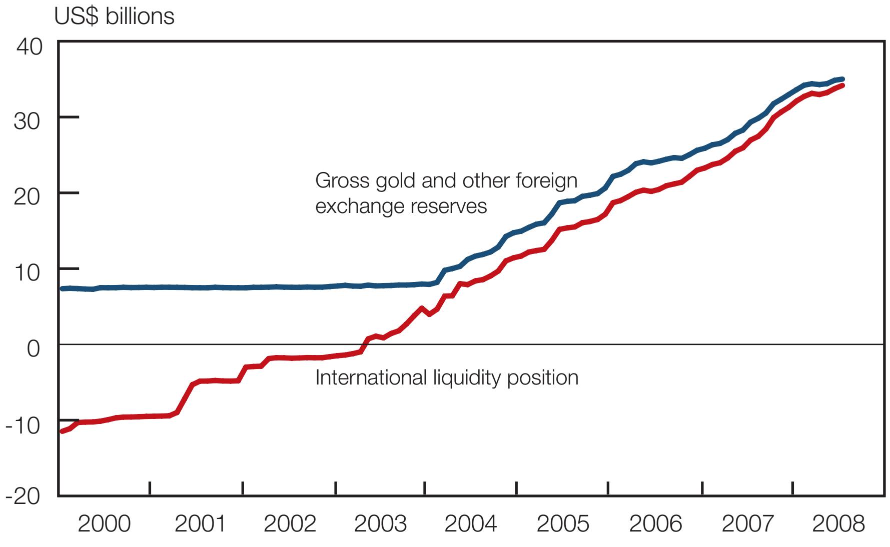
International reserves and liquidity

Net capital inflows on the financial account of the balance of payments continued to finance the deficit on the current account of the balance of payments. The country's overall balance of payments consequently recorded a surplus of R5,7 billion in the second quarter of 2008, compared with a surplus of R6,8 billion in the first quarter.

Measured in US dollars, the value of the gross international reserves of the South African Reserve Bank increased from US$34,4 billion at the end of March 2008 to US$34,9 billion at the end of June and further to US$35 billion at the end of July. At the same time, the utilisation of the Bank's short-term credit facilities declined from US$1,4 billion at the end of March 2008 to US$1,1 billion at the end of June 2008 and further to US$0,9 billion at the end of July. The level of import cover (the value of gross international reserves relative to the value of imports of goods, services and income) increased slightly from 13,6 weeks at the end of December 2007 to 13,9 weeks at the end of June 2008.

The Bank's international liquidity position increased from US$33,1 billion at the end of March 2008 to US$33,8 billion at the end of June 2008 and further to US$34,2 billion at the end of July.

Gross reserves and international liquidity position of the South African Reserve Bank



Exchange rates

After declining notably during the first quarter of 2008, the nominal effective exchange rate of the rand recovered some of its losses during the second quarter. On balance, the weighted average exchange rate of the rand increased by 3,6 per cent from the end of March 2008 to the end of June.

Exchange rates of the rand

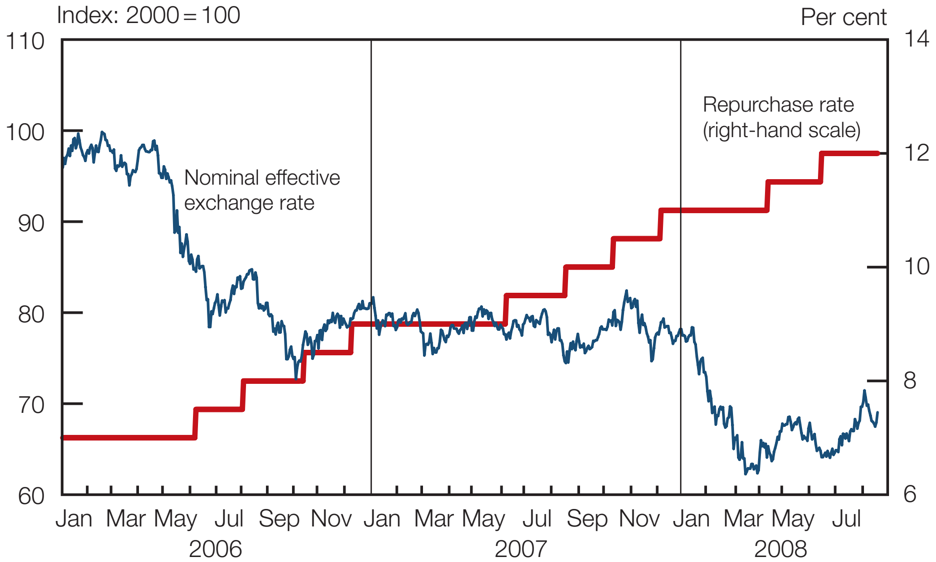
Percentage change

	28 Sep 2007 to 31 Dec 2007	31 Dec 2007 to 31 Mar 2008	31 Mar 2008 to 30 Jun 2008	30 Jun 2008 to 22 Aug 2008
Weighted average*	-0,4	-20,2	3,6	7,8
Euro	-2,3	-22,2	3,0	9,6
US dollar	1,4	-16,4	3,1	2,9
British pound	2,9	-15,9	2,6	10,0
Japanese yen	-1,4	-25,9	9,1	6,9

* Against a basket of 13 currencies

The strengthening of the domestic currency mainly occurred during April and May and was probably supported by the further tightening of the country's monetary policy. In addition, the continuation of the international credit-market turmoil during the second quarter probably helped to attract investors' excess funds to South Africa's financial markets in search of higher yields. During June 2008 the exchange value of the rand declined in response to a lower-than-anticipated interest rate increase by the MPC and the announcement of a larger-than-expected current-account deficit in the first quarter of 2008. The depreciation of the nominal effective exchange rate of the rand in June 2008 was further aggravated by a ratings agency's decision to change the outlook for South Africa's long-term issuer default rating from positive to stable.

Repurchase rate and nominal effective exchange rate



Despite lower international prices of certain commodities, and partly supported by the rebound in domestic output during the second quarter 2008, the exchange rate of the rand strengthened by 7,8 per cent from June 2008 to 22 August.

Following a decline of 15,4 per cent during the first quarter of 2008, the real effective exchange rate of the rand increased by 7,5 per cent in the second quarter. On balance, the inflation-adjusted effective exchange rate of the rand declined by 9 per cent in the first half of 2008.

The net average daily turnover in the domestic market for foreign exchange declined from US$17,3 billion in the first quarter of 2008 to US$17,1 billion in the second quarter. Non-resident investor participation in the spot market decreased gradually over the period.

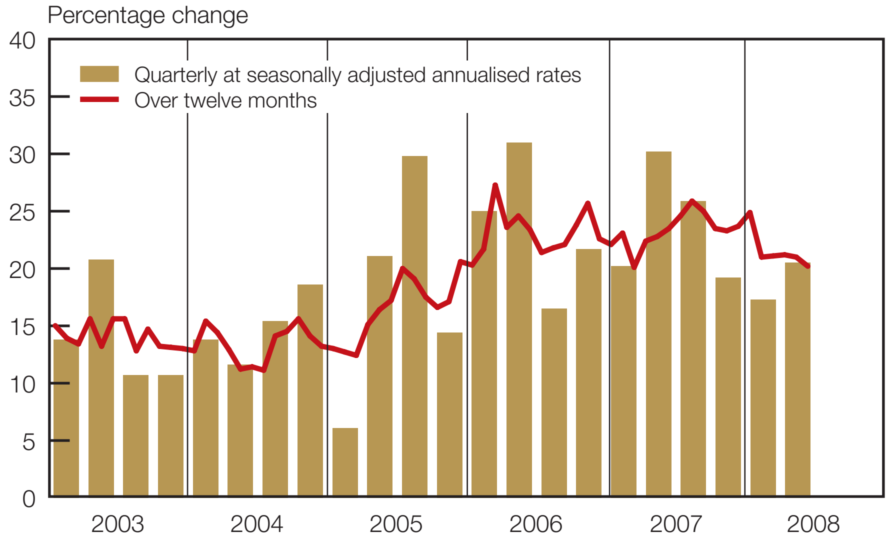
Monetary development, interest rates and financial markets

Money supply

2 The quarter-to-quarter growth rates referred to in this section are based on seasonally adjusted and annualised data.

Growth over twelve months in the broadly defined money supply (M3) fluctuated around 23 per cent in 2006 and 2007, but decelerated to levels of 21 per cent and lower from February 2008. Twelve-month growth in M3 stood at 20,1 per cent in June 2008. The slowdown in M3 growth is evident from the quarterly growth rates,[2] which have been in decline from a recent peak in the second quarter of 2007 and amounted to 17,3 per cent in the first quarter of 2008, picking up to 20,5 per cent in the second quarter.

Growth in M3



While growth in M3 was apparently restrained by the tighter credit and general economic environment, it remained comparatively high, supported by accelerating inflation with its impact on nominal income and expenditure. Lustreless share, bond and real-estate prices may also have triggered a stronger precautionary and speculative demand for money balances, as negative wealth effects impacted on confidence levels and created uncertainty about near-term economic prospects.

In the first and second quarters of 2008 market conditions noticeably affected the distribution of deposits across the various monetary aggregates. Uncertainty, coupled with rising interest rates, contributed towards strong growth in term deposits. Notes and coin in circulation accelerated somewhat as demand for cash increased, possibly reflecting the rising level of prices in the economy.

The corporate sector continued to be the main contributor towards growth in M3 in the second quarter of 2008, accounting for R56,6 billion of the overall increase of R78,7 billion in M3 deposits. Institutional investors continued to seek the relative safety of interest-bearing assets against the backdrop of volatility in financial markets and attractive rates of return offered on money-market instruments. Household-sector depositors contributed R22,1 billion towards growth in M3 over the same period.

Maturity analysis of growth in M3

Per cent at seasonally adjusted annualised rates

Component	2007		2008	
	3rd qr	4th qr	1st qr	2nd qr
Notes and coin	6,1	4,9	7,3	13,5
Cheque and transmission deposits	14,5	12,4	9,0	6,7
Call and overnight deposits	50,2	14,1	55,4	-33,5
Other short- and medium-term deposits*	47,5	16,7	-8,8	71,2
Long-term deposits**	-11,0	50,4	65,7	10,4
M3	25,9	19,2	17,3	20,5

* Unexpired maturities of more than one day and up to six months, and savings deposits
** Unexpired maturities of more than six months

The income velocity of circulation of M3 continued its downward trend to a new all-time low of 1,27 in the second quarter of 2008 as M3 grew at a faster pace than nominal gross domestic product.

The statistical counterparts of change in M3 are presented in the following table.

Counterparts of change in M3

R billions

	2007		2008	
	3rd qr	4th qr	1st qr	2nd qr
Net foreign assets	0,9	2,0	6,6	-7,5
Net claims on the government sector	2,6	-17,9	35,7	15,7
Claims on the private sector	88,0	75,0	108,5	48,8
Net other assets and liabilities	-10,7	4,9	-68,0	21,7
Total change in M3	**80,8**	**64,1**	**82,8**	**78,7**

Statistically, the increase in M3 during the first and second quarters of 2008 continued to be more than fully explained by the increase in banks' claims on the private sector, mainly as a consequence of growth in both mortgages and other loans and advances. Net claims on the government sector rose somewhat less vigorously in the second quarter compared with the first quarter of 2008, partly as a result of an increase in government deposits.

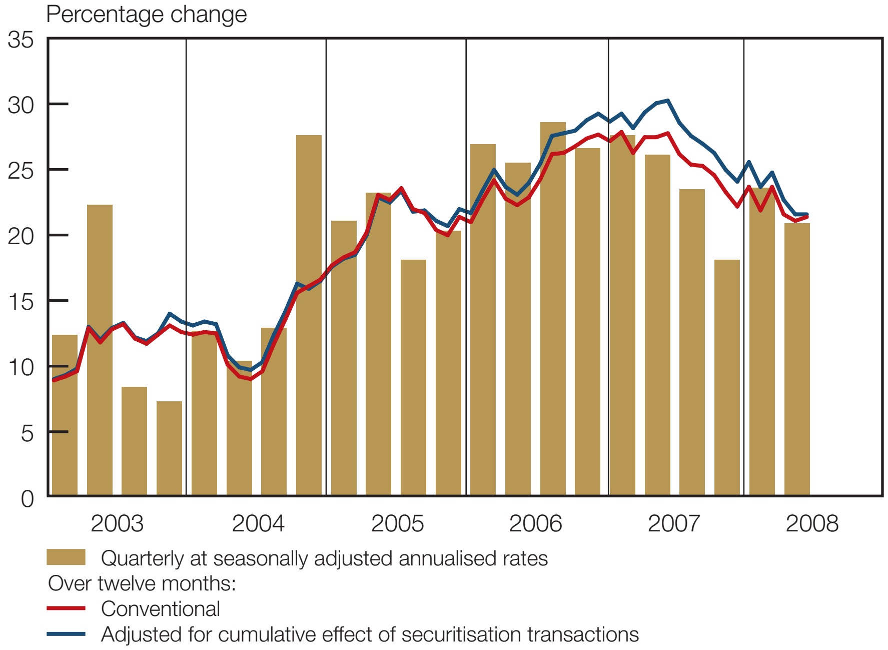
Credit extension

The tightening of credit conditions, concurrent with weaker consumer and business confidence about near-term economic prospects, contributed towards a moderation in growth of credit extended to the private sector during the second quarter of 2008. The twelve-month rate of growth in banks' total loans and advances[3] decelerated from 23,6 per cent in March 2008 to 21,0 per cent in May and 21,3 per cent in June. This was substantially lower than the growth rates which, on average, exceeded 25 per cent in 2007. Adjusted for securitisation transactions, growth over twelve months decelerated

3 Total loans and advances to the domestic private sector consist of instalment sale credit, leasing finance, mortgage advances, overdrafts, credit card and general advances. The first three categories are referred to as 'asset-backed credit', while the last three categories together are referred to as 'other loans and advances'.

from 24,7 per cent in March 2008 to 21,5 per cent in June. While private-sector banks had securitised R33,8 billion in asset-backed debt during 2007, securitisation transactions dwindled to only R1,4 billion during the first half of 2008.

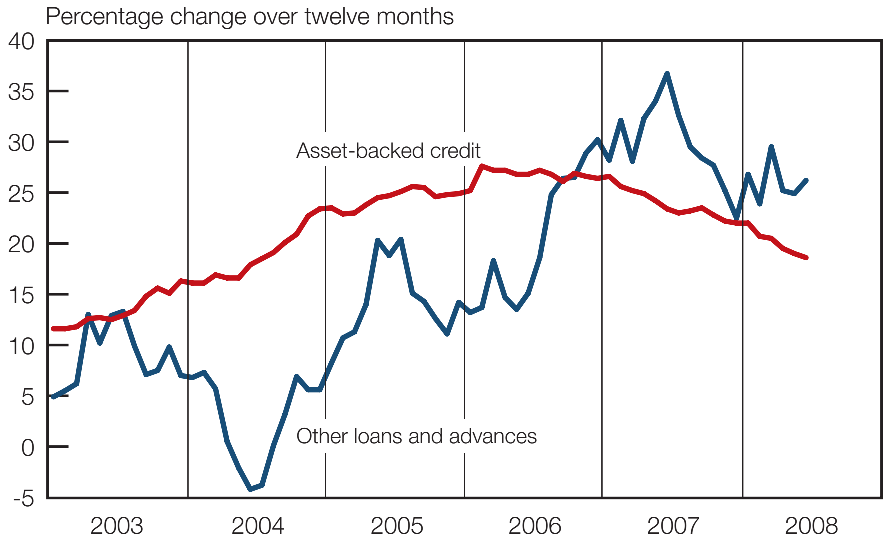
Total loans and advances to private sector



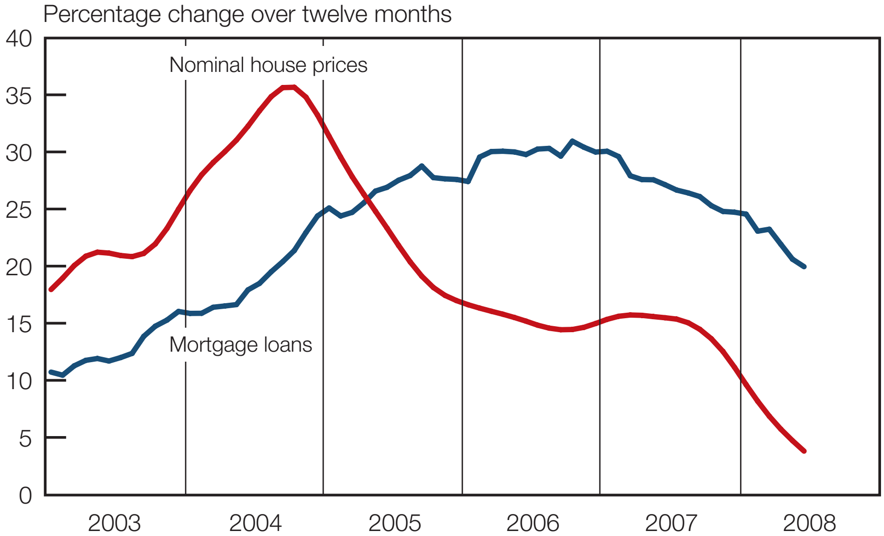
The quarterly growth in total loans and advances decelerated from 23,6 per cent in the first quarter of 2008 to 20,9 per cent in the second quarter.

In the first quarter of 2008 the category of other loans and advances was the main driver of the R118,4 billion expansion in total loans and advances, contributing R80,1 billion or 68 per cent to the overall increase. During the second quarter of 2008 this was surpassed by asset-backed credit, which contributed R31,3 billion to the overall increase of R53,1 billion in total loans and advances. However, twelve-month growth in asset-backed credit decelerated from 20,5 per cent in March 2008 to 18,6 per cent in June.

Loans and advances to private sector



Mortgage borrowing and house prices



Sources: Absa and own calculations

The further slowdown in growth in asset-backed credit in the second quarter of 2008 was concentrated in mortgage advances, which decelerated from a year-on-year growth rate of 23,2 per cent in March 2008 to 19,9 per cent in June, in tandem with less buoyant conditions in the real-estate market. Banks' mortgage advances were also reduced when one of the reporting banks transferred part of its mortgage book to a non-bank subsidiary.

Quarterly changes in banks' total loans and advances by type

R billions

	2008	
	1st qr	2nd qr
Mortgage advances	28,2	27,2
Instalment sale credit and leasing finance	10,0	4,1
Other loans and advances	80,1	21,8
Overdrafts	25,7	1,2
Credit card advances	1,4	0,8
General advances	53,1	19,9
Total loans and advances	**118,4**	**53,1**
Of which: To household sector	84,4	13,8
To corporate sector	34,0	39,3

Despite increasing by only R0,5 billion in May 2008 and R1,1 billion in June, twelve-month growth in *instalment sale credit and leasing finance* accelerated from 11,6 per cent in March 2008 to 14,0 per cent in June. The growth in this credit category can partly be attributable to the low base value recorded in the previous year when the implementation of the e-Natis vehicle registration system delayed some transactions in the motor-trade sector.

Other loans and advances, which mainly comprise borrowing by the corporate sector, recorded negative month-on-month growth in April and May 2008 before increasing sharply in June, probably on account of corporate tax payments. Nevertheless, growth over twelve months in this credit category remained high at 26,2 per cent in June 2008, although it was a significant decline from the rate of 29,5 per cent recorded in March.

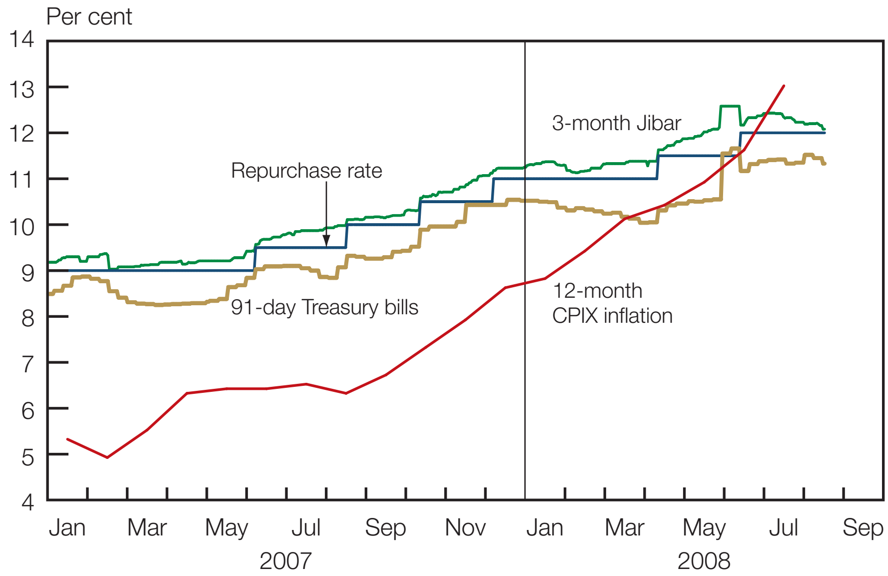
Growth in total loans and advances extended to the household sector temporarily surpassed that to the corporate sector in the first quarter of 2008, but dominance in this category reverted to the corporate sector in the second quarter. Of the R53,1 billion extended to the private sector, some R13,8 billion flowed to the household sector, while R39,3 billion flowed to the corporate sector.

Interest rates and yields

So far in 2008 the MPC raised the repurchase rate at its April and June meetings, to bring the rate to 12,0 per cent. Since the beginning of the interest-rate tightening cycle in June 2006, the MPC has raised the repurchase rate ten times, by 50 basis points on each occasion, as the inflation outlook deteriorated on account of sustained food and petrol price increases, and mounting broad-based price pressures or second-round effects. In August 2008 the repurchase rate was left unchanged. The MPC statement discussing developments underlying the August decision is reproduced elsewhere in this *Bulletin.*

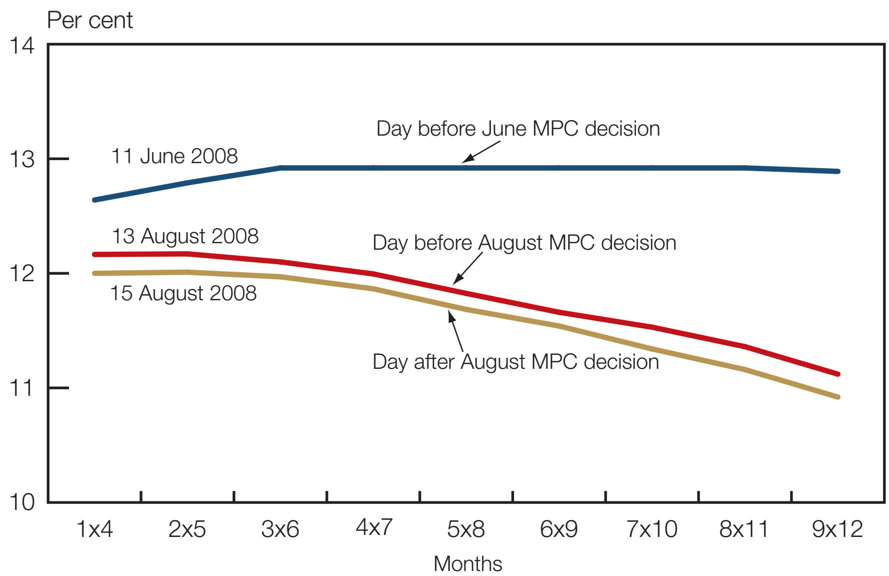
Other money-market interest rates generally adjusted upwards from May 2008, as further tightening of the monetary policy stance in June became imminent. The three-month Johannesburg Interbank Agreed Rate (Jibar), for example, rose by 50 basis points from 12,08 per cent on 27 May 2008 to 12,58 per cent at the end of May. It stabilised at that level before declining to 12,17 per cent on 13 June, following the lower-than-expected increase in the repurchase rate. The Jibar again edged higher to 12,43 per cent on 3 July 2008 before declining to 12,08 per cent on 23 August 2008, following the August repurchase rate decision.

Money-market rates and CPIX inflation



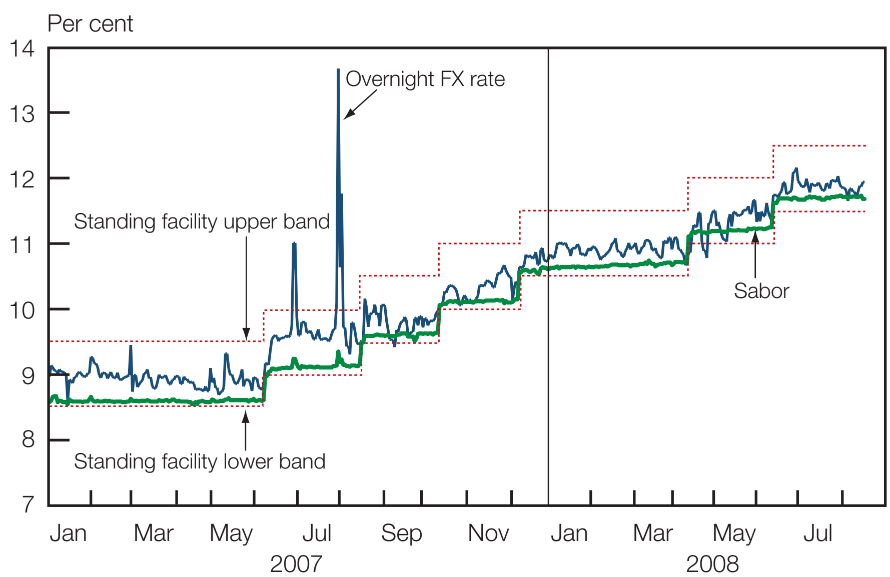
Rates on forward rate agreements (FRAs) followed suit and generally displayed an upward trend from May 2008 to mid-June 2008, as market participants increasingly expected a further tightening of the monetary policy stance. However, following the lower-than-expected repurchase rate increase of only 50 basis points on 13 June 2008, the FRA rates declined significantly. As indicated by the FRA yield curve, expectations of further increases in interest rates diminished significantly after the June MPC meeting. FRA rates trended lower from the beginning of July, alongside a moderate appreciation in the exchange value of the rand and a decline in international oil prices. The envisaged reweighting and rebasing of inflation measures by Stats SA also created expectations of a lower inflation rate from January 2009 than had been anticipated previously.

Forward rate agreement yield curves



The South African Benchmark Overnight Rate on deposits (Sabor) remained anchored to movements in the repurchase rate, and adjusted higher by a total of 48 basis points from 11,19 per cent at the beginning of May 2008 to 11,67 per cent on 23 August. The Sabor was quite stable during the period under review and remained well within the upper and lower standing facility limits.

Benchmark overnight rates



The implied rate on one-day rand funding in the foreign-exchange swap market (overnight FX rate) generally remained slightly above the Sabor rate, deviating only periodically during May when it temporarily fell below the Sabor rate. Overall, the overnight FX rate increased by 48 basis points from the beginning of May 2008 to 11,98 per cent on 23 August.

Both the *prime overdraft rate* and the *predominant rate on mortgage loans* of the private-sector banks aligned themselves with tighter market conditions and rose in conjunction with the repurchase rate increases in April and June 2008. The post-June 2008 level of these rates – 15,5 per cent – was previously observed in June 2003.

On 13 June 2008 the *prescribed interest rates* as stipulated in the National Credit Act increased as indicated in the following table:

National Credit Act maximum interest rates: Changes on 13 June 2008

Category	Maximum rate per annum Per cent
Mortgage agreements	30,3 to 31,4
Credit facilities	35,3 to 36,4
Unsecured credit transactions	45,3 to 46,4
Developmental credit agreements:	
For the development of a small business	45,3 to 46,4
For low-income housing (unsecured)	45,3 to 46,4
Short-term credit transactions	60 (unchanged)
Other credit agreements	35,3 to 36,4
Incidental credit agreements	24 (unchanged)

Similarly, on 20 June 2008 the *maximum annual finance charge rates* on money loans, credit and leasing transactions – as determined by the Usury Act – increased by one percentage point to 27 per cent for amounts below R10 000 and to 24 per cent for amounts above R10 000, but not exceeding R500 000.

The *standard interest rate* on loans granted by government from the State Revenue Fund, as defined in the Public Finance Management Act, increased from 14 per cent to 15 per cent on 1 July 2008.

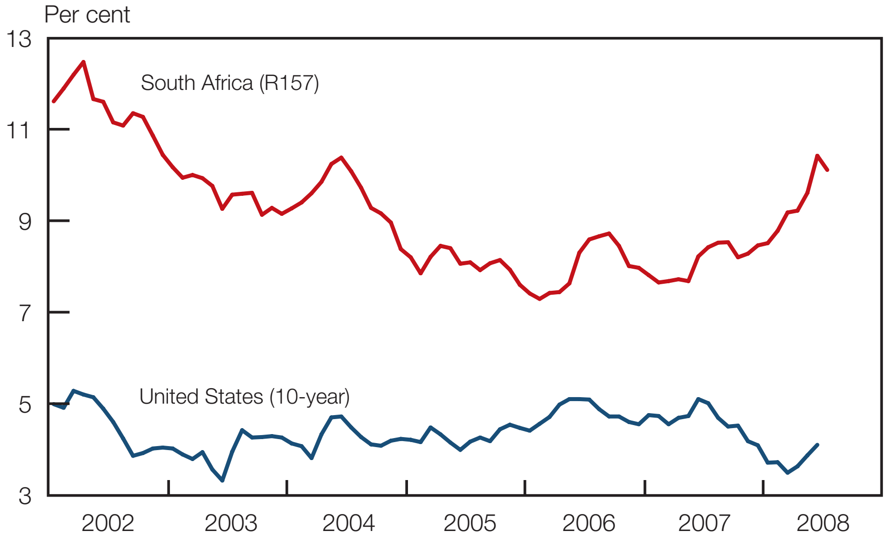
Interest rates on RSA fixed-rate and inflation-linked retail bonds
Per cent

Effective from	2-year bond	3-year bond	5-year bond
Fixed rate:			
1 Mar 2008	9,50	9,75	10,25
1 May 2008	9,75	10,00	10,50
1 Jun 2008	10,00	10,25	10,75
1 Jul 2008	10,50	10,75	11,25
	3-year bond	5-year bond	10-year bond
Inflation linked:			
1 Dec 2007	3,25	3,00	2,75
1 Jun 2008	3,00	2,75	2,50

Interest rates on the *RSA government fixed-rate and inflation-linked retail bonds* are priced off the government bond yield curves on a monthly and semi-annual basis, respectively. The table on page 34 depicts how rates on fixed-rate and inflation-linked bonds have changed in 2008.

The daily *average yield on the R157 government bond* (maturing in 2015) rose significantly from 8,33 per cent on 15 January 2008 to 10,82 per cent on 1 July in response to inflationary concerns arising from record-high prices of oil and food. The bond yield then declined to 9,17 per cent on 21 August on account of an improvement in inflation expectations following a firmer exchange value of the rand, a lower oil price, and the announcement of the rebasing of the inflation index and reweighting of the inflation basket. Similarly, though less pronounced, the daily closing yield on the US government's ten-year bond fluctuated higher from 3,34 per cent on 20 March 2008 to 4,27 per cent on 20 June before edging lower to 3,83 per cent on 21 August. The spread between the South African R157 bond yield and the US ten-year bond yield widened from 456 basis points on 14 January 2008 to 534 basis points on 21 August as currency risk in the South African bond market and uncertainty in the US financial sector remained high.

Government bond yields



From January 2008 the level of the *yield curve* trended upwards across all maturities, as bond yields continued to rise in response to the tightening of the monetary policy stance, depreciation in the exchange value of the rand and exacerbated inflation expectations. From July the level of the yield curve, especially at the long end of the maturity spectrum, moved downwards, while the short end remained broadly anchored to the repurchase rate. Bond yields declined on the back of the recent appreciation in the exchange value of the rand, lower oil prices and the easing inflation outlook. The *yield gap* narrowed from a negative 341 basis points on 15 January 2008 to a negative 172 basis points on 1 July, before widening to a negative 351 basis points on 21 August.

The *break-even inflation rate* in the five-year maturity range escalated from a recent low of 5,43 per cent on 15 January 2008 to 9,03 per cent on 1 July as inflation concerns worsened. Emerging-market risk aversion, depreciation in the exchange value of the rand and soaring oil prices resulting in high inflation contributed to an apparently relentless upward trend in nominal yields on conventional government bonds and declining real yields on inflation-linked government bonds. Thereafter, the break-even inflation rate declined to 6,54 per cent on 21 August, following an appreciating rand and some improvement in inflation expectations.

The *currency risk premium*[4] on South African government bonds widened significantly from 280 basis points in January 2008 to 421 basis points in June, following a more pronounced increase in the yield on domestic rand-denominated bonds than in the yield on dollar-denominated bonds. Subsequently, the currency risk premium narrowed to 297 basis points in July.

As investor confidence in emerging markets improved, the JPMorgan Emerging Markets Bond Index Plus (EMBI+)[5] spread narrowed from 308 basis points in March 2008 to 283 basis points in July. Similarly, the sovereign risk premium on the South African government's US dollar-denominated bonds in the six-year maturity range trading in international markets narrowed from 286 basis points in March 2008 to 240 basis points in July.

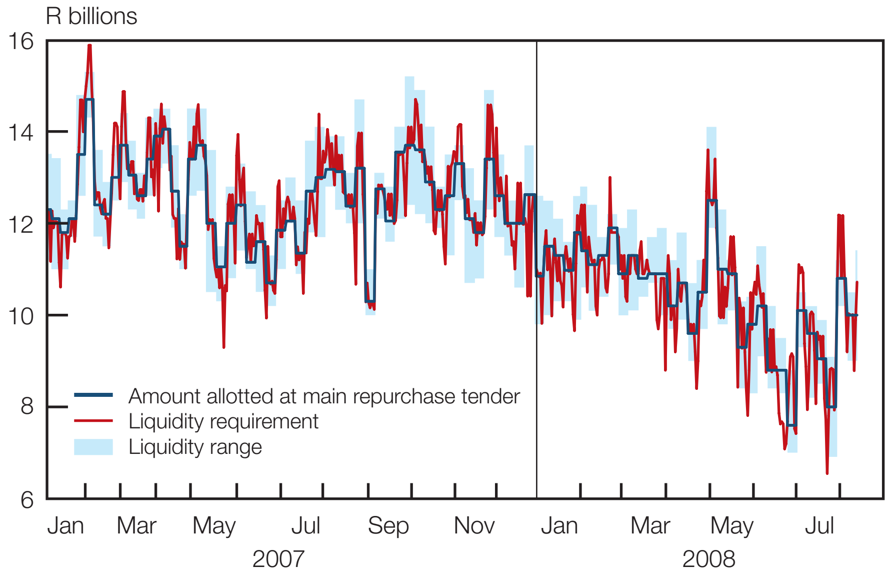
4 Measured as the differential between South African government bond yields on rand-denominated debt in the seven-year maturity range issued in the domestic market and South African dollar-denominated debt in the nine-year maturity range issued in the US market.

5 EMBI+ measures total returns on US dollar-denominated debt instruments of emerging markets.

Money market

Money-market conditions remained relatively accommodative during the second quarter of 2008 and the ensuing month to July 2008. This was largely reflected in the daily liquidity requirement of the private-sector banks, which trended lower and fluctuated below the level of R10 billion for the better part of the period. The liquidity provided by the Bank at the weekly main refinancing tender varied between R7,6 billion and R12,5 billion over the same period.

Liquidity requirement, ranges and amount allotted



Banks continued to utilise their cash reserve accounts with the Bank as the main mechanism to square off their end-of-day liquidity positions. Standing and supplementary reverse repurchase facilities were also used on occasion to smooth out daily liquidity fluctuations.

The accompanying table depicts the statistical counterparts of money-market liquidity flows from April to July 2008.

Money-market liquidity flows

R billions (easing + tightening -)

	Apr–Jun 2008	Jul 2008
Notes and coin in circulation	-0,4	0,1
Required cash reserve deposits	-0,7	0,0
Money-market effect of SARB foreign-exchange transactions	14,3	4,3
Government deposits with SARB	0,8	-0,2
Use of liquidity management instruments	-0,2	-4,0
Reverse repurchase transactions	2,5	-2,5
SARB debentures	-2,7	-1,5
Other items net	-10,5	-3,4
Banks' liquidity requirement (decrease + increase -)	3,3	-3,2

SARB: South African Reserve Bank

The Bank's purchases of foreign exchange injected liquidity amounting to R14,3 billion into the money market during the second quarter of 2008, compared with an injection of only R3,3 billion during the first quarter of 2008. The final repayment on the five-year US$1,5 billion dual-currency-syndicated term loan, entered into in July 2005, was effected on 30 June 2008. This repayment amounted to US$0,25 billion.

During the second quarter of 2008 tightening effects were recorded on account of higher required cash reserve balances held with the Bank, and an increase in notes and coin in circulation.

Redemptions of outstanding reverse repurchase agreements were more than fully neutralised by the issuance of SARB debentures during the quarter under review so that, on balance, liquidity to an amount of R0,2 billion was absorbed. During July reverse repurchase transactions amounted to R2,5 billion and SARB debentures of R1,5 billion were issued. At the end of July 2008, the total outstanding balances on these instruments were R19,8 billion for SARB debentures and R7,5 billion for reverse repurchase agreements.

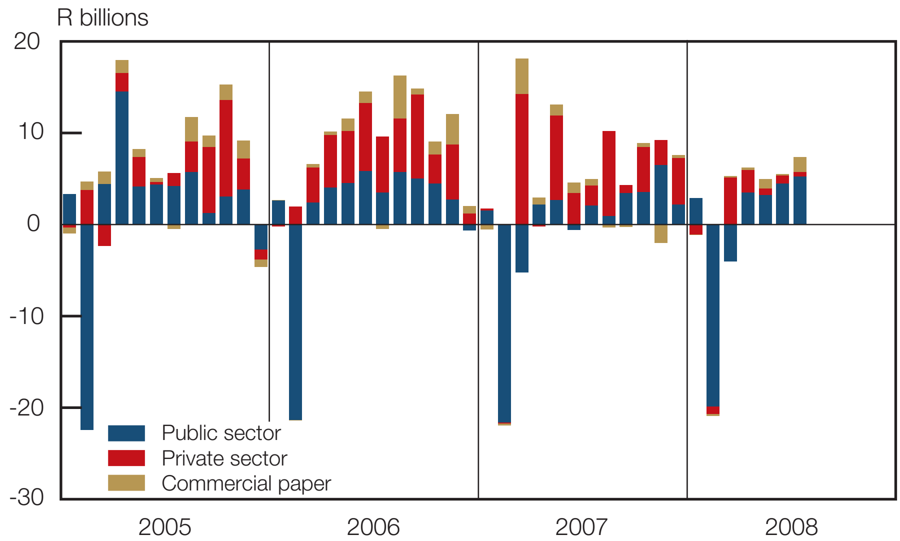
Special Treasury bills with a maturity of twelve days amounting to R1,8 billion were issued during June 2008, which further assisted the Bank in smoothing liquidity flows in the market. The total amount of Treasury bills issued during the second quarter of 2008 came to R9,9 billion, compared with only R2,5 billion at the same time a year earlier. The proceeds of these issues were reflected in higher government tax and loan account balances with the private banks, in part to be utilised for coupon payments on various government bonds from June 2008 onwards.

Bond market

The City of Cape Town issued bonds amounting to R1,0 billion in June 2008. The CCT01 bond, which was issued under the newly established Domestic Medium Term Note (DMTN) programme of R7,0 billion, has a fixed coupon interest rate of 12,57 per cent and matures in 2023. Cape Town was the second municipality in South Africa to list its bond issuance on the Bond Exchange of South Africa Limited (BESA), following the City of Johannesburg's first issuance in 2004. The nominal amount of the City of Johannesburg's listed bond issuance increased by R1,8 billion so far in 2008 to reach R5,7 billion at the end of July.

Central government recorded net redemptions of R9,8 billion in the first seven months of 2008 and net issues of debt by public corporations amounted to R2,4 billion over the same period. *Private-sector funding* activity in the domestic bond market remained subdued in 2008 as the outstanding nominal value of private-sector loan stock (excluding commercial paper) listed on BESA increased by R7,8 billion in the first seven months of 2008, compared with the R29,0 billion raised in the corresponding period of 2007. Banks were responsible for conventional net bond issuance of R19,6 billion in 2008. Net redemptions of securitised instruments (excluding commercial paper) amounted to R7,9 billion in the seven months to July 2008, consistent with the reduced appetite for securitisation in many parts of the world.

Net issues in domestic primary bond market



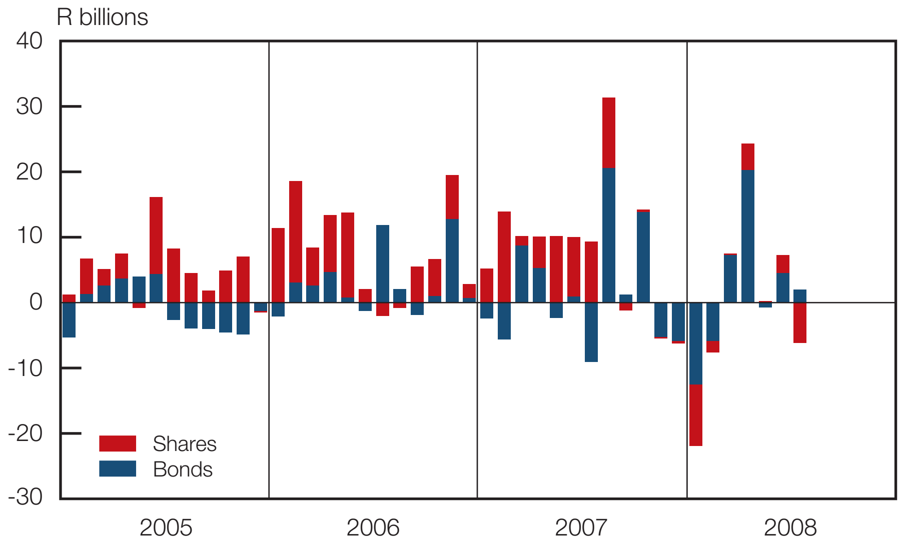
The outstanding nominal value of commercial paper listed on BESA increased by R3,0 billion in the first seven months of 2008 as net issues of R3,1 billion by the private sector were partly offset by net redemptions of R0,1 billion by the public sector. The total outstanding nominal value of all debt listed on BESA increased by R8,1 billion during the same period, bringing the total outstanding nominal amount to R785,4 billion at the end of July.

Issuance of rand-denominated bonds by foreign borrowers in the *Japanese Uridashi bond market* remained fluid in 2008. The total nominal value of R16,2 billion issued in the first seven months of 2008 was more than the R13,1 billion recorded in the entire 2007. Gross issuance of rand-denominated bonds in the *European bond markets* amounted to R15,0 billion in the seven months to July 2008 and net issuance amounted to R8,9 billion, some 14 per cent less than in the corresponding period of 2007.

Trading activity in the *secondary bond market* continued at a steady pace in 2008, alongside significant movements in bond prices. Turnover of R12,0 trillion in the first seven months of 2008 was 26 per cent more than in the corresponding period of 2007. The daily average value traded reached a record high of R92,3 billion in June 2008, contributing to an average of R82,3 billion in the first seven months of 2008. The National Treasury conducted a switch auction in May 2008, giving participants the option to switch from the R196 (2009) government bond to any of the R207 (2020), R209 (2036) or R205 (2012) bonds; and another one in June, giving participants the option to switch from the R153 (2010) government bond to any of the R207 (2020), R208 (2021) or R186 (2026) bonds. Demand for the longer-term bonds was sluggish, possibly due to uncertainty regarding the inflation and interest rate outlook. As such, the R153 bond remains the most liquid government bond traded with annualised turnover that is 93,9 times the amount in issue in the first seven months of 2008, followed by the R157 bond with a liquidity ratio of 73,2 over the same period. These two bonds are by far the most traded bonds in the secondary bond market.

Non-residents' net sales of bonds to the value of R11,1 billion in the first quarter of 2008 were followed by record-high net purchases of R24,0 billion in the second quarter, alongside a lower exchange value of the rand and notably higher nominal bond yields. Thereafter, non-residents recorded net purchases of bonds to the value of R2,0 billion in July, bringing their net purchases to R14,9 billion in the first seven months of 2008, compared with net sales of R4,5 billion in the corresponding period of 2007. Non-residents' participation in the bond market, measured as the sum of their purchases and sales as a percentage of total purchases and sales, declined from an average of 19 per cent in 2007 to 15 per cent in the first seven months of 2008.

Net purchases of shares and bonds by non-residents



Transactions on JSE and BESA

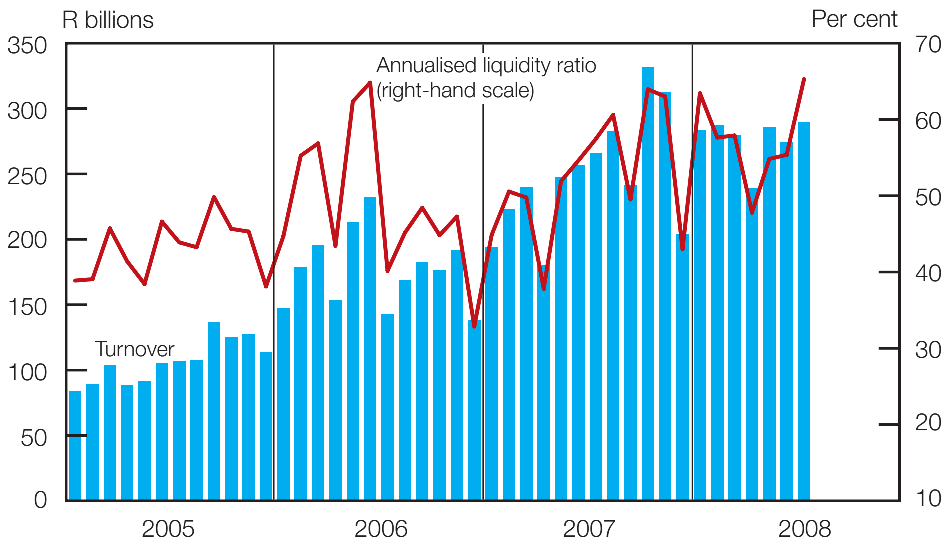
Share market

Share-price volatility and the prospect of weaker global economic growth impacted on the amount of funding sought in the domestic and international *primary share markets* by companies listed on the JSE Limited (JSE). The total value of equity capital raised amounted to R54,8 billion in the first seven months of 2008, less than the R60,6 billion raised in the corresponding period of 2007. Companies constituting the resources sector accounted for 42 per cent of the total amount raised thus far in 2008, mainly through rights issues of ordinary shares, as the commodity boom was conducive to company expansion. The financial sector accounted for 35 per cent and industrials for 18 per cent.

In the first seven months of 2008, 15 new listings were recorded on the JSE, compared with 22 new listings in the corresponding period of 2007. Of the new listings in 2008, 4 occurred on Alt^{X}, bringing the total number of listings on this exchange to 76 at the end of July. The 13 delistings in the seven months to July 2008 fell far below the 33 delistings in the corresponding period of 2007. The number of companies listed on the JSE therefore increased marginally from 422 in December 2007 to 424 in July 2008.

Trading activity in the *secondary share market* remained lively in 2008 amid unsteady financial and energy shares, buoyed by the heightened volatility in share prices as reflected in the South African Volatility Index, which increased from 21 per cent on 19 May to 29 per cent on 21 August. The value of shares traded on the JSE amounted to R1,9 trillion in the first seven months of 2008 – 21 per cent more than the turnover in the corresponding period of 2007. From a daily average turnover of R10,3 billion in December 2007, a new record high of R14,1 billion was recorded in March 2008 before receding to R12,0 billion in July. In the first seven months of 2008 the daily average turnover amounted to R12,8 billion. Only accounting for a fraction of the total, daily average turnover on Alt^x amounted to R23,7 million in the first seven months of 2008 – 45 per cent higher than the R16,4 million per day traded in the corresponding period of 2007.

Secondary share market

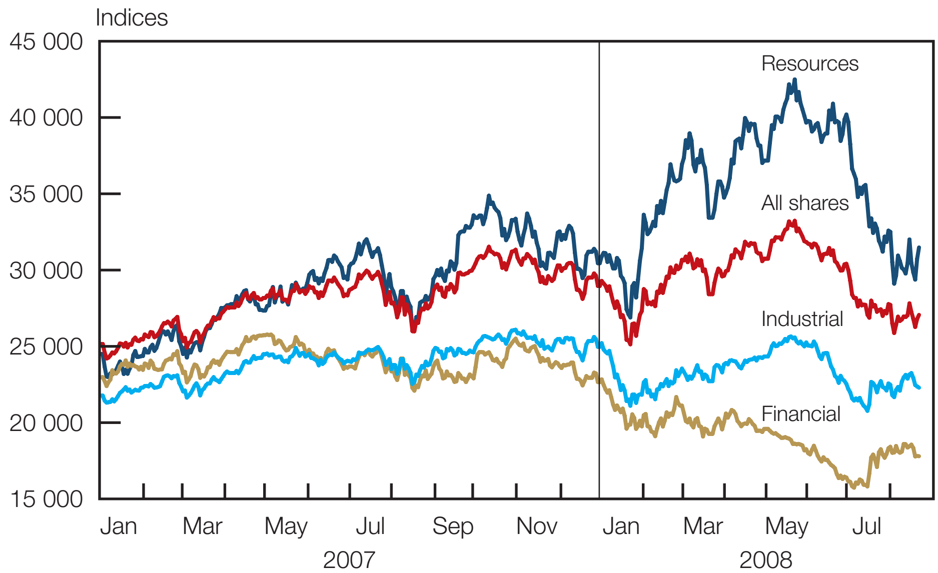


The total *market capitalisation* of the JSE increased from R5,7 trillion in December 2007 to a record high of R6,3 trillion in May 2008. Although the number of shares in issue continued to rise, the market capitalisation declined to R5,3 trillion in July due to lower share prices. The combined market capitalisation of all companies listed on Alt^x increased from R19,1 billion in July 2007 to R31,2 billion in December, before declining to R23,5 billion in July 2008. Total market liquidity, measured by expressing annualised turnover as a percentage of market capitalisation, increased from 43 per cent in December 2007 to 65 per cent in July 2008.

Non-resident interest in the domestic secondary share market waned significantly in 2008 alongside concerns of a global economic slowdown, and net sales of shares amounting to R11,0 billion were recorded in the first quarter of 2008. Thereafter, non-residents recorded net purchases of shares amounting to R7,0 billion in the second quarter of 2008 alongside record-high domestic share prices, before switching to net sales of R6,1 billion in July. From the beginning of 2008 to the end of July, non-residents' cumulative net sales of shares amounted to R10,0 billion compared with net purchases of R54,0 billion recorded in the corresponding period of 2007. Non-residents' activity in the share market, measured as their purchases and sales as a percentage of total purchases and sales on the JSE, declined from an average of 21 per cent in 2007 to 19 per cent in the first seven months of 2008.

The FTSE/JSE all-share price index (Alsi) reached a peak of 33 233 points on 22 May 2008, before declining by 6 168 points or 19 per cent to 21 August. The Alsi fell as a result of a combination of economic fundamentals: uncertainty regarding the domestic interest rate outlook; risks of higher inflationary pressures buoyed by the announcement of increases in electricity tariffs; weaker global equity markets; and lower commodity prices. Similarly, measured in US dollar terms, the Alsi of the JSE decreased by 21 per cent from a recent high on 19 May 2008 to 21 August, while the Standard & Poor's 500 composite index (S&P500) declined by 10 per cent over the same period. International equity markets were influenced by unfavourable economic data, rising crude oil prices, and weak corporate earnings of banks and other institutions that are active in distressed credit markets.

Share prices



After increasing strongly from January 2008, the daily price of the *resources index* fell by 26 per cent from a recent high on 22 May 2008 to 21 August. Reduced earnings prospects for the mining industry resulted from a decline in metal prices, an appreciating exchange value of the rand, severe mining cost pressures and disruptions in production activity. During the period under review inflationary concerns and local interest rate fears contributed to a decline of 13 per cent in the prices of *industrial shares* while *financial share prices* – already trending downward since November 2007 – recorded a loss of 4 per cent, although some renewed interest in these shares had been evident since the middle of July.

The *dividend yield* on all classes of shares decreased from a recent high of 2,6 per cent in January 2008 to 2,3 per cent in May, before increasing to 3,1 per cent in July, reflecting emerging pressures on earnings prospects. The *earnings yield* on all classes of shares similarly receded from a high of 7,2 per cent in January 2008 to 6,1 per cent in May, before increasing again to 7,2 per cent in July. Conversely, the *price-earnings ratio* of all classes of shares increased from a low of 13,9 in January 2008 to 16,3 in May, before reverting to 13,9 in July.

Market for exchange-traded derivatives

In June 2008, the JSE enhanced its product range by introducing futures and options on the Mini Alsi (ALMI). The underlying instrument for these new contracts is the FTSE/JSE Top 40 Index, but they trade at a tenth of the spot price and approximately a hundredth of the current Alsi futures contracts in value terms, enabling more retail investor participation.

During the first seven months of 2008, turnover in *financial derivatives* on the JSE was boosted by high levels of share price volatility, alongside increased turbulence and uncertainty in global markets. In recent years futures activity on markets intensified as retail and institutional investors amplified their exposure to derivative instruments. Single-stock futures have become the predominant instrument whereby investors obtain gearing to changes in prices of listed shares, while having to finance only a fraction of their full market exposure.

Turnover in *commodity futures* and *options* increased during the first seven months of 2008 as local prices of all agricultural products continued to soar in line with international prices. International grain prices were driven by, among other things, increased profit-motivated demand from institutional investors, including sovereign wealth funds and government and corporate pension funds, which view commodity futures as an alternative asset class for long-term investment, leading to virtual stockpiling of commodities via the futures market. Commodity prices came under further upward pressure from record-high oil prices, leading to escalating costs of farming inputs such as fertiliser and diesel, along with rising transport and freight charges. Other factors affecting agricultural commodity prices include increasing demand from the growing global middle-income population, the expanding bio-fuels industry and supply constraints due to adverse weather conditions in some crop-growing countries.

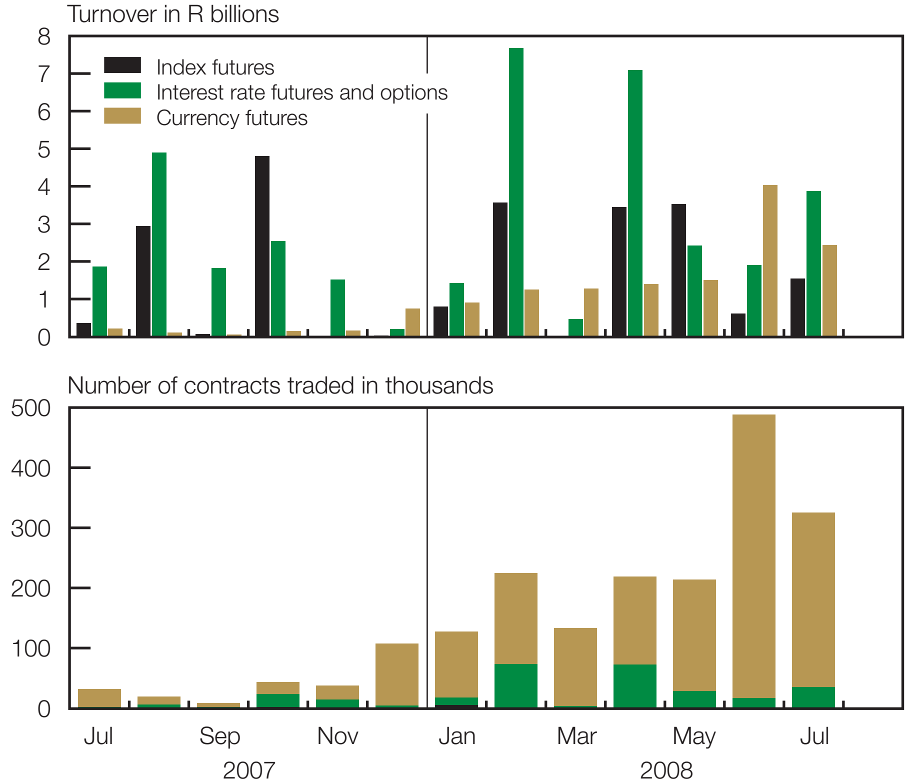
Derivatives turnover on the JSE, January to July 2008

	Value R billions	Change over one year Per cent
Financial futures and options on futures	3 261	36
Warrants	2	33
Agricultural commodity futures and options	230	49
Interest rate derivatives	51	150

After a lacklustre performance in 2007, trade in *warrants* picked up in the first seven months of 2008. Turnover in derivatives traded on the JSE during the first seven months of 2008 is indicated in the table above.

Trading activity on *Yield-X* recorded robust growth in the first seven months of 2008. Currency futures dominated trade, representing 86 per cent of the total number of contracts traded, with dollar/rand futures contracts continuing to be the most favoured. Investors sought protection against currency erosion or participation in alternative hedging or speculative strategies.

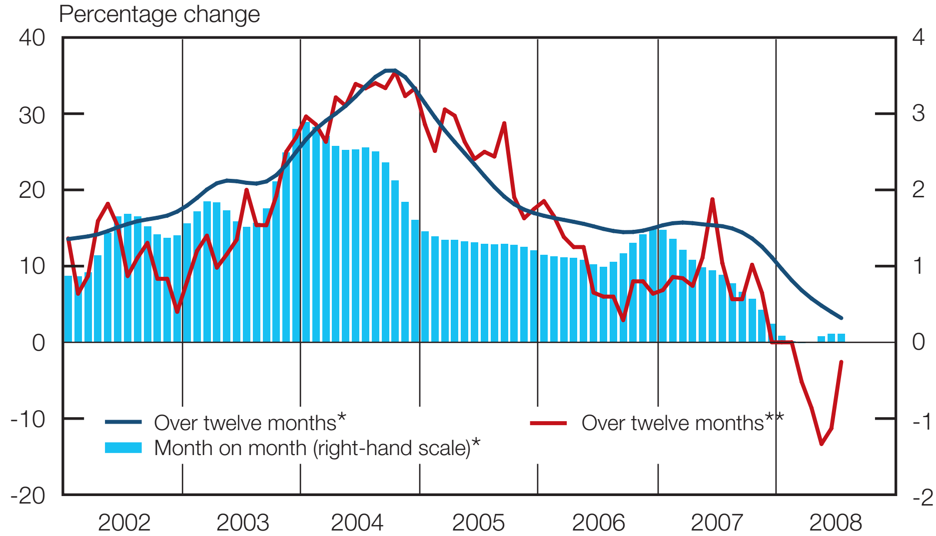
Yield-X activity



Real-estate market

The year-on-year rate of increase in the average price of residential property in the middle segment of the market, as measured by Absa, decelerated from a recent high of 15,7 per cent in March 2007 to 3,2 per cent in July 2008 – the lowest rate of increase since 1999. The month-on-month rate of increase slowed more pronouncedly from 1,5 per cent in December 2006 to 0,1 per cent in July 2008. The slowdown in property

Nominal house prices



Sources: * Absa ** Standard Bank

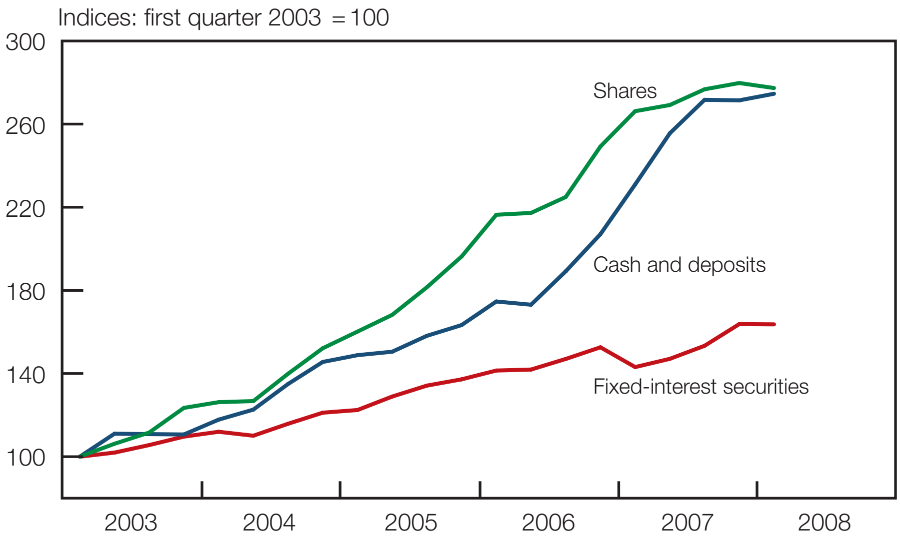
prices was, among other things, in response to a reduction in affordability due to rising house prices and the higher cost of mortgage financing. In real terms, the twelve-month rate of change in average house prices declined from February 2008 and recorded a negative rate of 7,3 per cent in June, since the nominal rate of increase was outpaced by the rate of consumer price inflation.

The year-on-year rate of change in the median price of houses, as measured by Standard Bank, declined from a zero rate in December 2007 to a negative 13,3 per cent in May 2008, before recording a decline of 2,6 per cent in July.

Non-bank financial intermediaries

The asset allocation preferences of non-bank financial intermediaries – insurers, unit trusts and pension funds – have recently reflected a more cautious stance, alongside the continued turbulence and uncertainty in global and local markets. Holdings of cash and deposits by non-bank financial intermediaries increased by about 32 per cent from the fourth quarter of 2006 to the second quarter of 2008. Money-market funds accounted for 29 per cent of the total funds invested with the unit trust industry in the second quarter of 2008, up from 26 per cent in the fourth quarter of 2006.

Financial assets of selected non-bank financial intermediaries



Public finance

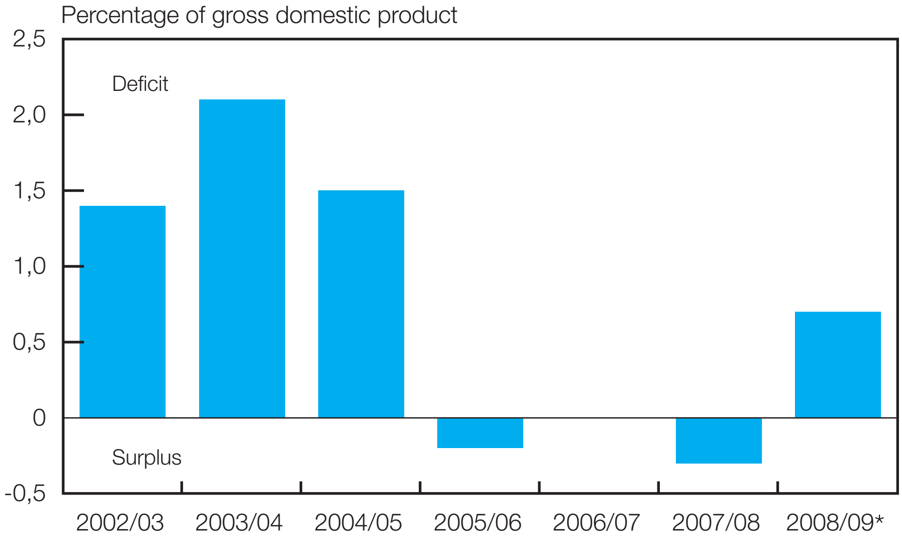
Non-financial public-sector borrowing requirement[6]

Infrastructural spending by consolidated general government continued to grow rapidly in the first quarter of fiscal 2008/09, consistent with the *Budget Review 2008* medium-term estimates. This investment spending underpinned the substantial broadening of the non-financial public-sector borrowing requirement in April–June 2008.

The *non-financial public-sector* cash deficit in the first quarter of fiscal 2008/09 was in contrast to the cash surplus in the same period a year earlier. Relative to gross domestic product, the non-financial public-sector borrowing requirement amounted to 0,7 per cent, compared with a surplus of 1,0 per cent recorded in the same period of the previous fiscal year.

6 Calculated as the cash deficit/surplus of the consolidated central, provincial and local government and non-financial public enterprises and corporations.

Non-financial public-sector borrowing requirement



* April–June 2008

The financial activities of the non-financial public sector at various levels of government are summarised in the following table:

Non-financial public-sector borrowing requirement
R billions

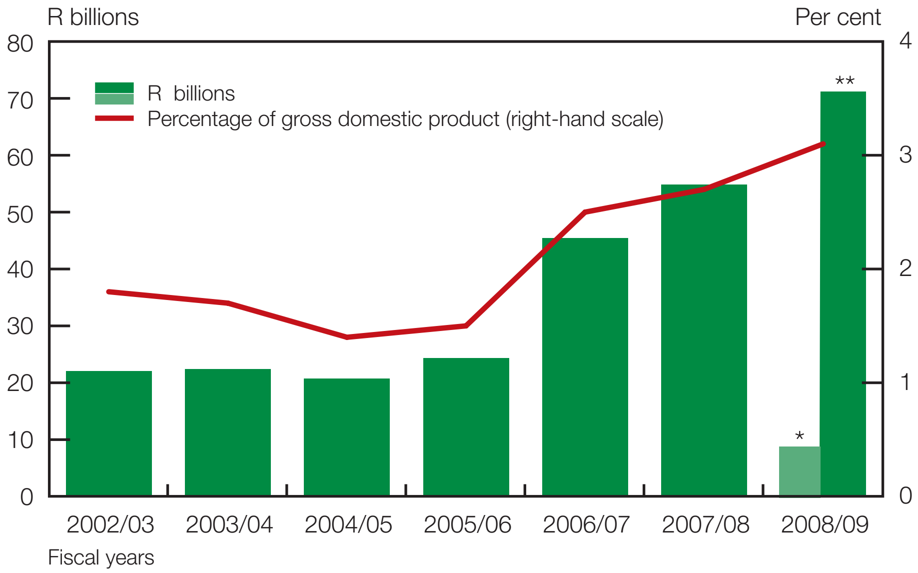
Level of government	Apr–Jun 2007*	Apr–Jun 2008*
National government	5,9	2,1
Extra-budgetary institutions	-2,4	-1,9
Social security funds	-1,5	-0,9
Provincial governments	-13,0	-2,1
Local governments	3,6	6,0
Non-financial public enterprises	2,6	1,0
Total	-4,7**	4,2**

* Deficit + surplus -
** Individual amounts may not add up to the totals due to rounding

In the first quarter of fiscal 2008/09 the consolidated financial activities of the *non-financial public enterprises and corporations* resulted in a cash deficit of R1,0 billion, substantially lower than the cash deficit recorded in the same period a year earlier. Total net investment in non-financial assets amounted to R8,9 billion in April–June 2008, compared with an investment amount of R9,3 billion in the corresponding quarter of the previous fiscal year.

Government's financial position is to a large degree influenced by compensation of public-sector employees, which accounts for approximately 65 per cent of government consumption expenditure and impacts meaningfully on the aggregate level of economic activity. In nominal terms, compensation of general government employees rose by 18,0 per cent during the period April–June 2008, when compared with the corresponding period in the previous fiscal year. This was higher than the 14,9-per-cent increase recorded in fiscal 2007/08 as a whole. In real terms, compensation of employees is expected to grow by 3,6 per cent per annum over the period 2006 to 2010.

Net investment in non-financial assets by public-sector enterprises



* April–June 2008 ** *Budget Review 2008*

An analysis of *national government* statistics revealed cash receipts from operating activities in April–June 2008 to the amount of R142,6 billion. This represented a year-on-year rate of increase of 11,3 per cent when compared with the same period in 2007. For the period under review, cash payments for operating activities increased by 7,8 per cent from the same period a year earlier and amounted to R143,7 billion. Net cash flow from operating activities of national government, together with the net investment in non-financial assets, resulted in a cash deficit of R2,1 billion in the first quarter of fiscal 2008/09 – R3,8 billion lower than the cash deficit recorded in the same period a year earlier.

Provincial governments recorded a cash surplus of R2,1 billion in the April–June quarter of 2008, substantially lower than the cash surplus of R13,0 billion recorded in the same period a year earlier. This decline in the cash surplus was mainly on account of a strong increase in net investment in non-financial assets. The main source of provincial governments' cash receipts – grants from national government – amounted to R60,1 billion in the first quarter of fiscal 2008/09, some 9,1 per cent more than in the same period of the previous fiscal year. Grants to provincial governments included equitable share transfers and conditional grants earmarked for specific purposes.

Cash payments for operating activities by provincial governments amounted to R53,1 billion in the first quarter of fiscal 2008/09, representing an increase of 32,3 per cent when compared with the same period a year earlier. Spending on the social services cluster (i.e., education, health and social welfare) comprised the bulk of total provincial expenditure. The education sector was the largest benefactor, followed by the health sector. For the period under review, net investment in non-financial assets amounted to R6,7 billion, 80,4 per cent more than a year earlier. This was owing to the inclusion of spending related to the Gautrain project.

The financial activities of provincial governments resulted in their deposits with the private-sector banks decreasing from R8,4 billion at the end of March 2008 to R7,2 billion at the end of June. At the same time, their bank overdrafts remained broadly unchanged at R0,4 billion between these respective dates. Provincial governments' deposits with the Corporation for Public Deposits increased from R2,4 billion to R5,0 billion over the same period.

Preliminary *local government* statistics indicated a cash deficit in April–June 2008 amounting to R6,0 billion, markedly higher than the cash deficit of R3,6 billion recorded in the same period a year earlier. The City of Johannesburg has been one of the major municipalities incurring deficits as a result of upgrading its infrastructure. The city introduced and started issuing conventional bonds in April 2004, with the latest issuance of R1,8 billion on 5 June 2008, bringing the total to R5,7 billion. The City of Cape Town had its first issuance on 23 June 2008 amounting to R1 billion.

In the first quarter of fiscal 2008/09 *extra-budgetary institutions* recorded an estimated cash surplus of R1,9 billion, lower than the cash surplus of R2,4 billion recorded in the same period a year earlier. The cash surplus of *social security funds* equalled R0,9 billion in the April–June quarter of fiscal 2008/09, lower than the cash surplus recorded in the corresponding period of the preceding fiscal year. The Unemployment Insurance Fund investment portfolio amounted to R27,8 billion at the end of May 2008, accruing to 7,4 million contributors.

Budget comparable analysis of national government finance

National government expenditure in the first quarter of fiscal 2008/09 rose by 8,1 per cent on a yearly basis to reach R136 billion. This increase was less than half the growth rate recorded in April–June 2007. It also fell below the year-on-year growth rate of 10,2 per cent recorded in the same period of fiscal 2006/07. The *Budget Review 2008* projected a 12,8-per-cent increase in national government expenditure for the current fiscal year as a whole. In real terms national government recorded negative growth in expenditure during the period under review, contrary to the real growth rate recorded in the corresponding quarter of the previous fiscal year. Spending by national government was projected to grow in real terms by 6,6 per cent in fiscal 2008/09.

Interest paid on national government debt during April–June 2008 was 14,6 per cent more than in the corresponding period of the previous fiscal year and partly reflected higher interest rates, especially on short-term debt instruments. As a ratio of gross domestic product, interest payments amounted to 1,8 per cent in the April–June quarter of fiscal 2008/09, almost equivalent to the ratio recorded in the first quarter of the previous fiscal year. Budget projections indicated that interest payments would decrease at a rate of 3,2 per cent to amount to R51,2 billion in fiscal 2008/09.

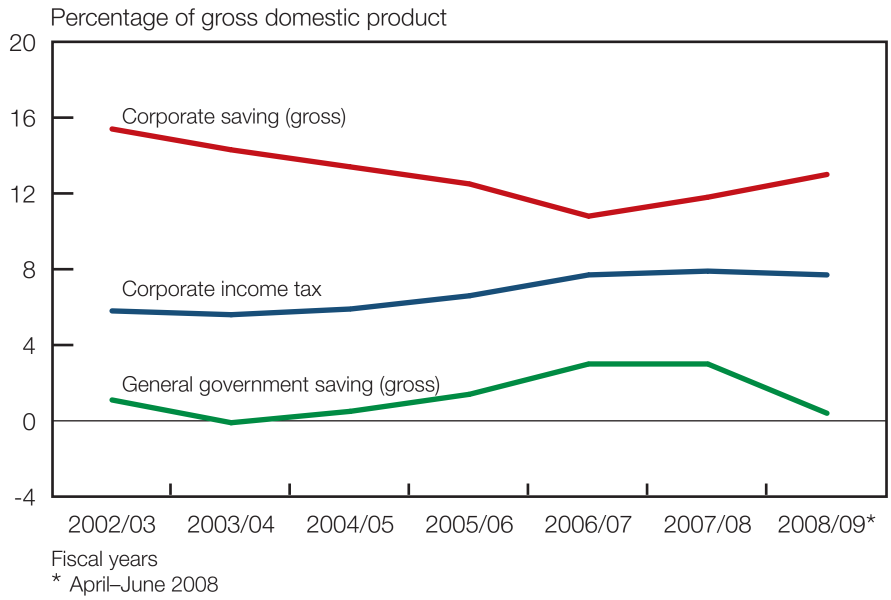
During the first quarter of the current fiscal year, transfers and subsidies rose marginally and amounted to R48,2 billion. Transfers include grants to other levels of government and social assistance benefits paid to qualifying households to help alleviate poverty. Social assistance benefits increased by 3,0 per cent on average between June 2006 and June 2008, possibly as a result of rising inflation and new beneficiaries. Subsidies are paid mainly to public corporations to supplement their infrastructural budgets. Payments for capital assets amounted to R1,0 billion in the April-June quarter of 2008 – some 34,5 per cent more than in the corresponding period of the previous fiscal year. For fiscal 2008/09 as a whole, budget projections indicated that payments for capital assets would amount to R7,5 billion.

7 Transactions arising from timing differences between the recording of transactions and bank clearances, and late departmental requests for funds.

After taking cash-flow adjustments[7] into account, national government cash-flow expenditure in the first quarter of fiscal 2008/09 amounted to R139 billion or 10,3 per cent more than a year earlier, mainly on account of outstanding transfers.

National government revenue for the first quarter of fiscal 2008/09 amounted to R136 billion, representing a year-on-year growth rate of 12,5 per cent. Taxes on income, profits and capital gains, as well as domestic taxes on goods and services were the main areas of buoyancy. The rate of increase in national government revenue was lower than the 15,8-per-cent increase recorded in April–June 2007, and probably reflected the tighter economic conditions that prevailed. The 2008 Budget projected that national government revenue would increase by 11,4 per cent in fiscal 2008/09.

Corporate income tax, and corporate and general government saving



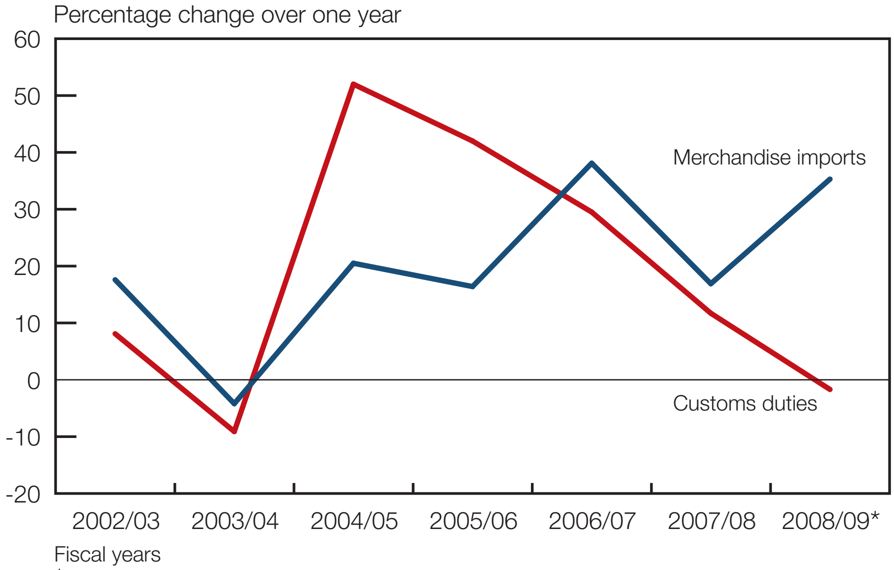
As shown in the table on page 49, taxes on income, profits and capital gains, emanating from individuals and companies, increased briskly in the April–June quarter of 2008. Higher income tax payments by companies were accompanied by an increase in the corporate saving rate and a decrease in the saving rate of the government sector on account of high consumption of fixed capital. At the other extreme, taxes on property in April–June 2008 were 9 per cent lower than in the corresponding quarter a year earlier, mainly as a result of the slowdown in the real-estate market.

National government revenue in fiscal 2008/09

Revenue source	Originally budgeted		Actual Apr–Jun 2008	
	R billions	Percentage change*	R billions	Percentage change*
Taxes on income, profits and capital gains	369,7	11,3	85,6	16,8
Payroll taxes	7,5	18,8	1,7	3,0
Taxes on property	14,2	19,6	2,6	-9,0
Domestic taxes on goods and services	218,4	12,2	45,5	7,0
Taxes on international trade and transactions	31,5	16,2	5,6	-0,5
Other revenue	12,9	-7,7	2,1	-7,4
Less: SACU** payments	28,9	17,0	7,2	-2,6
Total revenue	625,4	11,4	135,9	12,5

* April–June 2007 to April–June 2008
** Southern African Customs Union

Customs duties and merchandise imports



* April–June 2008

Netting national government revenue and expenditure in April–June 2008 resulted in an almost balanced budget, in contrast with a cash-book deficit of R4,9 billion recorded in the same period of the previous fiscal year. The deficit, as a ratio of gross domestic product, was negligible in the first three months of the current fiscal year, compared with the ratio recorded in the same period of fiscal 2007/08.

National government recorded a cash-flow deficit before borrowing and debt repayment of R3,0 billion in the first quarter of fiscal 2008/09 – some R2,4 billion lower than the cash-flow deficit recorded in the corresponding period of the previous fiscal year. After taking into account extraordinary transactions and the cost on revaluation of foreign debt at redemption, the net borrowing requirement of national government for the period under review amounted to R5,0 billion.

As indicated in the table on page 50, the net borrowing requirement in the April–June quarter of 2008 was financed mainly through the issuance of debt instruments in the domestic capital market.

National government financing in fiscal 2008/09

R billions

Item or instrument	Originally budgeted 2008/09	Actual Apr–Jun 2008	Actual Apr–Jun 2007
Budget balance*	-14,3	3,0**	5,4**
Plus: Extraordinary payments	0,0	0,0	0,7
Cost on revaluation of foreign debt at redemption	1,8	1,9	1,4
Less: Extraordinary receipts	0,3	0,0	0,5
Net borrowing requirement*	**-12,7**	**5,0**	**7,0**
Treasury bills	5,8	9,9	2,5
Domestic government bonds	5,9	5,6	7,1
Foreign bonds and loans	-1,7	-2,8	0,6
Change in available cash balances***	-22,7	-7,7	-3,2
Total net financing	**-12,7**	**5,0**	**7,0**

* Deficit + surplus -
** Cash-flow deficit
*** Increase - decrease +

The National Treasury announced a switch auction in the first quarter of fiscal 2008/09 from short- to long-term bonds where primary market participants were allowed to switch the R196 bond to the R205, R207 and R209 bonds.

Domestic long-term funding was obtained at an average rate of 9,6 per cent per annum, while domestic short-term instruments were sold at an average rate of 11,1 per cent.

Government recorded net redemptions of foreign bonds and loans to the amount of R2,8 billion during the first quarter of 2008/09.

The financial activities of national government resulted in an increase in government's bank balances from R94,5 billion at the end of March 2008 to R102,2 billion at the end of June. These included deposits held with the South African Reserve Bank, which are used to sterilise the liquidity injected by the Bank in the process of acquiring foreign assets.

Total loan debt of national government increased from R572 billion at the end of March 2008 to R581 billion at the end of June. Owing to foreign-debt buy-backs and exchanges, foreign debt as a proportion of total loan debt decreased from 16,8 per cent to 15,1 per cent between these two dates, thereby mitigating external vulnerability. Nonetheless, the average maturity of the foreign marketable bonds of national government increased from 81 months at the end of March 2008 to 85 months at the end of June. The average maturity of the domestic marketable bonds issued by national government remained unchanged, amounting to 104 months at both the end of March and end of June 2008. Although loan debt increased marginally, well-managed debt levels were set to create space for greater borrowing on the domestic and international capital markets by public corporations to finance infrastructure development and capacity expansion. As a ratio of gross domestic product, total national government loan debt amounted to 27,1 per cent at the end of June 2008, compared with 27,7 per cent at the end of March 2008.

Government-guaranteed debt declined from R69,8 billion at the end of December 2007 to R66,4 billion at the end of March 2008.

Statement of the Monetary Policy Committee
14 August 2008

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

Introduction

The outlook for inflation remains uncertain. Food and oil price increases continue to cloud the inflation outlook, but there are tentative signs that these pressures may be moderating. Domestic consumption expenditure also remains subdued. However, electricity price increases are set to have an impact on inflation going forward, and there is evidence that underlying inflation has maintained some of its upward momentum. Conflicting pressures are being felt from the global economy, which is experiencing slower growth and higher inflation.

While there are clear signs that the economy is responding to the less accommodative monetary policy stance, the MPC had to assess whether recent monetary policy actions are sufficient to bring inflation back to within the inflation target range over the medium term.

Recent developments in inflation

CPIX inflation increased at a year-on-year rate of 11,6 per cent in June 2008, compared with 10,9 per cent in May. Food price inflation accelerated from 16,9 per cent in May to 18,2 per cent in June, mainly as a result of significant increases in the prices of grain products, as well as fats and oils. Petrol prices increased by almost 36 per cent in June, and together with food prices accounted for about 56 per cent of the increase in CPIX. However, if food and petrol were excluded, CPIX inflation would have measured 6,3 per cent. Services price inflation has been increasing consistently over the past few months and reached a level of 6,7 per cent in June.

Producer price inflation increased at a year-on-year rate of 16,8 per cent in June, driven mainly by petroleum products and mining output prices. Food price increases at the producer price level continue to show some moderation. Agricultural food price increases measured 2,0 per cent in June, while manufactured food price increases, while still high, measured 19,4 per cent, compared with a peak of 20,4 per cent in March 2008.

The outlook for inflation

The central forecast of the Bank has been complicated by the impending rebasing and reweighting of the CPI basket, to be implemented by Statistics South Africa from January 2009. In trying to account for these changes, certain assumptions have to be made, and the central forecast is therefore subject to additional uncertainty.

The central forecast generated on the above basis indicates a near-term deterioration of the inflation outlook when compared with the previous forecast. CPIX inflation is expected to peak at an average rate of around 13 per cent in the third quarter of 2008, compared with 12 per cent. Thereafter, inflation is expected to decline significantly in the first quarter of 2009, partly as a result of the reweighting and rebasing effects. Inflation is then expected to decline gradually, and to fall below the upper end of the inflation target range in the second quarter of 2010. Inflation is expected to average about 7,2 per cent in 2009 and 5,9 per cent in 2010. The forecast takes account of the additional electricity price increases granted to Eskom in June. However, there is some uncertainty about the timing of these increases, or the full extent of the increases that will be passed on to household consumers by the municipalities.

Forecasts by private-sector economists have also been influenced by the coming technical adjustments to the inflation basket. Between June and July, the Reuters consensus CPIX forecast for 2009 declined from 8,2 per cent to 7,5 per cent, while the forecast for 2010 declined from 6 per cent to 5,9 per cent. Since July, the break-even inflation rates, measured as the yield differential between conventional government bonds and inflation-linked bonds, have also reflected some improvement in medium-term inflation expectations. The yield curve moved down markedly, particularly at the long end of the curve, with the R157 having declined by about 100 basis points since the previous MPC meeting.

The higher inflation outcomes and expectations have had an impact on wage settlements. According to the Wage Settlement Survey of Andrew Levy Employment Publications, the average level of wage settlements for the first half of 2008 was 8,3 per cent, compared with 6,8 per cent in the same period in 2007. Unit labour costs increased by 10,2 per cent in the first quarter of 2008, compared with the same quarter in the previous year, while unit labour cost increases in manufacturing measured 6,6 per cent. These trends, while not unexpected, were noted by the MPC.

Significant risks to the inflation outlook remain, although there are tentative signs that some of the risk factors may have moderated somewhat. International oil prices are well below the levels reached in early July 2008 when the price of North Sea Brent crude oil was around US$145 per barrel. Currently oil is trading at around US$112 per barrel, compared with around US$140 per barrel at the time of the previous MPC meeting. These price developments were reflected in domestic petrol price adjustments. In July the price of 95 octane petrol in Gauteng increased by 74 cents per litre, but in August the price declined by 30 cents per litre. If current oil price and exchange rate levels are maintained, a further sizeable decline can be expected in September. It is still too early to tell if the lower international oil price is a temporary phenomenon.

The risks to inflation posed by food price developments remain. Grain product prices in particular appear to have gained some momentum at both the producer price and consumer price levels. As noted earlier, however, manufactured food producer price inflation remains high, but agricultural food inflation has declined to low levels, indicating the possibility of some price relief in the future. The spot price of yellow maize declined in early August following the release of local crop estimates. Wheat prices have also declined on international markets, but nevertheless remain high.

The exchange rate of the rand has exhibited some volatility since the previous meeting of the MPC when it was trading at around R8,00 per US dollar. In late July the rand began to appreciate and reached a level of around R7,20 against the US dollar, but has since depreciated to current levels of around R7,85 per US dollar. On a trade-weighted basis the rand has appreciated by about 4 per cent since the previous meeting.

The outlook for most of the other determinants of inflation has been relatively unchanged since the previous meeting.

Growth in household consumption expenditure appears to have remained subdued. Real retail sales declined on a year-on-year basis in the four consecutive months to June 2008. In May and June retail sales declined by 3,4 per cent and 2,6 per cent respectively. Motor vehicle sales also remain under pressure with the total number of vehicles sold in July declining by over 20 per cent when compared with the same time last year. In the second quarter of 2008, the FNB/BER Consumer Confidence Index experienced its largest quarter-on-quarter decline in 24 years.

Credit extension to the private sector exhibited further moderation, although it still remained at relatively high levels. Growth over twelve months in mortgage advances measured 19,9 per cent in June 2008, while growth in instalment sale credit and leasing finance grew by 14 per cent. Growth in credit extension to households remains on a downward trend.

Real growth in gross domestic product also appears to be lower than the rates achieved in the past few years, although growth in the second quarter is expected to exceed the first quarter growth rate of 2,1 per cent. This improvement will be a result of base effects and improved performances of mining and manufacturing in the second quarter. The expected subdued trend in output growth is evident in a number of indicators. The South African Reserve Bank composite leading business cycle indicator, which has been declining since March 2007, continued its downward trend in May 2008, while the RMB/BER Business Confidence Index also declined significantly in the second quarter of 2008. The Investec/BER Purchasing Managers Index also points to continued slow growth in the manufacturing sector, primarily due to sluggish new sales orders. The utilisation of production capacity in manufacturing declined in both of the first two quarters of 2008. The real value of building plans passed and approved also declined in the past three months.

The lower growth trend has also been reflected in asset prices, and the associated negative wealth effects could moderate consumption expenditure growth further. Equity prices have declined in recent weeks as a result of a weaker economy and lower commodity prices. The all-share index on the JSE Limited has declined by 7 per cent since the beginning of the year, and by about 13 per cent since the previous MPC meeting. All the major sub-indices are lower than they were at the beginning of 2008. The housing market is also subdued, with both the Absa and Standard Bank indices reflecting negative real house price growth.

The global economy is characterised by slowing growth, particularly in the industrialised countries, and intensified inflationary pressures. Growth prospects in the US are being clouded by the persistent weakness in the local housing market and continued financial market uncertainty. Growth in emerging markets also shows some signs of moderation, but nevertheless remains relatively strong. Most central banks have recently either adopted a tighter monetary policy stance or have kept their policy rates unchanged.

The MPC also noted economic developments in Lesotho, Namibia and Swaziland – South Africa's Common Monetary Area (CMA) partners. Food and energy price developments have also intensified in these countries, raising inflation to high levels. Recent developments in real sector indicators have been mixed. Government financial balances are supported by high import duty revenue, and government debt levels are well contained. While interest rates throughout the CMA increased significantly over the past two years, it was noted that most recently not all of the countries have tightened monetary policy.

Monetary policy stance

The MPC has considered recent economic developments and the outlook for inflation and has concluded that, notwithstanding certain risks to future inflation outcomes, the current monetary policy stance is appropriate. Consequently, the repurchase rate will for now remain unchanged at 12 per cent per annum. The MPC will continue to monitor developments closely and will not hesitate to act to deliver on its mandate.

Note on flow of funds in South Africa's national financial accounts for the year 2007

by Z Nhleko and C Monyela[1]

1 The views expressed are those of the authors and do not necessarily reflect the views of the South African Reserve Bank (the Bank). The Bank wishes to express its sincere appreciation to all the reporting organisations – government departments, financial market and other public and private-sector institutions – for their co-operation in furnishing the data used for the compilation of South Africa's financial accounts.

Introduction

The national financial accounts, also referred to as the 'flow-of-funds accounts', provide a synopsis of the financial and real interrelationships among the major sectors of the South African economy. The quarterly accounts for 2007 are appended to this note and the annual summary appears on pages S–44 to S–45 in this issue of the *Quarterly Bulletin*.

Flow of funds summarise, in an integrated framework, transaction flows among economic agents that emanate from their financial and real activities. In total, 21 institutional sectors are identified and provide the building blocks for flow-of-funds compilation in South Africa. These sectors are consolidated into 11 economic sectors for the simplified depiction of national financial flows published in the statistical tables of the *Quarterly Bulletin*.

Financing balances

In 2007 gross capital formation in South Africa increased by some 20 per cent. Each sector, by definition, financed its capital expansion by utilising its own savings and making use of borrowed funds. Table 1 presents the saving and investment activity of the main sectors of the economy for 2006 and 2007.

Table 1 Financing balances,[a,b] 2006 and 2007

R millions Surplus units (+)/deficit units (-)

	2006			2007		
	Gross saving	Gross capital formation	Net lending (+)/ net borrowing (-)	Gross saving	Gross capital formation	Net lending (+)/ net borrowing (-)
Foreign sector[c]	112 141	–	112 141	144 819	–	144 819
Financial intermediaries	33 317	6 205	27 112	46 216	6 305	39 911
General government	19 176	47 198	-28 022	25 590	53 106	-27 516
Non-financial business enterprises						
Public	70 360	65 585	4 775	54 550	54 951	-401
Private	91 217	185 434	-94 217	121 380	249 648	-128 268
Households[d]	29 213	51 002	-21 789	34 109	62 654	-28 545
Total	355 424	355 424	–	426 664	426 664	–

a Gross saving plus net capital transfers less gross capital formation. Gross capital formation consists of total fixed-capital formation and total changes in inventories, before providing for consumption (depreciation) of fixed capital.
b A positive amount reflects a net lending position and by implication the net acquisition of financial assets, whereas a negative amount reflects a net borrowing position and by implication the net incurrence of financial liabilities.
c A positive amount reflects a surplus for the rest of the world and is therefore a deficit on South Africa's balance on the current account of the balance of payments. A negative amount represents a deficit for the rest of the world and is a surplus on South Africa's current account.
d Including unincorporated business enterprises and non-profit institutions serving households.

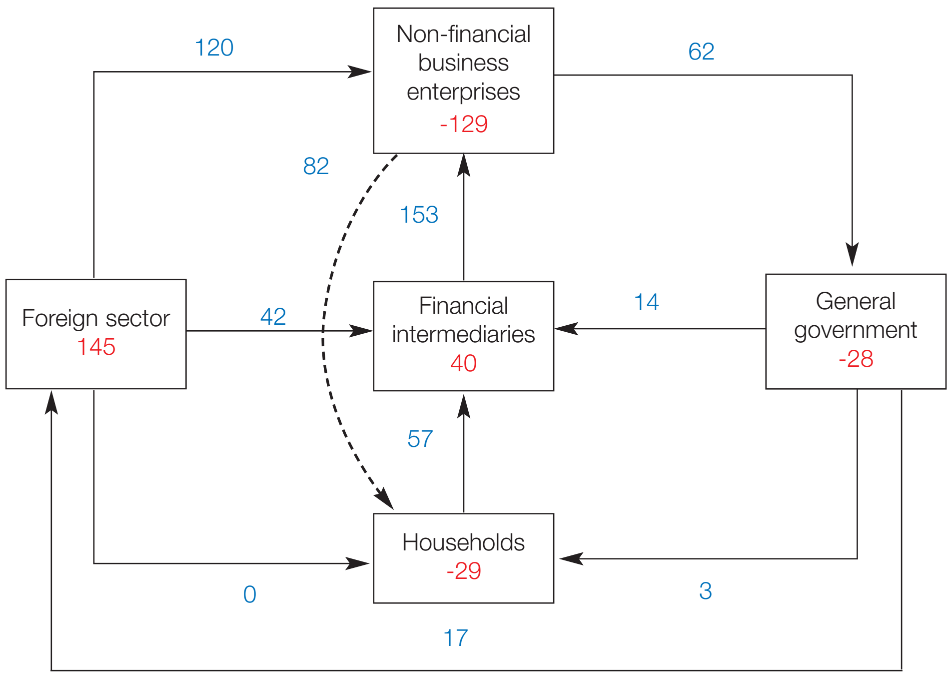
In 2006 and 2007 the foreign sector was a net supplier of funds to the domestic economy thereby augmenting the available gross domestic savings, which generally fell short of gross capital formation activity requirements. The private non-financial business enterprise sector stood out in the measured flows since it was both the largest saver and investor domestically in both years. In 2007 this sector recorded gross saving of 6 per cent of gross domestic product and gross capital formation of 13 per cent of gross domestic product – up from 5 per cent and 11 per cent respectively in 2006. Financial intermediaries stepped up their net lending in 2007, while other sectors such as households recorded higher net borrowing positions than in 2006.

The accompanying sector-to-sector flow diagram (Figure 1) presents a summary of the inter-sectoral net flow of funds among the main sectors of the economy. The net lending (+) or borrowing (-) positions of the sectors are shown inside the boxes, and the inter-sectoral flow-of-fund amounts and the direction of flows are shown outside the boxes.[2] As a leading player in the domestic economy, non-financial business enterprises remained the largest beneficiary of flows from the foreign and domestic financial intermediaries sectors.

2 The net lending or borrowing position of each sector is calculated by treating inflows as negatives and outflows as positives. Numbers may be slightly out due to minor rounding effects.

Figure 1 Net intersectoral flow of funds, 2007

R billions



As depicted in Table 2 on page 56, economic sectors generally preferred to allocate their funds to cash and deposits, while taking up more credit in 2007. Fixed interest securities accounted for 7 per cent of the total financing activity, while the holdings of shares amounted to 4 per cent.

Table 2 Flow of funds: Selected issuer and investor activities,* 2007

	Percentage of total flows	
	2006	2007
Cash and deposits	33	26
Credit extension	29	27
Fixed-income securities	5	7
Ordinary shares	3	4

* Do not sum to 100 as not all activities are covered

Sectoral analysis

A brief analysis of the individual sectors' net lending and/or net borrowing positions in 2007 is given below.

Foreign sector

The foreign sector encapsulates all transactions entered into between South African and non-resident units. In 2007 this sector was a net supplier of funds amounting to R144,8 billion, bridging the saving–investment gap as required by the domestic institutional sectors for the fifth consecutive year.

Accordingly, the domestic economy incurred net financial liabilities in excess of its net acquisition of financial assets, as shown in Table 3. Non-residents supplied excess funds, mainly through their acquisition of domestic shares and the extension of long-term loans, trade credit and short-term loans to domestic sectors.

Table 3 Flow of funds: Foreign sector and combined domestic sectors, 2007
R millions

	Domestic institutional sectors	Rest of the world	Total
Gross saving	281 845	144 819	426 664
Gross capital formation	426 664	–	426 664
Net lending (+)/net borrowing (-)	**-144 819**	**144 819**	**–**
Net acquisition of financial assets	1 194 436	227 979	1 422 415
Net incurrence of financial liabilities	1 339 255	83 160	1 422 415

Financial intermediaries

Financial intermediaries receive funds from surplus economic units and transform them into financial instruments that suit the requirements of deficit units. In South Africa this group consists of five sectors, namely (1) the monetary authority; (2) other monetary institutions; (3) the Public Investment Corporation; (4) insurers and retirement funds; and (5) other financial institutions. A brief review of each of these sectors is discussed in the paragraphs that follow.

Monetary authority

The monetary authority sector, comprising the South African Reserve Bank and the Corporation for Public Deposits, transacts mainly with other monetary institutions, the central government and the foreign sector. The sector received deposits amounting to R38,6 billion in 2007 and, in turn, increased its holdings of foreign-exchange reserves by R40,2 billion[3] in its continued effort to expand reserves. The flows of this sector contributed 7 per cent of the total financial intermediary asset flows in 2007.

3 After adjusting for Special Drawings Rights and monetisation/demonetisation of gold.

Other monetary institutions

The other monetary institutions sector consolidates the accounts of banks, mutual banks, the Land Bank and the Postbank. In 2007 other monetary institutions recorded gross saving amounting to R39,5 billion and gross capital formation of R3,8 billion, as illustrated in Table 4. The sector incurred R384,6 billion in total financial liabilities, of which 79 per cent were in the form of monetary deposits. Despite tighter monetary conditions in 2007, funds were extended to borrowers mainly through the extension of mortgage loans amounting to R172,0 billion, and other loans and advances amounting to R148,3 billion. Other monetary institutions decreased their deposits with foreign institutions by R10,6 billion in 2007.

The sector used 99 per cent of its total inflows to acquire financial assets and continued to be the largest link between lenders and borrowers since it represented 52 per cent of the total financial intermediary asset flows.

Table 4 Flow of funds: Other monetary institutions, 2007

Transaction items	Sources/ liabilities R millions	Uses/ assets R millions
Gross saving	39 458	
Gross capital formation		3 756
Net lending (+)/net borrowing (-)	35 702	
Net financial investment (+/-)		35 702
Net incurrence of financial liabilities	384 553	
Net acquisition of financial assets		420 255
Monetary deposits	303 761	11 885
Deposits with other institutions	–	-10 687
Foreign	–	-10 633
Domestic	–	-54
Bank loans and advances	-1 413	148 338
Bills, bonds and loan stock	-2 048	25 399
Mortgage loans	–	172 018
Other assets/liabilities	84 253	73 302
Total sources/liabilities and uses/assets	**424 011**	**424 011**
	Per cent	
Percentage of total sources used for gross capital formation	1,0	
Percentage of total sources used to acquire financial assets	99,0	
Percentage of total asset flows	22,0	
Percentage of total financial intermediary asset flows	52,0	
Total asset/liability flows as a percentage of gross domestic product	21,0	

Public Investment Corporation

The Public Investment Corporation operates as a fund manager of public-sector entities such as official pension and provident funds, social security funds and other government funds. As such, the corporation received inflows of R111,1 billion in 2007. Of this amount, R45,4 billion was invested in shares, R36,6 billion held in more liquid instruments, and R19,3 billion was invested in other loan stock and preference shares. The corporation represented 14 per cent of total financial intermediary asset flows in 2007.

Insurers and retirement funds

Table 5 shows that members contributed R75,7 billion towards insurers and retirement funds in 2007. This sector acquired net financial assets amounting to R124,6 billion, which included monetary deposits of R21,3 billion and other deposits (which included deposits with the Public Investment Corporation) of R122,4 billion at non-bank financial institutions. Heightened uncertainty in share markets and risk aversion contributed to a significant reduction in the holdings of shares during 2007. A financing deficit of R2,9 billion was recorded, mainly due to rising expenditure on capital formation. In 2007 the insurers and retirement funds sector contributed 15 per cent to the total financial intermediary asset flows.

Table 5 Flow of funds: Insurers and retirement funds, 2007

	R millions
Financing balance	-2 850
Net incurrence of financial liabilities	127 486
Members' interest in the reserves of retirement and insurance funds	75 737
Other liabilities	51 749
Net acquisition of financial assets	124 636
Monetary deposits	21 264
Other deposits	122 430
Public Investment Corporation	87 706
Foreign deposits	10
Other	34 714
Bills and bonds	-501
Short-term government bonds	-7 190
Long-term government bonds	1 901
Other	4 788
Other loan stock and preference shares	14 574
Domestic	9 810
Foreign	4 764
Shares	-45 421
Domestic	-15 983
Foreign	-29 438
Other assets	12 290
	Per cent
Percentage of total asset flows	7,0
Percentage of total financial intermediary asset flows	15,0
Total asset/liability flows as percentage of gross domestic product	6,0

Other financial institutions

Other financial institutions comprise non-bank financial institutions such as collective investment schemes (unit trusts and participation bond schemes), trust companies finance companies, and public financial enterprises that acquire funds and invest them on behalf of their clients. Unit trusts, which acquire funds largely through selling units in unit trusts, while investing the proceeds in various financial instruments, dominated the activities of this sector, which recorded a surplus of R5,6 billion in 2007. Having received a total of R56,9 billion from investors in 2007, other financial institutions invested these and other funds mainly in monetary deposits, foreign shares, and bills and bonds. The total asset/liability flows of this sector amounted to 5 per cent of gross domestic product in 2007, while its share of total financial intermediary asset flows was 12 per cent, as presented in Table 6.

Table 6 Flow of funds: Other financial institutions, 2007

	R millions
Financing balance	5 596
Net incurrence of financial liabilities	86 157
Deposits received	56 924
Long-term loans	3 583
Other liabilities	25 650
Net acquisition of financial assets	91 753
Monetary deposits	115 234
Other deposits	9 526
Foreign deposits	10 011
Other	-485
Bills and bonds	18 921
Short-term government bonds	-3 969
Long-term government bonds	3 169
Other bills	19 721
Trade credit and short-term loans	-4 823
Other loan stock and preference shares	391
Domestic	1 021
Foreign	-630
Shares	-31 755
Domestic	-37 479
Foreign	5 724
Other assets	-15 741
	Per cent
Percentage of total asset flows	5,0
Percentage of total financial intermediary asset flows	12,0
Total asset/liability flows as a percentage of gross domestic product	5,0

Central and provincial governments

As presented in Table 7, central and provincial governments recorded a financing surplus amounting to R8,4 billion in 2007. This surplus position of around 0,4 per cent of gross domestic product enabled a reduction in the issuance of government bonds. Treasury bills amounting to R8,5 billion were issued instead and other debt amounting to R23,2 billion was incurred.

Table 7 Flow of funds: Central and provincial governments, 2007

	R millions
Financing balance	**8 398**
Net acquisition of financial assets	22 146
Net incurrence of financial liabilities by financial instrument	**13 748**
Treasury bills	8 509
Short-term government bonds	-1 517
Long-term government bonds	-13 210
Non-marketable government bonds	-3 234
Other	23 200
Financing by sector	**13 748**
Foreign sector	-9 824
Public Investment Corporation	-2 038
Insurers and retirement funds	-5 715
Other financial institutions	-694
Other domestic sectors	19 589

Local governments

Local governments recorded a financing deficit of R35,9 billion in 2007. Financing of this deficit was partly made possible by the utilisation of trade credit and the incurrence of other short-term loans.

Public non-financial corporate business enterprises

The public non-financial corporate business enterprises sector recorded gross capital formation amounting to R54,9 billion in 2007. This slightly exceeded its saving, resulting in a small deficit of R0,4 billion. This sector financed its deficit primarily by issuing bills, bonds and loan stock, and taking up bank loans and advances.

Private non-financial corporate business enterprises

As indicated in Table 8, private non-financial corporate business enterprises recorded gross capital formation in excess of this sector's gross saving in 2007. The financing deficit of the sector amounted to R128,3 billion in 2007 – much higher than the R94,2 billion recorded in 2006. The deficit was funded through a variety of financial instruments, including bank loans and advances, and mortgage loans, the issuance of bills, bonds and loan stock, and long-term loans. Excess funds were invested in monetary deposits and in shares of companies abroad.

This sector continued to play a leading role in gross capital formation. It contributed R249,6 billion or 59 per cent of the total gross capital formation in 2007. The total asset/liability flows of private non-financial business enterprises amounted to 21 per cent of gross domestic product during the review period.

Households

Own savings, together with access to funding through bank loans and advances, and trade credit and short-term loans enabled households to finance a deficit of R28,5 billion in 2007. Despite their deficit, households were able to increase their interest in retirement and life funds, bank deposit holdings, as well as deposits in other financial institutions such as unit trusts.

Table 8 Flow of funds: Private non-financial corporate business enterprises, 2007

Transaction items	Sources/ liabilities R millions	Uses/ assets R millions
Gross saving	120 672	
Capital transfers	741	33
Gross capital formation		249 648
Net lending (+)/net borrowing (-)	-128 268	
Net financial investment (+/-)		-128 268
Net incurrence of financial liabilities	306 715	
Net acquisition of financial assets		178 447
Monetary deposits	–	82 111
Other deposits	-433	-25 096
Bank loans and advances	79 045	–
Trade credit and short-term loans	13 557	68 126
Bills, bonds and loan stock	75 052	-10 868
Shares	14 860	30 496
Domestic	-43 191	-30 545
Foreign	58 051	61 041
Long-term and mortgage loans	116 905	12 553
Other assets/liabilities	7 729	21 125
Total sources/liabilities and uses/assets	428 128	428 128
	Per cent	
Percentage of total sources used for gross capital formation	58,0	
Percentage of total sources used to acquire financial assets	42,0	
Percentage of total asset flows	23,0	
Gross capital formation as a percentage of gross domestic product	13,0	
Total asset/liability flows as a percentage of gross domestic product	21,0	

Summary and conclusion

Many institutional sectors demonstrated greater caution in their financial activity in 2007 amid heightened market uncertainty. Cash and liquid instruments were often preferred. The following are highlights from the analysis of South Africa's national financial accounts for the year 2007:

- Augmentation for the fifth consecutive year of domestic saving by the foreign sector to finance capital formation
- The pace of capital formation by non-financial business enterprises continued
- Financial intermediaries maintained their importance in matching surplus and deficit units
- The household sector's incurrence of large amounts of debt was partly offset by strong increases in households' interest in retirement and life funds
- The increase in gold and foreign currency holdings of the monetary authority and other monetary institutions continued
- The financial surplus of the central and provincial government contributed to a lower supply of government bonds in the domestic financial markets.

References

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National financial account

Flow of funds for the first quarter 2007[1]

R millions

Sectors / Transaction items	Foreign sector		Financial intermediaries: Monetary authority		Other monetary institutions[2]		Public Investment Corporation[3]		Insurers and retirement funds		Other financial institutions	
	S	U	S	U	S	U	S	U	S	U	S	U
1. Net saving[4]	27 081		613		6 148				- 813		576	
2. Consumption of fixed capital[4]			5		1 015				20		195	
3. Capital transfers	21	73										
4. Gross capital formation[4]				71		1 280				141		387
5. Net lending (+)/net borrowing (-) (S)	27 029		547		5 883				- 934		384	
6. Net financial investment (+) or (-) (U)		27 029		547		5 883				- 934		384
7. Net incurrence of financial liabilities (Total S 9 - 32)	11 974		12 477		94 632		52 712		55 029		36 942	
8. Net acquisition of financial assets (Total U 9 - 32)		39 003		13 024		100 515		52 712		54 095		37 326
9. Gold and other foreign reserves	5 327			5 327								
10. Cash and demand monetary[5] deposits		- 5 119	- 2 410	3 235	17 933	- 881		19 527		4 490		13 977
11. Short/medium-term monetary[5] deposits		- 3 247		- 37	- 2 971			- 8 002		1 456		8 693
12. Long-term monetary[5] deposits		- 1 483		101	58 153			26 814		6 103		25 342
13. Deposits with other financial institutions		240				- 734		5 139		13 715	23 593	
14. Deposits with other institutions	- 1 053					- 8 292	52 712	69	69	35 990		2 847
15. Treasury bills				1 453		4 315		- 547		- 25		- 4
16. Other bills	1 428			950	2 408	197		2 175		- 876	- 697	5 177
17. Bank loans and advances	4 208		5 029	1 696	1 674	53 132					- 42	
18. Trade credit and short-term loans	1 415	11 742	532	667	15 059	6 459			9 800	- 8 264	3 037	1 652
19. Short-term government bonds				- 282		- 7 264		- 9 162		- 14 932		- 1 478
20. Long-term government bonds		881				2 959		1 940		53		
21. Non-marketable government bonds[6]		327		- 2 608				111				
22. Securities of local governments						1		10		355		- 384
23. Securities of public enterprises		4	942			2 015		- 4		1 678	356	- 246
24. Other loan stock and preference shares	1 215	466			- 569	2 363		6 300	83	- 925	3	- 981
25. Ordinary shares	5 231	34 960			8 929	402		18 953	46	30 630		- 20 952
26. Foreign branch/head office balances												
27. Long-term loans	- 277	489	7 994	8		- 495		1	- 9	11 021	6 030	2 807
28. Mortgage loans	1 269					32 444				- 38		- 70
29. Interest in retirement and life funds[7]		320							16 118			
30. Amounts receivable/payable	- 2 724	- 421	57	20	- 4 966	3 660		21	10 140	- 9 778	372	- 406
31. Other assets/liabilities	- 4 065	- 156	333	2 494	- 763	9 925		- 10 633	18 587	- 16 418	3 968	1 264
32. Balancing item					- 255	309			195	- 140	322	88

S = Sources, i.e. net increase in liabilities at transaction value.
U = Uses, i.e. net increase in assets at transaction value.

KB230

1. A negative amount reflects a decrease in that item. In the case of liabilities (sources) it denotes a reduction in the available sources of funds and in the case of assets (uses) it indicates an additional source of funds.
2. Including mutual banks and the Postbank.
3. Before April 2005 the Public Investment Commissioners.
4. As taken from the national income (and production) accounts.
5. Namely deposits with the SA Reserve Bank (including coin liabilities), Corporation for Public Deposits, banks, the Land Bank, mutual banks and the Postbank.
6. Non-marketable bonds and other Treasury bills.
7. Members' interest in the reserves of retirement and all insurance funds.

National financial account (continued)
Flow of funds for the first quarter 2007[1]

R millions

General government				Corporate business enterprises								Sectors
Central and provincial governments		Local governments		Public sector		Private sector		Households, etc.		Total		
S	U	S	U	S	U	S	U	S	U	S	U	Transaction items
19 180		- 11 746		- 1 199		- 3 734		772		36 878		1. Net saving[4]
5 413		3 707		6 879		35 099		8 065		60 398		2. Consumption of fixed capital[4]
	15 201	3 957		8 564		366	7	2 387	14	15 295	15 295	3. Capital transfers
	6 788		6 172		12 183		55 952		14 302		97 276	4. Gross capital formation[4]
2 604		- 10 254		2 061		- 24 228		- 3 092		-		5. Net lending (+)/net borrowing (-) (S)
	2 604		- 10 254		2 061		- 24 228		- 3 092		-	6. Net financial investment (+) or (-) (U)
- 14 037		7 096		3 468		39 086		64 912		364 291		7. Net incurrence of financial liabilities (Total S 9 - 32)
	- 11 433		- 3 158		5 529		14 858		61 820		364 291	8. Net acquisition of financial assets (Total U 9 - 32)
										5 327	5 327	9. Gold and other foreign reserves
	- 23 166		2 470		178		- 8 748		9 560	15 523	15 523	10. Cash and demand monetary[5] deposits
	3 476		3 277		- 3 183		- 12 001		6 597	- 2 971	- 2 971	11. Short/medium-term monetary[5] deposits
	- 237		- 289		502		- 259		1 559	58 153	58 153	12. Long-term monetary[5] deposits
			60		1 099		- 708		4 782	23 593	23 593	13. Deposits with other financial institutions
	16 514			- 358		264	4 072		434	51 634	51 634	14. Deposits with other institutions
4 260							- 932			4 260	4 260	15. Treasury bills
	1 372			1 012	- 1 779	3 870	805			8 021	8 021	16. Other bills
868		- 128		1 647		23 864		17 708		54 828	54 828	17. Bank loans and advances
1 822	538	6 337	- 933	1 098	- 2 018	- 10 101	31 811	14 666	2 011	43 665	43 665	18. Trade credit and short-term loans
- 33 140					- 20				- 2	- 33 140	- 33 140	19. Short-term government bonds
5 676			8		- 167				2	5 676	5 676	20. Long-term government bonds
- 3 759			- 6						- 1 583	- 3 759	- 3 759	21. Non-marketable government bonds[6]
		- 30			2		- 9		- 5	- 30	- 30	22. Securities of local governments
	65			2 173			- 2		- 39	3 471	3 471	23. Securities of public enterprises
	209		81	3 240	1 347	5 358	471		- 1	9 330	9 330	24. Other loan stock and preference shares
	881			- 785	25	17 637	- 33 859		18	31 058	31 058	25. Ordinary shares
												26. Foreign branch/head office balances
297	6 758	- 4	137	1 445	839	8 489	2 491		- 91	23 965	23 965	27. Long-term loans
			1 087	23		10 185		21 946		33 423	33 423	28. Mortgage loans
	- 11 291				- 5 090		- 6 414		38 593	16 118	16 118	29. Interest in retirement and life funds[7]
5 645	- 552	- 261		- 3 913	4 576	998	7 711	- 532	- 15	4 816	4 816	30. Amounts receivable/payable
4 220	- 6 000	886	- 9 038	- 2 085	9 163	- 21 778	29 826	11 124		10 427	10 427	31. Other assets/liabilities
74		296	- 12	- 29	55	300	603			903	903	32. Balancing item

S = Sources, i.e. net increase in liabilities at transaction value.
U = Uses, i.e. net increase in assets at transaction value.

KB231

1. A negative amount reflects a decrease in that item. In the case of liabilities (sources) it denotes a reduction in the available sources of funds and in the case of assets (uses) it indicates an additional source of funds.
2. Including mutual banks and the Postbank.
3. Before April 2005 the Public Investment Commissioners.
4. As taken from the national income (and production) accounts.
5. Namely deposits with the SA Reserve Bank (including coin liabilities), Corporation for Public Deposits, banks, the Land Bank, mutual banks and the Postbank.
6. Non-marketable bonds and other Treasury bills.
7. Members' interest in the reserves of retirement and all insurance funds.

National financial account

Flow of funds for the second quarter 2007[1]

R millions

Sectors / Transaction items	Foreign sector		Financial intermediaries: Monetary authority		Other monetary institutions[2]		Public Investment Corporation[3]		Insurers and retirement funds		Other financial institutions	
	S	U	S	U	S	U	S	U	S	U	S	U
1. Net saving[4]	34 549		638		6 510				- 3 709		2 579	
2. Consumption of fixed capital[4]			6		1 037				21		198	
3. Capital transfers	23	60										
4. Gross capital formation[4]				24		619				170		464
5. Net lending (+)/net borrowing (-) (S)	34 512		620		6 928				- 3 858		2 313	
6. Net financial investment (+) or (-) (U)		34 512		620		6 928				- 3 858		2 313
7. Net incurrence of financial liabilities (Total S 9 - 32)	40 040		12 540		110 225		21 018		32 720		6 691	
8. Net acquisition of financial assets (Total U 9 - 32)		74 552		13 160		117 153		21 018		28 862		9 004
9. Gold and other foreign reserves	11 861			11 861								
10. Cash and demand monetary[5] deposits		2 908	15 225	5 548	19 254	2 749		- 6 392		2 498		403
11. Short/medium-term monetary[5] deposits		92	- 44	293	38 880			5 661		483		3 062
12. Long-term monetary[5] deposits		- 1 417		- 101	21 955			- 4 596				28 651
13. Deposits with other financial institutions		- 214				895		5 056		9 271	11 917	
14. Deposits with other institutions	15 174					15 499	21 018	157	157	19 156		4 708
15. Treasury bills				44		2 198				- 132		11
16. Other bills	166			1 844	- 738	1 923		- 622		- 474	- 1 257	3 809
17. Bank loans and advances	- 3 511		5 596	465	466	30 285					- 117	
18. Trade credit and short-term loans	- 7 459	- 10 306	- 1 983	- 888	6 409	5 191			2 697	261	2 284	1 118
19. Short-term government bonds				- 357		2 677		2 717		- 1 562		- 3 599
20. Long-term government bonds		- 3 132				- 2 926		7 605				3 767
21. Non-marketable government bonds[6]		834		- 172								
22. Securities of local governments	- 21					- 9		8		- 38		43
23. Securities of public enterprises		13	1 326			1 312		- 1 255		5 743	184	314
24. Other loan stock and preference shares	2 283	27 977			- 227	759		2 921	3 101	7 125	71	- 1 183
25. Ordinary shares	15 802	10 926			1 885	1 121		6 844	518	- 13 387		- 32 616
26. Foreign branch/head office balances												
27. Long-term loans	1 992	39 346	- 4 927	- 73	15 143	379		- 3	- 48	- 663	- 1 226	- 371
28. Mortgage loans	660					42 972				- 17		- 179
29. Interest in retirement and life funds[7]		53							14 161			
30. Amounts receivable/payable	3 581	4 260	- 326	- 3 966	- 5 100	2 998		- 48	4 562	2 784	- 871	- 248
31. Other assets/liabilities	- 488	3 212	- 2 327	- 1 338	11 973	9 098		2 965	7 429	- 1 889	- 4 221	1 235
32. Balancing item					325	32			143	- 297	- 73	79

S = Sources, i.e. net increase in liabilities at transaction value.
U = Uses, i.e. net increase in assets at transaction value.

KB230

1. A negative amount reflects a decrease in that item. In the case of liabilities (sources) it denotes a reduction in the available sources of funds and in the case of assets (uses) it indicates an additional source of funds.
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6. Non-marketable bonds and other Treasury bills.
7. Members' interest in the reserves of retirement and all insurance funds.

National financial account (continued)
Flow of funds for the second quarter 2007[1]

R millions

General government				Corporate business enterprises								Sectors
Central and provincial governments		Local governments		Public sector		Private sector		Households, etc.		Total		
S	U	S	U	S	U	S	U	S	U	S	U	Transaction items
2 300		- 6 145		1 114		603		10 370		48 809		1. Net saving[4]
5 610		3 860		7 035		36 470		8 390		62 627		2. Consumption of fixed capital[4]
	6 079	913		4 059		110	8	1 057	15	6 162	6 162	3. Capital transfers
	6 484		6 140		13 233		69 075		15 227		111 436	4. Gross capital formation[4]
- 4 653		- 7 512		- 1 025		- 31 900		4 575		-		5. Net lending (+)/net borrowing (-) (S)
	- 4 653		- 7 512		- 1 025		- 31 900		4 575		-	6. Net financial investment (+) or (-) (U)
7 384		3 153		- 2 474		75 908		56 820		364 025		7. Net incurrence of financial liabilities (Total S 9 - 32)
	2 731		- 4 359		- 3 499		44 008		61 395		364 025	8. Net acquisition of financial assets (Total U 9 - 32)
										11 861	11 861	9. Gold and other foreign reserves
	4 535		866		757		12 291		8 316	34 479	34 479	10. Cash and demand monetary[5] deposits
	2 934		- 3 169		- 1 984		17 916		13 548	38 836	38 836	11. Short/medium-term monetary[5] deposits
	1 721		- 522		- 1 485		- 35		- 261	21 955	21 955	12. Long-term monetary[5] deposits
			27		121		- 5 485		2 246	11 917	11 917	13. Deposits with other financial institutions
	1 579			141	20	309	- 4 432		112	36 799	36 799	14. Deposits with other institutions
2 750							629			2 750	2 750	15. Treasury bills
	454			- 153	- 5 397	6 312	2 793			4 330	4 330	16. Other bills
- 1 147		908		- 992		24 486		5 061		30 750	30 750	17. Bank loans and advances
- 886	- 200	306	95	- 516	1 426	16 929	19 772	2 166	3 478	19 947	19 947	18. Trade credit and short-term loans
- 112					14		- 1		- 1	- 112	- 112	19. Short-term government bonds
5 404			- 5		95					5 404	5 404	20. Long-term government bonds
560			- 16						- 86	560	560	21. Non-marketable government bonds[6]
		- 5			- 4		- 25		- 1	- 26	- 26	22. Securities of local governments
	- 113		- 2	4 467			- 2		- 33	5 977	5 977	23. Securities of public enterprises
	450		- 194	- 4 002	- 872	32 096	- 3 689		28	33 322	33 322	24. Other loan stock and preference shares
	77			- 865	7	- 20 125	24 223		20	- 2 785	- 2 785	25. Ordinary shares
												26. Foreign branch/head office balances
617	- 3 646	1 039	627	- 1 813	- 952	24 601	1 235	503	2	35 881	35 881	27. Long-term loans
			- 421	109		11 997		29 589		42 355	42 355	28. Mortgage loans
	287				5 852		- 20 561		28 530	14 161	14 161	29. Interest in retirement and life funds[7]
198	502	- 19	521	7 336	- 723	- 13 993	- 280	15 929	5 497	11 297	11 297	30. Amounts receivable/payable
	- 5 849	693	- 1 875	- 5 889	- 281	- 6 134	- 670	3 572		4 608	4 608	31. Other assets/liabilities
		231	- 291	- 297	- 93	- 570	329			- 241	- 241	32. Balancing item

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U = Uses, i.e. net increase in assets at transaction value.

KB231

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4. As taken from the national income (and production) accounts.
5. Namely deposits with the SA Reserve Bank (including coin liabilities), Corporation for Public Deposits, banks, the Land Bank, mutual banks and the Postbank.
6. Non-marketable bonds and other Treasury bills.
7. Members' interest in the reserves of retirement and all insurance funds.

National financial account
Flow of funds for the third quarter 2007[1]

R millions

Sectors / Transaction items	Foreign sector		Financial intermediaries: Monetary authority		Other monetary institutions[2]		Public Investment Corporation[3]		Insurers and retirement funds		Other financial institutions	
	S	U	S	U	S	U	S	U	S	U	S	U
1. Net saving[4]	45 314		219		8 057				3 406		615	
2. Consumption of fixed capital[4]			6		1 063				21		201	
3. Capital transfers	26	84										
4. Gross capital formation[4]				18		1 079				170		461
5. Net lending (+)/net borrowing (-) (S)	45 256		207		8 041				3 257		355	
6. Net financial investment (+) or (-) (U)		45 256		207		8 041				3 257		355
7. Net incurrence of financial liabilities (Total S 9 - 32)	31 734		10 410		110 618		30 986		31 927		35 830	
8. Net acquisition of financial assets (Total U 9 - 32)		76 990		10 617		118 659		30 986		35 184		36 185
9. Gold and other foreign reserves	10 582			10 582								
10. Cash and demand monetary[5] deposits		- 2 959	9 951	- 36	27 953	1 401		6 640		1 876		2 903
11. Short/medium-term monetary[5] deposits		17 963	- 172	591	79 390			20 032		- 482		26 013
12. Long-term monetary[5] deposits		- 1 298	23		- 22 616			- 19 570		4 340		- 8 640
13. Deposits with other financial institutions		19				330		3 119		5 650	14 520	
14. Deposits with other institutions	8 122					9 251	30 986	118	118	29 099		- 1 383
15. Treasury bills				- 1 997		3 596				29		574
16. Other bills	- 304			1 290	199	2 004		- 480	192	2 085	5 948	- 5 036
17. Bank loans and advances	4 829		3 788	- 678	- 671	38 100					- 4	
18. Trade credit and short-term loans	2 757	16 843	- 2 216	333	10 815	- 103			9 103	- 842	3 097	1 871
19. Short-term government bonds				729		10 815		14 438		3 158		3 327
20. Long-term government bonds		- 3 596		- 748		- 6 022		- 18 622		- 1 748		960
21. Non-marketable government bonds[6]		77										
22. Securities of local governments	4					3		19		85		13
23. Securities of public enterprises		- 88	- 199			- 1 411		2 421		3 438	176	- 224
24. Other loan stock and preference shares	1 552	6 932			- 772	1 003		6 216	- 2 413	2 887	- 2	- 790
25. Ordinary shares	3 911	24 983			9 550	- 398		11 674	- 300	- 15 830		24 681
26. Foreign branch/head office balances												
27. Long-term loans	1 736	6 196	- 928	12		- 4 215		- 245	- 37	94	353	816
28. Mortgage loans	364					49 820				- 1 643		238
29. Interest in retirement and life funds[7]		84							23 659			
30. Amounts receivable/payable	2 219	6 991	278	- 3	9 892	6 011		- 69	49	2 776	3 384	612
31. Other assets/liabilities	- 4 038	4 843	- 115	542	- 3 092	8 355		5 295	1 417	159	8 268	- 9 562
32. Balancing item					- 30	119			139	53	90	- 188

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U = **Uses**, i.e. net increase in assets at transaction value.

KB230

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6. Non-marketable bonds and other Treasury bills.
7. Members' interest in the reserves of retirement and all insurance funds.

National financial account (continued)
Flow of funds for the third quarter 2007[1]

R millions

General government				Corporate business enterprises								Sectors
Central and provincial governments		Local government		Public sector		Private sector		Households, etc.		Total		
S	U	S	U	S	U	S	U	S	U	S	U	Transaction items
8 183		- 9 103		1 631		- 12 200		- 1 106		45 016		1. Net saving[4]
5 790		3 993		7 256		37 968		8 698		64 996		2. Consumption of fixed capital[4]
	11 030	3 768		5 642		110	9	1 594	17	11 140	11 140	3. Capital transfers
	6 958		6 344		13 987		64 887		16 108		110 012	4. Gross capital formation[4]
- 4 015		- 7 686		542		- 39 018		- 6 939		-		5. Net lending (+)/net borrowing (-) (S)
	- 4 015		- 7 686		542		- 39 018		- 6 939		-	6. Net financial investment (+) or (-) (U)
18 019		4 899		- 4 309		71 461		55 913		397 488		7. Net incurrence of financial liabilities (Total S 9 - 32)
	14 004		- 2 787		- 3 767		32 443		48 974		397 488	8. Net acquisition of financial assets (Total U 9 - 32)
										10 582	10 582	9. Gold and other foreign reserves
	2 705		- 324		1 978		20 350		3 370	37 904	37 904	10. Cash and demand monetary[5] deposits
	- 3 490		- 1 573		4 212		5 466		10 486	79 218	79 218	11. Short/medium-term monetary[5] deposits
	- 1 198		1 363		- 1 335		3 514		231	- 22 593	- 22 593	12. Long-term monetary[5] deposits
			27		179		- 148		5 344	14 520	14 520	13. Deposits with other financial institutions
	2 743			205	31	- 1 008	- 1 571		135	38 423	38 423	14. Deposits with other institutions
1 399							- 803			1 399	1 399	15. Treasury bills
	- 1 181			- 836	3 014	1 229	4 732			6 428	6 428	16. Other bills
- 172		- 96		1 180		20 206		8 362		37 422	37 422	17. Bank loans and advances
4 444	- 626	4 377	- 944	- 1 867	- 3 172	- 7 649	16 937	5 873	- 1 563	28 734	28 734	18. Trade credit and short-term loans
32 481			7		- 21		8		20	32 481	32 481	19. Short-term government bonds
- 29 975			- 7		- 169		- 1		- 22	- 29 975	- 29 975	20. Long-term government bonds
1 960			- 2						1 885	1 960	1 960	21. Non-marketable government bonds[6]
		- 40			3		- 159			- 36	- 36	22. Securities of local governments
	203		2	4 205			- 9		- 150	4 182	4 182	23. Securities of public enterprises
	485		23	415	4 523	7 996	- 14 509		6	6 776	6 776	24. Other loan stock and preference shares
	532			639	311	21 492	- 10 667		6	35 292	35 292	25. Ordinary shares
												26. Foreign branch/head office balances
43	- 1 381	1	- 434	- 393	1 398	11 341	9 966	111	20	12 227	12 227	27. Long-term loans
			2 014	101		16 123		33 841		50 429	50 429	28. Mortgage loans
	1 853				228		- 13 946		35 440	23 659	23 659	29. Interest in retirement and life funds[7]
4 839	4 117	19	189	- 9 136	- 6 129	- 1 829	6 253	4 799	- 6 234	14 514	14 514	30. Amounts receivable/payable
3 000	9 181	478	- 3 096	1 134	- 8 614	3 751	6 627	2 927		13 730	13 730	31. Other assets/liabilities
	61	160	- 32	44	- 204	- 191	403			212	212	32. Balancing item

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KB231

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6. Non-marketable bonds and other Treasury bills.
7. Members' interest in the reserves of retirement and all insurance funds.

National financial account

Flow of funds for the fourth quarter 2007[1]

R millions

Sectors / Transaction items	Foreign sector		Financial intermediaries: Monetary authority		Other monetary institutions[2]		Public Investment Coporation[3]		Insurers and retirement funds		Other financial institutions	
	S	U	S	U	S	U	S	U	S	U	S	U
1. Net saving[4]	38 072		140		14 538				- 1 166		2 755	
2. Consumption of fixed capital[4]			6		1 090				21		205	
3. Capital transfers	24	**74**										
4. Gross capital formation[4]				**57**		**778**				**170**		**416**
5. Net lending (+)/net borrowing (-) (S)	38 022		89		14 850				- 1 315		2 544	
6. Net financial investment (+) or (-) (U)		**38 022**		**89**		**14 850**				**- 1 315**		**2 544**
7. Net incurrence of financial liabilities (Total S 9 - 32)	- 588		20 861		69 078		6 417		7 810		6 694	
8. Net acquisition of financial assets (Total U 9 - 32)		**37 434**		**20 950**		**83 928**		**6 417**		**6 495**		**9 238**
9. Gold and other foreign reserves	12 415			**12 415**								
10. Cash and demand monetary[5] deposits		**6 763**	15 734	**9 836**	56 176	**8 616**		**3 882**		**- 3 730**		**14 049**
11. Short/medium-term monetary[5] deposits		**- 7 598**	252	**- 1 452**	- 3 399			**- 8 833**		**- 3 467**		**- 5 010**
12. Long-term monetary[5] deposits		**- 931**	- 4		13 053			**1 468**		**7 697**		**5 791**
13. Deposits with other financial institutions		**- 522**				**- 157**		**3 731**		**6 026**	6 894	
14. Deposits with other institutions	- 32 876					**- 27 145**	6 417	**176**	176	**3 523**		**3 354**
15. Treasury bills				**1 997**		**- 3 911**				**- 247**		**- 475**
16. Other bills	27 356			**26 220**	- 2 274	**578**		**- 279**	28	**996**	- 203	**15 665**
17. Bank loans and advances	13 941		- 5 987	**- 2 849**	- 2 882	**26 821**					107	
18. Trade credit and short-term loans	- 9 606	**13 416**	1 460	**21**	10 541	**5 974**			- 5 215	**9 108**	- 914	**- 9 464**
19. Short-term government bonds				**33**		**- 2 108**		**- 2 384**		**6 146**		**- 2 219**
20. Long-term government bonds		**492**		**51**		**1 199**		**1 992**		**3 596**		**- 1 558**
21. Non-marketable government bonds[6]		**104**		**- 52**				**- 111**				
22. Securities of local governments						**- 7**		**74**		**- 6**		**- 68**
23. Securities of public enterprises		**107**	- 1 921			**1 136**		**5 753**		**- 7 823**	779	**2 687**
24. Other loan stock and preference shares	6 231	**- 550**			- 75	**8 004**		**3 817**	4 763	**5 487**	86	**3 345**
25. Ordinary shares	11 089	**- 962**			1 294	**200**		**7 883**	- 9	**- 46 834**		**- 2 868**
26. Foreign branch/head office balances												
27. Long-term loans	3 159	**9 796**	2 384	**8**		**- 187**		**- 7**	81	**- 2 626**	- 1 574	**1 739**
28. Mortgage loans	500					**46 782**				**- 90**		**- 129**
29. Interest in retirement and life funds[7]		**- 50**							21 799			
30. Amounts receivable/payable	- 16 301	**9 761**	- 147	**- 3**	6 326	**9 111**		**- 5 783**	- 9 561	**11 043**	335	**- 6 147**
31. Other assets/liabilities	- 16 496	**7 608**	9 090	**- 25 275**	- 9 512	**8 766**		**- 4 962**	- 3 939	**17 522**	1 138	**- 9 340**
32. Balancing item					- 170	**256**			- 313	**174**	46	**- 114**

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KB230

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National financial account (continued)
Flow of funds for the fourth quarter 2007[1]

R millions

General government				Corporate business enterprises								Sectors
Central and provincial governments		Local governments		Public sector		Private sector		Households, etc.		Total		
S	U	S	U	S	U	S	U	S	U	S	U	Transaction items
28 428		- 11 461		- 527		- 12 930		- 16 921		40 928		1. Net saving[4]
5 909		4 074		7 408		39 396		8 903		67 012		2. Consumption of fixed capital[4]
	12 360	3 630		6 688		155	**9**	1 961	**15**	12 458	**12 458**	3. Capital transfers
	7 515		**6 705**		**15 548**		**59 734**		**17 017**		**107 940**	4. Gross capital formation[4]
14 462		- 10 462		- 1 979		- 33 122		- 23 089		-		5. Net lending (+)/net borrowing (-) (S)
	14 462		**- 10 462**		**- 1 979**		**- 33 122**		**- 23 089**		**-**	6. Net financial investment (+) or (-) (U)
2 382		9 051		- 1 334		120 260		55 980		296 611		7. Net incurrence of financial liabilities (Total S 9 - 32)
	16 844		**- 1 411**		**- 3 313**		**87 138**		**32 891**		**296 611**	8. Net acquisition of financial assets (Total U 9 - 32)
										12 415	**12 415**	9. Gold and other foreign reserves
	10 303		**- 1 693**		**- 2 346**		**24 847**		**1 383**	71 910	**71 910**	10. Cash and demand monetary[5] deposits
	- 4 434		**- 411**		**5 170**		**17 737**		**5 151**	- 3 147	**- 3 147**	11. Short/medium-term monetary[5] deposits
	- 3 398		**977**		**- 1 495**		**1 033**		**1 907**	13 049	**13 049**	12. Long-term monetary[5] deposits
			2 321		**- 213**		**- 8 659**		**4 367**	6 894	**6 894**	13. Deposits with other financial institutions
	1 865			- 117	**- 45**	2	**- 8 165**		**39**	- 26 398	**- 26 398**	14. Deposits with other institutions
100							**2 736**			100	**100**	15. Treasury bills
	- 564			187	**- 1 058**	3 661	**- 12 803**			28 755	**28 755**	16. Other bills
299		558		- 341		10 489		7 788		23 972	**23 972**	17. Bank loans and advances
- 66	**- 254**	3 894	**- 1 672**	2 497	**- 470**	14 378	**- 394**	1 736	**2 440**	18 705	**18 705**	18. Trade credit and short-term loans
- 746					**- 6**		**- 207**		**- 1**	- 746	**- 746**	19. Short-term government bonds
5 685					**- 87**					5 685	**5 685**	20. Long-term government bonds
- 1 995			**36**						**- 1 972**	- 1 995	**- 1 995**	21. Non-marketable government bonds[6]
					2		**5**					22. Securities of local governments
	- 29			2 969					**- 4**	1 827	**1 827**	23. Securities of public enterprises
	- 385		**- 31**	420	**- 3 868**	14 530	**10 104**		**32**	25 955	**25 955**	24. Other loan stock and preference shares
				3		- 4 144	**50 799**		**15**	8 233	**8 233**	25. Ordinary shares
												26. Foreign branch/head office balances
- 32	**3 196**	141	**47**	- 184	**1 436**	9 450	**- 1 139**	- 1 165	**- 3**	12 260	**12 260**	27. Long-term loans
			- 1 195	62		24 719		20 087		45 368	**45 368**	28. Mortgage loans
	- 238				**- 211**		**3 023**		**19 275**	21 799	**21 799**	29. Interest in retirement and life funds[7]
- 863	**4 642**	3 964	**100**	- 4 100	**- 350**	24 249	**8 800**	27 534	**262**	31 436	**31 436**	30. Amounts receivable/payable
	5 855	370	**83**	- 2 547	**171**	22 241	**- 83**			345	**345**	31. Other assets/liabilities
	285	124	**27**	- 183	**57**	685	**- 496**			189	**189**	32. Balancing item

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U = Uses, i.e. net increase in assets at transaction value.

KB231

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6. Non-marketable bonds and other Treasury bills.
7. Members' interest in the reserves of retirement and all insurance funds.

Note on the cost of servicing household debt

by J Mokoena[1]

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

Introduction

Rising income and employment levels, and the broadening of access to banking products and services have allowed increasing numbers of households to borrow and increase their debt levels over time. Servicing such debt encumbers a significant proportion of household disposable income. Various approaches can be used to quantify the debt-service cost to households.

This note presents the tentative results of experimental work undertaken to include principal repayments in the calculation of household debt-service cost.

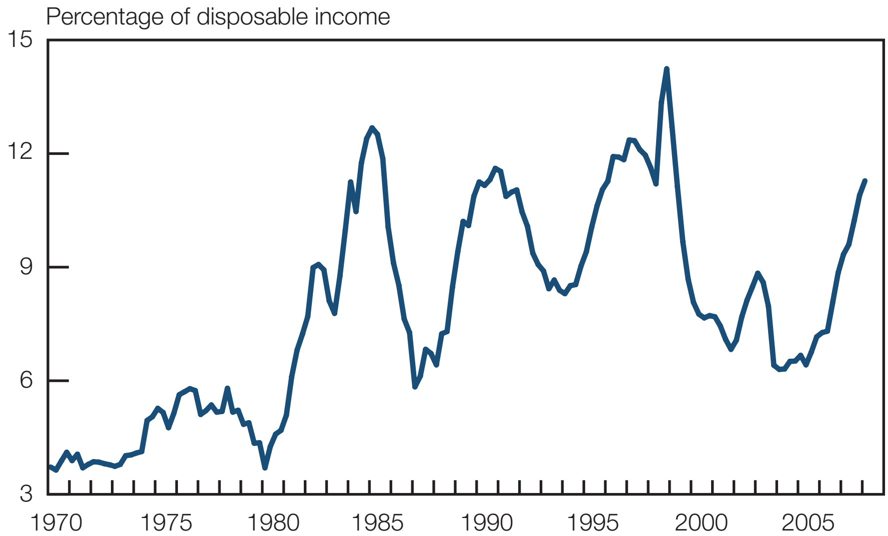
Conventional measure of household debt-service cost

The conventional measure of household debt-service cost used by the South African Reserve Bank considers interest payments on debt as the only cost to households of servicing such debt. An alternative approach is to include interest payments and principal repayments in debt-servicing costs.

The conventional measure recognises the flexibility of modern credit extension practices. Loans can easily be rolled over or refinanced and, as a consequence, the binding constraint is deemed to be the household's ability to afford the interest payable on the outstanding debt from the household's disposable income. In calculating the interest-only debt-service cost, it is assumed that contracts provide for adjustable interest rates, and a quarterly average interest rate (i.e., prime overdraft rate and predominant mortgage rate for dwellings) is applied to all outstanding amounts of different types of loans extended to the household sector. It should be noted that the household sector includes unincorporated businesses.

Figure 1 indicates developments in South Africa's household debt-service cost as a ratio of disposable income since 1970. This measure only considers interest burden and reflects interest payable by households relative to disposable income.

Figure 1 Debt-service cost: Conventional measure



Debt-service cost incorporating principal repayments

For certain types of loans such as instalment sale credit, punctual payment of each full instalment, including interest and principal repayment, may be a quite rigid requirement and refinancing may be impossible to obtain, not least because of the finite lifespan of the asset being financed, which also serves as security for the loan. In such instances it is appropriate to include required principal repayments together with interest when calculating debt-service cost.

To estimate the debt-service cost incorporating principal and interest payments, assumptions were made about initial and remaining time to maturity of different types of loans outstanding, as indicated in Table 1. Three types of loans were distinguished, namely (1) mortgage advances; (2) instalment sale and leasing finance; and (3) other loans and advances (which include overdraft facilities on current account, credit card advances, personal loans and the like).

Table1 Average maturity of, and interest rate on, various types of loans

Loan type	Average initial maturity in months	Average remaining maturity in months	Average interest rate
Mortgage advances	244	202	Mortgage rate: dwellings
Instalment sale and leasing finance	54	38	Prime rate
Other loans and advances	Revolving	Revolving	Prime rate

Source: Selected South African banks

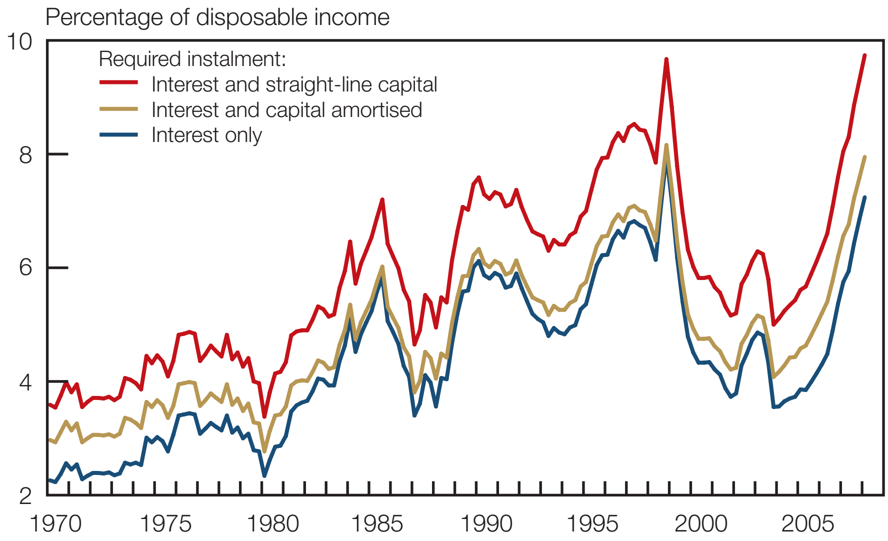
Quarterly principal repayments and interest payments on the first two types of loans were estimated in two ways. First, the outstanding amounts of the loans were amortised. In calculating the required instalment, the current interest rate was applied and the instalment per unit borrowed was calculated for a loan of average initial maturity. At the point in the repayment schedule corresponding to a loan of average remaining maturity, the ratio of the total instalment to the interest component of the instalment was established. This ratio was applied to the amount of interest only on the outstanding amount of loans, to obtain an aggregate instalment amount. Second, the capital repayment per unit borrowed was approximated by assuming a straight-line capital repayment schedule. For instalment sale and leasing finance, for instance, the capital repayment per month was set at 1/54 multiplied by the outstanding amount of such finance. To this was added the monthly interest on such outstanding amount, to obtain the total instalment.

Estimated debt-service cost of the household sector

Mortgage advances

The accumulation of mortgage debt over the years has translated into higher debt-service cost of households, as illustrated in Figure 2. As a percentage of disposable income, in recent quarters all measures of debt-service cost have approached or exceeded the record levels established in the late 1990s, reflecting significant pressure on household disposable income because of rising interest rates. More than 50 per cent of the banks' mortgage portfolios were originated in the past three to four years, largely driven by the boom in the property market. As a result, the bulk of households' payments towards servicing their mortgage debt consists of the interest component.

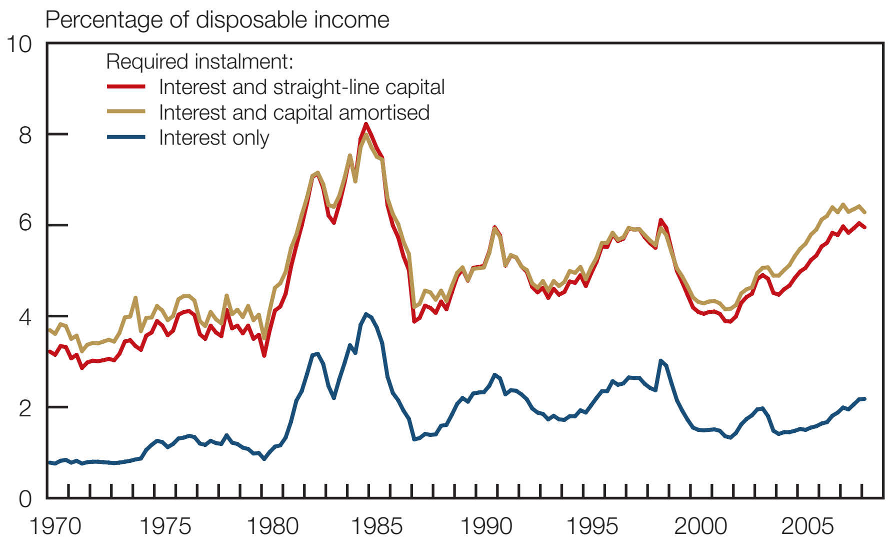
Figure 2 Debt-service cost: Mortgage advances



Instalment sale and leasing finance

Instalment sale and leasing finance is used extensively by the household sector to finance its expenditure on motor vehicles and other durable goods. The bulk of the required instalments (including capital and interest) that households have to meet is in the form of principal repayments because of shorter maturities embedded in this type of credit, as indicated in Figure 3.

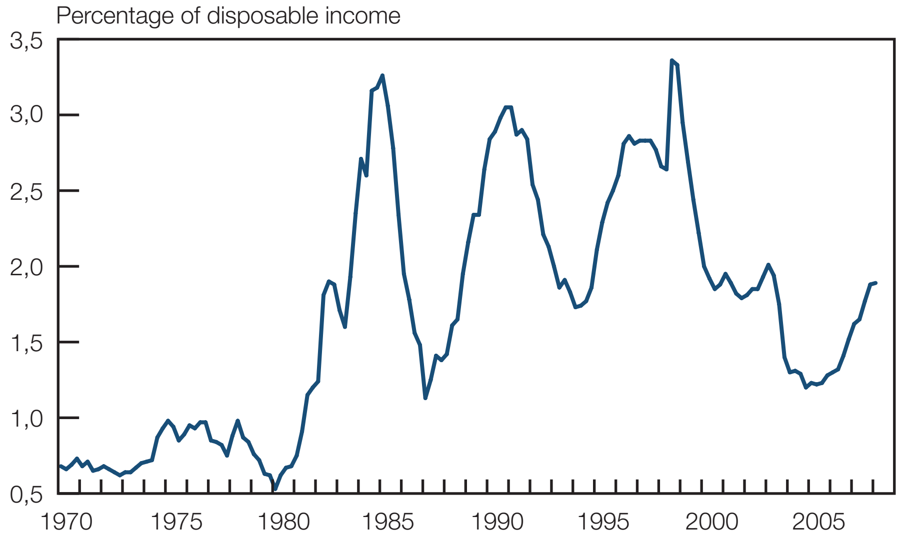
Figure 3 Debt-service cost: Instalment sale and leasing finance



Other loans and advances

An interest-only approach was considered in respect of other loans and advances because a significant amount of this credit category is in the form of credit card advances and bank overdrafts, which are routinely rolled over or are of a revolving nature and often do not have a fixed number of payments. As a percentage of disposable income, this element of debt-service cost has picked up in recent years, but nevertheless remained at relatively low levels, as reflected in Figure 4. Banks' other loans and advances are mainly used by the corporate sector; hence they carry less weight in household-sector debt.

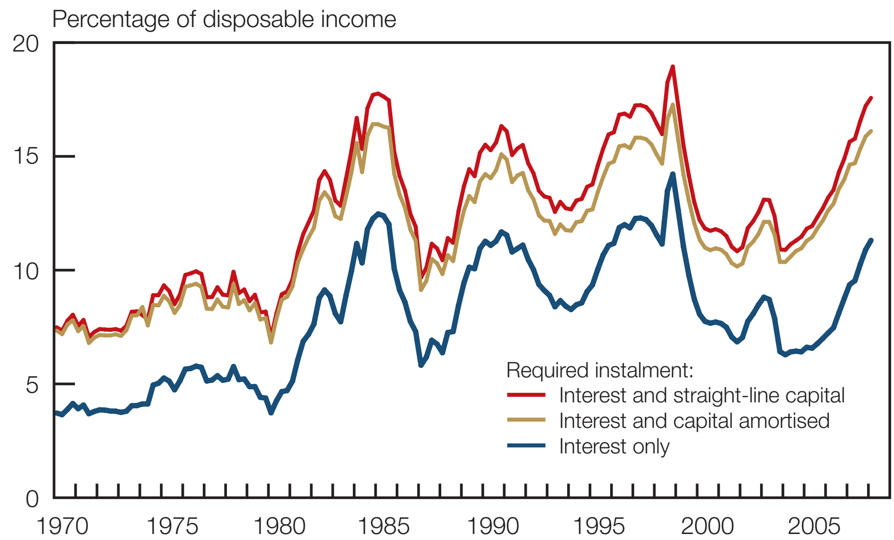
Figure 4 Debt-service cost: Other loans and advances



Total loans and advances

Figure 5 indicates developments in debt-service cost of households calculated by adding the estimated debt-service payments on mortgage advances, instalment sale and leasing finance, and other loans and advances, relative to disposable income. If capital repayments are included in the debt-service cost of the first two types of finance, the cost of servicing the household debt increases considerably, to almost 18 per cent of disposable income most recently if the straight-line capital approach is used. This may be compared with 11,6 per cent if interest only is considered.

Figure 5 Debt-service cost: Total loans and advances



Conclusion

Additional approaches to estimating the debt-service cost of households are introduced in this note. The existing measure, which incorporates the interest cost only, is broadened by incorporating principal repayments together with interest. This results in a substantial increase in the estimated household debt-service ratio.

Owing to innovative, flexible credit products, which make refinancing debt comparatively easy, these elevated debt-service ratios may, however, overstate the true cash-flow impairment faced by households arising from the need to service their indebtedness. There are numerous avenues that may be used to effectively postpone the repayment of capital on amounts borrowed. The capital-and-interest measures of debt-service cost should therefore be used with caution.

References

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