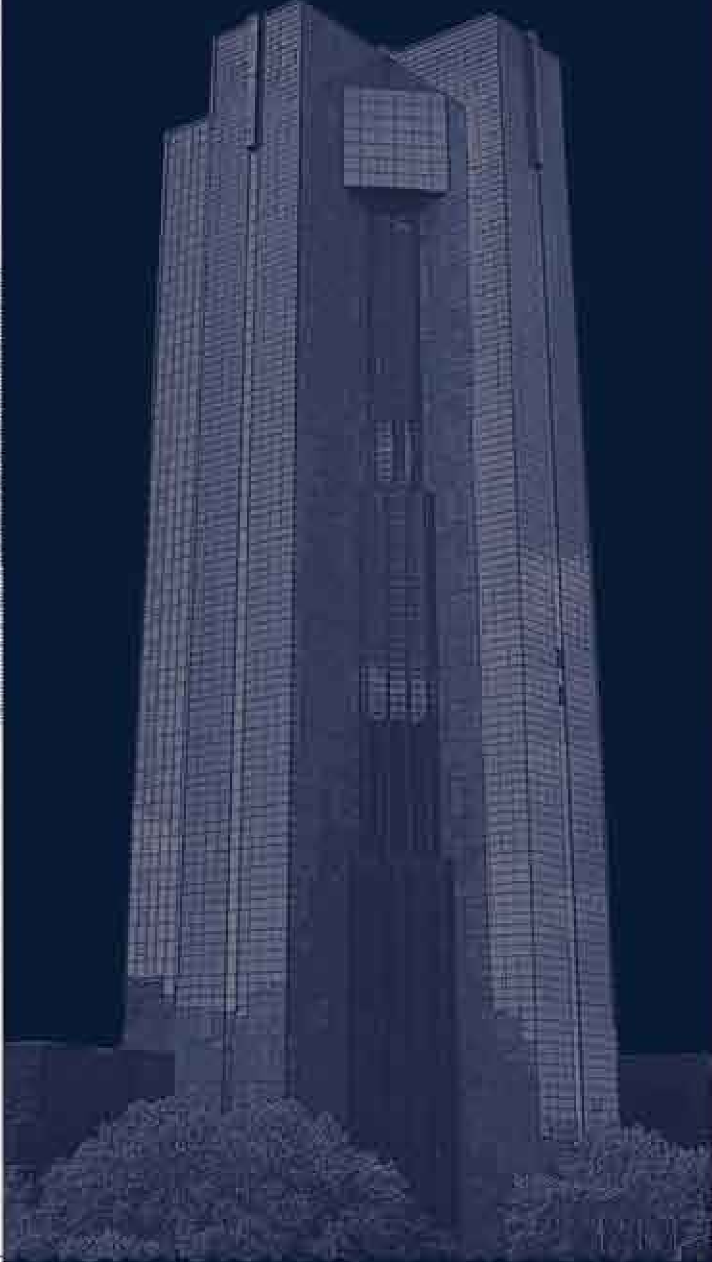

Quarterly Bulletin

March 2011

South African Reserve Bank

90th

Anniversary

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ISSN 0038-2620

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Introduction

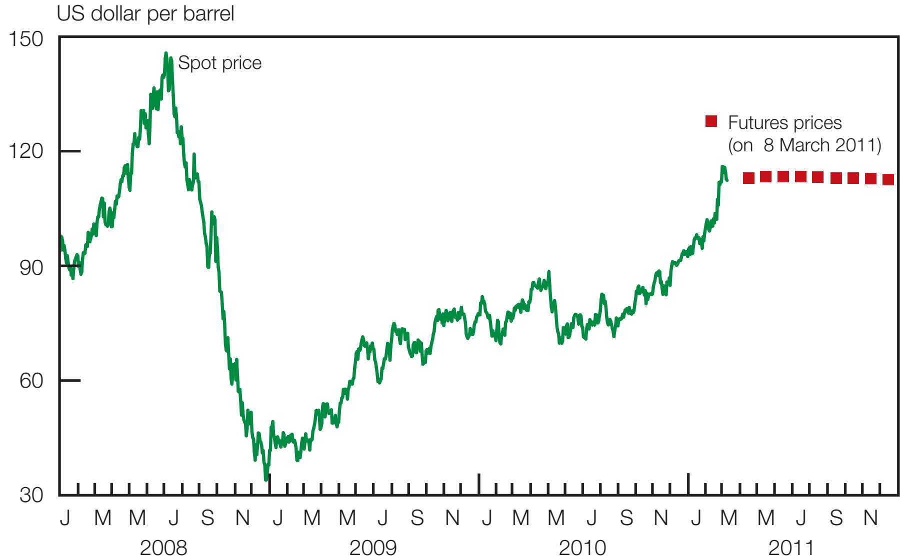
The global economic recovery continued in the final quarter of 2010 and in the early months of 2011, its momentum somewhat stronger than many observers had expected. Major developing countries maintained high rates of economic growth and, mindful of the dangers of overheating and inflation, tightened their monetary policies. In the major advanced economies the recovery remained fragile and the stance of monetary policies remained accommodative in order to support growth, although the earlier fiscal stimuli were reduced or withdrawn in the interest of fiscal sustainability.

International commodity prices trended higher, supported by strong growth in the developing countries and, in some instances, propelled by logistical and geopolitical concerns arising from the upheaval in the political order in a number of countries in the Middle East and North Africa (MENA). The spot price of crude oil rose as high as US$118 a barrel in late February and early March 2011, while international food prices also continued their rising trajectory, recently reaching their highest level since January 1990. Under these circumstances consumer price inflation trended higher, which resulted in a general trend towards monetary policy tightening – the major advanced economies being the exception so far, as noted above.

In sub-Saharan Africa growth prospects were bolstered by the buoyant prices of key export commodities, the recovery in global demand, the improvement in macroeconomic stability in general and, more structurally, the increase in the proportion of national resources devoted to capital formation.

In South Africa annualised growth in real gross domestic product accelerated to 4,4 per cent in the final quarter of 2010, lifting the economy's growth rate for the year as a whole to 2,8 per cent. The improvement in the growth momentum in the final quarter of 2010 partly reflected the normalisation of production in manufacturing and government services, which rebounded following strike action in the third quarter. Mining output rose at a strong pace in the fourth quarter against the background of high commodity prices and strong export demand, with platinum and coal making the largest contributions to the higher production levels. Real value added by agriculture also expanded at a double-digit rate in the final quarter of the year, buoyed by horticultural and livestock production. Over the period higher growth was posted by all the

Brent crude oil prices



Source: Bloomberg

subsectors in the tertiary sector. However, the economy continued to be characterised by a significant degree of underutilisation of production capacity.

Among the domestic expenditure components, household consumption expenditure provided the major and most consistent part of the growth momentum throughout 2010. This was driven by rising real income levels, lower interest rates, a modest reduction in the household debt ratio and fairly high levels of consumer confidence. In the final quarter of 2010 growth in real final consumption expenditure by households moderated somewhat alongside a slower pace of increase in households' real disposable income. The moderation made itself felt especially in expenditure on durable goods, where pre-emptive buying of vehicles ahead of the introduction of a carbon emissions tax from 1 September 2010 had established a relatively high base in the third quarter, and on non-durable goods.

Real final consumption expenditure by government rebounded in the fourth quarter of 2010 as the real expenditure on public servants' salaries and wages normalised, having been pulled down in the third quarter by a public-sector strike.

Real fixed capital spending inched higher in the final quarter of 2010, the third successive quarter of very slow but positive growth in this aggregate, following five quarters of contraction. In the final quarter of 2010 public corporations raised their capital outlays, particularly in the electricity and transport subsectors. Private business enterprises also increased their real fixed capital formation marginally, notably in the mining and communication sectors. By contrast, there was a slight contraction in real capital expenditure by general government over the period.

Having declined for ten successive quarters, the aggregate level of real inventories increased marginally in the fourth quarter of 2010. Restocking started from a very low base and was prompted by rising sales volumes and facilitated by low interest rates.

Employment increased moderately in the final quarter of 2010, although this was probably largely for seasonal reasons. Simultaneously, the number of discouraged work-seekers also rose somewhat, culminating in a reduction in the unemployment rate. The average wage settlement rate in 2010 amounted to 8,2 per cent – lower than in 2009 – while increases in unit labour cost also decelerated somewhat. Labour productivity continued rising, although it lost some of its earlier momentum in the third quarter when industrial action had a negative impact on output.

Consumer price inflation remained in the lower half of the target range during the second half of 2010 and in early 2011, held in check by the strength of the exchange rate, moderate domestic food price increases, surplus capacity in the economy and, in some instances, overhead costs being spread across rising sales volumes.

The buoyant prices of key export commodities were reflected in a further improvement in the terms of trade in the fourth quarter of 2010. In combination with sluggish imports and a recovery in export volumes of especially mining products, and vehicles and transport equipment, this led to a significant narrowing of the deficit on the current account of the balance of payments. At the same time, the surplus on the financial account of the balance of payments fell steeply as inward portfolio investment, having recorded sizeable inflows in 2009 and the first three quarters of 2010, switched to an outflow.

Both the effective exchange value of the rand and the international liquidity position of the South African Reserve Bank (the Bank) trended higher in 2010. While the international liquidity position continued rising in the first two months of 2011, the exchange rate of the rand depreciated somewhat over the period, not least on account of net sales by non-residents of South African equity and debt securities.

As the economic recovery progressed growth in the M3 money supply accelerated in the course of 2010, although remaining far below the levels recorded from 2005 to 2008. In the fourth quarter the pace of M3 growth was, however, exceeded by that of the nominal gross domestic product, resulting in a renewed increase in the velocity of circulation of the money supply. Bank loans and advances to the private sector also picked up in 2010. Whereas previously mortgage advances to the household sector had been the only area of consistently rising credit extension, advances to the corporate sector started recovering in the third quarter of 2010 but lost momentum in the final months of the year.

Money-market interest rates declined in response to the reduction in the repurchase rate on 19 November 2010 and subsequently remained at or around 30-year lows; adjusted for expected inflation, real money-market rates were quite low during this period. Fears of rising global inflationary pressures and geopolitical pressures resulted in a marked increase in rates on forward rate agreements from January 2011, while yields on bonds also rose significantly from their lows in November 2010.

South African share prices approached their record levels of early 2008 towards the end of 2010 and in early 2011, and turnover in major financial markets was brisk. However, activity in the real-estate market remained subdued and house prices lustreless.

The February 2011 National Budget provided support for the New Growth Path through actions to bolster employment creation, consistent with government's countercyclical approach within the context of fiscal sustainability. The Budget estimates displayed a slightly slower pace of narrowing of the fiscal deficit and a somewhat higher government debt trajectory than in earlier official projections.

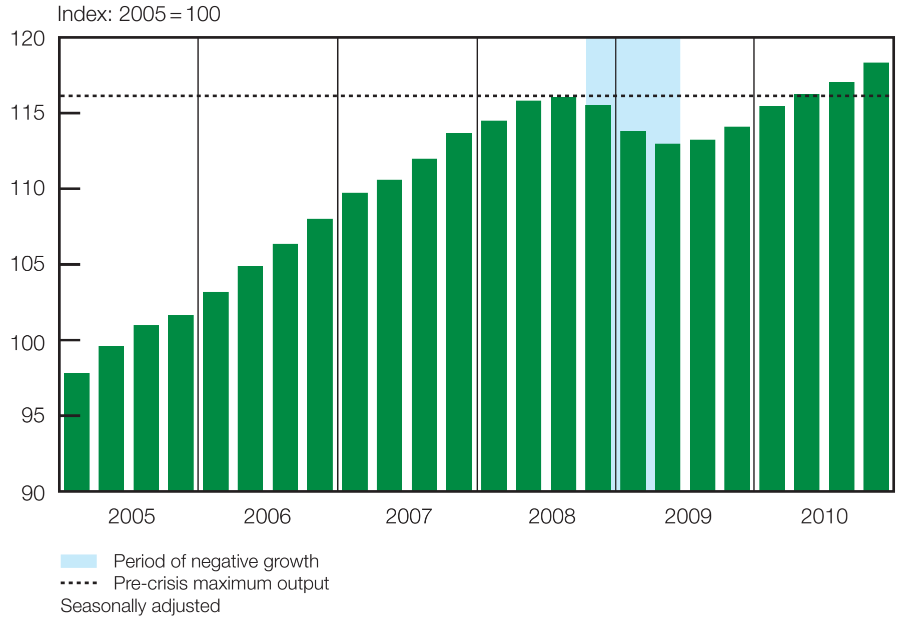
Domestic economic developments

Domestic output[1]

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

The South African economy expanded robustly in the fourth quarter of 2010 as growth in *real gross domestic production* accelerated from an annualised rate of 2,7 per cent in the third quarter of 2010 to 4,4 per cent in the fourth quarter. The stronger quarter-to-quarter growth in the fourth quarter mainly reflected a rebound in the real value added by the secondary sector alongside stronger growth in the real value added by the tertiary sector. These positive contributions to economic growth were partly offset by a slower pace of increase in the real value added by the primary sector. For 2010 as a whole, real output increased at a rate of 2,8 per cent, following a decline of 1,7 per cent in 2009.

Real gross domestic product

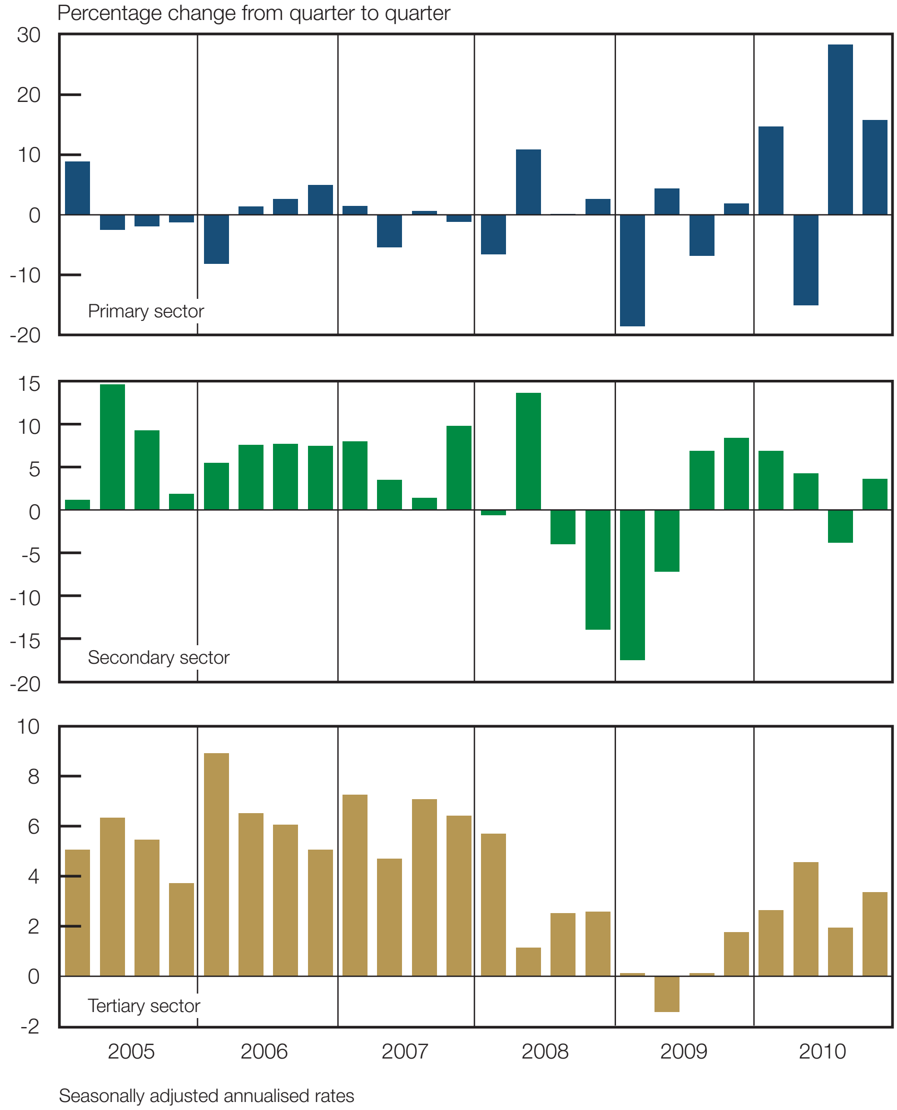


The real value added by the *primary sector* increased at a slower pace in the fourth quarter than in the third quarter of 2010. Growth in the fourth quarter moderated to a still-high annualised rate of 15,8 per cent following a rate of increase of no less than 28,3 per cent in the previous quarter. This moderation resulted from a slower rate of increase recorded in both the agricultural and the mining sectors. However, for the year 2010 as a whole, the real value added by the primary sector increased by 4,3 per cent following a contraction of 3,9 per cent in 2009.

Growth in the real value added by the *agricultural sector* slowed from an annualised rate of 16,3 per cent in the third quarter of 2010 to 12,5 per cent in the fourth quarter. This slower growth can be attributed to lower field crop production. By contrast, horticultural and livestock production increased further in the fourth quarter. However, measured over a year, real growth in the agricultural sector accelerated from a decline of 3 per cent in 2009 to an increase of 0,9 per cent in 2010, mainly on account of an improvement in horticultural and livestock production over this period.

The real output of the *mining sector* increased at a slower pace in the fourth quarter of 2010. Growth in the real value added by the mining sector moderated to an annualised rate of 17,1 per cent in the fourth quarter of 2010 from 33,7 per cent in the third quarter. Although all mineral groups contributed to the increase in production volumes, platinum and coal mining made the largest contributions to the higher production levels. Platinum production benefited from the decrease in safety-related shutdowns, whereas the production of coal was boosted by the robust global demand due to extremely cold European winter conditions. Following four consecutive years of declining mining production, the real value added by the mining sector rose by 5,8 per cent in 2010.

Real gross domestic product by main sector



Growth in the real value added by the *secondary sector* accelerated to an annualised rate of 3,6 per cent in the fourth quarter of 2010, following a decline of 3,8 per cent in the preceding quarter. Both the manufacturing, and the electricity, gas and water sectors contributed to the improved growth in the secondary sector; by contrast growth in the real value added by the construction sector slowed further over the period. The real value added by the secondary sector increased by 4,1 per cent in 2010 as a whole, compared with a contraction of 7,1 per cent in 2009.

The real value added by the *manufacturing sector* rebounded in the fourth quarter of 2010 and contributed 0,6 percentage points to the 4,4 per cent overall rate of growth over the period. Manufacturing output increased at an annualised rate of 4,1 per cent in the fourth quarter of 2010 following a decline of 4,9 per cent in the third quarter. Major contributions to the increased level of manufacturing production came from the subsectors manufacturing motor vehicles, parts and accessories and other transport equipment; food and beverages; and basic iron, steel and non-ferrous metal products. The recovery in the manufacturing sector in the fourth quarter was underpinned by improved domestic and export demand, and the normalisation of production following industrial action in the transport sector in the third quarter of 2010.

Consistent with higher production levels, capacity utilisation in manufacturing increased from 79,2 per cent in the third quarter to 80,7 per cent in the final quarter of 2010. In the third quarter of 2008, immediately prior to the contraction in the domestic economy, the utilisation of production capacity amounted to 84,5 per cent.

Measured on a calendar-year basis, the real value added by the manufacturing sector which contracted by 10,4 per cent in 2009 turned around to an increase of 5 per cent in 2010. Notwithstanding the increase in activity, the level of real production was still well below its peak registered in 2008. The recovery in the manufacturing sector in 2010 was primarily brought about by the strong rebound in the subsector for the manufacturing of motor vehicles, parts and accessories and other transport equipment, following a revival in both external and domestic demand. The subdued performance of other manufacturing subsectors in 2010 reflected, in part, a slowdown in infrastructure projects combined with a lack of new private-sector investment projects, the relative strength of the rand and unfavourable economic fundamentals in some of South Africa's key export markets.

Real gross domestic product

Percentage change at seasonally adjusted annualised rates

Sector	2009	2010				
	Year	1st qr	2nd qr	3rd qr	4th qr	Year
Primary sector	-3,9	14,7	-15,0	28,3	15,8	4,3
Agriculture	-3,0	4,9	13,6	16,3	12,5	0,9
Mining	-4,2	18,7	-24,5	33,7	17,1	5,8
Secondary sector	-7,1	6,9	4,3	-3,8	3,6	4,1
Manufacturing	-10,4	8,3	5,7	-4,9	4,1	5,0
Tertiary sector	0,7	2,6	4,6	1,9	3,4	2,2
Non-agricultural sector	*-1,5*	*4,6*	*2,4*	*2,3*	*4,3*	*2,9*
Total	**-1,7**	**4,8**	**2,8**	**2,7**	**4,4**	**2,8**

The real value added by the sector supplying *electricity, gas and water* advanced at an annualised rate of 5,7 per cent in the fourth quarter of 2010, after contracting at a rate of 2,2 per cent in the preceding quarter. In addition to stronger demand from the manufacturing and mining sectors, the volume of electricity sold to neighbouring countries also increased over this period. Following a contraction of 1,6 per cent in 2009, the real value added by the electricity, gas and water sector increased at a rate of 2 per cent in 2010 as a whole.

Growth in the real value added by the *construction sector* slowed from 0,8 per cent in the third quarter of 2010 to a mere 0,2 per cent in the fourth quarter. Construction activity as well as activity in the residential and non-residential building sectors remained subdued in the final quarter due to weak demand for housing, relatively high vacancy rates in the commercial building subsector and a lack of new construction projects. For 2010 as a whole, the real value added by the construction sector increased by 1,5 per cent, that is at a much slower pace than the rate of increase of 7,4 per cent recorded in 2009 when preparations for the 2010 FIFA World Cup™ tournament were still in full swing. A number of factors inhibited growth in the construction sector in 2010, including a lack of new investment projects and relatively subdued business confidence levels.

The real value added by the *tertiary sector* increased at an annualised rate of 3,4 per cent in the fourth quarter of 2010, compared with an increase of 1,9 per cent in the third quarter. Higher growth was posted by all the subsectors in the tertiary sector.

Following an annualised increase of 3,3 per cent in the third quarter of 2010, the real value added by the *trade sector* increased at a broadly similar rate of 3,5 per cent in the fourth quarter. This was mainly due to improved growth in the wholesale and retail trade and motor trade subsectors.

Growth in the motor trade subsector recovered in the fourth quarter of 2010, boosted by positive sentiment among consumers, replacement demand among buyers of commercial vehicles, the low interest rate environment and the normalisation of production of motor vehicles following the industrial action in the previous quarter.

The real value added by the trade sector increased by 2,2 per cent in 2010 compared with a decline of 2,5 per cent in 2009. Lower interest rates, improved consumer confidence levels and higher real income mainly contributed to the recovery in the trade sector in the year 2010 as a whole.

Real output of the *transport, storage and communication sector* edged higher from an annualised rate of 3 per cent in the third quarter of 2010 to 4,2 per cent in the fourth quarter. Freight transport volumes increased concurrently with the increase in merchandise export volumes. This was partly offset by a moderate decline in the volume of imports. In the communication subsector growth maintained its momentum in the fourth quarter of 2010. Overall, the real value added by the transport, storage and communication sector rose by 2,9 per cent in 2010, compared with a rate of increase of 0,6 per cent in 2009.

The real value added by the *finance, insurance, real-estate and business services sector* recorded subdued growth in the second half of 2010 when real output increased at annualised rates of 1,4 per cent and 1,7 per cent in the third and fourth quarter of 2010 respectively. The slightly stronger performance of the sector in the final quarter of 2010 primarily reflected an increase in the real output of the banking sector. By contrast, trading activity in the domestic securities market lost momentum over this period. For the year 2010 as a whole, growth in real value added by the finance, real-estate and business services sector accelerated to 1,9 per cent, compared with an increase of 0,9 per cent in the preceding year.

Growth in the real value added by *general government* accelerated to an annualised rate of 5,3 per cent in the fourth quarter of 2010, following an increase of 0,4 per cent in the third quarter. The strong performance of general government mainly reflected a recovery from the strike-related low base in the third quarter. Overall, the real value added by the general government sector rose by 3 per cent in 2010, lower than the growth rate of 4,1 per cent recorded in 2009, indicating the slower pace of increase in employment in general government during 2010.

Real gross domestic expenditure

Growth in aggregate *real gross domestic expenditure* slowed from an annualised rate of 6,2 per cent in the third quarter of 2010 to 1,2 per cent in the fourth quarter. This moderation in total expenditure partly reflected slower growth in real final consumption expenditure by the household sector. For the calendar year 2010, real gross domestic expenditure, however, increased at a rate of 4,2 per cent, rebounding following the contraction of 1,7 per cent recorded in 2009.

Real gross domestic expenditure

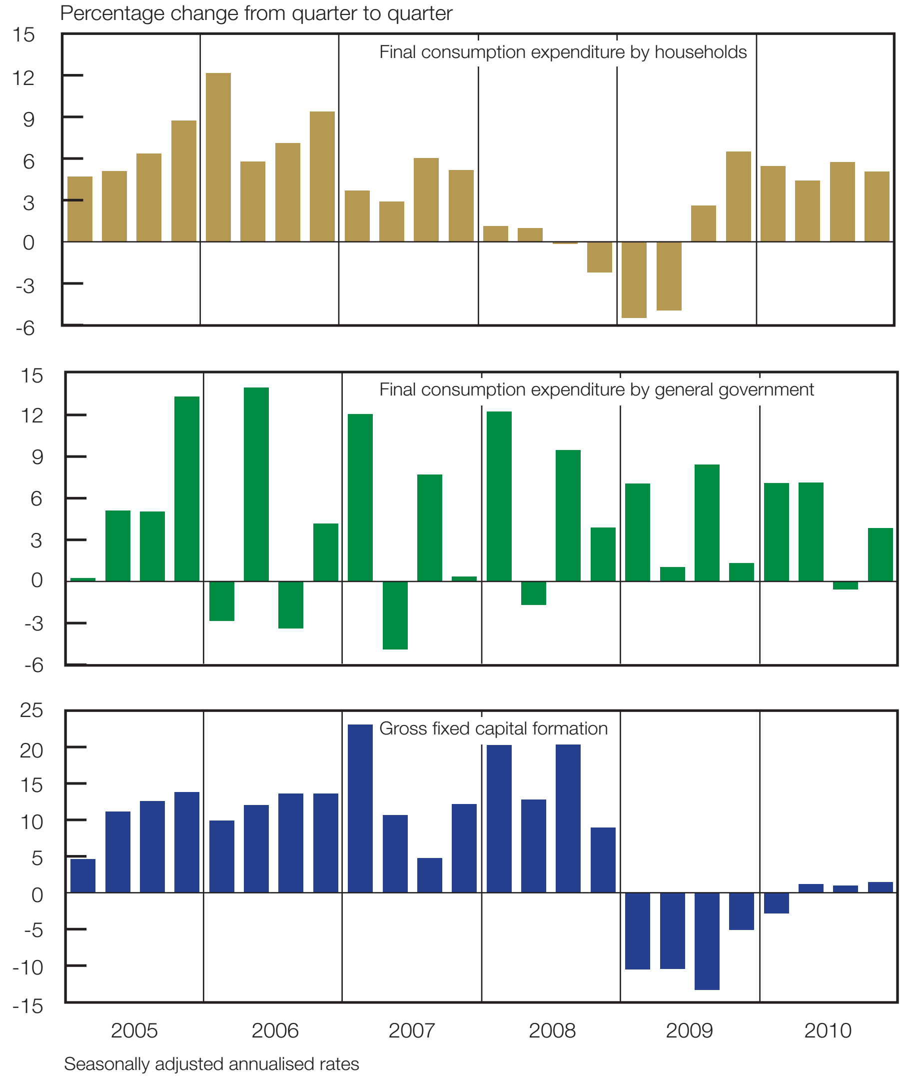
Percentage change at seasonally adjusted annualised rates

Component	2009	2010				
	Year	1st qr	2nd qr	3rd qr	4th qr	Year
Final consumption expenditure						
Households	-2,0	5,5	4,4	5,7	5,1	4,4
General government	4,8	7,1	7,1	-0,6	3,9	4,6
Gross fixed capital formation	-2,2	-2,8	1,2	1,0	1,5	-3,7
Domestic final demand	-0,8	4,1	4,3	3,6	4,2	2,8
Change in inventories (R billions)*	-34,5	-7,9	-7,6	-0,9	1,1	-3,8
Gross domestic expenditure	**-1,7**	**11,5**	**2,9**	**6,2**	**1,2**	**4,2**

* At constant 2005 prices

Growth in *real final consumption expenditure* by households slowed to an annualised rate of 5,1 per cent in the fourth quarter of 2010, following a brisk increase of 5,7 per cent in the third quarter.

Final demand



The moderation in spending by households resulted from a slower pace of increase in consumption expenditure on durable goods alongside subdued spending on non-durable goods. Having declined by 2,0 per cent in 2009, real consumption expenditure by households increased by 4,4 per cent in the 2010 calendar year.

Real consumer expenditure on *durable goods* increased at an annualised rate of 6,9 per cent in the fourth quarter of 2010, slower than the increase of 13,4 per cent recorded in the third quarter. Brisk increases in the preceding five quarters were followed by lower growth as a result of a contraction in spending on furniture and household appliances, alongside slower growth in expenditure on personal transport equipment. This was partly offset by increased spending on medical equipment; recreational and entertainment equipment; and computers and related equipment. The contraction in demand for furniture and household appliances could be ascribed to demand for these products running out of steam subsequent to a period of elevated spending in the four preceding quarters.

Having declined by 4,8 per cent in the third quarter of 2010, real expenditure on *semi-durable goods* increased at an annualised rate of 4,6 per cent in the fourth quarter. This rebound could be attributed to increases in spending on household textiles and furnishings; motor car tyres, parts and accessories; and other miscellaneous goods. This more than outweighed the decline in spending on clothing and footwear; and recreational and entertainment goods. The increased spending by households on motor car tyres, parts and accessories was partly a reflection of the expanding pool of vehicles owned by South Africans.

Real final consumption expenditure by households

Percentage change at seasonally adjusted annualised rates

Component	2009	2010				
	Year	1st qr	2nd qr	3rd qr	4th qr	Year
Durable goods	-9,6	39,3	45,4	13,4	6,9	24,2
Semi-durable goods	-1,8	30,2	9,8	-4,8	4,6	6,5
Non-durable goods	-2,7	12,1	-2,3	2,9	0,2	2,1
Services	0,2	-10,3	0,7	9,3	8,9	1,9
Total	**-2,0**	**5,5**	**4,4**	**5,7**	**5,1**	**4,4**

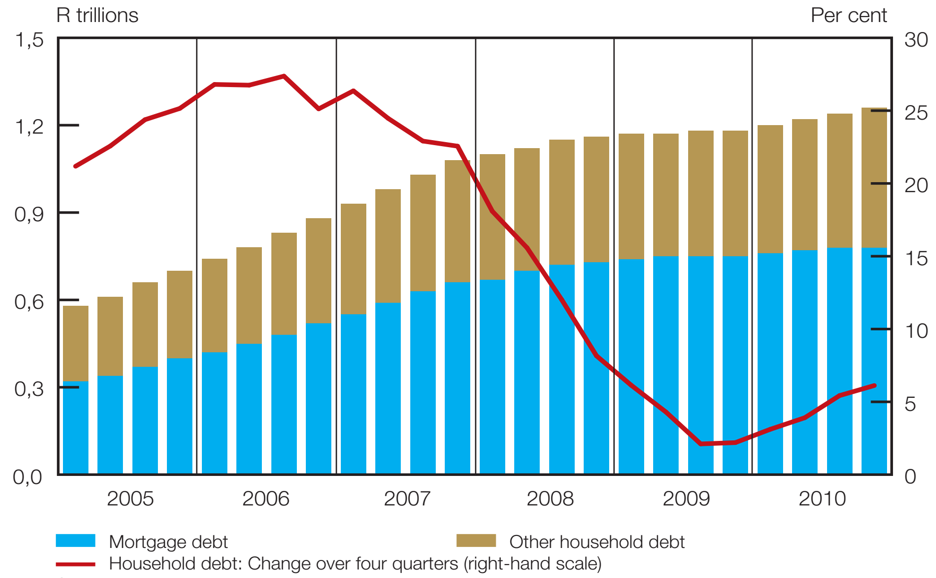
Growth in household spending on *non-durable goods* slowed from an annualised rate of 2,9 per cent in the third quarter of 2010 to a mere 0,2 per cent in the fourth quarter. This slower pace of increase was the net result of a contraction in consumer outlays on beverages and tobacco; petroleum products; and recreational and entertainment goods, along with increased spending on food, household fuel and power; and medical and pharmaceutical products.

Real outlays on *services* increased at an annualised rate of 8,9 per cent in the fourth quarter of 2010, following an increase of 9,3 per cent in the third quarter. The pace of growth in spending on household services, transport and communication, as well as on recreational services slowed. This was partly offset by increased spending on medical services and the net effect of expenditure by South African residents travelling abroad and travel receipts from foreign visitors to South Africa.

Growth in real *disposable income of households* moderated from an annualised rate of 5,5 per cent in the third quarter of 2010 to a still-high 5,3 per cent in the fourth quarter. This slower pace of increase reflected more moderate growth in compensation of employees during this period.

In addition, the financial position of households as measured by their net wealth continued to improve in the fourth quarter of 2010, although at a somewhat slower pace. A rise in the market value of equity holdings was partly offset by a moderation in house prices during this period. Consequently, the year-on-year increase in *net wealth* slowed to 10,4 per cent in the fourth quarter of 2010 from 12,9 per cent recorded in the third quarter. The ratio of net wealth to disposable income edged higher to 365 per cent compared with 363 per cent registered in the preceding quarter.

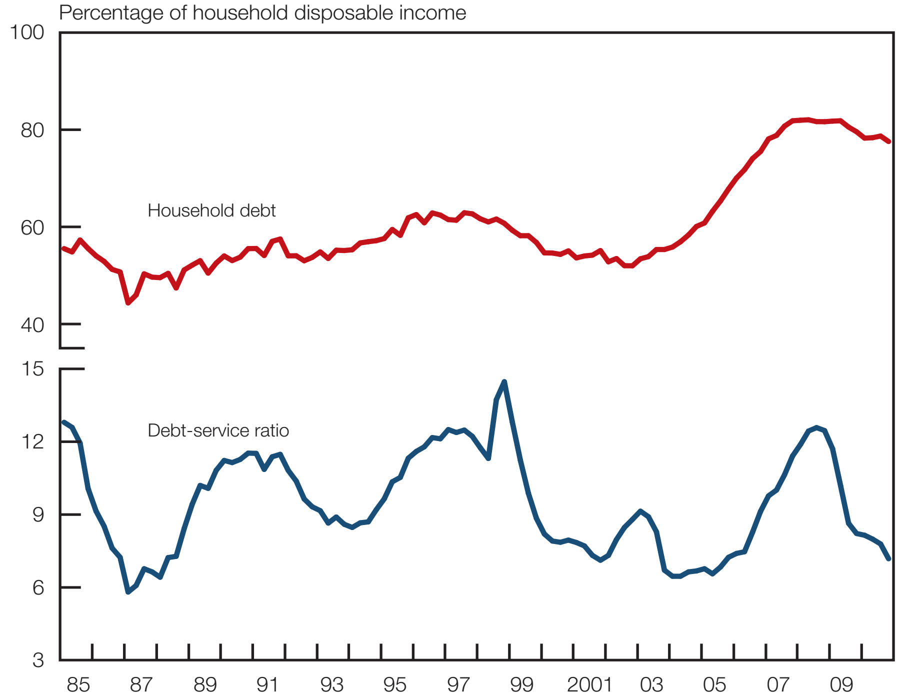
Household debt



Seasonally adjusted

Growth in household indebtedness inched higher in the fourth quarter of 2010. However, relative to the disposable income of households, household debt receded from 78,7 per cent in the third quarter of 2010 to 77,6 per cent in the fourth quarter. Sustained low levels of interest rates resulted in a further decrease in the ratio of debt-service cost to disposable income of the household sector from 7,8 per cent in the third quarter of 2010 to 7,2 per cent in the fourth quarter.

Household debt and debt-service ratios



Seasonally adjusted

Following a contraction at an annualised rate of 0,6 per cent in the third quarter of 2010, *real final consumption expenditure by general government* reverted to growth of 3,9 per cent in the fourth quarter. The stronger growth could mainly be explained by increased spending on compensation of employees, the biggest subcomponent of general government expenditure. Real compensation of employees normalised in the fourth quarter as salary and wage accruals in the third quarter of 2010 had been reduced on account of the public-sector strike.

The improvements in the conditions of service agreed to by government made provision for higher salaries and housing allowances payable to government employees from mid-2010, boosting government's salary and wage bill over the period. Consequently, the ratio of government consumption expenditure to gross domestic product increased from 21,5 per cent in the third quarter of 2010 to 21,8 per cent in the fourth quarter.

Real *gross fixed capital formation* rose at subdued annualised rates of 1 per cent in the third quarter of 2010 and 1,5 per cent in the fourth quarter. Lower capital outlays by private business enterprises and the prolonged contraction in investment by general government held back growth in fixed capital formation in the final quarter of 2010. Real spending by public corporations, however, increased further over the period. On an annual basis, overall real gross fixed capital formation contracted by 3,7 per cent in 2010 following a decline of 2,2 per cent in 2009.

Real gross fixed capital formation by *private business enterprises* moderated from an annualised rate of increase of 2,0 per cent in the third quarter of 2010 to 1,6 per cent in the fourth quarter. This sluggishness in capital spending was evident in most subsectors. Owing to a lack of new investment projects, construction activity remained fairly subdued over this period. However, favourable demand for especially South African mineral resources helped to sustain capital spending in the mining sector. Development and exploration at several coal mines and the extension of opencast pits to extract pyroxenite ore contributed meaningfully to capital formation in the mining sector.

Real gross fixed capital formation

Percentage change at seasonally adjusted annualised rates

Component	2009	2010				
	Year	1st qr	2nd qr	3rd qr	4th qr	Year
Private business enterprises	-8,9	-2,9	2,2	2,0	1,6	-4,4
Public corporations	26,1	2,6	2,9	0,7	3,3	3,5
General government	-4,0	-10,3	-5,3	-3,0	-1,9	-10,9
Total	-2,2	-2,8	1,2	1,0	1,5	-3,7

Capital spending on commercial vehicles continued to trend higher in the fourth quarter of 2010. The strong growth in the commercial vehicle market could partly be attributed to the replacement cycle which comes into play after three to four years of weak vehicle sales. In addition, the communications subsector continued with capital spending to expand fibre networks and roll out high-speed networks.

Real gross fixed capital formation by *public corporations* accelerated, rising at an annualised rate of 3,3 per cent in the fourth quarter of 2010 from 0,7 per cent in the third quarter. The faster pace of capital spending by public corporations could be attributed to higher capital outlays by, in particular, the electricity and transport subsectors. Eskom's ongoing power station projects such as Medupi, Kusile and Ingula involved increased spending on construction works, vehicles, and machinery and equipment, as did the ongoing investment in the new pipeline project between Durban and Johannesburg. Capital outlays on the elimination of bottlenecks and the widening of roads also continued with added momentum coming from the construction of Intelligent Transport and Electronic Toll Collection Systems.

The pace of contraction in real gross fixed capital expenditure by *general government* slowed from an annualised rate of 3 per cent in the third quarter of 2010 to 1,9 per cent in the fourth quarter. As in the past, the contraction partly reflected bottlenecks and capacity constraints in awarding contracts, hampering infrastructure maintenance and the expansion of water supply and treatment plants. However, government capital spending on transport, housing and health edged higher during the quarter under review.

Having declined uninterruptedly for ten quarters, the aggregate level of *real inventory holdings* increased by R1,1 billion in the fourth quarter of 2010. This accumulation in inventory levels added 0,4 percentage points to the growth in real gross domestic expenditure in the fourth quarter of 2010. On an annual basis, the level of real inventories declined by R3,8 billion in 2010, significantly less than the R34,5 billion decline recorded in 2009.

The accumulation of inventories in the fourth quarter of 2010 resulted mainly from a build-up of inventories in the mining and construction sectors. Inventories in the construction sector edged higher in the fourth quarter of 2010 as some contractors increased stock to deal with the ongoing rehabilitation of roads.

As a percentage of annualised non-agricultural gross domestic product, industrial and commercial inventories declined from 12,0 per cent in the third quarter of 2010 to 11,3 per cent in the fourth quarter. This was its lowest quarterly level ever registered and substantially below the ratio of 16,5 per cent recorded in 2008 and 13,6 per cent recorded in 2009.

Factor income

Growth over four quarters in total *nominal factor income* edged higher from a rate of 10,8 per cent in the third quarter of 2010 to 11,6 per cent in the fourth quarter, mainly as a result of increased growth in the gross operating surpluses of business enterprises. On an annual basis, higher price and wage inflation was reflected in total factor income rising by 10,6 per cent in 2010, from a rate of 6,3 per cent in 2009.

The rate of increase in *compensation of employees* measured over four-quarter periods decelerated from 11,5 per cent in the third quarter of 2010 to 9,1 per cent in the fourth quarter. The slower growth in the compensation of employees was evident in most of the major sectors, especially the general government sector. The ratio of compensation of employees to total factor income declined from 51,5 per cent in the third quarter of 2010 to 50,7 per cent in the fourth quarter. Growth in compensation of employees was higher in 2010 compared with 2009.

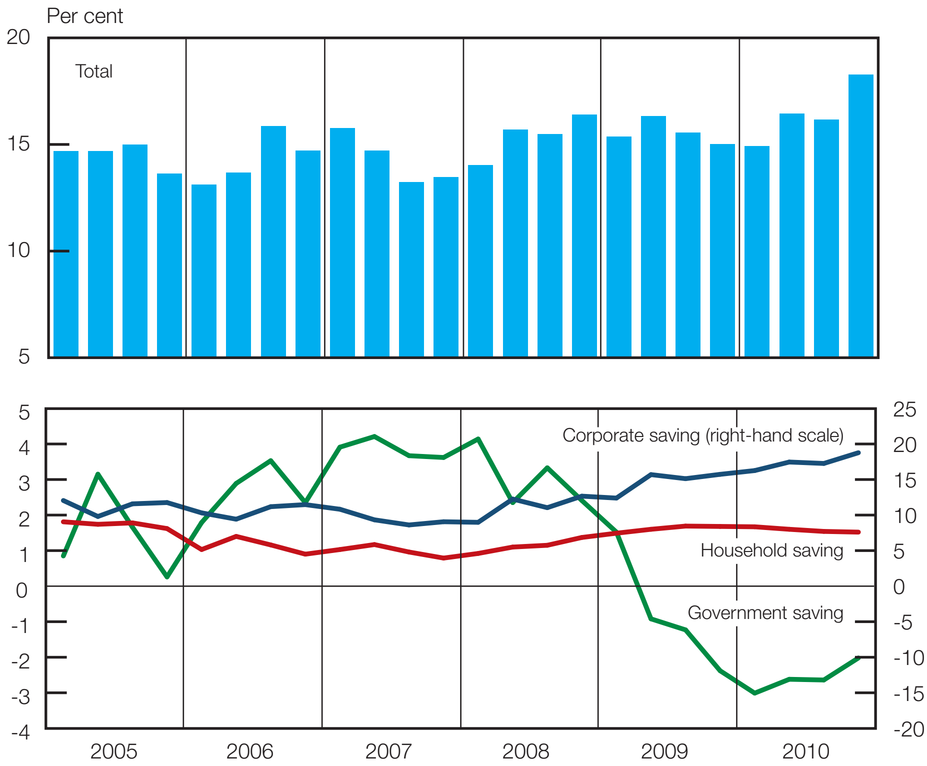
The year-on-year growth in the total *gross operating surplus* accelerated from 10 per cent in the third quarter of 2010 to 14,5 per cent in the fourth quarter. Consequently, the share of the gross operating surplus in total factor income increased from 48,5 per cent in the third quarter of 2010 to 49,3 per cent in the fourth quarter. The improvement in operating surpluses was evident in most sectors, especially in the mining sector. The increased growth in the operating surplus in the fourth quarter was mainly on account of high commodity prices and the effect of improved domestic and global consumption on corporate earnings.

On an annual basis, the rate of increase in total gross operating surplus accelerated from 4,2 per cent in 2009 to 10,6 per cent in 2010. The share of the operating surplus in total factor income, however, remained at 49,5 per cent in both 2009 and 2010.

Gross saving

Gross saving as a percentage of gross domestic product increased throughout 2010, rising from 16,2 per cent in the third quarter to 18,3 per cent in the fourth quarter. The improvement in the saving performance can be attributed to stronger growth in the gross saving of corporate business enterprises and a lower rate of dissaving by general government. As a result, South Africa's saving ratio advanced from 15,6 per cent in 2009 to 16,5 per cent in 2010 lowering the country's dependency on foreign capital from 20,7 per cent of total capital formation in 2009 to 14,4 per cent in 2010.

Gross saving as a percentage of gross domestic product



Seasonally adjusted

Gross saving by the corporate sector as a percentage of gross domestic product rose from 14,7 per cent in 2009 to 17,5 per cent in 2010. This reflects stronger growth in the operating surpluses of incorporated business enterprises, from a recent low of 2,4 per cent in 2009 to a much healthier 12,8 per cent in 2010. Dividend payment growth remained benign in the course of 2010, while corporate tax payments declined.

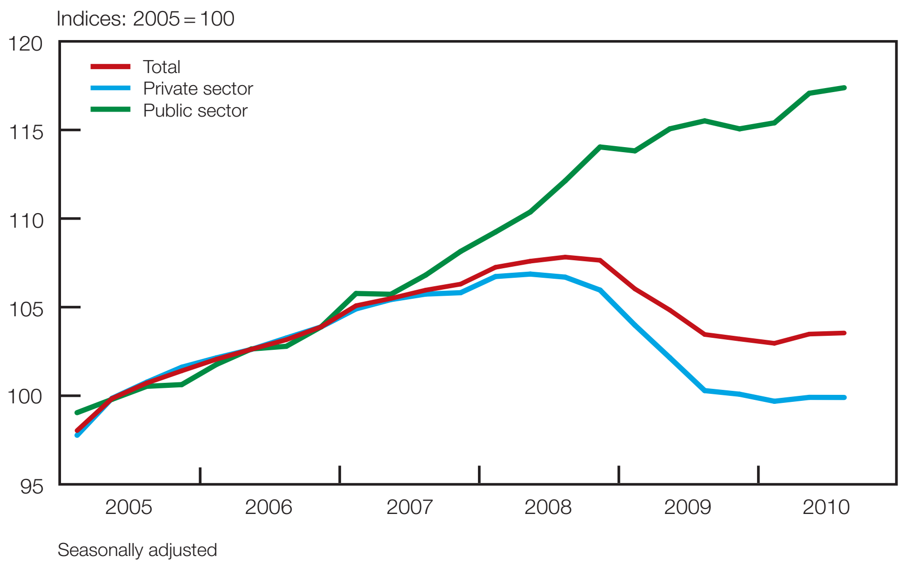
Gross dissaving by general government as a ratio of gross domestic product improved from 2,6 per cent in the third quarter of 2010 to 2 per cent in the fourth quarter. Measured over a year, the improved savings performance in the fourth quarter of 2010 can also be attributed to a slower increase in government expenditure, specifically on compensation of employees during this period. However, for the year as a whole, gross dissaving by general government deteriorated from 0,8 per cent of gross domestic product in 2009 to 2,6 per cent in 2010.

The gross saving rate of the household sector remained at 1,5 per cent in both the third and fourth quarters of 2010. High income growth helped to sustain the level of household saving.

Employment

The pace of employment creation remained sluggish, despite the recovery in domestic economic activity during the past year and a half. Formal non-agricultural employment increased moderately in the third quarter of 2010, following a more significant increase in the second quarter. Employment levels in the private sector remained roughly unchanged in the third quarter of 2010 compared with the preceding quarter, whereas employment levels in the public sector continued to increase, albeit at a much slower pace than in the second quarter.

Formal non-agricultural employment



Enterprise-surveyed data from the *Quarterly Employment Statistics (QES)* publication indicate that formal non-agricultural employment expanded marginally in the third quarter of 2010, recording a seasonally adjusted and annualised increase of 0,2 per cent and thereby adding some 4 800 jobs to the economy. During the third quarter of 2010, employment numbers in the private sector inched lower, decreasing by approximately 300 whereas at the same time, the public sector created approximately 5 100 employment opportunities, especially at the provincial level.

Job losses in the construction sector continued in the third quarter of 2010 as employment numbers contracted at an annualised rate of 4,6 per cent. This was consistent with the usual behaviour of the sector, which tends to lag the business cycle, and with the completion of a number of construction projects which had to be ready for the FIFA World Cup™ tournament.

Subdued conditions prevailed in the residential and non-residential building sector and also extended to the civil construction sector, although a number of large projects continued with government reconfirming its commitment to infrastructure investment.

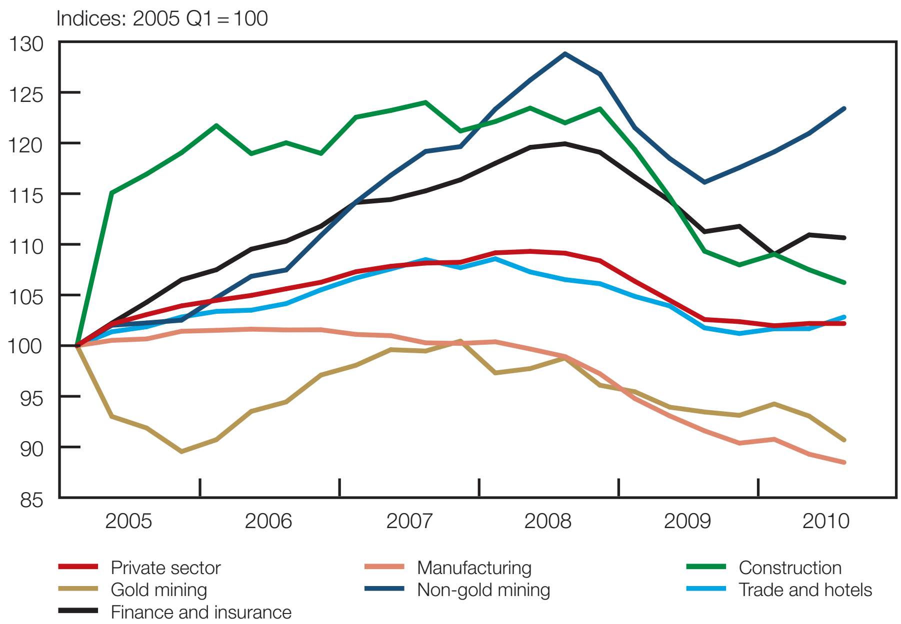
Following an uptick in manufacturing employment in the first quarter of 2010, employment levels resumed their downward trend in the second and third quarters of the year, recording rates of decline of 6,3 per cent and 3,6 per cent respectively. Labour paring was partly related to structural changes in the economy favouring higher levels of productivity in the face of fierce international competition. Stronger growth in manufacturing output would apparently be required for the sector to act as a conduit for accelerated employment creation.

Employment growth in the non-gold mining sector accelerated robustly in the past year, from a seasonally adjusted and annualised rate of 5,1 per cent in the fourth quarter of 2009 to 8,4 per cent in the third quarter of 2010. Mining activity benefited from increased global demand for commodities, stemming from enhanced economic growth in especially emerging-market economies, notably Brazil, China and India, leading to a revival in commodity prices following the slump in 2008 and 2009. The expansion of capacity in the electricity-supply sector contributed to a steady increase in job creation in the sector, with some 2 300 jobs being added in the second and third quarters of 2010.

In the trade, catering and accommodation services sector, employment levels increased at an annualised rate of 4,6 per cent with roughly 18 500 jobs being created in the third quarter of 2010, following virtually no employment gains in the preceding quarter. The sector benefited from a pickup in household spending in an environment of improved consumer confidence.

Between the first quarter of 2005 and the peak of the employment cycle (i.e., the third quarter of 2008) public-sector employment increased by 13,2 per cent, while employment levels in the private sector rose by only 9,1 per cent. Consequently, overall formal non-agricultural employment increased by 10,0 per cent over this period. Conversely, during the downward phase of the employment cycle, private-sector employment contracted by 6,6 per cent to the first quarter of 2010, whereas public-sector employment increased by 2,9 per cent. Consistent with the requirement for accelerated service delivery in the country, the recent expansion of the public-sector staff complement occurred primarily at provincial and local government level.

Private-sector employment



Seasonally adjusted

In the accompanying table, job losses between the third quarter of 2008 (the peak in the employment cycle) and the first quarter of 2010 (the lower turning point in the employment cycle) are contrasted with those between the first quarter of 2010 and the third quarter. The table also contrasts the contributions of the various sectors to total employment at the peak with the most recently available outcome.

Change in employment levels and employment shares in the formal non-agricultural sector

	Job losses (-) gains (+) (number)		Share of employment (per cent)	
	3rd qr of 2008 to 1st qr of 2010	1st qr of 2010 to 3rd qr of 2010	3rd qr of 2008	3rd qr of 2010
Finance, insurance, real-estate and business services	-174 600	26 000	22,6	21,7
Manufacturing	-107 000	-29 900	15,3	14,2
Trade, catering and accommodation services	-78 300	18 700	20,3	20,4
Construction	-49 700	-10 700	5,5	5,0
Mining	-34 800	5 900	6,2	6,1
Gold mining	-7 700	-6 000	2,0	1,9
Non-gold mining	-27 000	12 000	4,2	4,2
Electricity	-3 500	2 300	0,7	0,7
Private transport, storage and communication services	-2 000	-1 700	3,0	3,1
Community, social and personal services	13 400	2 768	4,7	5,1
Private sector	-436 600	13 400	78,4	76,4
Provinces	51 600	21 400	11,3	12,6
Local governments	14 800	4 500	2,7	3,0
National departments	-5 500	8 900	4,9	5,1
Public sector: Transport, storage and communication	-4 900	-1 600	1,3	1,2
Other public-sector enterprises	-2 400	-700	1,6	1,6
Public sector	53 600	32 500	21,6	23,6
Grand total	-383 000	45 800	100,0	100,0

More than half of the private-sector job losses between the third quarter of 2008 and the first quarter of 2010 occurred in the finance, insurance, real-estate and business services sector and the manufacturing sector. The share of the private sector in total employment shrank in the past two years, whereas the public sector claimed the residual increase as its staff complement rose, especially at the provincial level. The public sector raised its share in total employment from 21,6 per cent to 23,6 per cent over the period.

For job creation to be sustained in the South African economy, the private sector is expected to play a key role. In the past, the finance, insurance, real-estate and business services sector, construction sector, non-gold mining sector and trade, catering and accommodation services sector accounted for the bulk of employment gains during extended upward phases of the employment cycle. For instance, between the first quarter of 2005 and the third quarter of 2008, jobs in the non-gold mining sector increased by 29 per cent, followed by the construction sector (21,9 per cent) and the finance, insurance, real-estate and business services sector (19,9 per cent).

According to the household-based *Quarterly Labour Force Survey (QLFS)* published by Statistics South Africa (Stats SA), the number of employed persons rose to 13,1 million in the fourth quarter of 2010. However, the economically active population was trimmed somewhat to 17,3 million persons, partly attributable to a further increase of 117 000 in the number of discouraged work-seekers. As a result, the official unemployment rate declined from 25,3 per cent in the third quarter of 2010 to 24,0 per cent in the fourth quarter.

Economically active and employed persons

Number (thousands)

	Dec 2009	Mar 2010	Jun 2010	Sep 2010	Dec 2010
Total employed persons......................................	13 250	13 076	13 061	12 975	13 132
Economically active population...........................	17 476	17 471	17 462	17 371	17 269
Unemployment rate (per cent)	24,2	25,2	25,2	25,3	24,0

Source: Statistics South Africa, *Quarterly Labour Force Survey*

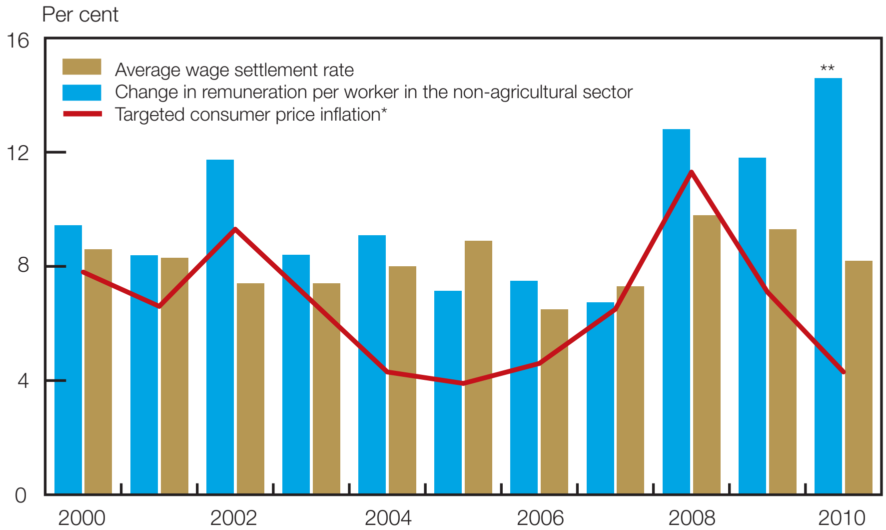
Industrial action surged during 2010 due to a prolonged strike by the public sector, a strike in the automotive manufacturing sector as well as sporadic industrial action in the mining sector, contributing to a cumulative loss of 14,6 million working days in 2010, compared with 2,9 million working days lost in 2009. According to Andrew Levy Employment Publications, about 99,3 per cent of working days lost and 69,7 per cent of the number of strikes in 2010 could be ascribed to wage disputes.

Following the presentation of the *New Growth Path* in the latter part of 2010, the President announced in his *State of the Nation Address* the creation of a job fund to the value of R9 billion to assist industries in financing job creation, in order to meet the objectives of halving unemployment and reducing poverty. In addition, the Industrial Development Corporation has set aside an amount of R20 billion to assist business enterprises with a high potential for employment creation in expanding their operations.

Labour cost and productivity

Despite the moderation in consumer price inflation in recent months, the year-on-year rate of increase in the nominal remuneration per worker in the formal non-agricultural sector accelerated consistently from the second quarter of 2009 to the first quarter of 2010. While it decelerated somewhat to 12,6 per cent in the third quarter, it continued to exceed consumer price inflation by a substantial margin.

Wages and targeted inflation



* CPIX up to December 2008; CPI for all urban areas from January 2009 onwards
** First three quarters of 2010 over the same period of 2009

Sources: Andrew Levy Employment Publications and Statistics South Africa

Even though job losses were fairly widespread in the private sector, most subsectors registered double-digit year-on-year rates of increase in remuneration per worker on a consistent basis from the second quarter of 2009 to the third quarter of 2010. Increases in the third quarter of 2010 ranged from as high as 19,8 per cent in the construction sector to 13,7 per cent in the financial sector, 12,1 per cent in the mining sector, 11,2 per cent in the manufacturing sector and 10,5 per cent in the community, social and personal services sector.

According to the *Wage Settlement Survey* conducted by Andrew Levy Employment Publications, the average wage settlement rate amounted to 8,2 per cent in 2010, lower than the average of 9,3 per cent in 2009. Wage settlements in 2010 ranged from 7,3 per cent in the communication sector to 9,3 per cent in the transport and freight sector. The consultancy anticipates a moderation in wage settlement rates in 2011 in accordance with the muted inflation environment.

With formal-sector employment improving more significantly than production over the year to the third quarter of 2010, labour productivity growth moderated from 4,3 per cent in the second quarter of 2010 to 3,1 per cent in the third quarter. The rate of increase in labour productivity in the manufacturing sector also moderated from 12,8 per cent in the year to the second quarter of 2010 to 8,3 per cent in the year to the third quarter, as manufacturing output increased and employment contracted at a slower pace.

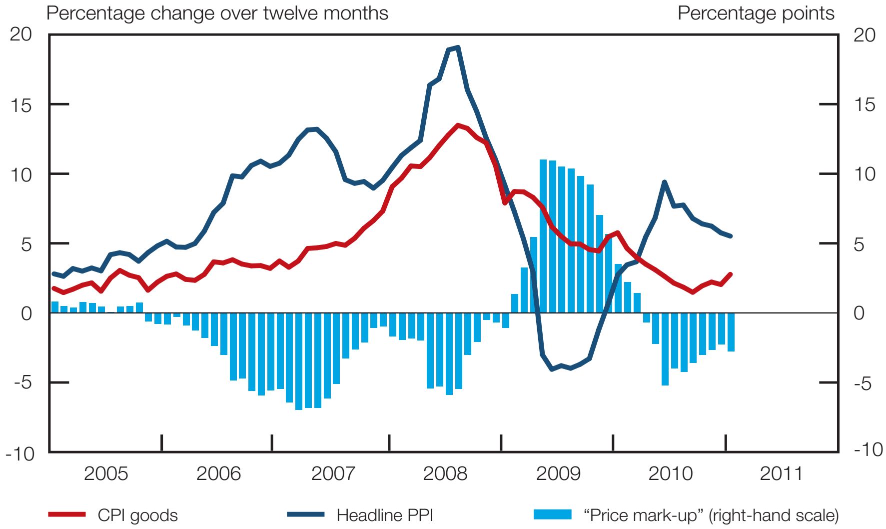
Owing to the faster pace of moderation in nominal remuneration relative to slowing real output growth in the economy, the year-on-year rate of increase in total non-agricultural nominal unit labour cost decelerated from 10,9 per cent in the second quarter of 2010 to 9,1 per cent in the third quarter. The increase in nominal unit labour cost in the manufacturing sector amounted to 2,6 per cent in the year to the third quarter of 2010 – the fifth consecutive quarter of deceleration, assisting in the containment of inflationary pressures in the economy.

Prices

While the official inflation target applies to consumer prices, it is noteworthy that most recently both consumer price and producer price inflation have fallen within the inflation target range of between 3 and 6 per cent.

Domestic consumer price inflation continued to moderate during 2010 within an environment of relatively subdued local demand and an appreciation in the external value of the rand throughout the year. Consumer price inflation accordingly slowed from an annual average of 7,1 per cent in 2009 to 4,3 per cent in 2010. Conversely, headline producer price inflation (which relates to domestic output prices) accelerated from zero per cent in 2009 to an annual average rate of 6,0 per cent in 2010.

Prices



* CPIX up to December 2008; CPI for all urban areas from January 2009 onwards

During the first half of 2010, year-on-year producer price inflation accelerated markedly to 9,4 per cent in June, before moderating in the latter half of the year to 5,8 per cent in December. The initial acceleration in headline producer price inflation can be attributed to base effects, steep increases in the producer prices of mining output, consistent with the rise in commodity prices, and sharp increases in electricity prices. Subsequently, the appreciation in the nominal exchange rate of the rand dampened price increases in the mining category and hence helped to moderate overall producer price inflation.

Encouragingly, twelve-month consumer price inflation has remained within the inflation target range of 3 to 6 per cent for an extended period. From levels around 6 per cent at the beginning of 2010 it reached a low of 3,2 per cent in September, before accelerating to 3,7 per cent in January 2011. The observed moderation in consumer price inflation, and the associated containment within the inflation target range, resulted mainly from significantly lower rates of increase in the prices of consumer goods, including food and petrol. The more recent acceleration in consumer price inflation also originated with these two aforementioned products, as their prices again started to rise.

Consumer and producer prices

Quarter-to-quarter percentage change at annual rates

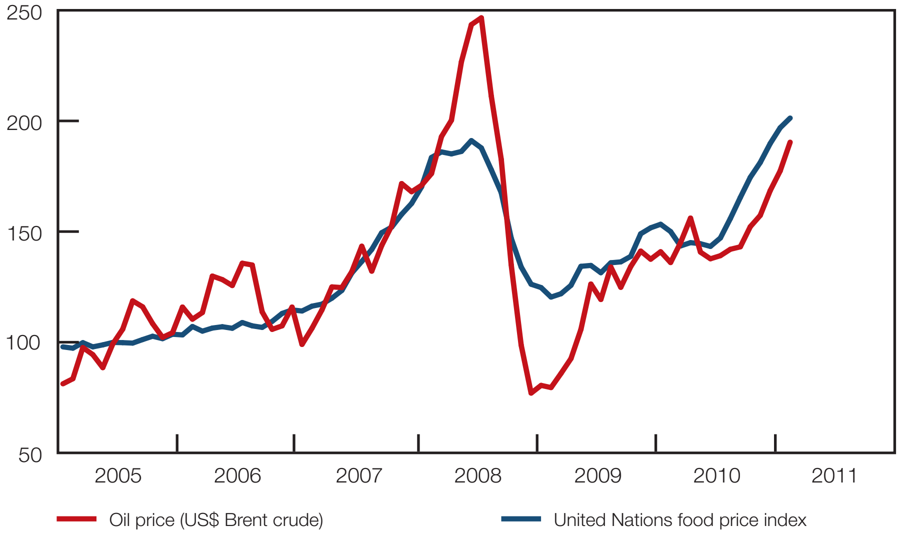
Period	Headline PPI	Headline CPI
2010: 1st qr	17,1	5,0
2nd qr	4,6	3,7
3rd qr	4,1	1,2
4th qr	0,6	4,5

The short-term pace of increase in the producer price index for domestic output moderated notably from a seasonally adjusted and annualised rate of 17,1 per cent in the first quarter of 2010 to 0,6 per cent in the fourth quarter. Similarly, the headline consumer price index also decelerated over the first three quarters of 2010, but accelerated again in the fourth quarter of 2010 following pronounced petrol price increases and a pickup in consumer food price inflation. Despite being buffered by the strengthening in the exchange value of the rand, the inland price of 95-octane petrol increased by a cumulative 135 cents per litre from September 2010 to March 2011.

Twelve-month producer food price changes continued to register rates of deflation, led by declines in the producer prices of food at especially the agricultural level. Price changes of

International oil and food prices

US dollar price indices: 2005 = 100



Sources: Food and Agriculture Organization of the United Nations and Bloomberg food at the manufactured level actually reverted to inflation from November 2010. Year-on-year consumer food price inflation decelerated markedly to zero per cent in June 2010, as lower food prices at the producer level impacted favourably on prices at the consumer level. Subsequently, consumer food price inflation picked up, amounting to 2,9 per cent in the year to January 2011.

Food prices

Percentage change over twelve months

	Domestic producer food prices			Headline consumer food prices		
	Agricultural food	Manufactured food	Total	Processed food	Unprocessed food	Total
2008	3,6	18,3	12,7	19,2	12,0	15,8
2009: Jan	13,2	12,0	12,5	19,6	13,0	16,1
Feb	4,4	10,9	8,3	18,4	13,6	15,8
Mar	-8,1	9,4	2,2	15,7	14,0	14,9
Apr	-2,0	8,4	4,5	13,7	13,7	13,7
May	-1,5	6,2	3,4	10,9	13,2	12,1
Jun	-6,5	3,7	0,0	8,7	10,9	9,9
Jul	-6,7	0,8	-2,0	7,0	8,2	7,6
Aug	-7,6	0,1	-2,7	5,9	6,5	6,2
Sep	-5,8	-1,8	-3,3	4,3	5,5	4,9
Oct	-2,1	-1,4	-1,6	3,6	5,9	4,8
Nov	-3,6	-1,1	-2,0	3,4	4,6	4,0
Dec	-2,3	-1,5	-1,8	2,8	2,7	2,8
2009	-2,4	3,8	1,5	9,5	9,3	9,4
2010: Jan	-18,7	-1,8	-8,8	2,3	0,9	1,6
Feb	-13,5	-1,2	-6,0	2,2	-0,2	1,0
Mar	-8,2	-1,5	-4,0	2,6	-1,4	0,5
Apr	-3,2	-1,7	-2,3	2,2	-1,5	0,3
May	-4,9	-1,3	-2,6	1,7	-1,4	0,1
Jun	-2,4	-0,7	-1,3	1,3	-1,1	0,0
Jul	-4,4	-0,9	-2,2	1,2	0,9	1,1
Aug	-0,7	-1,3	-1,1	1,5	1,4	1,5
Sep	-4,5	-0,1	-1,6	1,5	0,9	1,2
Oct	-3,1	-0,1	-1,2	1,7	-0,5	0,5
Nov	-3,2	0,6	-0,8	2,5	-0,3	1,1
Dec	-3,3	1,1	-0,5	2,5	0,3	1,4
2010	-5,9	-0,8	-2,7	1,9	-0,2	0,8
2011: Jan	-4,9	1,5	-0,9	3,7	2,1	2,9

Internationally, food price inflation has accelerated notably in recent months, driven by tight food supplies, changing weather patterns, rising demand in emerging-market economies and a higher oil price which raises production costs and the prices of biofuel alternatives. To date, South Africa has been largely shielded from these price increases due to the stronger exchange value of the rand and a bumper maize crop. Although developments in the producer prices of food suggest that domestic food price inflation will remain contained in the short term, accelerating global food price inflation as well as import parity pricing practices could in time ignite a new round of domestic consumer food price inflation.

Based on the classification of individual consumption by purpose (COICOP), the accompanying table shows the annual average rates of change in all the categories. Of note is the marked deceleration in price inflation that has occurred in the *recreation and culture* category, compared with the acceleration in the *transport* category, following substantial petrol price increases in the final quarter of the year.

Headline CPI inflation in COICOP categories

Percentage change over twelve months

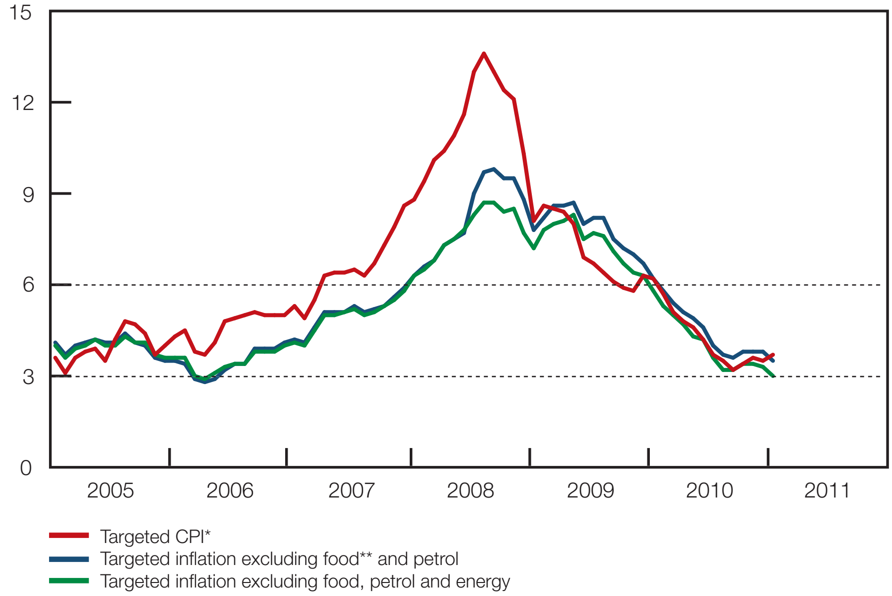
	Weights	2009	2010	Jan 2011
Education	2,19	9,9	9,4	9,2
Alcoholic beverages and tobacco	5,58	11,1	9,2	7,2
Health	1,47	10,8	7,5	7,4
Housing and utilities	22,56	7,9	6,6	6,3
Restaurants and hotels	2,78	11,0	7,1	4,9
Miscellaneous goods and services	13,56	11,6	6,8	3,7
Food and non-alcoholic beverages	15,68	9,7	1,4	3,1
Transport	18,80	-0,4	2,7	2,5
Clothing and footwear	4,11	4,9	1,9	0,9
Household contents, maintenance and equipment	5,86	6,0	0,4	0,5
Recreation and culture	4,19	11,6	0,2	-2,3
Communication	3,22	0,7	-1,6	-2,4
Total headline CPI	100,00	7,1	4,3	3,7

Some underlying inflationary pressures have persisted in the economy as is evident from the accompanying table, indicating that four categories still exhibited price increases at rates in excess of the upper limit of the inflation target range in January 2011.

When the impact of the food, non-alcoholic beverages and petrol prices is excluded from the headline consumer price index, underlying annual average inflation amounted to 4,6 per cent in 2010, receding to within the inflation target range for the first time since 2007. Furthermore, excluding electricity prices from the calculation of headline CPI inflation, the rate of increase is somewhat lower at 4,1 per cent in 2010.

Measures of underlying inflation

Percentage change over twelve months



* CPIX up to December 2008; CPI for all urban areas from January 2009 onwards

** Food, including non-alcoholic beverages

Unlike headline consumer price inflation, administered price inflation recorded a rate well above the upper limit of the inflation target range in 2010. Annual average administered price inflation accelerated from 2,3 per cent in 2009 to 10,2 per cent in 2010 as petrol prices increased by

11 per cent in the latter year. Except for the communication category, all the remaining categories in the administered prices basket, representing a total weight of 81,2 per cent, registered rates of increase well above the upper limit of the inflation target range, with some even increasing at double-digit rates in 2010. When the effect of petrol and electricity prices is excluded from the calculation of administered prices, the increase still amounted to 6,7 per cent in 2010, validating the general concern regarding upward price pressures emanating from elevated administered price increases.

Box 1: Response of consumer prices to an oil price increase of US$10 per barrel

In the core model of the Bank, the oil price is an important exogenous variable. A sustained increase of US$10 per barrel results in an increase in the year-on-year rate of inflation of around 0,3 percentage points in the quarter that the oil price increases. This rises to slightly more than 0,6 percentage points after four quarters. The impact on inflation then decreases slightly at the start of the second year due to base effects. Thereafter the inflationary impact resumes an increasing trend due to second-round effects which run through channels such as increased inflation expectations, and higher salaries and wages. This analysis assumes no tightening of monetary policy to counter the second-round effects.

Additional inflation in consumer prices

The *Inflation Expectations* survey conducted by the Bureau for Economic Research (BER) in the fourth quarter of 2010 indicates that all surveyed participants expected inflation to accelerate from 2010 to 2012. Only the financial analysts' inflation expectations equalled actual headline inflation for 2010, while the expectations of business and labour representatives were significantly higher. Furthermore, financial analysts were of the opinion that inflation will remain within the target range during the next two years, while the other groups were less optimistic.

Headline consumer price inflation expectations

Per cent, as surveyed in the fourth quarter of 2010

Average inflation expected for:	Financial analysts	Business representatives	Trade union representatives	All surveyed participants
2010..	4,3	5,7	6,1	5,4
2011..	4,5	6,0	6,0	5,5
2012..	5,4	6,4	6,6	6,2

Source: Bureau for Economic Research, Stellenbosch University

Foreign trade and payments

International economic developments

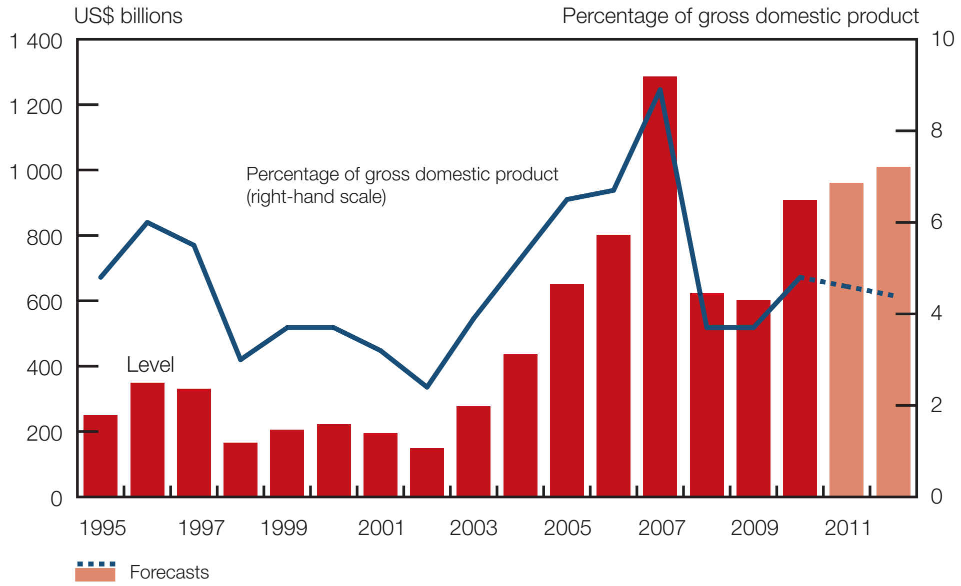
Preliminary estimates suggest that global economic growth amounted to about 4 per cent in the fourth quarter of 2010 following a moderation in the third quarter. In general, global output has expanded at an average quarterly rate in excess of 5 per cent since the third quarter of 2009, supporting the view that the global economic recovery is on track.

In its January 2011 *World Economic Outlook Update*, the International Monetary Fund (IMF) projected that global output would expand by 4,4 per cent in 2011 and 4,5 per cent in 2012. The growth outlook for 2011 was revised upwards by 0,2 percentage points, while the forecast for 2012 was left unchanged. Growth in advanced economies was revised upwards by 0,3 percentage points to 2,5 per cent in 2011 and downwards by 0,1 percentage points to 2,5 per cent in 2012. Simultaneously, growth in emerging-market and developing economies was revised upwards by 0,1 percentage points to 6,5 per cent in 2011, but left unchanged at 6,5 per cent in 2012. The IMF noted that economic growth remains uneven among advanced and emerging-market economies, with growth moderating less than expected in advanced economies.

Over the past two years many emerging-market currencies appreciated substantially on account of sizeable capital inflows, resulting in significant changes in international competitiveness. The Brazilian real, for example, has appreciated by almost 40 per cent since January 2009. As a result, Brazil and a number of other emerging-market economies introduced capital controls and other prudential measures aimed at capital inflows in an attempt to neutralise upward pressure on exchange rates. Quantitative easing in advanced economies, a surge in commodity prices, the stronger growth performance, higher interest rates and more favourable fiscal conditions in emerging-market economies resulted in sizeable capital inflows to these countries. According to the Institute of International Finance (IIF),[2] net private capital inflows to emerging-market economies rose by more than 50 per cent to US$908 billion in 2010 and are expected to increase to US$960 billion in 2011 and US$1 009 billion in 2012.

2 Institute of International Finance, *Research Note: Capital flows to Emerging Market Economies*, 24 January 2011.

Emerging-market economies: Net private capital inflows



Source: Institute of International Finance

Output growth in advanced economies slowed somewhat in the fourth quarter of 2010 mainly due to negative growth in Japan and the United Kingdom (UK). Real output growth in the euro area moderated from an annualised rate of 1,4 per cent in the third quarter of 2010 to 1,1 per cent in the fourth quarter. Economic activity in the three largest countries in the region – Germany, France and Italy – advanced at a slower pace than expected. Germany, the main driver of economic growth in the region, grew at a rate of 1,5 per cent in the fourth quarter of 2010, considerably slower than the rate of 2,8 per cent in the previous quarter. The construction industry, which has been primarily responsible for the moderation in growth, was adversely affected by the exceptionally cold and snowy weather. A self-sustaining recovery in private spending was evident in the United States (US). The US economy grew at a rate of 2,8 per cent in the fourth quarter of 2010 following growth of 2,6 per cent in the third quarter. Positive contributions to growth came from personal consumption expenditure and net exports. Private inventory investment and government consumption and investment, however, subtracted from output growth.

The latest economic estimates indicate a resurgence of growth in the fourth quarter of 2010 across emerging-market economies following slower growth in the preceding quarter. Economic growth moderated sharply in the third quarter of 2010 in a number of the major emerging-market economies including Brazil, Mexico and Argentina, while output in Russia declined. Preliminary indications are that conditions had improved in the fourth quarter of 2010 with China recording strong growth of 12,7 per cent as domestic demand and exports improved significantly. The growth momentum in most emerging-market economies is likely to accelerate due to improved global demand, which will likely support export growth, particularly in the export-dependent Asian economies, while the steady improvement in household income should spur domestic consumer sentiment. Rising commodity prices, however, may pose a threat to strong and sustainable growth in emerging-market economies.

Brent crude oil prices trended higher during the fourth quarter of 2010, averaging US$87 per barrel compared with a level of around US$76 per barrel in the preceding quarter. Oil price developments were mainly underpinned by positive market sentiment caused by growing demand in both developed and emerging-market economies and adverse weather conditions in the northern hemisphere, which raised the demand for heating oil and diesel. Declining US commercial crude oil inventories and political tensions in several North African and Middle East countries, furthermore, added upward pressure on oil prices, which reached levels of around US$118 per barrel in late February and early March 2011.

In its February 2011 *Oil Market Report,* the International Energy Agency (IEA) estimated global oil demand to have reached 87,8 million barrels a day in 2010 and projected an increase to 89,3 million barrels a day in 2011. According to the IEA, both the Organization of the Petroleum Exporting Countries (OPEC) and non-OPEC supply would increase over the period. OPEC crude oil production rose gradually in 2010, reaching its highest level in two years during the final quarter of the year. OPEC ministers left production targets unchanged at the organisation's December 2010 meeting, but Saudi Arabia and a few other OPEC countries subsequently announced their intentions to increase oil production.

According to the January 2011 IMF *World Economic Outlook Update,* the inflation forecast for advanced economies has been revised upwards by 0,3 percentage points to 1,6 per cent for 2011 and by 0,1 percentage points to 1,6 per cent for 2012. Inflation projections for emerging-market and developing economies have been revised upwards by 0,8 percentage points to 6,0 per cent for 2011 and by 0,3 percentage points to 4,8 per cent for 2012. The IMF noted that inflationary pressures were beginning to emerge, especially in emerging-market economies, partly due to rising food and energy prices.

Consumer price inflation rose in several advanced economies, mainly reflecting higher energy and other commodity prices. Annual headline inflation has recently accelerated in the Organisation for Economic Co-operation and Development (OECD) area, while core inflation (i.e., excluding food and energy prices) remained subdued. Although still fairly subdued, rising fuel prices have recently pushed headline inflation higher in the US. Core inflation, excluding food and energy prices, however, remained well contained during the fourth quarter of 2010. Deflation continues to hinder the Japanese economy with the severity of deflation even more apparent in the core measures. The Bank of Japan, however, expects the year-on-year pace of decline in consumer prices to slow as the aggregate supply-demand balance improves gradually.

Annual consumer price inflation continues to trend upwards across major emerging-market economies. Inflationary pressures continued to increase steadily in all the regions in recent months after decreasing slightly in the early part of the second half of 2010. Inflationary pressures have increased significantly in emerging Europe and signs of higher inflation are gaining momentum in emerging Asia and Latin America. The upside risks to inflation have increased due to the global recovery, the gradual rise in commodity prices and adverse weather conditions. Food prices have also been rising steadily since the middle of 2009 across emerging-market economies due to tight supplies, changing weather patterns and rising demand in emerging-market economies as consumption patterns transform, pointing to a long-term structural change. Inflationary pressures appear to have been the highest in Argentina, China, India, Russia, Turkey and Venezuela.

Monetary policies remained accommodative in advanced economies during the fourth quarter of 2010 due to considerable spare capacity and fragile private demand. Official interest rates were left unchanged in the US, the euro area and the UK during 2010, while the European Central Bank (ECB) continued with its Security Market Programme. The ECB has purchased an amount of €67 billion since the launch of the programme in May 2010. In addition to the interest rate reduction in October 2010, the Bank of Japan announced a new programme of asset purchases amounting to ¥5 000 billion, while the US Federal Reserve announced a renewed commitment to quantitative easing in November 2010.

Following asset purchases of around £165 billion by September 2009 and around £175 billion by the end of October 2009, the Bank of England's Monetary Policy Committee voted in November 2009 to increase total asset purchases to £200 billion. The Bank has not made any further purchases of government bonds since January 2010 as the programme has been completed. The central banks of Australia and Sweden increased their benchmark interest rates during the fourth quarter of 2010 due to rising inflation expectations and a favourable outlook for economic growth. China, India, South Korea, Taiwan and Thailand raised their official interest rates during the fourth quarter of 2010 as monetary authorities seek to avert economic overheating in the region leading the global rebound. Conversely, the central bank of Turkey decided to cut the one-week repo rate in December 2010 in an attempt to curb capital inflows amid subdued inflationary pressures. The central banks of Brazil, Chile, India, Israel, Russia, South Korea, Sweden and Thailand increased their policy rates in recent months, while New Zealand has reduced its Official Cash Rate in the wake of the negative economic impact of the earthquake.

Current account[3]

3 Unless stated to the contrary, the current-account transactions referred to in this section are all seasonally adjusted and annualised.

The fairly robust expansion in global economic activity in the fourth quarter of 2010, alongside firm international commodity prices and the continuous improvement in South Africa's terms of trade, paved the way for a further notable increase in the value of merchandise exports despite the further strengthening in the exchange value of the rand. Simultaneously, the value of merchandise imports receded somewhat due to restrained growth in capital spending in the aftermath of the completion of a number of infrastructure projects related to the hosting of the 2010 FIFA World Cup™ tournament. As a result, the country's trade surplus almost tripled from R30,3 billion in the third quarter of 2010 to R86,0 billion in the fourth quarter. In addition, the deficit on the services, income and current transfer account with the rest of the world narrowed markedly, mainly on account of lower net income and current transfer payments to the rest of the world.

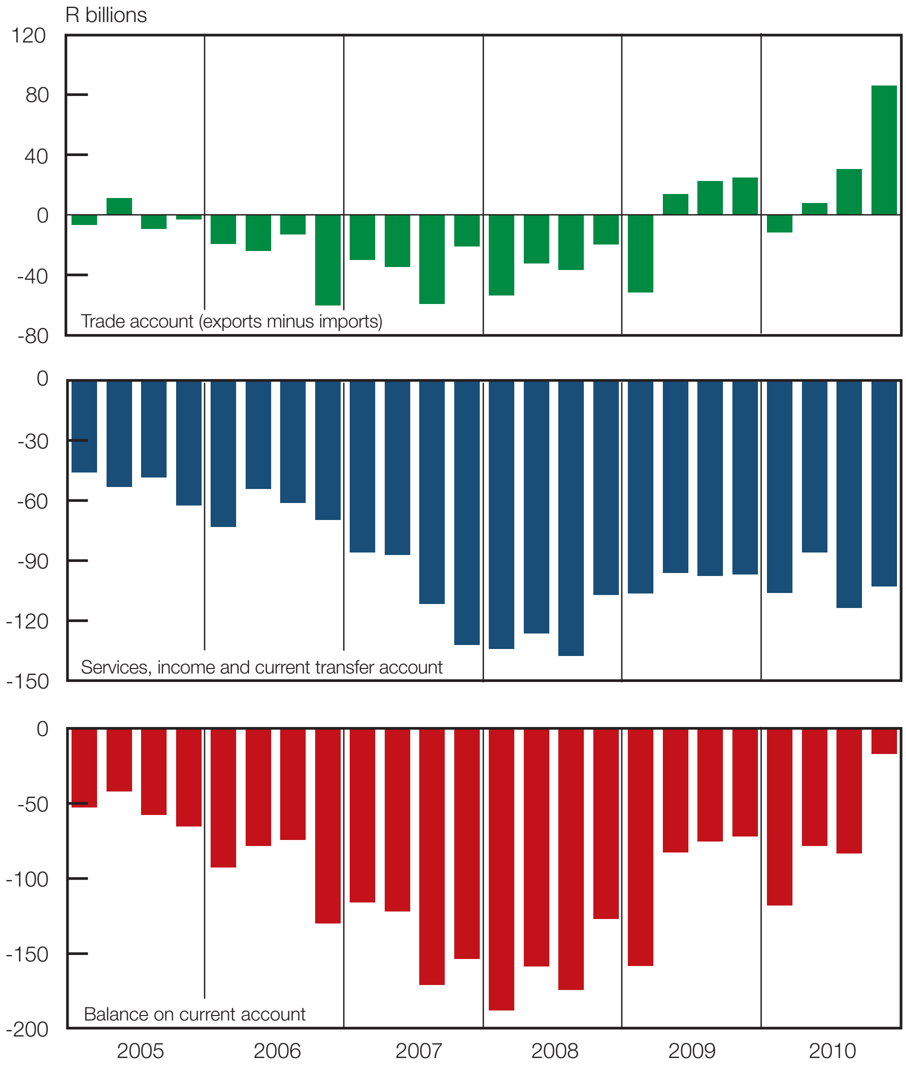
Consequently, the balance on current account registered a significantly smaller deficit of R17,0 billion or 0,6 per cent of gross domestic product in the fourth quarter of 2010 – a similar magnitude was last recorded in the fourth quarter of 2003. The smaller current-account deficit in the second half of 2010 also reflects the much reduced savings-investment gap in the South African economy, indicative of the subdued pace of fixed capital formation and the resulting lower levels of imports, particularly of capital and intermediate goods.

Balance of payments on current account

Seasonally adjusted and annualised
R billions

	2009	2010				
	Year	1st qr	2nd qr	3rd qr	4th qr	Year
Merchandise exports	503,7	515,1	549,7	585,5	616,7	566,8
Net gold exports	52,8	49,5	59,0	63,0	66,4	59,5
Merchandise imports	-554,2	-576,4	-600,9	-618,2	-597,1	-598,2
Trade balance	2,3	-11,8	7,8	30,3	86,0	28,1
Net service, income and current transfer payments	-99,4	-106,1	-86,0	-113,5	-103,0	-102,2
Balance on current account	-97,1	-117,9	-78,2	-83,2	-17,0	-74,1
As a percentage of gross domestic product	*-4,1*	*-4,6*	*-3,0*	*-3,1*	*-0,6*	*-2,8*

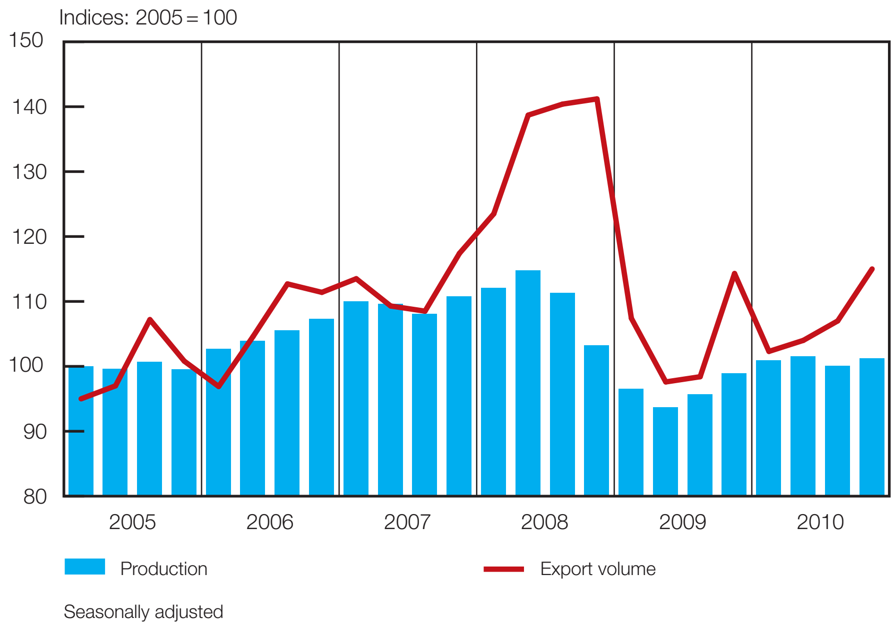
Balance of payments: Current account



Seasonally adjusted annualised rates

The sustained economic recovery in advanced and emerging-market economies and the concomitant higher demand for South African commodities boosted export volumes of especially mining commodities in the final quarter of 2010. Exceptional cold winter conditions in the northern hemisphere raised the demand for South African-produced coal, while iron ore exports also advanced strongly over the period. At the same time, exports of vehicles and transport equipment, as well as optical, and professional equipment rose notably; the higher volume of exported vehicles and transport equipment partly reflected the backlog that emanated from the strike action in the automotive industry during the third quarter of 2010. As a result, the overall volume of merchandise exports rose by 3,4 per cent in the fourth quarter of 2010 following an increase of 6,7 per cent in the preceding quarter. Relative to South Africa's real gross domestic product, export volumes rose to 18,8 per cent in the fourth quarter of 2010; for calendar year 2010, this ratio amounted to 17,9 per cent compared with a ratio of 17,3 per cent in 2009.

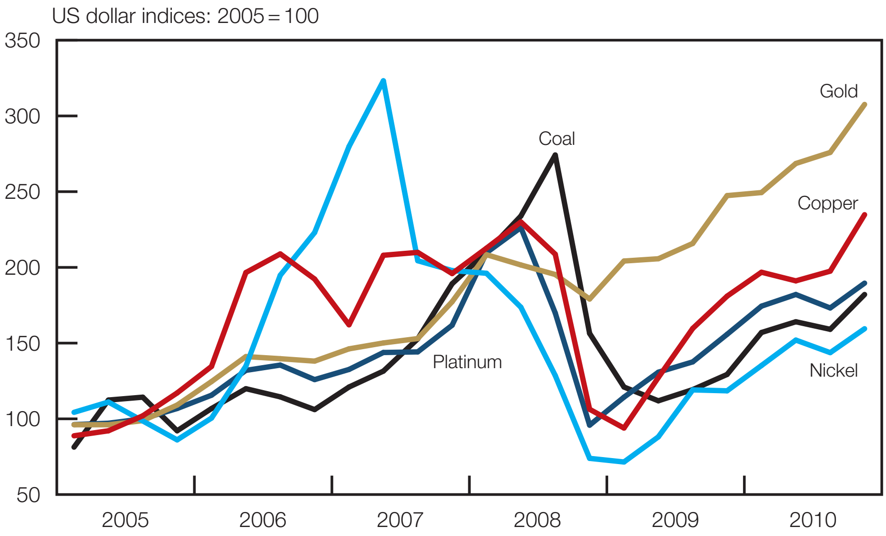
Manufacturing: Production and export volume



The value of merchandise exports rose by almost 5,5 per cent as gains from rising international commodity prices were almost fully negated by the strengthening in the exchange value of the rand. The rand price of exported goods advanced by 1,9 per cent in the fourth quarter of 2010.

The upward trend in international commodity prices continued in the fourth quarter of 2010, mainly buoyed by the surge in the prices of platinum, coal, nickel and gold. The price of platinum advanced from US$1 551 per fine ounce in the third quarter of 2010 to US$1 698 a fine ounce in the fourth quarter, coinciding with increased production levels of catalytic converters used in the automotive industry in most European markets. In addition, the price of platinum also benefited from, among other factors, a rise in the price of gold and a weaker US dollar. The upward trend in the price of coal reflected increased demand in response to the cold weather conditions in Europe. More notably, the price of gold on the London market advanced from US$1 227 a fine ounce in the third quarter of 2010 to US$1 368 a fine ounce in the fourth quarter, or by 11,5 per cent. In US dollar terms, international commodity prices increased by 11,1 per cent in the fourth quarter of 2010; for the year as a whole, these prices surged by no less than 33,7 per cent when compared to 2009.

International prices of selected South African export commodities



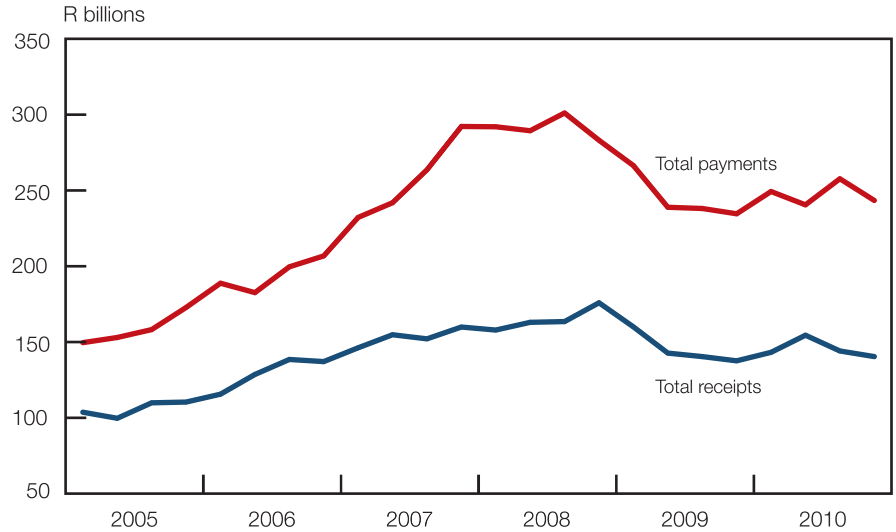
Owing to the appreciation of the exchange rate of the rand, the increase in the realised rand price of gold was limited to 4,8 per cent in the fourth quarter of 2010. Simultaneously, the volume of net gold exports increased marginally in the final quarter of 2010 following steady increases in the preceding two quarters. As a result, net gold export proceeds advanced by 5,3 per cent from the third quarter of 2010 to the fourth quarter.

The volume of merchandise imports, which increased unabatedly from the fourth quarter of 2009, receded by about 2,2 per cent in the fourth quarter of 2010. The contraction in import volumes in the final quarter of 2010 could largely be attributed to a decline in intermediate imports, more in particular crude oil imports, alongside a decline in the physical quantity of manufactured goods imported. Lower crude oil imports were, however, partly substituted by the importation of petrol and certain prepared oil products in anticipation of the increased demand during the festive period. In the category for manufactured imports, declines were registered in especially the subcategories for machinery and electrical equipment, as well as vehicles and transport equipment. The lower import volumes in these subcategories could largely be ascribed to fairly sluggish growth in private-sector capital spending and the availability of surplus capacity in the manufacturing sector.

The prolonged period of low inflation in South Africa's most important trading-partner countries alongside the persistent strengthening in the exchange value of the rand exerted downward pressure on the rand price of merchandise imports. Owing to the combination of lower import volumes and marginally lower import prices, the value of merchandise imports receded by 3,4 per cent in the fourth quarter of 2010. For the year as a whole, the value of merchandise imports, however, still exceeded that in 2009.

The shortfall on the services, income and current transfer account of the balance of payments narrowed by about R10 billion to R103 billion in the fourth quarter of 2010 – a balance more or less equal to the average quarterly deficit registered for the year 2010 as a whole. The sharp contraction in the deficit in the second quarter of 2010 was largely attributable to increased tourism receipts during the hosting of the 2010 FIFA World Cup™ tournament in the middle quarters of 2010. Despite the hosting of the football tournament, the deficit on the services, income and current transfer account widened marginally from 2009 to 2010. As a percentage of gross domestic product, the deficit, however, remained relatively stable at around 4 per cent over the period.

Services, income and current transfer account



Seasonally adjusted annualised rates

The smaller deficit in the fourth quarter of 2010 can mainly be attributed to considerably lower gross dividend payments to non-resident investors. However, following a decline of almost 30 per cent in 2009, gross dividend payments to the rest of the world rose by about 5 per cent in 2010 as a whole. The resumption of higher income distributions to non-resident investors was partly a reflection of the domestic economic recovery in the course of 2010. Furthermore, freight-related payments to non-resident carriers decreased, consistent with the lower inward movement of merchandise. In addition, the narrowing of the deficit was also underpinned by a decline in net current transfers to members of the Southern African Customs Union in the fourth quarter of 2010.

These lower gross payments were, however, partially offset by a decline in travel receipts in the fourth quarter of 2010, following a relatively high base stemming from tourism activities related to the football event during the middle quarters of 2010. In addition, payments for travel-related activities by South African residents temporarily travelling abroad increased further during the fourth quarter of 2010. Net payments for "other services" also increased further, mainly due to higher gross payments for services of a technical nature rendered by non-resident parties relating to infrastructural development during the second phase of the Gautrain project.

South Africa's terms of trade improved further in the final quarter of 2010 as the rand price of merchandise imports continued to be weighed down by the relative strength of the domestic currency. However, the rand price of merchandise exports trended upwards as the surge in international commodity prices surpassed the downward pressure exerted by the appreciation of the rand.

Financial account

Notwithstanding some concerns regarding sovereign and banking-sector risk in the financial markets of the euro area periphery, financial and economic conditions in the US and in other advanced economies improved somewhat in the fourth quarter of 2010, supported by ongoing monetary and fiscal stimulus measures. These developments, alongside concerns about overheating and a build-up of inflationary pressures in some emerging-market countries, caused a slowdown in capital flows into these economies. In South Africa the inward movement of capital on the financial account of the balance of payments (including unrecorded transactions) shrank significantly to an amount of R1,7 billion in the fourth quarter. However, for the year 2010 as a whole, the flow of capital into the country compared well with inward capital movements registered in 2009.

Net financial transactions not related to reserves

R billions

	2009	2010				
	Year	1st qr	2nd qr	3rd qr	4th qr	Year
Change in liabilities						
Direct investment	45,4	3,1	2,9	1,1	4,3	11,4
Portfolio investment	107,2	44,1	28,4	45,8	-10,4	107,9
Other investment	-40,0	-16,0	-1,5	15,1	13,3	10,9
Change in assets						
Direct investment	-9,8	0,1	-3,3	-7,0	6,9	-3,3
Portfolio investment	-13,4	-5,6	-2,2	-9,7	-10,8	-28,3
Other investment	23,6	-3,4	10,2	-6,5	-18,0	-17,7
Total financial transactions*	**113,9**	**49,9**	**24,0**	**29,5**	**1,7**	**105,1**
Financial transactions as a percentage of gross domestic product	*4,8*	*8,0*	*3,6*	*4,3*	*0,2*	*3,9*

* Including unrecorded transactions

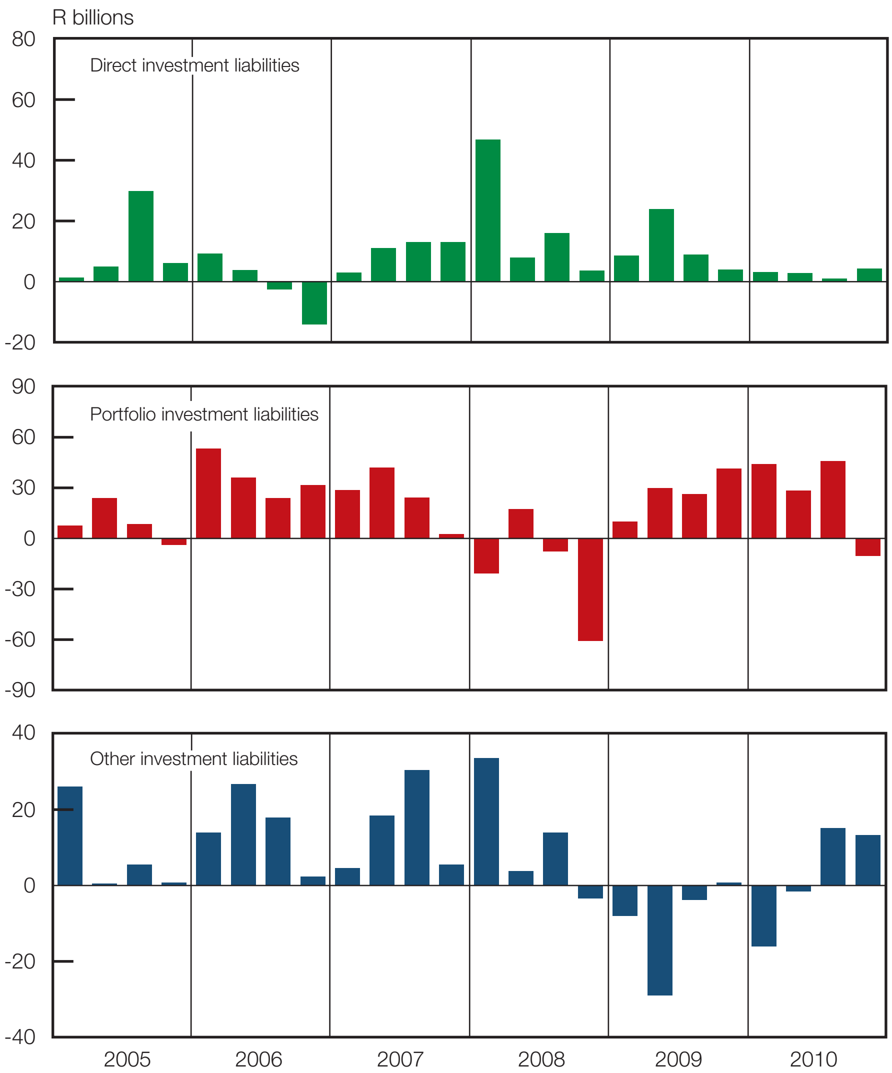
Foreign-owned assets in South Africa

Foreign direct investment into South Africa amounted to R4,3 billion in the fourth quarter of 2010 following inward investment of R1,1 billion in the third quarter. The inward movement of capital in the fourth quarter of 2010 mainly took the form of long-term loans extended by non-resident parent companies to direct investment enterprises in South Africa for the financing of capital formation in the mining sector. On an annual basis, the inflow of direct investment capital amounted to R11,4 billion in 2010 compared with R45,4 billion in 2009. The significantly smaller inflow of direct investment capital continued to reflect some degree of uncertainty regarding the global economic recovery, domestic economic fundamentals and the long-term outlook for the domestic economy.

Foreign portfolio investment into the domestic market recorded an outflow of R10,4 billion in the fourth quarter of 2010 – the first reduction in portfolio liabilities to be recorded since 2008. The change in market sentiment and the subsequent reduction in speculative capital flows were evident in most developing economies, as renewed financial turbulence in the peripheral euro area economies along with concerns about narrowing output gaps in some emerging-market economies caused global investors to redirect investment funds to the US economy where growth prospects seemed to have improved. In South Africa the risk aversion of foreign investors was evident when non-resident investors reduced their holdings of domestic debt securities. This reduction was, however, partly countered by the acquisition of equity securities by some foreign investors. For the year 2010 as a whole, however, inward portfolio investment remained at almost the same level as in 2009.

Other investment into South Africa recorded an inflow of R13,3 billion in the fourth quarter of 2010. The elevated level of capital flows in this category mainly reflected an increase in short-term loans granted to the domestic private banking sector. By contrast, non-resident investors reduced their deposit holdings with the South African banking sector. The higher demand for short-term loans by the domestic banking sector could partly be attributed to an increased demand for credit by the non-bank private sector during the final quarter of 2010. The inflow of other investment capital was further supplemented by long-term foreign loans granted to domestic parastatals as part of their ongoing infrastructural development programme. While the calendar year 2009 and the first half of 2010 were characterised by the repayment of foreign loans, the second half of 2010 was marked by the renewed use of foreign loans by South African entities.

Financial account: Liabilities



South African-owned assets abroad

Outward direct investment moved from an outflow of R7,0 billion in the third quarter of 2010 to an inflow of R6,9 billion in the fourth quarter. This inflow of capital mainly reflected the selling by a South African company of its foreign direct investment interest in an information and communications technology company. For the year 2010 as a whole, capital outflows in the amount of R3,3 billion were recorded.

Foreign portfolio investment by South African entities registered a further outflow of R10,8 billion in the fourth quarter of 2010. The accumulation of foreign portfolio assets could largely be ascribed to foreign investment by the domestic banking sector, individual investors and institutional investors, as these entities took advantage of investment opportunities and the strength of the rand to diversify their portfolios. The acquisition of portfolio investment assets increased by R28,3 billion in 2010 compared with an outflow of R13,4 billion in 2009.

Other outward investment from South Africa recorded a sizeable outflow of R18,0 billion in the fourth quarter of 2010 compared with an outflow of R6,5 billion in the third quarter. The outflow of capital largely reflected an increase in foreign currency-denominated deposits with, and short-term loans extended to, non-resident banks by the South African banking sector; the sector experienced ample international liquidity. The offshore rand-denominated deposits of the domestic banking sector contracted in the fourth quarter of 2010.

Foreign debt

South Africa's total foreign debt increased by US$14,0 billion in the third quarter of 2010 to US$93,9 billion at the end of the quarter. The substantial increase in the country's outstanding external debt mainly resulted from a marked increase in rand-denominated foreign debt; foreign currency-denominated foreign debt rose moderately over the period.

The strong increase in the country's rand-denominated foreign debt reflected non-resident investors' net purchases of domestically issued bonds which more than doubled from the second quarter of 2010 to the third quarter. Apart from the South African bond market that continued to offer attractive yields, non-residents also increased their holdings of rand-denominated deposits with the South African banking sector. The strength of the rand during this period also contributed to the increase in rand-denominated debt when converted to US dollar terms.

Foreign debt of South Africa

US$ billions at end of period

	2009		2010		
	3rd qr	4th qr	1st qr	2nd qr	3rd qr
Foreign currency-denominated debt	**42,3**	**42,1**	**42,1**	**40,9**	**43,5**
Bearer bonds	15,6	15,4	16,8	16,0	17,0
Public sector	5,8	5,7	5,4	5,5	6,1
Monetary sector	9,4	10,6	9,2	8,3	9,1
Non-monetary private sector	11,5	10,4	10,7	11,1	11,3
Rand-denominated debt	**34,5**	**36,5**	**39,0**	**39,0**	**50,4**
Bonds	9,5	11,6	13,5	15,2	22,7
Other	25,0	24,9	25,5	23,8	27,7
Total foreign debt	**76,8**	**78,6**	**81,1**	**79,9**	**93,9**
As a percentage of gross domestic product	*29,4*	*27,7*	*26,0*	*24,1*	*27,2*

The increase in foreign currency-denominated foreign debt was largely due to long-term foreign funding acquired by domestic parastatals and a South African bank. The relative weakness of the US dollar against the euro contributed to an increase in the foreign debt expressed in US dollar terms.

Measured in rand, South Africa's foreign debt advanced from R611 billion at the end of June to R654 billion at the end of September 2010. The increase in rand terms was held back as a result of the appreciation of the rand against the US dollar over this period.

During January 2011 the credit rating agencies Fitch and Standard & Poor's revised South Africa's sovereign credit ratings outlook from negative to stable, following the country's emergence from the recession and the agencies' assessment that its credit fundamentals were roughly in line with that of its peers.

International reserves and liquidity

South Africa's overall balance-of-payments position (i.e., the change in the country's net gold and foreign-exchange reserves due to balance-of-payments transactions) deteriorated in the fourth quarter of 2010; this was the first quarterly decline to be recorded since 2003. Notwithstanding the decrease of R2,1 billion in the final quarter of 2010, South Africa's net international reserves rose by R31,3 billion in 2010 compared with an increase of R17,0 billion in 2009.

Measured in US dollars, the country's gross gold and other foreign reserves (i.e., the international reserves before accounting for reserve-related loans) declined from US$44,1 billion at the end of September 2010 to US$43,8 billion at the end of December 2010 before rising to US$47,3 billion at the end of February 2011 as the authorities stepped up reserve accumulation.

The level of imports covered by reserves receded from 18,9 weeks at the end of September 2010 to 18,4 weeks at the end of December.

The international liquidity position increased from US$40,9 billion at the end of September 2010 to US$43,4 billion at the end of December, before rising to US$44,8 billion at the end of February 2011.

Exchange rates

Having increased, on balance, by almost 6,3 per cent in the first nine months of 2010, the nominal effective exchange rate of the rand advanced by a further 5,4 per cent in the fourth quarter. The trade-weighted exchange rate of the rand decreased by 1,8 per cent in October and increased by 1,4 per cent and 5,9 per cent respectively during November and December 2010. For the calendar year 2010 as a whole, the weighted average exchange rate of the rand increased by 12,0 per cent compared to an increase of 22,9 per cent in 2009. The further strengthening in the exchange value of the rand during the fourth quarter of 2010 can be attributed to, among other factors, sound macroeconomic policy measures, the sustained increase in commodity prices and the expectation of sizeable inflows of direct investment capital into the country.

Exchange rates of the rand

Percentage change

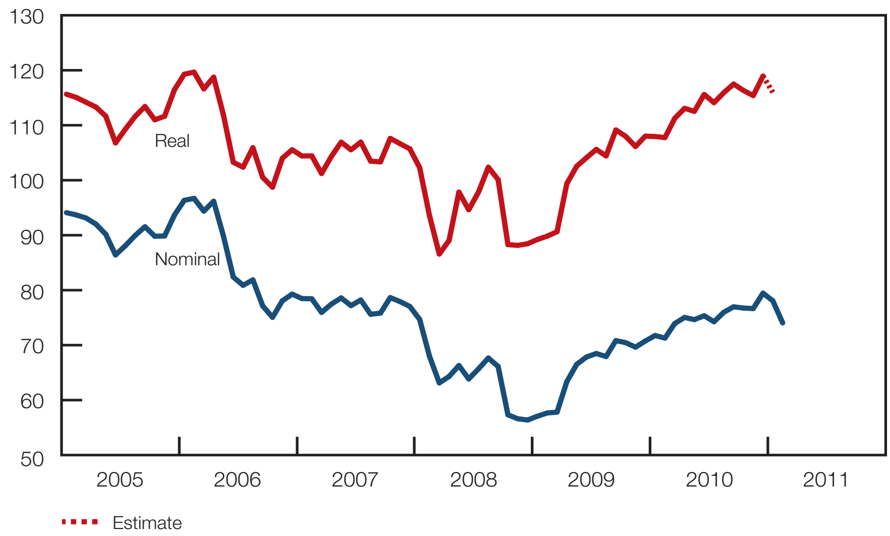
	31 Mar 2010 to 30 Jun 2010	30 Jun 2010 to 30 Sep 2010	30 Sep 2010 to 31 Dec 2010	31 Dec 2010 to 28 Feb 2011
Weighted average*	-0,8	3,0	5,4	-6,7
Euro	5,2	-1,3	7,3	-8,2
US dollar	-4,2	9,9	5,1	-5,2
Chinese yuan	-4,8	8,2	3,6	-5,5
British pound	-3,8	4,1	7,8	-9,0
Japanese yen	-9,0	3,2	2,8	-4,9

* Against a basket of 15 currencies

From the end of December 2010 to the end of February 2011, the nominal effective exchange rate of the rand declined by 6,7 per cent, affected by developments in the euro/dollar exchange rate and net sales by non-residents of South African equity and debt securities during the first two months of 2011.

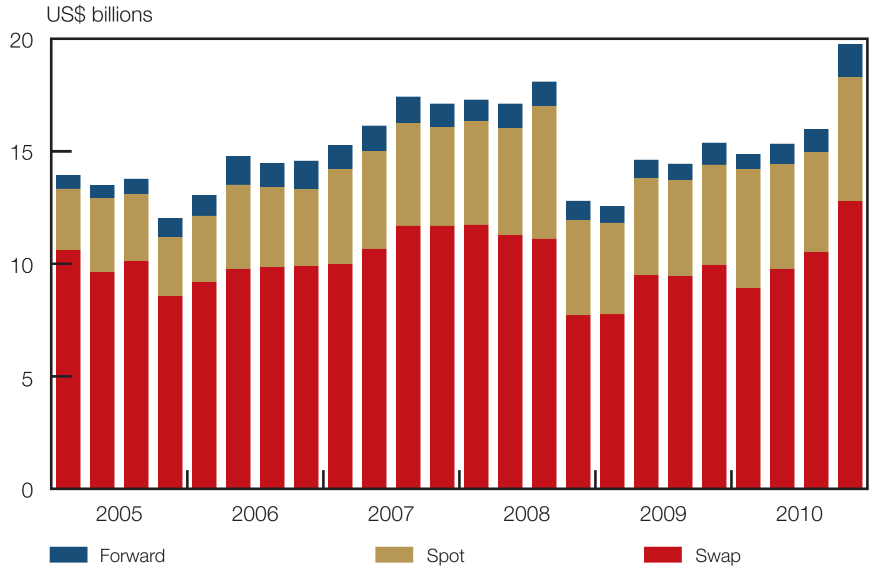
Effective exchange rates of the rand

Indices: 2000 = 100



The real effective exchange rate of the rand increased by 10,1 per cent in the year to December 2010, adversely affecting the country's external competitiveness.

Average net daily turnover in the South African foreign-exchange market



The average net daily turnover in the domestic market for foreign exchange increased from US$16,0 billion in the third quarter of 2010 to US$19,8 billion in the fourth quarter as spot, forward and swap transactions increased. The increase of US$2,3 billion in the average net daily turnover in the swap market partly reflects non-resident activity in the domestic bond market. The turnover attributable to non-residents remained around 72,5 per cent of the total turnover in both quarters.

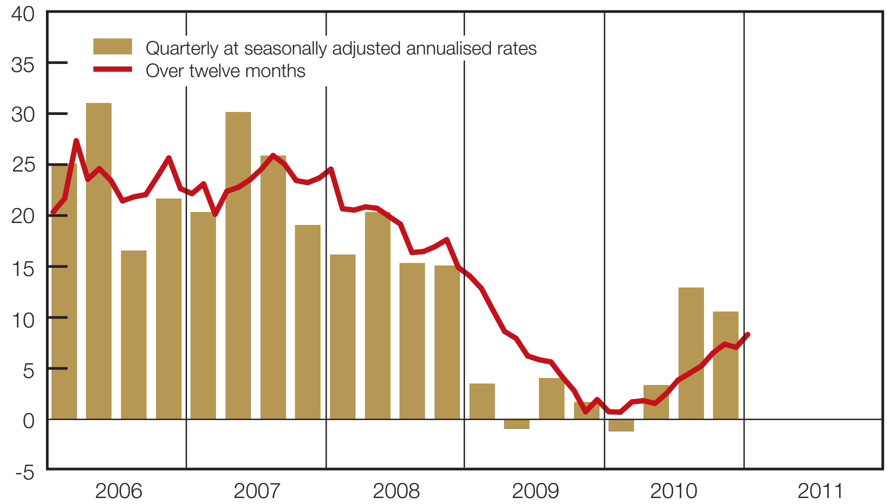
Monetary developments, interest rates and financial markets

Money supply

After increasing at a subdued pace during the first half of 2010, growth in the broadly defined money supply (M3) regained some momentum during the second half of the year. Year-on-year growth in M3 picked up from an all-time low of 0,5 per cent in February 2010 to a recent high of 7,2 per cent in November. After easing slightly to 6,9 per cent in December growth in M3 rebounded to 8,2 per cent in January 2011. During the second half of 2010 growth in M3 was buoyed, in part, by wealth effects generated by robust increases in the prices of financial assets, allowing investors to apportion some of these funds towards low-risk monetary assets. The long-term deposits benefited the most, as they offered higher yields in an environment of low and declining interest rates.

Growth in M3

Percentage change



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

The recovery in M3 growth was also evident in the quarter-to-quarter[4] growth rates of 12,9 and 10,6 per cent in the third and the fourth quarters of 2010 respectively – the first double-digit growth since 2008.

Maturity analysis of growth in M3

Per cent, at seasonally adjusted annualised rates

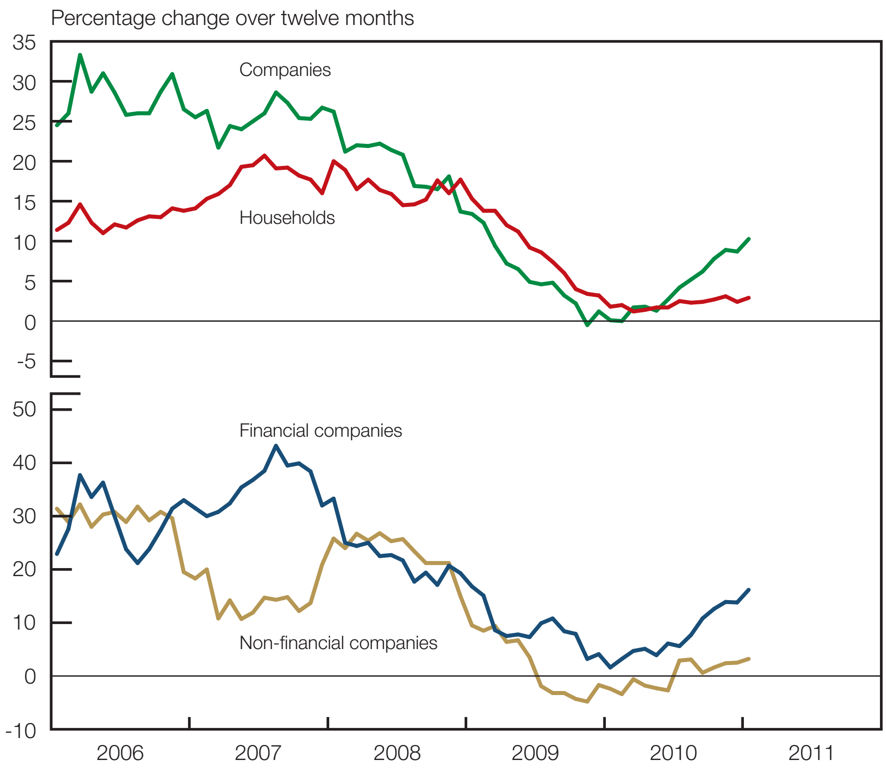
	2010			
	1st qr	2nd qr	3rd qr	4th qr
Notes and coin	17,3	-7,7	4,9	6,9
Cheque and transmission deposits	-7,0	19,6	15,0	24,3
Call and overnight deposits	38,5	-3,8	4,2	-1,0
Other short- and medium-term deposits*	5,4	-8,9	-1,9	8,8
Long-term deposits**	-35,5	16,3	61,1	17,4
M3	-1,2	3,4	12,9	10,6

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

After rebounding from negative growth rates at the beginning of the year, cheque and transmission and long-term deposits dominated growth in M3 deposits during the remainder of 2010. Rising transaction values in the economy probably supported the increase in cheque and transmission deposits. By contrast, call and overnight, and short- and medium-term deposits, which underpinned growth in the first quarter of 2010, contracted in the second quarter and remained relatively sluggish in subsequent quarters, consistent with low returns on those deposits. Growth in notes and coin in circulation remained relatively subdued for most of the year, reflecting low inflation – including food inflation – and the increased popularity of non-cash payments.

The overall increase in M3 amounted to R134,8 billion during 2010, having risen by a mere R34,0 billion in 2009. The bulk of the increase, amounting to R100,3 billion, occurred during the second half of 2010. The corporate sector was the main contributor to the increase in M3 deposits throughout 2010, accounting for a significant 90 per cent, or R121,5 billion, while the household sector contributed the balance of R13,2 billion. Growth over twelve months in the M3 deposit holdings of the corporate sector improved noticeably in 2010, rebounding from close to zero growth earlier in the year to 8,7 per cent in December and 10,3 per cent in January 2011. At the same time, growth in the M3 deposit holdings of the household sector remained relatively subdued, maintaining an average twelve-month growth rate of around 2 per cent in 2010. Year-on-year growth in the deposit holdings of the household sector came to 2,9 per cent in January 2011. The non-bank financial institutions were the dominant drivers behind the growth in corporate-sector deposit holdings in 2010, largely reflecting portfolio rebalancing which favoured cash holdings, and strong turnover in certain financial markets.

M3 holdings of households and companies



Statistically, the dominant counterpart to the increase in M3 during 2010 was the expansion in claims on the private sector, supported by an increase in net foreign assets. The overall increase in banks' claims on the private sector resulted from a combination of increases in mortgage advances, other loans and advances, and investments. Net claims on the government sector, which declined during the first two quarters 2010, rose in the remaining two quarters of 2010, largely on an increase in the banks' holdings of government bonds, coupled with a small decline in government deposits. With the exception of the second quarter of 2010, net other assets and liabilities declined during most of the year, as the rise in other liabilities exceeded the increase in other assets.

Statistical counterparts of change in M3

R billions

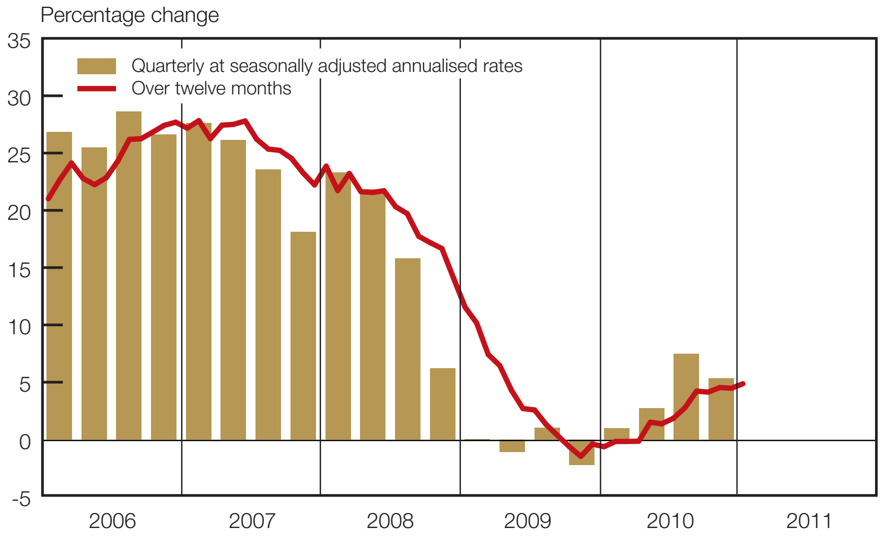
	2010				
	1st qr	2nd qr	3rd qr	4th qr	Year
Net foreign assets	42,7	0,5	4,6	11,5	59,4
Net claims on the government sector	-30,5	-14,1	9,6	13,3	-21,7
Claims on the private sector	16,3	16,1	55,0	22,5	110,0
Net other assets and liabilities	-19,5	23,0	-12,0	-4,3	-12,8
Total change in M3	8,9	25,5	57,3	43,0	134,8

In spite of the recovery in money supply growth the income velocity of M3 generally trended higher during 2010, as growth in deposits was generally surpassed by growth in nominal gross domestic product in the course of the year. The income velocity of M3 increased from 1,31 in the first quarter of 2010 to 1,35 in the fourth quarter.

Credit extension

The severe deceleration in banks' total loans and advances extended to the private sector abated in the early months of 2010 and started a modest recovery during the second half of the year. The twelve-month growth rate in total loans and advances fluctuated slightly above the 4 per cent level in the last four months of the year, a significant improvement from the negative growth rates experienced from October 2009 to April 2010. In January 2011 the growth rate came to 4,7 per cent. The delayed and slow adjustment of bank credit to more accommodative monetary policy was hampered by the already high level of household debt and, despite tentative signs of improvement, still-weak labour market conditions. In addition, the corporate sector's low demand for credit was reflective of a sluggish pickup in new investment alongside the protracted recovery in economic conditions.

Total loans and advances to the private sector



The quarter-to-quarter[5] growth rate of total loans and advances decelerated from 7,5 per cent in the third quarter of 2010 to 5,4 per cent in the fourth quarter. Despite the slower rate of growth, the rate of increase remained higher than that observed throughout 2009 and the first half of 2010.

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

Quarterly changes in banks' private-sector loans and advances by type

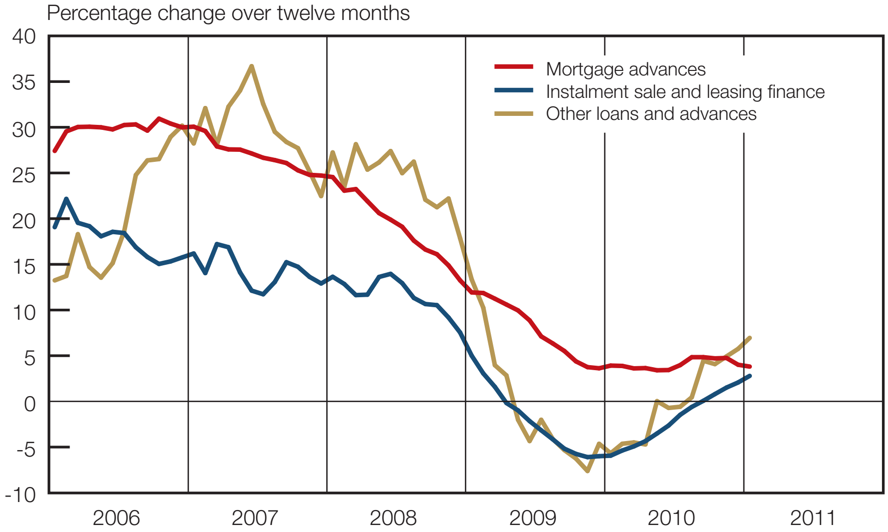
R billions

	2010			
	1st qr	2nd qr	3rd qr	4th qr
Mortgage advances	14,7	6,8	18,4	0,4
Instalment sale credit and leasing finance	-0,8	0,6	2,2	2,9
Other loans and advances	0,3	5,7	27,7	2,1
Overdrafts	1,5	-3,8	1,2	-1,6
Credit card advances	0,3	0,0	0,5	0,2
General advances	-1,4	9,5	26,1	3,5
Total loans and advances	14,1	13,1	48,3	5,3
Of which: To household sector	19,1	11,2	28,6	11,8
To corporate sector	-4,9	1,9	19,7	-6,5

Mortgage advances, the main contributor towards growth in banks' total loans and advances extended to the private sector during the first two quarters of 2010, was surpassed by the categories for *other loans and advances,* and *instalment sale credit and leasing finance* in the third and fourth quarter respectively. Technical adjustments related to a securitisation vehicle artificially boosted growth in mortgage advances during the third quarter of 2010, but this was again reversed during the fourth quarter. Nonetheless, the year-on-year growth in mortgage advances improved moderately from average year-on-year growth of 3,6 per cent in the first half of 2010 to 4,5 per cent in the latter half of the year, as the muted growth in house prices and lower interest rates helped to stimulate demand for real estate. In January 2011 growth in mortgage advances came to 3,8 per cent.

After turning positive in September 2010, growth over twelve months in *instalment sale credit and leasing finance* accelerated further to 2,8 per cent in January 2011. The improvement in this category occurred against the backdrop of stable new vehicle prices, lower debt-servicing costs and improvements in loan finance approval rates.

Loans and advances to the private sector by type



Among the various categories of total loans and advances extended to the private sector, *other loans and advances* was most severely affected by the downturn in domestic economic activity. This category of loans, which includes overdrafts, credit card and general advances, recovered strongly in the course of 2010. The twelve-month growth in other loans and advances surpassed the annual growth in mortgage advances in November 2010 and reached a growth rate of 5,7 per cent in December 2010 and 6,9 per cent in January 2011. *General loans*, predominantly used by the corporate sector for working capital requirements, remained the biggest driver of the growth in other loans and advances in 2010, aligned with the recovery in economic activity.

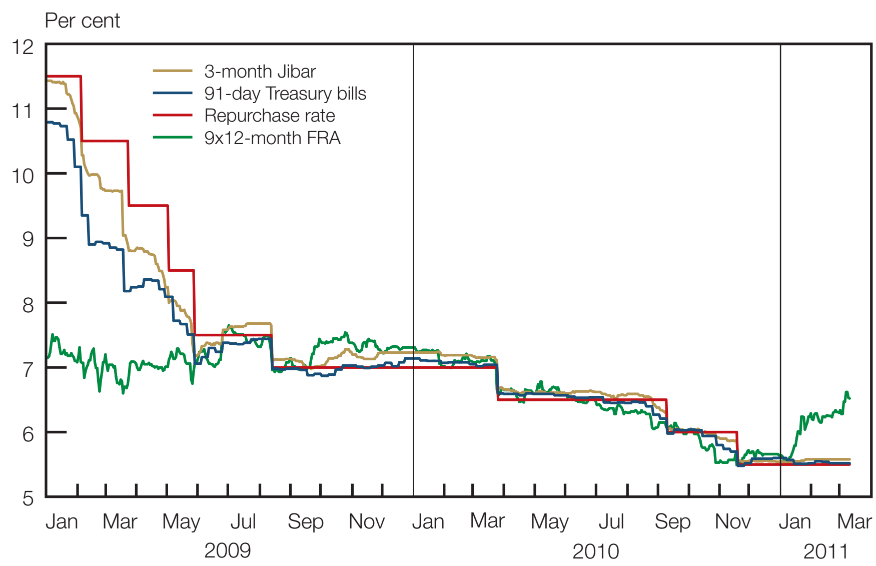
In 2010 bank credit extended to the household sector continued to increase more than that taken up by the corporate sector, with households accounting for R70,7 billion of the overall increase of R80,9 billion in total loans and advances. During the fourth quarter of 2010, whereas loans and advances to the household sector rose somewhat, the corporate sector decreased its credit uptake. Bank-intermediated funding to the corporate sector rebounded substantially in 2010, changing from negative growth of R39,6 billion in 2009 to positive growth of R10,1 billion in 2010. Growth over twelve months in credit extended to the corporate sector registered consistent positive year-on-year growth rates from September 2010 and reached 1,2 per cent in December, and 1,3 per cent in January 2011.

Twelve-month growth in credit extended to the household sector maintained a steady pace of growth as it increased from 2,9 per cent in December 2009 to 6,3 per cent in September 2010 and further to 7,5 per cent in January 2011, reaching its highest level since January 2009.

Interest rates and yields

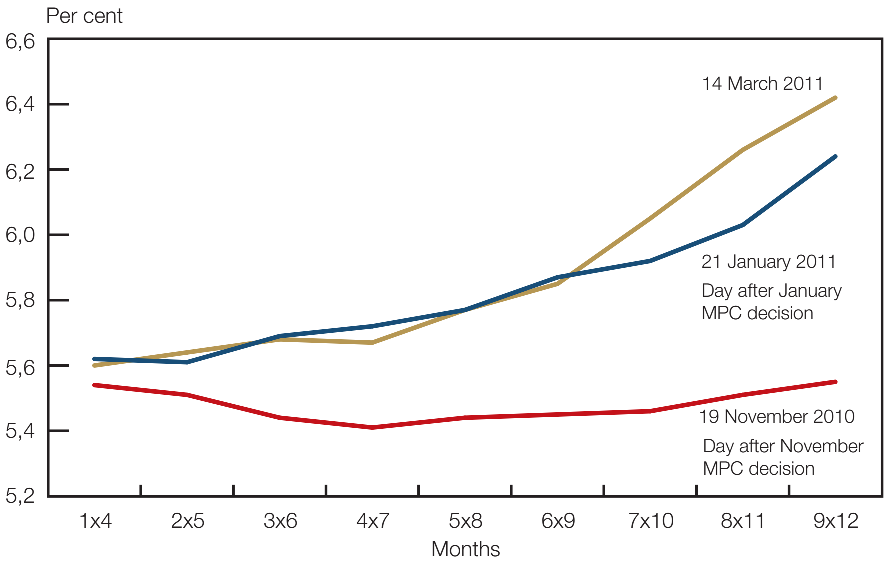
Subdued inflationary pressures allowed the Monetary Policy Committee (MPC) to adopt an easier monetary policy stance in the course of 2010, thereby supporting the recovery in domestic economic activity. The repurchase rate was subsequently reduced three times during the year by a cumulative one-and-half percentage point to 5,5 per cent in November. On 20 January 2011 the MPC decided to keep the repurchase rate unchanged, against the backdrop of the improving growth outlook, a seemingly sustained recovery in domestic expenditure and expectations that inflation would remain within the target range during the assessed period. The decision was reached despite prevailing risks emanating from global commodity prices, particularly oil and food prices, and domestic cost-push factors, most notably administered prices and wage settlements. The MPC statement discussing developments underlying recent monetary policy decisions is reproduced in full on page 69 of this *Bulletin*.

Money-market rates



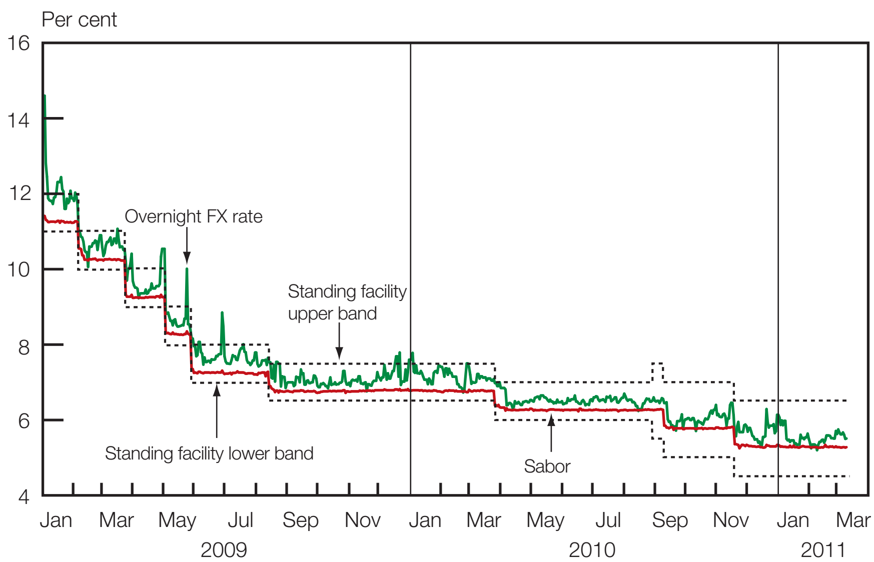
Alongside the lowest level of the repurchase rate in more than 30 years, other money-market rates continued to hover at historically low levels during the fourth quarter of 2010 and the first two months of 2011. The three-month Johannesburg Interbank Agreed Rate (Jibar), for example, displayed a moderate downward trend from 6,03 per cent on 1 October 2010 to 5,86 per cent on 18 November, before receding by a further 31 basis points to 5,55 per cent on 19 November 2010 when the repurchase rate was reduced. The Jibar remained relatively stable thereafter and amounted to 5,58 per cent on 11 March 2011. Similarly, the 91-day Treasury bill rate declined by 56 basis points from 6,04 per cent to 5,48 per cent between 1 October 2010 and 19 November. The rate fluctuated slightly higher thereafter to reach 5,51 per cent on 11 March 2011.

Forward rate agreement yield curves



Forward rate agreements (FRAs) reflected positive market sentiment during the fourth quarter of 2010, as market participants remained optimistic about the inflation outlook. The trend reversed abruptly in early January 2011, when global inflationary pressures started to surface due to rising food and oil prices, and market participants became increasingly concerned about

Benchmark overnight rates



geopolitical tensions. The rate on the 9x12-month FRA, in particular, increased sharply by 76 basis points from a low of 5,53 per cent on 5 January 2011 to 6,29 per cent on 5 February 2011, before easing slightly to 6,47 per cent on 11 March 2011. Since January 2011, the FRA yield curve has shifted higher across all maturities, particularly in the medium to longer-term maturity range, indicating market expectations that monetary policy would be tightened towards the latter part of 2011.

The South African Benchmark Overnight Rate on Deposits (Sabor) remained fairly stable and well within the standing facility limits during the last quarter of 2010. The rate hovered around 5,78 per cent from the beginning of October 2010 to 18 November, before declining by more than 40 basis points to 5,36 per cent on 19 November alongside the reduction in the repurchase rate. The Sabor amounted to 5,28 per cent on 11 March 2011. Simultaneously, the implied rate on one-day rand funding in the foreign-exchange market (overnight FX rate), while displaying a greater measure of volatility, also remained within the standing facility limits, fluctuating between a broad range of 6,46 per cent and 5,33 per cent from 1 October 2010 to the end of December due to, among other things, typical short-term liquidity pressures towards the end of the year. The rate amounted to 5,59 per cent on 11 March 2011.

Reflecting the pass-through of monetary policy to lending rates, the prime overdraft rate and the predominant rate on mortgage loans were uniformly reduced by a cumulative 150 basis points to 9,00 per cent, alongside the three reductions in the repurchase rate during 2010. Both interest rates were maintained at these levels up to early March 2011.

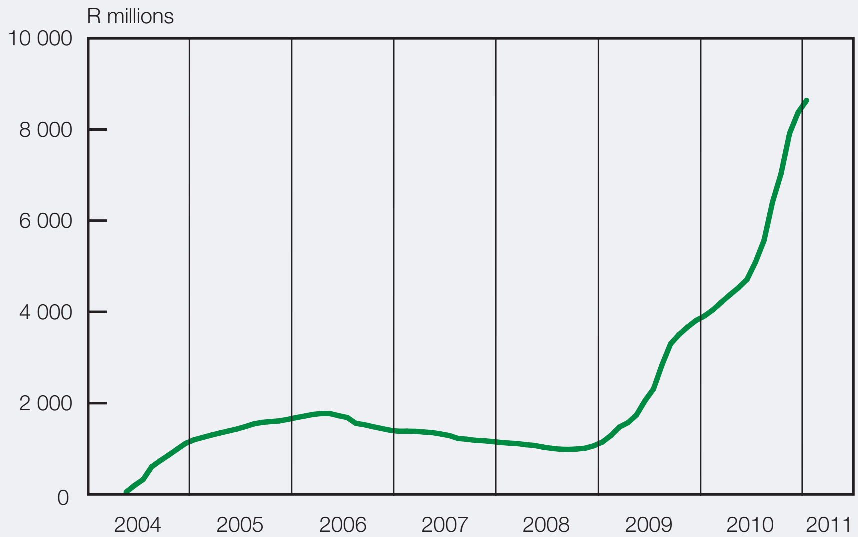
The *standard interest rate* on loans granted by government from the State Revenue Fund, as defined by the Public Finance Management Act, declined from 9,5 to 8,5 per cent on 1 January 2011.

The *official rate of interest* applicable to fringe benefit taxation, as defined in the Income Tax Act, declined from 7,0 to 6,5 per cent on 1 March 2011.

Box 2: Rising popularity of RSA retail bonds

Government unveilled RSA retail bonds in May 2004 to encourage South African citizens to save. These government bonds are easily accessible through various distribution channels, including certain retail shops, the Post Office and over the Internet. Offering competitive interest rates, RSA retail bonds have proven to be quite successful, particularly in the past two years, with an amount of R3,2 billion being raised in the 2009 calendar year, followed by R4,9 billion in 2010.

Outstanding amount of South African retail bonds



The retail bonds are offered in two different types, (i) nominal fixed-rate and (ii) inflation-linked bonds; each type is available with three initial maturities. The yields on these retail bonds are shown in the accompanying table.

Yields on South African retail bonds

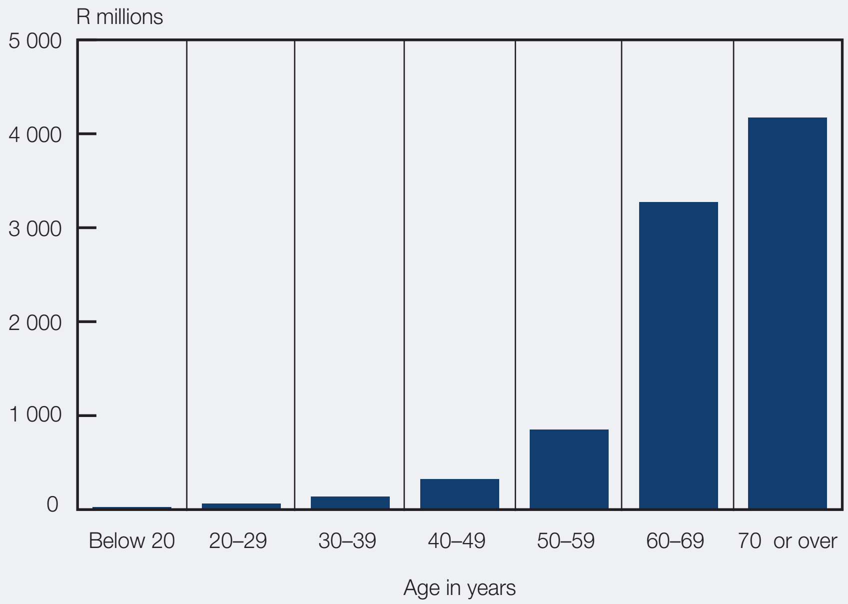
March 2011

Initial maturity	Yield* (per cent)
Nominal fixed-rate bonds	
2-year	7,25
3-year	7,50
5-year	8,00
Inflation-linked bonds	
3-year	2,00
5-year	2,25
10-year	2,75

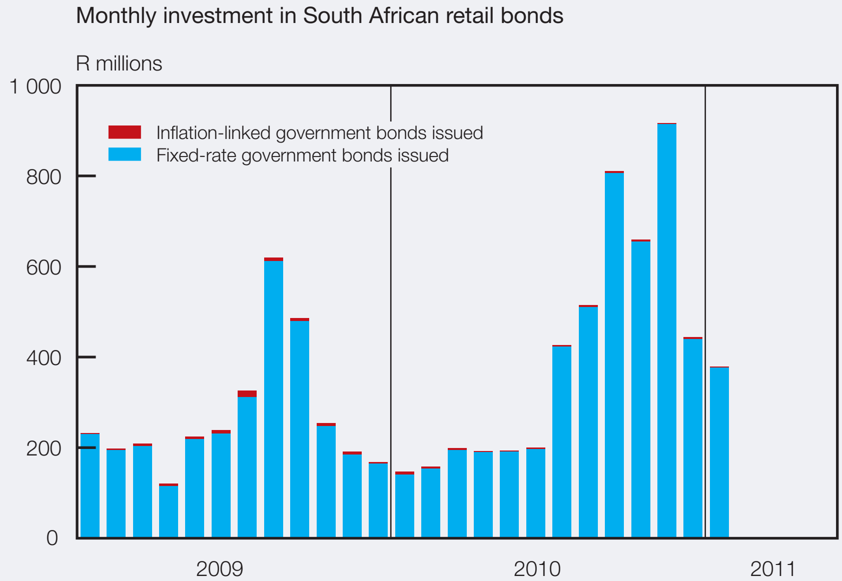
Source: National Treasury
* Yield on new issues

Fixed-rate retail bonds earn a market-related fixed coupon rate, which is priced off the current government bond yield curve. Inflation-linked retail bonds are adjusted for inflation, resetting nominal values semi-annually over the term of the bond.

Amount invested in South African retail bonds by age of investor, February 2011



The accompanying graph shows how holdings of RSA retail bonds are distributed according to the age group of investors. People of pensionable age form the largest investor category in RSA retail bonds. People older than 70 years hold almost half of the overall amount of RSA retail bonds in issue, with people aged from 60 to 69 not far behind them. Together these senior citizens held R7,4 billion in such bonds in February 2011, while persons in their fifties held R0,9 billion. Adults below the age of 50 held R526 million while the youth (aged below 20 years) held R27 million worth of retail bonds. Conservative elderly people interested in a low-risk instrument offering fair returns, form the core market for RSA retail bonds.



The issuance ratio between fixed-rate and inflation-linked bonds in 2010 was around 32:1. After increasing from R165 million in January 2010, the issuance of RSA retail bonds peaked at R914 million in November 2010 – the highest ever in a single month – before receding to R379 million in January 2011. The recent issuance was mainly in the 2-year fixed-rate bond.

Internationally and locally, capital market yields trended lower in the first ten months of 2010, but subsequently reversed course as inflation expectations worsened.

The daily average *yield on the R157 government bond* (maturing in the years 2014/15/16) fluctuated lower from a recent high of 8,61 per cent on 12 January 2010 to 6,92 per cent on 5 November, following the appreciation in the exchange value of the rand, the release of better-than-expected consumer inflation data, the lowering of the repurchase rate and firm demand for local bonds by non-residents. Subsequently, the bond yield rose to 7,87 per cent on 10 March 2011, in response to, among other things, the depreciation in the exchange value of the rand and the spillover of risk aversion emanating from the political turmoil in a number of countries in North Africa and the Middle East. Similarly, the daily closing yield on US government 5-year bonds declined from a high of 2,72 per cent on 5 April 2010 to 1,02 per cent on 4 November, before increasing to 2,11 per cent on 10 March 2011. The resultant spread between the South African R157 bond yield and the US 5-year bond yield narrowed from 611 basis points on 12 January 2010 to 576 basis points on 10 March 2011.

While yields at the short end of the *yield curve* tracked the movements in the repurchase rate, the medium to long end of the curve first moved lower from January 2010 to September, before increasing to 10 March 2011, following inflation concerns arising from the depreciation in the exchange value of the rand and the increasing commodity prices. The *yield gap*[6] widened from 187 basis points on 15 September 2010 to 378 basis points on 10 March 2011.

The *break-even inflation rate*[7] recorded its highest level for 2010 on 12 January when it reached 6,48 per cent, but subsequently fluctuated lower to 4,90 per cent on 5 November. It thereafter started rising and came to 5,72 per cent on 10 March 2011, indicating a worsening of inflation expectations as nominal yields on conventional government bonds increased while real yields on inflation-linked government bonds declined.

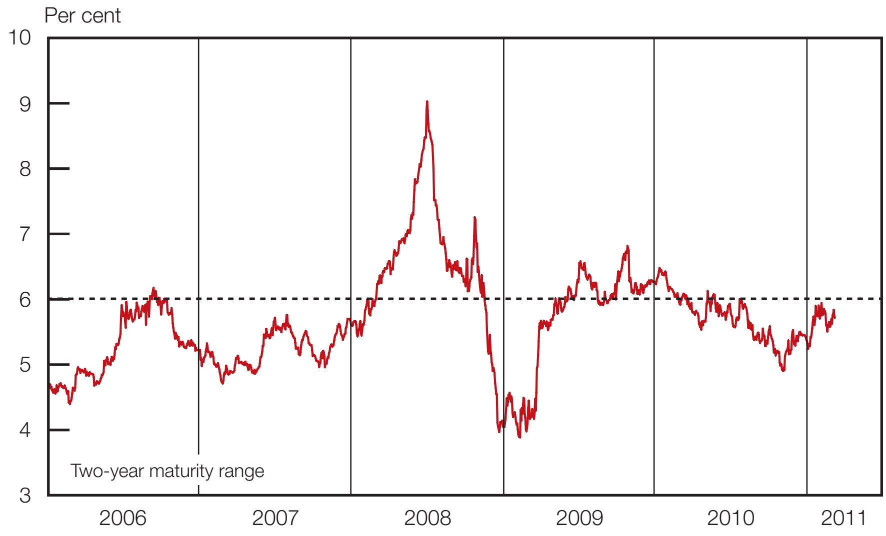
The *currency risk premium*[8] on South African government bonds narrowed from 423 basis points in November 2010 to 388 basis points in February 2011, as the yield on the dollar-denominated bond increased more than the yield on the domestic rand-denominated bond.

6 The differential between the yields at the extreme long and short ends of the curve.

7 The differential between the nominal yield on conventional government bonds and the real yield on inflation-linked government bonds within the two-year maturity range.

8 The differential between South African government bond yields on rand-denominated debt issued in the domestic market and on dollar-denominated debt issued in the US in the six-year maturity range.

Break-even inflation rate

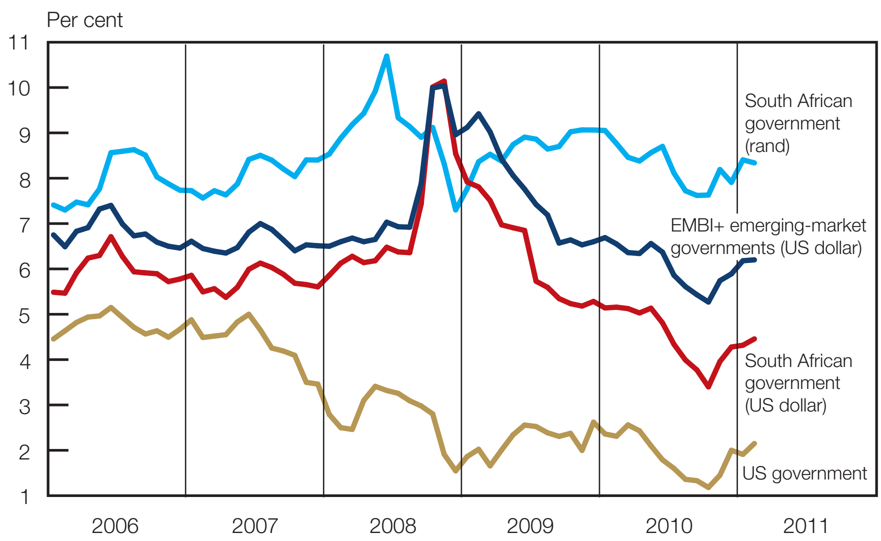


The JPMorgan Emerging Markets Bond Index Plus (EMBI+)[9] yield spread had been volatile in recent months. It narrowed from a recent high of 337 basis points in June 2010 to 245 basis points in October, before widening to 272 basis points in February 2011, on increased risk aversion towards emerging markets. Similarly, the *sovereign risk premium*[10] on the South African government US dollar-denominated bonds in the six-year maturity range trading in international markets narrowed from a high of 224 basis points in June 2010 to 154 basis points in December, before widening to 195 basis points in February 2011.

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

10 Premium above the yield on US government bonds that are denominated in US dollar.

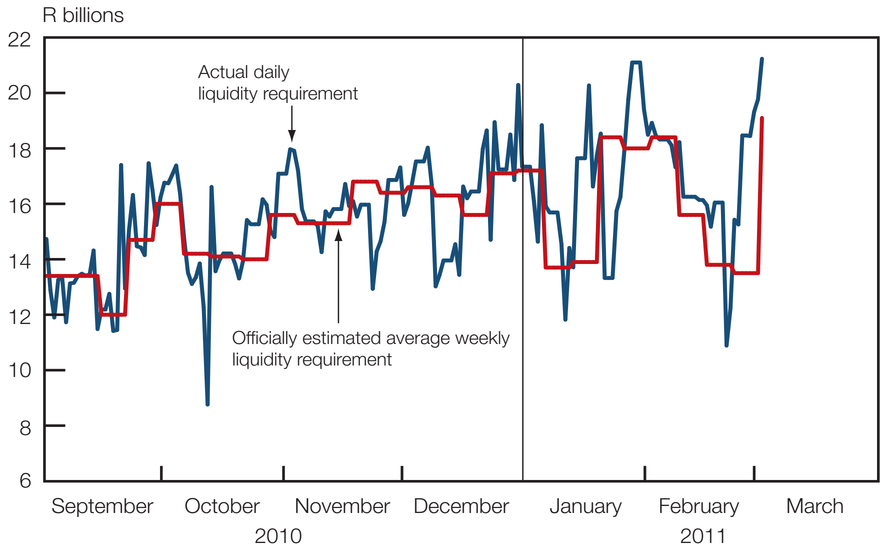
Government bond yields



Money market

During the fourth quarter of 2010, conditions in the money market tightened somewhat, reflected in the higher liquidity requirement experienced during that period. The daily liquidity requirement of private-sector banks occasionally registered values far removed from the estimated weekly liquidity requirement, and fluctuated between a minimum of R18,5 billion and a maximum of R20,3 billion during the fourth quarter of 2010, compared with a range of between R6,2 billion and R17,1 billion recorded during the third quarter. The liquidity provided by the Bank at the weekly main refinancing auctions also increased, on balance, from a low of R6,7 billion recorded during the first quarter of 2010 to a high of R18,8 billion during the fourth quarter. The prevailing level of the money-market shortage was in line with the changes implemented during the third quarter of 2010, which aim to improve the efficacy of the monetary policy operational procedures.

Liquidity requirement



During the fourth quarter of 2010, liquidity to the net amount of R1,3 billion was drained from the money market, compared with a more substantial net drainage of R5,9 billion recorded in the third quarter. Notes and coin in circulation, and required cash reserve deposits, jointly drained liquidity to the value of R7,7 billion from the money market, with the bulk of this amount emanating from notes and coin in circulation due to the seasonal increase in demand for cash over the festive season. The drainage was mainly counter-balanced by the use of liquidity management instruments and the Bank's foreign-exchange transactions, which respectively injected liquidity amounting to R5,8 billion and R1,4 billion.

Money-market liquidity flows

R billions (easing + tightening –)

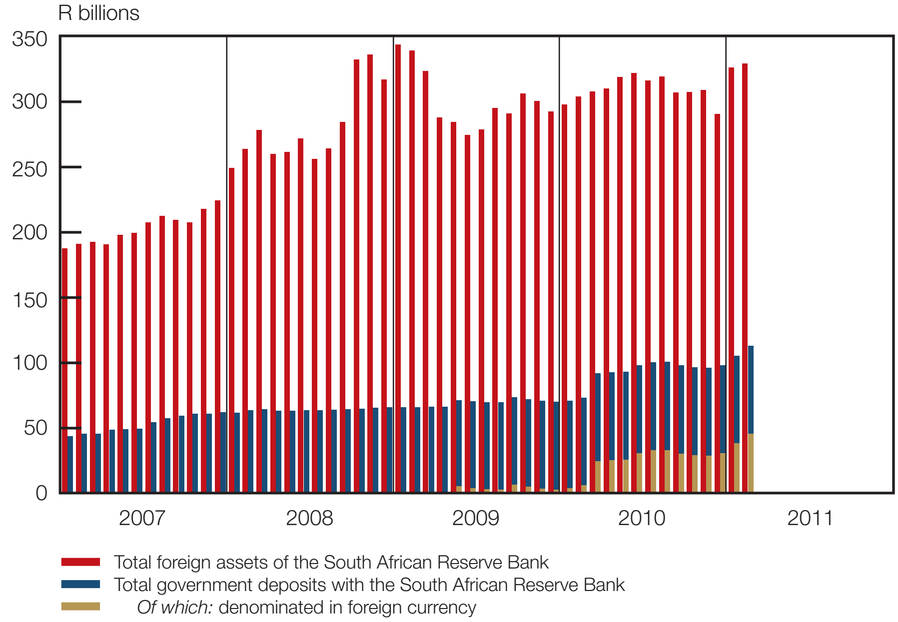
	2010	
	3rd qr	4th qr
Notes and coin in circulation	-1,4	-7,4
Required cash reserve deposits	-1,2	-0,3
Money-market effect of SARB* foreign-exchange transactions	4,6	1,4
Government deposits with the SARB	0,1	0,1
Use of liquidity management instruments	-5,0	5,8
Reverse repurchase transactions	-5,0	1,9
SARB debentures	0,0	3,9
Other items net	-3,0	-0,9
Banks' liquidity requirement (decrease + increase –)	**-5,9**	**-1,3**

* South African Reserve Bank

The decline in the money-market effect of the Bank's foreign-exchange transactions coincided with a significant decline of R16,6 billion in the Bank's foreign-exchange reserves in the fourth quarter of 2010, primarily due to an appreciation in the exchange value of the rand. At the same time, government deposits with the Bank edged lower in the fourth quarter of 2010 after they had increased significantly from the first quarter of 2010, mainly on account of a sharp rise in foreign-currency deposits. In January and February 2011 government deposits with the Bank resumed an upward trend.

Coupon interest payments on various government bonds amounting to R14,0 billion were effected from the government tax and loan account during the fourth quarter of 2010, with only R0,1 billion of this amount accruing to the Bank.

Foreign reserves and government deposits



Bond market

The increase in the total *outstanding nominal value of debt securities listed* on the JSE Limited (JSE) amounted to R187 billion in 2010 compared with R118 billion recorded in 2009. This primarily reflected the continued higher demand for funds by public-sector borrowers, whose net issues of R113 billion in 2009 rose significantly to R175 billion in 2010. In the first two months of 2011 the nominal value of public-sector bonds listed increased by R23,9 billion.

Driven by net issues of banks, the outstanding nominal value of private-sector loan stock listed on the JSE rose by R14,9 billion in 2010, while funding through commercial paper declined by R3,7 billion.

The buoyancy of issuances in the bond market continued into the first two months of 2011, adding a net total of R25,8 billion in the primary bond market to bring the total outstanding nominal amount to R1,2 trillion for this market at the end of February 2011.

Public corporations raised funds in the *international bond markets* in January 2011 for the first time since March 2006 when Eskom issued a US$1,75 billion ten-year bond. In March 2011 National Treasury issued a US$750 million 30-year bond with a coupon rate of 6,25 per cent at a spread of 180 basis points over equivalent US Treasuries.

Redemptions of rand-denominated bonds exceeded the issuances in both the *Japanese Uridashi and European bond markets* during 2010, as shown in the accompanying table. However, in the first two months of 2011 gross issuances of R6,8 billion in both markets exceeded redemptions by R2,4 billion.

Rand-denominated bonds issued in international bond markets

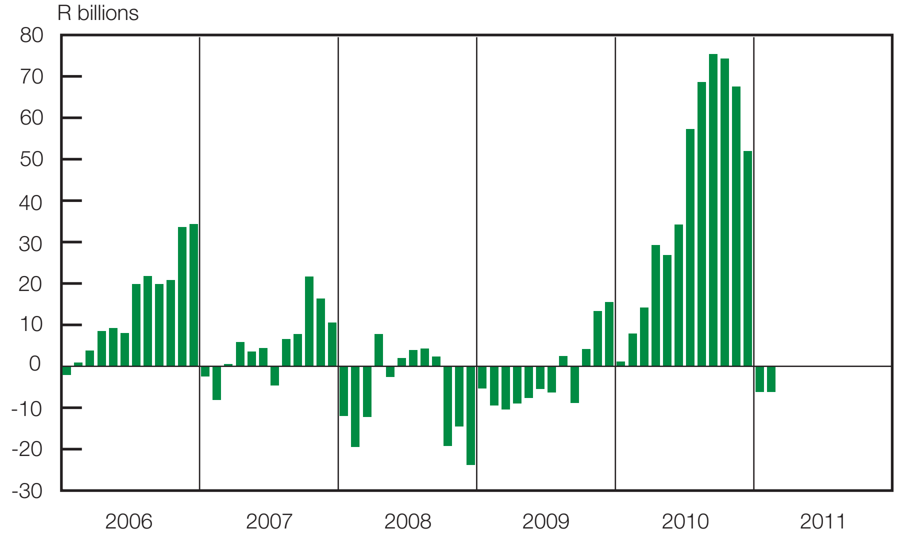
R millions

	Eurorand		Uridashi		Total	
	2010	Jan–Feb 2011	2010	Jan–Feb 2011	2010	Jan–Feb 2011
Issues	7 151	4 775	17 643	1 989	24 794	6 764
Redemptions	21 503	1 650	26 326	2 728	47 829	4 378
Net	-14 352	3 125	-8 683	-739	-23 035	2 386

Turnover in the domestic secondary bond market amounted to R18,6 trillion in 2010, some 25 per cent more than in 2009, reflecting higher bond prices and volumes traded. This trend was also exhibited in the daily average value traded, which increased by 17 per cent from R63,0 billion to R73,7 billion over the same period. In the first two months of 2011 daily turnover averaged R87,5 billion.

Non-residents have consistently been net sellers of South African debt securities from October 2010. They reduced their holdings of domestic bonds by R23,4 billion during the final quarter of 2010, following some profit-taking. Further net sales of local debt securities by non-residents to the value of R6,2 billion were recorded during the first two months of 2011, as investor risk appetite receded alongside the emergence of the political unrest in the MENA region. Non-residents' net accumulation of domestic listed bonds, however, amounted to an all-time annual high of R52,0 billion in 2010, compared with net purchases of R15,5 billion in 2009. Their trading activity in the secondary bond market, measured as their purchases and sales as a percentage of the total value of bonds traded on the JSE, increased slightly from 12 per cent in 2009 to 13 per cent in 2010.

Annual cumulative net purchases of bonds by non-residents



Share market

Total *equity capital raised* in the domestic and international primary share markets by companies listed on the JSE amounted to R80,9 billion in 2010, some 24 per cent less than the R107 billion raised in 2009 and 5 per cent more than the R76,7 billion raised in 2008. The resources sector was the main contributor to the capital-raising activity in 2010 at 49 per cent, followed by the financial sector contribution of 34 per cent. In 2010 capital was mainly raised through the waiver of pre-emptive rights to the amount of R43,3 billion and rights issues of R20,2 billion. Equity financing amounted to R35,7 billion in the first two months of 2011.

In February 2011 the JSE launched the Black Economic Empowerment (BEE) Board, offering a facility where only BEE-compliant parties will be able to list and trade BEE scheme shares. One BEE share scheme was listed in February 2011. Changes in the *number of companies listed* on the JSE are shown in the following table, indicating that in the past two years delistings exceeded new listings.

Number of listings on the JSE

	Alt^X	Venture and Development Capital boards	Main board	Africa board	BEE board	Total
December 2008	77	13	335	...	...	425
December 2009	76	12	321	1	...	410
December 2010	68	9	328	2	...	407
February 2011	68	9	326	2	1	405

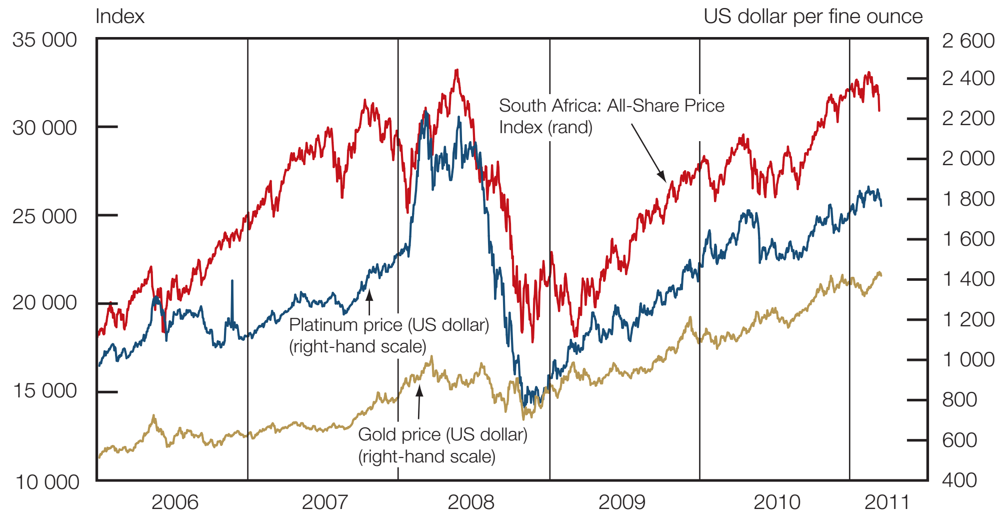
Although the number of shares traded was lower, the total *value of turnover* in the secondary share market in 2010 of R3,0 trillion was 7 per cent higher than the turnover recorded in 2009, lifted by higher share prices. Daily turnover averaged R11,7 billion in 2010 and R13,3 billion in the first two months of 2011. Turnover on Alt^X remained subdued during 2010 and amounted to only R1,3 billion – the lowest level in four years and 45 per cent below the already low turnover of R2,3 billion recorded in 2009. The total *market capitalisation* of the JSE increased by 17 per cent from R5,8 trillion in August 2010 to an all-time high level of R6,8 trillion in February 2011. In early 2011 share prices recovered to reach similar high levels attained in 2008. However, in the first two months of 2011 liquidity[11] amounted to 48 per cent, as opposed to the 72 per cent recorded in 2008, indicating less frenetic trading conditions notwithstanding the recovery in share prices.

11 The liquidity ratio on the JSE is calculated as annualised secondary market turnover of shares as a percentage of market capitalisation.

Non-residents' interest in domestic securities remained skewed towards the debt market for most of 2010. They accumulated only R36,4 billion worth of shares listed on the JSE in 2010, compared with high net purchases of R75,4 billion in 2009. Net share purchases of R16,9 billion in the fourth quarter of 2010, however, represented the highest quarterly net purchases in 2010, alongside a rally in domestic share prices. Non-residents were, however, net sellers of shares listed on the JSE to the value of R1,4 billion in the first two months of 2011. For 2010 as a whole, non-residents' participation rate, measured as their purchases and sales as a percentage of the total value of shares traded on the JSE, came to 16 per cent compared with 18 per cent in 2009.

Nervousness and volatility in share markets were evident during the first eight months of 2010, along with sovereign debt problems in some European countries. Subsequently, the

Share and commodity prices



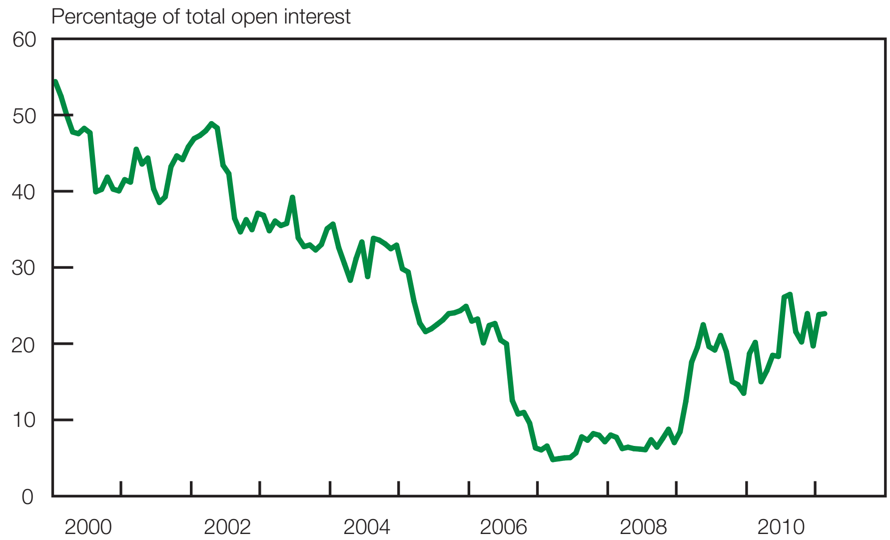
FTSE/JSE All-Share Price Index (Alsi) soared by 17 per cent from 25 August 2010 to an index value of 30 899 on 10 March 2011 – with a recent high of 33 094 index points reached on 14 February 2011. This was in line with higher commodity prices and the improvement in global equity markets as expectations increased for the success of action plans by various governments and designated lenders of last resort. This upward movement was especially supported by the performances of the local resources and industrial sectors. The Alsi, in US dollar terms, and the Standard & Poor's (S&P) 500 Composite Index rose by 24 and 23 per cent respectively over the same period.

As dividends declared in the past twelve months increased, the historical *dividend yield* on all classes of shares increased from 1,9 per cent in April 2010 to 2,4 per cent in February 2011. Similarly, the *earnings yield* increased from 5,2 per cent to 6,2 per cent over the same period. Conversely, the *price-earnings ratio* for all classes of shares declined from 19,2 in April 2010 to 16,3 in February 2011.

Market for exchange-traded derivatives

Turnover in *equity derivatives* on the JSE increased briskly in 2010 and was 15 per cent higher when compared with 2009, supported by the bullish underlying equity market along with the moderation in expected share price volatility, as indicated by the decline in the South African Volatility Index from an average of 29 per cent in 2009 to 25 per cent in 2010. However, the number of equity derivatives contracts traded on the Equity Derivatives Division of the JSE abated marginally to 160,5 million contracts in 2010 when compared with the 2009 volumes. Turnover increased in the first two months of 2011 when compared with the corresponding period of 2010. Over the past decade non-resident participation in the domestic equity derivatives market, in terms of open contracts, first declined sharply from an average of 46 per cent in 2000 to only 6 per cent in 2007, before rising to 20 per cent in 2010 and further to 24 per cent in the first two months of 2011.

Non-resident open interest in the equity derivatives market



In November 2010 the *interest rate derivatives market* of the JSE, Yield-X, extended its product range to include US Dollar/Rand Maxi Currency Futures Contracts aimed at enhancing trade on larger-size contracts. In December 2010 trade in the new Inflation Linked Index (IGOV) futures contract started. The latest addition was in February 2011 when the JSE added new Can-Do Dollar/Rand Currency Futures and Options Contracts.

Dominated by trade in currency futures and options contracts, the *Yield-X* market maintained relatively stable trading conditions in 2010, registering only a slight decline to 8,4 million contracts traded when compared with 2009. Turnover, however, increased by 84 per cent over the same period and remained brisk in the first two months of 2011.

Box 3: Recent developments in the commodity derivatives market

The formal commodities market has created an environment in which farmers, traders and other participants are able to react to market-related, transparent prices. Commodity futures and options are effectively a way of spreading risk and obtaining greater certainty regarding prices.

The Safex Agricultural Derivatives Division (the division) opened in January 1995 to facilitate trade in grain futures contracts. After soya bean contracts had been listed in April 2002, nearly seven years elapsed before several products were introduced to the commodity derivatives market.

The first such new product was launched in January 2009 when the JSE Limited (JSE) signed an agreement with the CME Group, that owns and operates large derivatives exchanges in the United States (US), to include the group's Chicago Board of Trade (CBOT) corn[1] futures. Subsequently, more foreign-referenced commodity futures followed as precious metal and energy products were added, namely gold, platinum and West Texas Intermediate (WTI) crude oil.

In September 2009 the division's name changed to the 'Commodity Derivatives Division' (CDD). In May 2010 the CDD reintroduced grade 2 white and yellow maize futures contracts for trade, and introduced soybean, soybean meal and soybean oil contracts based on CBOT settlement prices. The sweet sorghum futures contracts, with physical settlement as a feature, opened for trade in May 2010. The foreign-referenced commodities are cash-settled as opposed to the domestic physically settled commodities. In June 2010 new trading software enabled both commodity and equity derivative memberships to access a common set of products in a specialised global trading window. The latest product enhancements were in August 2010 when the JSE extended its licensing agreement with the CME Group to include rand-denominated copper and silver futures contracts to provide local investors with enhanced exposure to the international metals market.

The current list of commodities at the JSE is shown in the accompanying table.

Commodities listed on the JSE

Commodity	Date when trade commenced	Settlement	Commodity type	Volume traded in the first two months of 2011 (actual number of contracts)
White maize	March 1996	P	Agricultural	200 244
Yellow maize	March 1996	P	Agricultural	57 796
Wheat	November 1997	P	Agricultural	88 805
Sunflower seeds	February 1999	P	Agricultural	19 243
Soya beans	April 2002	P	Agricultural	29 171
Sweet sorghum	May 2010	P	Agricultural	28
Corn	January 2009	C	Agricultural	17 823
Gold	October 2009	C	Metal*	440
Platinum	October 2009	C	Metal*	98
WTI crude oil	October 2009	C	Energy*	3 322
Soybean	May 2010	C	Agricultural	109
Soybean meal	May 2010	C	Agricultural	18
Soybean oil	May 2010	C	Agricultural	2
Copper	August 2010	C	Metal*	203
Silver	August 2010	C	Metal*	414

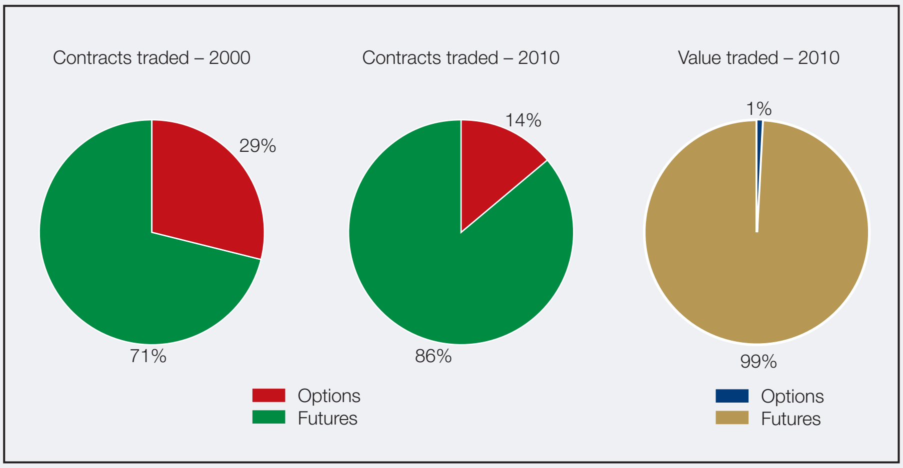
P – Physical C – Cash
* Global market

An *option* contract gives the holder the right, but not the obligation, to buy or sell an underlying instrument at an agreed price. Options are described as either puts or calls and are said to be European style when the contract can only be exercised at the end of the life, while American-style options can be exercised at any time before expiry, as is the case on the JSE. Options on agricultural futures contracts were introduced on the JSE in March 1998. Over the past decade, the contribution of trade in option contracts to the total number of contracts traded declined from 29 to 14 per cent, while the value of option contracts traded continued to contribute only 1 per cent to total turnover over this period. At

1 "Corn" in the US is the same product as "maize" in South Africa.

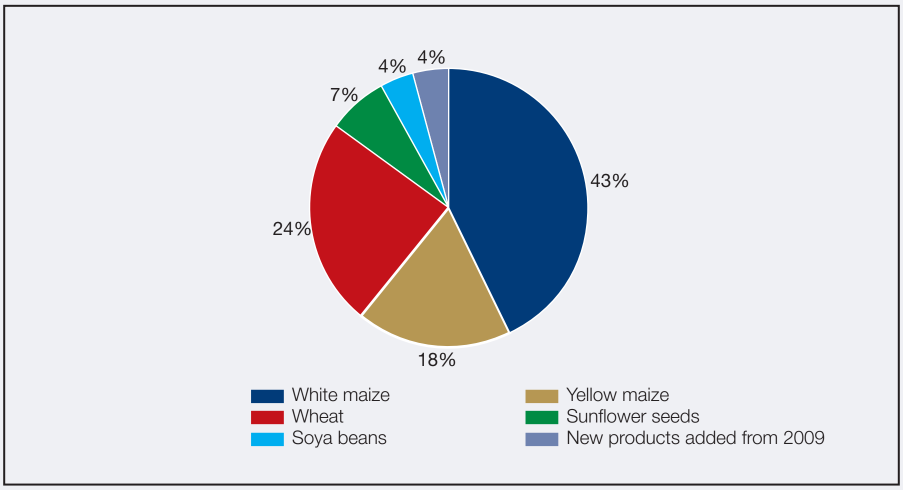
present, options are only traded in respect of white maize, yellow maize, wheat, sunflower seeds, soya beans, sweet sorghum and the foreign-referenced corn.

Contribution to number of contracts and value traded



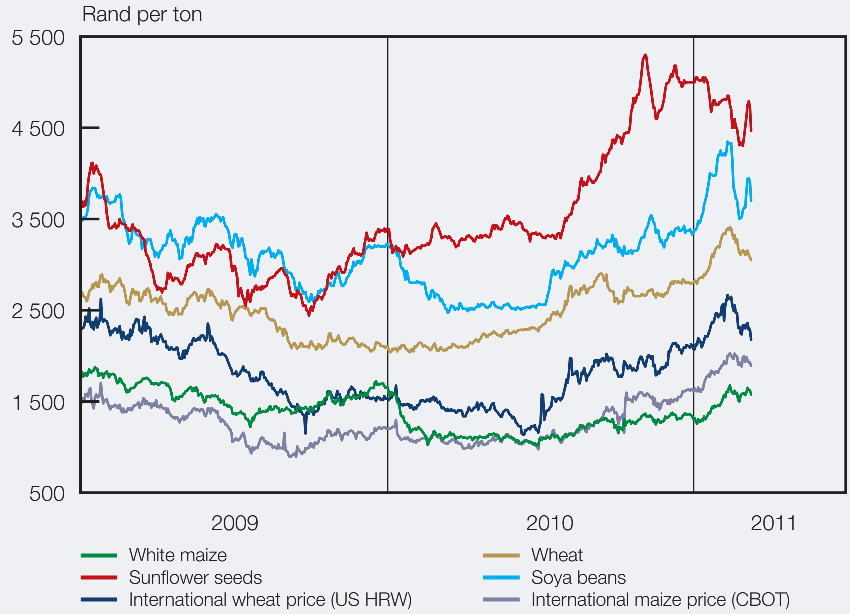
The value traded of the various commodities differs considerably. In 2010 trade in white maize contracts contributed the largest share of 43 per cent to total turnover, followed by wheat contracts at 24 per cent.

Contribution to value traded, 2010



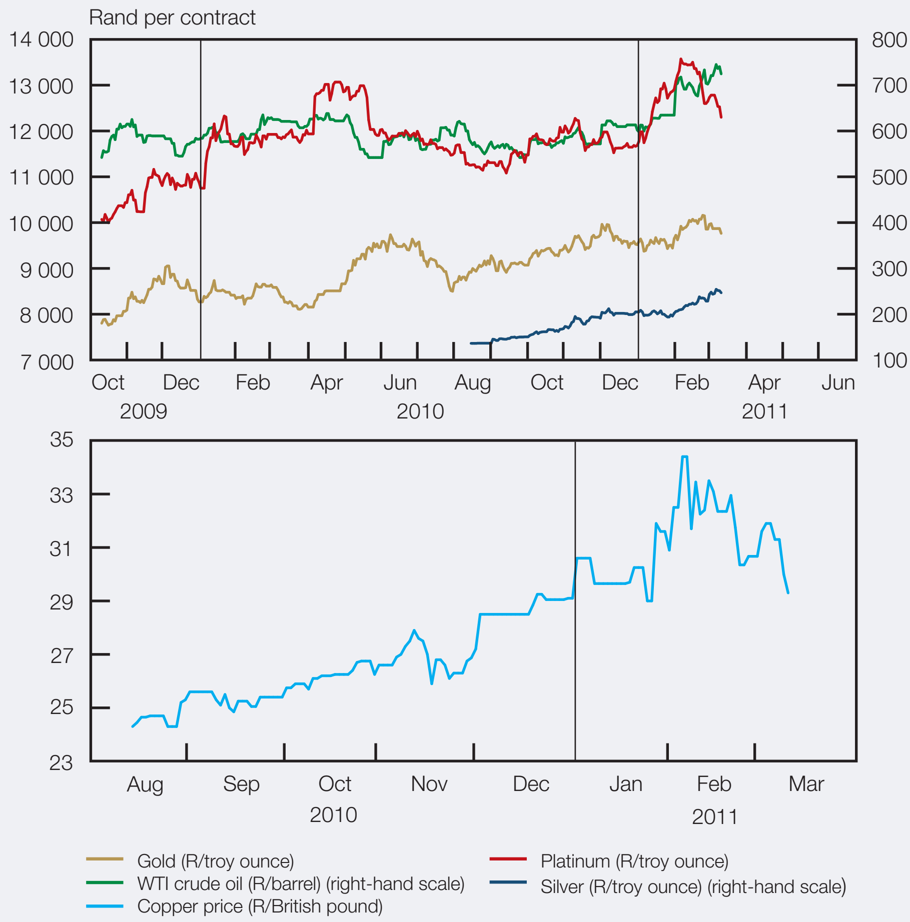
Although the number of commodity derivative contracts traded increased by 12 per cent from 2009 to 2010, the value traded declined by 2 per cent, as most commodity prices were, on average, lower. Domestic commodity prices, however, started to move higher during the second half of 2010 alongside higher international commodity prices. This upward trend in the prices of most domestic commodities intensified in early 2011, as the depreciation in the exchange value of the rand and higher international oil prices, together with the already rising international commodity prices, added upward pressure. This increase in prices may affect inflation, particularly food inflation, negatively in the future.

Agricultural commodity prices



Prices of near-term contracts

Metal and energy commodity prices



Prices of near-term contracts

Consistent with the lower number of *warrants* listed, demand was frail in this market segment during 2010, despite the noticeable recovery in the underlying share market. Some 70 per cent of total warrants traded in 2010 related to the resources sector. Turnover in all derivatives traded on the JSE during the first two months of 2011 is indicated in the accompanying table.

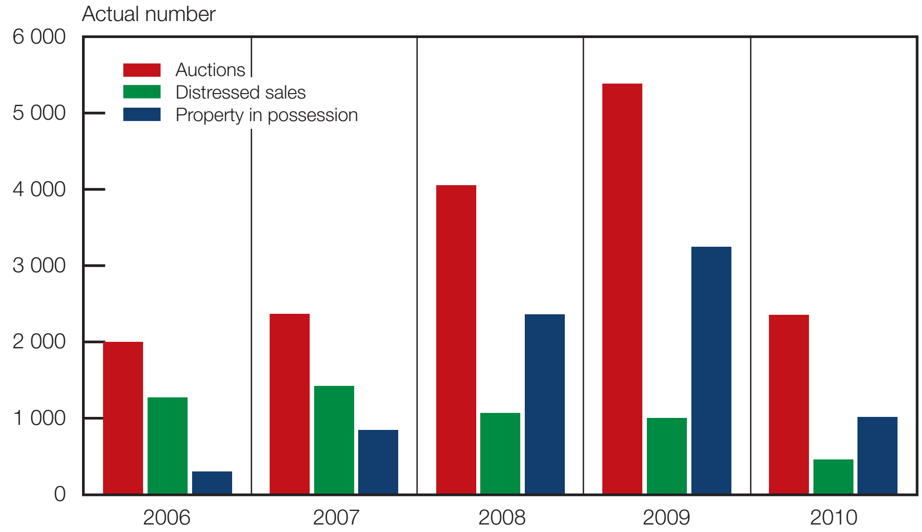
Derivatives turnover on the JSE, January to February 2011

	Value (R billions)	Change over one year (per cent)
Equity futures and options on futures	466	16
Warrants	0,2	-53
Commodity futures and options	54	47
Interest rate derivatives	62	69

Real-estate market

The issuing of a sale in execution notice can lead to forced sales in the real-estate market. All three outcomes of forced sales, namely auctions, distressed sales and property in possession declined in 2010 compared with 2009, indicating some improvement in the risk environment for banks.

Forced sales in the real-estate market

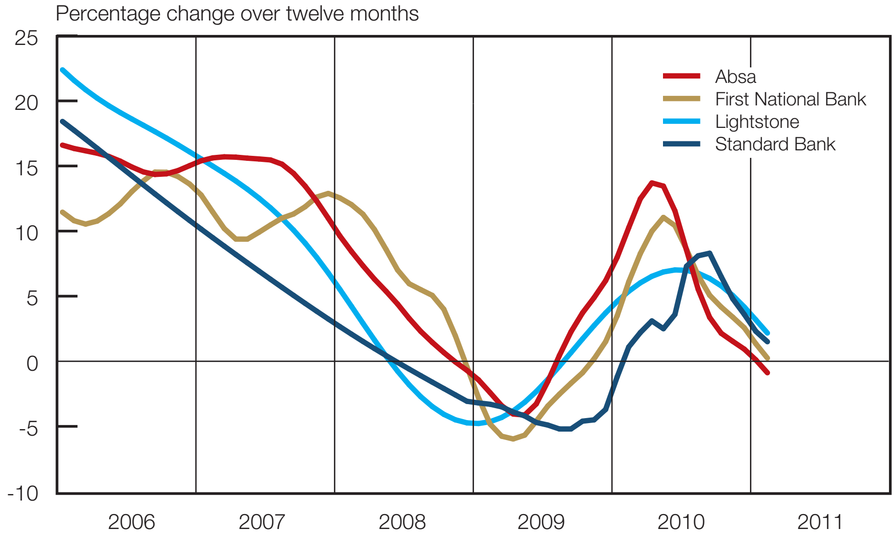


Source: Lightstone

Notwithstanding the low interest rate environment, the lower forced sales levels could possibly be attributable to the weak residential property demand, since the lacklustre purchasing activity in this market remained reflective of the current household financial discomfort.

The year-on-year rate of change in the average price of residential property in the middle segment of the market, as measured by Absa, slowed from a rate of change of 13,7 per cent in April 2010 to a negative 0,9 per cent in February 2011. Similarly, the year-on-year rate of change in First National Bank's average house price of 0,2 per cent in February 2011 was much slower than the 11,0 per cent recorded in May 2010. The median house price of Standard Bank also lost momentum on a year-on-year basis from 8,3 per cent in September 2010 to 1,5 per cent in February 2011. The extended repeat sales house price index of Lightstone also decelerated on a year-on-year basis from 7,0 per cent in June 2010 to 2,2 per cent in February 2011.

House prices



Non-bank financial intermediaries

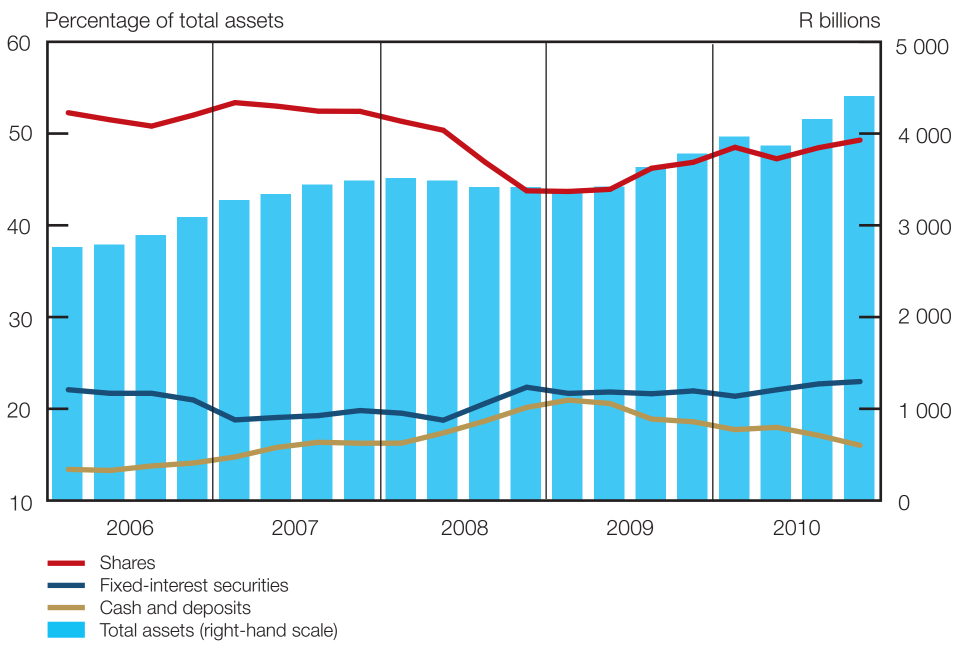
Activity of the non-bank financial institutions[12] was influenced by increasing asset prices, notably equity prices, in line with the anticipated rebound in domestic economic activity and declining bond yields. The balance sheet of these intermediaries increased to an all-time high of R4,4 trillion at the end of 2010, representing growth rates of about 29 per cent and 17 per cent from 2008 and 2009 respectively.

Holdings of ordinary shares by these institutions increased from 47 per cent of total assets in the fourth quarter of 2009 to 49 per cent in the final quarter of 2010 – this was some 1 percentage point higher than the ten-year average. The reallocation of assets into ordinary shares was bolstered by, among other things, a general moderation in the level of risk aversion in the financial markets and an increase in equity prices.

The percentage of assets invested by the non-bank financial intermediaries in fixed-interest securities increased from 22 per cent of the total balance sheet in the fourth quarter of

12 Defined as unit trusts, insurers and pension and provident funds.

Asset holdings of selected non-bank financial intermediaries



2009 to 23 per cent in the final quarter of 2010. Meanwhile, holdings of public corporations' bonds by these intermediaries grew to 4 per cent of total assets over the same period. The increased appetite for bonds issued by state-owned enterprises could be attributed to the improved liquidity of these bonds and relatively high yields offered when compared with those of conventional government bonds.

The proportion of funds invested in cash and cash equivalents has been on a gradual decline since the first quarter of 2009. As a ratio of total assets, holdings of cash and cash equivalents fell from 19 per cent of total assets in 2009 to 16 per cent in 2010. The reallocation out of cash reflects an improvement in investors' sentiment and optimism about the economy. Inflows[13] to non-bank financial intermediaries grew by 9 per cent from R403 billion in 2009 to R440 billion in 2010.

13 Consist of net sales of unit trusts, premiums of insurers and contributions of pension and provident funds.

The National Treasury released a final draft Regulation 28 of the Pension Funds Act, which prescribes investment limits for pension funds. The changes in the regulation, which will be effective from 1 July 2011, aim, among other things, to ensure that pension fund members' investments are not overly exposed to high-risk investment strategies, to review investment in alternative asset classes such as hedge and private equity funds which are not explicitly catered for in the current regulation, and to ensure that all retirement products, including retirement annuity funds, are Regulation 28-compliant at both member and fund level. The proposed changes in foreign investment limits for retirement funds, long-term insurers and collective investment schemes will allow for an additional R220 billion for offshore investment purposes.

Revised foreign investment limits for institutional investors

Percentage of total assets

	2008	2010
Retirement funds	20	25
Collective investment schemes	30	35
Investment managers	30	35
Long-term insurers (investment-linked)	30	35
Long-term insurers (non-investment linked)	20	25

Public finance

Non-financial public-sector borrowing requirement[14]

The financial activities of the *non-financial public sector* resulted in a cash deficit of R46,5 billion in the third quarter of fiscal 2010/11, in comparison to a cash deficit of R61,8 billion in the same period a year earlier. This brought the cash deficit of the non-financial public sector in April–December 2010 to R129 billion, or R60,7 billion lower than in the first nine months of fiscal 2009/10. The smaller borrowing requirement stemmed mainly from a lower cash-book deficit recorded by non-financial public enterprises and corporations and a surplus recorded by provincial governments.

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

As a ratio of gross domestic product, the non-financial public-sector borrowing requirement amounted to 6,3 per cent for the first nine months of the current fiscal year, compared with a borrowing requirement ratio of 10,5 per cent in the corresponding period of the previous fiscal year. Financial activities at various levels of the non-financial public sector are summarised in the accompanying table.

Non-financial public-sector borrowing requirement

R billions

Level of government	Apr–Dec 2009*	Apr–Dec 2010*
Consolidated general government	123,6	98,4
National government	118,4	112,1
Extra-budgetary institutions	-5,1	-0,8
Social security funds	-10,2	-7,2
Provincial governments	5,7	-9,8
Local governments	14,7	4,1
Non-financial public enterprises and corporations	66,3	30,8
Total	189,9**	129,2**
As a percentage of gross domestic product	*10,5*	*6,3*

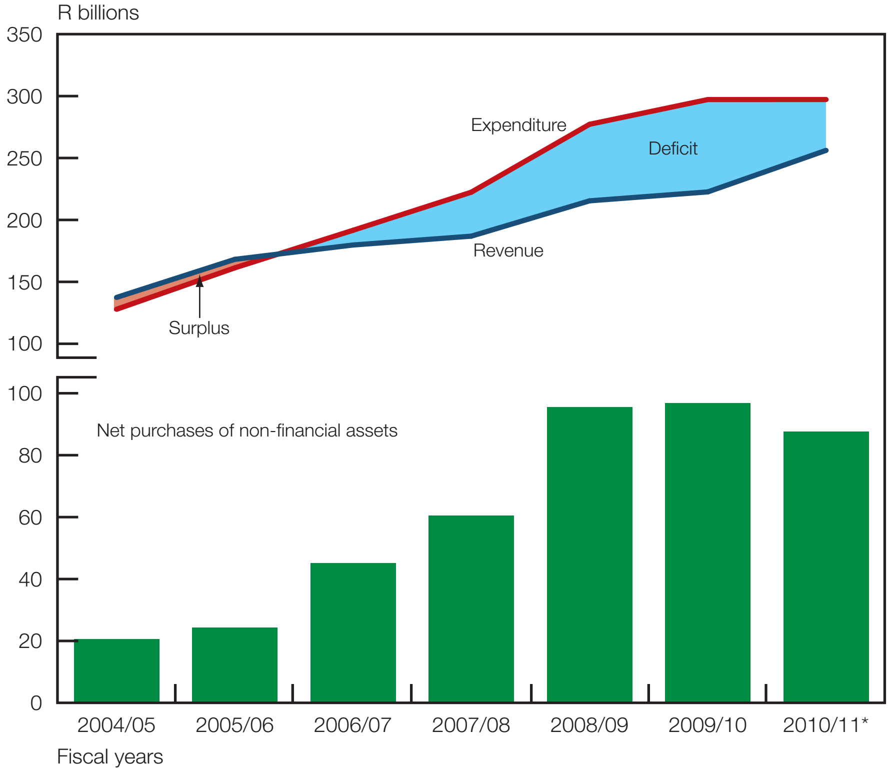
* Deficit + surplus –
** Components may not add up to totals due to rounding

Amid a gradual recovery in the domestic economic activity, the preliminary cash deficit of *non-financial public enterprises and* corporations improved significantly during April–December 2010. The cash deficit amounted to R30,8 billion when compared with a cash deficit of R66,3 billion recorded in the corresponding period a year earlier. Part of the reason for the smaller deficit was the higher prices charged by key institutions. Net investment in non-financial assets also declined to R65,5 billion in April–December 2010, lower than the net investment of R77,7 billion recorded in April–December 2009.

An analysis of *national government* statistics showed that with improved tax collections, cash receipts from operating activities rose to R485 billion in the first nine months of fiscal 2010/11, representing a year-on-year growth rate of 11,5 per cent when compared with the corresponding period a year earlier. On a similar basis, cash payments for operating activities increased by 8,1 per cent to amount to R593 billion. Net cash flow from operating activities of national government, together with net investment in non-financial assets, resulted in a cash deficit of R112 billion in April–December 2010. This was lower than the cash deficit recorded in the corresponding period a year earlier.

Provincial governments recorded a cash deficit of R4,1 billion in the third quarter of fiscal 2010/11, bringing their cash surplus for the first nine months of fiscal 2010/11 to R9,8 billion – a turnaround from the deficit recorded in the same period of the previous fiscal year. The *Medium Term Budget Policy Statement 2010 (MTBPS)* provided for a provincial cash surplus of R2,0 billion for fiscal 2010/11 as a whole.

Finances of non-financial public enterprises



* Annualised

Provincial revenue was predominantly spurred by grant transfers from national government and amounted to R252 billion during April–December 2010. Total provincial grants accounted for about 70 per cent of transfers paid by national government and comprised equitable share transfers of R199 billion and conditional grants of R46,7 billion. Together, these grants increased at a year-on-year rate of 14,0 per cent during the first nine months of fiscal 2010/11.

Higher provincial expenditure was driven by personnel costs, which amounted to R145 billion, or 59,8 per cent of total expenditure. Spending in this category was 15,3 per cent higher when compared with April–December 2009. This increase could largely be attributed to the agreed improvement in conditions of service, which provided for salary and housing allowance increases for non-senior management service officials that was implemented as from 5 November 2010, but backdated to 1 July 2010.

At the end of December 2010, the Gautrain project reached its seventeenth quarter and has been financed by contributions received from government and the private sector. During the first nine months of fiscal 2010/11, R2,8 billion was spent on this project. Including this amount, total provincial net investment in non-financial assets amounted to R17,0 billion after three quarters, or 18,4 per cent lower than in the corresponding period a year earlier. The *MTBPS 2010* forecasts provincial spending on non-financial assets and capital transfers to amount to R44,2 billion in fiscal 2010/11 as a whole.

The financial activities of provincial governments resulted in an increase in their bank deposits with private-sector banks from R8,6 billion at the end of March 2010 to R9,8 billion at the end of December. Deposits of provincial governments with the Corporation for Public Deposits (CPD) increased considerably from R0,2 billion to R5,3 billion between these dates, while their overall indebtedness to banks decreased from R2,1 billion to R0,7 billion over the same period.

Extra-budgetary institutions' cash surplus amounted to R0,8 billion in April–December 2010 – some R4,2 billion lower than the cash surplus recorded in the corresponding period a year earlier. Preliminary estimates show that the cash surplus of *social security funds* deteriorated moderately.

These funds recorded a cash surplus of R7,2 billion compared with a cash surplus of R10,2 billion in the same period a year earlier.

Preliminary data show that *local governments* recorded a cumulative cash deficit of R4,1 billion during the first nine months of the fiscal 2010/11, or R10,6 billion less than the cash deficit recorded in the same period a year earlier. Notwithstanding pronounced growth in operating expenses, this improvement can be attributed to a significant rise in municipal own revenue collections, alongside decreased infrastructure investment spending owing to completion of the 2010 FIFA World Cup™ tournament event. For the period under review, municipal own revenue collections amounted to R104 billion and accounted for 70,8 per cent of total local government revenue. This was R17,1 billion more than in April–December 2009.

From April to December 2010, net investment in non-financial assets by municipalities declined somewhat and amounted to R28,3 billion, or R3,8 billion less when compared with the corresponding period of the previous fiscal year. Over this period, municipalities showed strong commitment towards funding infrastructure investment through the domestic bond market. In the first nine months of fiscal 2010/11 the outstanding municipal marketable bond debt rose by R1,8 billion to a level of R11,6 billion at the end of December.

Budget comparable analysis of national government finance

National government expenditure in the first nine months of fiscal 2010/11 increased at a slower pace than the revised budgetary projections, while growth in revenue collections exceeded budgeted expectations, thus resulting in a lower cash-book deficit.

Expenditure by national government reached R585 billion in the first three quarters of fiscal 2010/11. This represented a year-on-year rate of increase of 10,2 per cent, which was lower than the initially budgeted increase of 11,8 per cent for the fiscal year as a whole. The rate of increase was also lower than the increase of 11,5 per cent projected in the *MTBPS 2010*.

National government expenditure amounted to 28,7 per cent of gross domestic product in April–December 2010, slightly lower than the ratio of 29,2 per cent recorded in the same nine months a year earlier.

Growth in spending was boosted by transfers and subsidies, along with current payments by some departments, while payments for capital assets actually contracted in April–December 2010. Higher expenditure on transfers and subsidies followed government's commitment towards improving the livelihood of the poor. Transfers and subsidies by the Department of Co-operative Governance and Traditional Affairs increased by 29,7 per cent during the period under review. The Municipal Infrastructure Grant, which supplements municipal capital budgets to eradicate infrastructure backlogs and build, repair and rehabilitate basic services contributed substantially towards this department's transfers and subsidies in the first nine months of fiscal 2010/11.

Transfers and subsidies by the Departments of Basic Education, and of Higher Education and Training rose by 32,6 per cent, following the introduction of the technical schools recapitalisation grant. The bulk of the Department of Social Development's spending is made up of transfers to households, which increased by 10,4 per cent. The Department of Social Development contributed 61,4 per cent to spending by the Social Services Cluster, which comprised mainly social security payments for old-age and child support grants.

Further contributions to national government spending stemmed from current payments made by the South African Police Service, which recorded an increase of 12,9 per cent in the first nine months of fiscal 2010/11.

The *Budget Review 2010* projected that payments for financial assets by national government would amount to R20,9 billion in fiscal 2010/11 as a whole, comprising mainly R20 billion[15] as the third tranche of a subordinated loan to Eskom. During the first nine months of fiscal 2010/11, Eskom received R15,0 billion of this amount from National Treasury.

15 This amount is not included in total expenditure in the Government Finance Statistics analysis.

Interest paid on national government debt amounted to R46,8 billion in the first three quarters of fiscal 2010/11, or 15,8 per cent more than in April–December 2009. This year-on-year increase in interest payments could be attributed to higher issuances of domestic government bonds to finance the deficit. Interest payments were originally budgeted to amount to R71,3 billion for fiscal 2010/11, but were revised downwards to R67,5 billion in the *MTBPS 2010* as a result of lower interest rates and net redemptions of foreign debt.

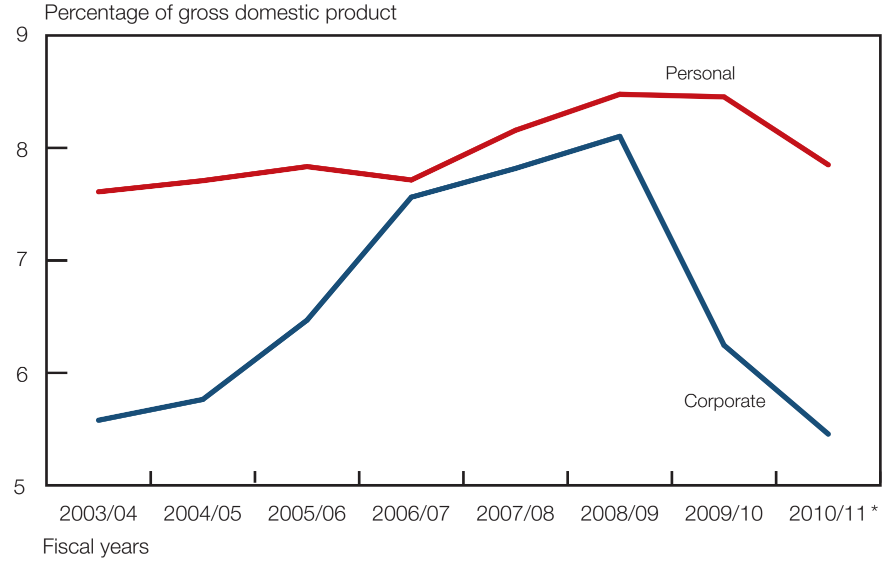
In the first nine months of fiscal 2010/11, equitable share transfers to provinces increased by 11,0 per cent compared with the corresponding period a year earlier, higher than the originally budgeted increase of 8,7 per cent. Growth in equitable share transfers to provinces reflected government's commitment to improve service delivery in the health and education sectors.

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

After taking into account cash-flow adjustments[16], national government's cash-flow expenditure equalled R593 billion in the first nine months of fiscal 2010/11 – 9,6 per cent higher than in the same period a year earlier.

National government revenue amounted to R472 billion in the first three quarters of fiscal 2010/11, representing a growth rate of 14,6 per cent when compared with the same period in the previous fiscal year. Receipts by national government were originally budgeted to rise by 11,0 per cent to total R643 billion in fiscal 2010/11. However, this amount was revised upwards in the *MTBPS 2010* to amount to R674 billion, a year-on-year rate of increase of 16,2 per cent. The upward revision of revenue reflected a positive turnaround following the global economic crisis, resulting in strong revenue growth across all major tax categories. As a ratio of gross domestic product, national government revenue amounted to 23,2 per cent in the first nine months of fiscal 2010/11, slightly lower than the ratio in the first three quarters of fiscal 2009/10.

Corporate and personal income tax collections



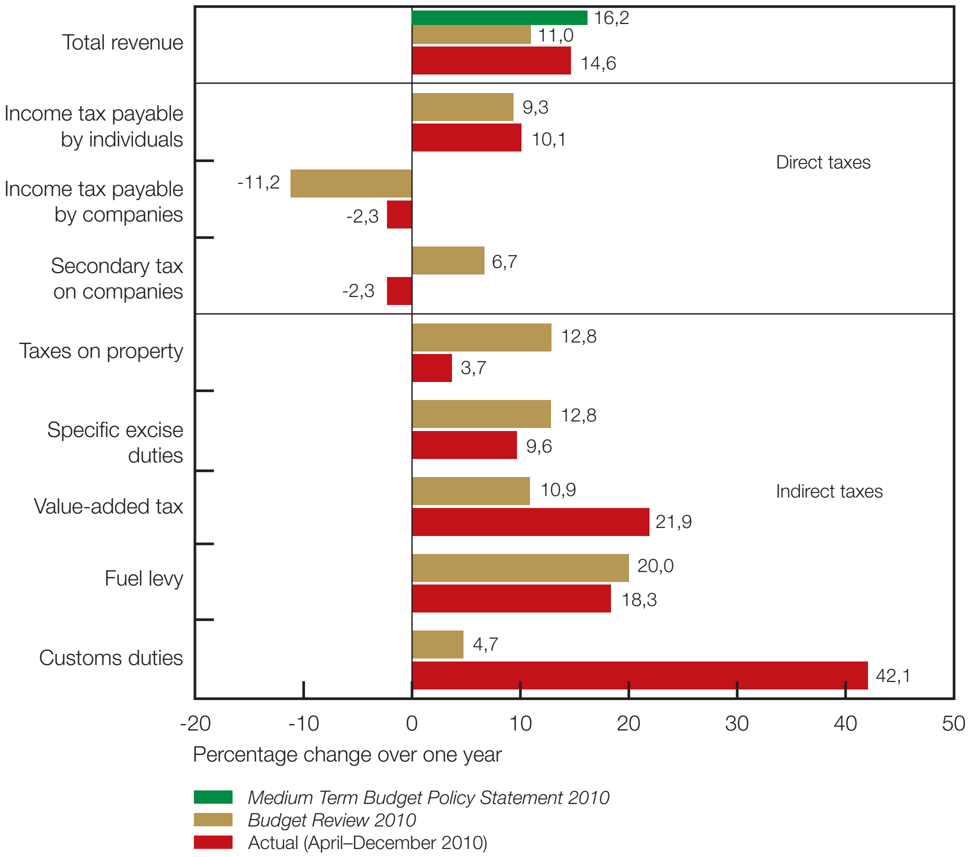
* April–December 2010

Collections from taxes on income, profits and capital gains increased at a rate of 4,6 per cent when compared with the corresponding period a year earlier. This increase was driven by moderate growth in personal income tax, despite a 2,3 per cent decline in corporate income tax collections. Lower assessment and provisional payments together with significantly higher refunds resulted in lower corporate income tax collections.

Receipts from taxes on property increased by 3,7 per cent in April–December 2010, reflecting the slow recovery in real-estate market activity. Taxes on goods and services recorded brisk growth, due to significantly higher collections of value-added tax (VAT) and fuel levy. Firm growth in consumer spending and lower VAT refunds contributed to the buoyant VAT collections. VAT refunds decreased by 7,4 per cent and stemmed from lower capital investment, mainly in the metal sectors, and from lower claims from VAT vendors.

Taxes on international trade and transactions increased significantly due to a substantial rise in customs duties. The robust growth in customs duties resulted from strong growth in vehicle imports on account of an upswing in household consumption expenditure.

National government revenue in 2010/11



In the first nine months of fiscal 2010/11, an amount of R14,2 billion in *SACU* payments was paid to Botswana, Lesotho, Namibia and Swaziland. Included in this total was an additional payment of R2,9 billion pertaining to adjustments made in respect of fiscal 2006/07 and 2007/08.

The net result of national government revenue and expenditure was a cash-book deficit before borrowing and debt repayment of R113 billion for the first nine months of fiscal 2010/11. This was R6,1 billion lower than the cash-book deficit recorded in the corresponding period of fiscal 2009/10. Strong growth in revenue collections and slower growth in expenditure resulted in a lower deficit. The *Budget Review 2010* projected a national government cash-book deficit of R154 billion for fiscal 2010/11 as a whole. However, in the *MTBPS 2010* the cash-book deficit was revised downwards to amount to R121 billion as national government revenue was expected to increase faster and expenditure was projected to slow towards the end of fiscal 2010/11.

The primary balance[17] reached a deficit of R66,3 billion – or 3,3 per cent of gross domestic product – in the first nine months of fiscal 2010/11. This may be measured against a primary deficit of R78,8 billion, or 4,3 per cent of gross domestic product recorded in the corresponding period of fiscal 2009/10. Improved revenue collections and slower growth in expenditure contributed to the narrowing of the primary deficit.

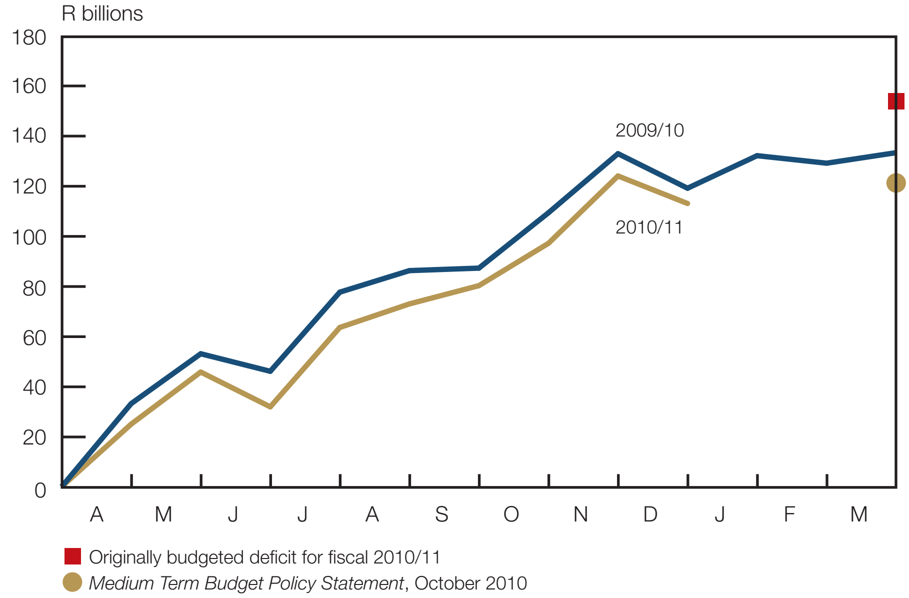
17 The deficit/surplus recalculated by excluding interest payments from total expenditure.

National government revenue in fiscal 2010/11

Revenue source	Originally budgeted		Actual Apr–Dec 2010	
	R billions	Percentage change*	R billions	Percentage change*
Taxes on income, profits and capital gains	377,7	5,2	271,0	4,6
Income tax on individuals	225,8	9,3	159,9	10,1
Income tax on companies	152,0	-0,4	111,1	-2,3
Payroll taxes	8,4	7,9	6,2	7,5
Taxes on property	10,0	12,8	6,8	3,7
Taxes on goods and services	230,6	13,4	172,5	21,2
Value-added tax	164,0	10,9	125,8	21,9
Taxes on international trade and transactions	20,9	7,9	19,2	37,5
Other revenue	10,7	16,2	10,2	109,0
Less: SACU** payments	15,0	-46,3	14,2	-32,4
Total revenue	643,2	11,0	471,7	14,6

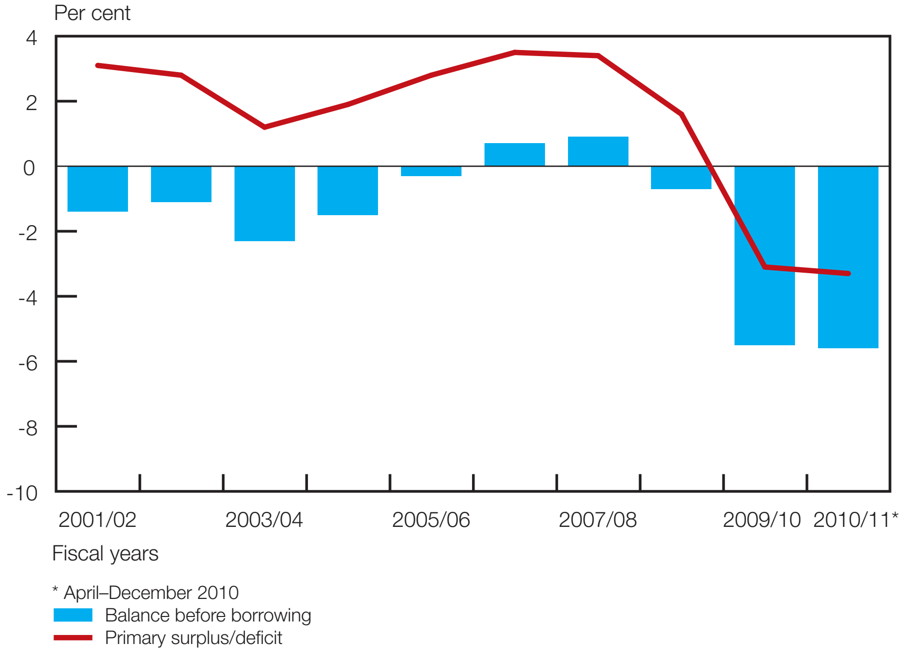
* April–December 2009 to April–December 2010
** Southern African Customs Union

Cumulative deficit of national government



The net outcome of national government cash-flow revenue and expenditure was a cash-flow deficit before borrowing and debt repayment of R121 billion, or R8,6 billion lower than in April–December 2009. After accounting for extraordinary transactions and the cost on revaluation of foreign debt at redemption, the net borrowing requirement equalled the cash-flow deficit for the first three quarters of fiscal 2010/11. This was R4,8 billion below the net borrowing requirement recorded in the same period a year earlier.

National government balances as a ratio of gross domestic product



As shown in the accompanying table, the net borrowing requirement in the first nine months of fiscal 2010/11 was funded through the issuance of Treasury bills and government bonds in the domestic capital market. During the first three quarters of fiscal 2010/11, the *R189* inflation-linked bond was partly redeemed and switched to the *R202*, *R211* and *R212* inflation-linked bonds to satisfy the market appetite for these instruments. In November 2010, the *Z109* zero coupon bond was partly redeemed and switched to the *R186* bond. Net issues of RSA Government Retail Savings Bonds equalled R4,2 billion in April–December 2010, bringing the total balance outstanding to R8,4 billion as at 31 December 2010.

National government financing in fiscal 2010/11

R billions

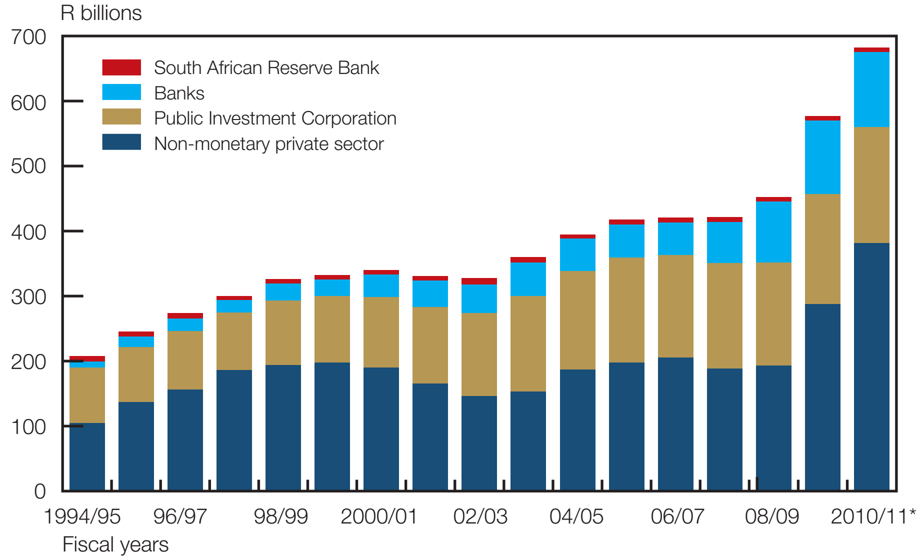
Item or instrument	Originally budgeted 2010/11	Actual Apr–Dec 2010	Actual Apr–Dec 2009
Deficit	174,9[1]	120,9[2]	129,5[2]
Plus: Extraordinary payments	-	0,7	0,6
Cost on revaluation of foreign debt at redemption	0,8	0,3	0,7
Less: Extraordinary receipts	-	0,6	4,7
Net borrowing requirement	175,7	121,3	126,1
Treasury bills	22,0	39,5	47,1
Domestic government bonds	137,7	97,7	66,3
Foreign bonds and loans	12,4	-1,6	9,9
Change in available cash balances[3]	3,6	-14,3	2,9
Total net financing [4]	175,7	121,3	126,1

1. Includes the subordinated loan to Eskom
2. Cash-flow deficit
3. Increase – decrease +
4. Components may not add up to totals due to rounding

Domestic funding from Treasury bills was obtained at an average rate of 6,2 per cent, while domestic long-term nominal yield instruments were sold at an average interest rate of 8,3 per cent per annum during the period under discussion. Between March and December 2010, the average outstanding maturity of national government's domestic marketable bonds increased from 122 months to 124 months.

National government recorded net redemptions of foreign bonds and loans to the value of R1,6 billion during the first nine months of fiscal 2010/11. The average outstanding maturity of the foreign marketable bonds of national government decreased from 97 months at the end of March 2010 to 88 months at the end of December, consistent with the time that had elapsed.

Ownership distribution of domestic marketable bonds of national government



As at 31 March of each fiscal year
* As at 31 December 2010

National government's funding activities increased the available cash balances by R14,3 billion during April–December 2010, bringing the level of these balances to R146 billion on 31 December 2010. Deposits with the South African Reserve Bank increased by R8,3 billion to R102 billion between March and December 2010.

Domestic debt of national government as a ratio of total loan debt amounted to 90,5 per cent at the end of December 2010, signalling the continued reliance on domestic funding rather than foreign funding. Total domestic debt accelerated substantially from R696 billion to R845 billion between March and December 2010 in order to finance the countercyclical budget deficit.

During the period under review, foreign debt of national government declined from R99,7 billion to R89,0 billion. This decrease was on account of the stronger exchange value of the domestic currency, alongside net redemptions of foreign bonds and loans.

Combining domestic and foreign debt, total loan debt of national government rose from R796 billion as at the end of March 2010 to R934 billion as at the end of December. Relative to gross domestic product, national government total loan debt increased from 32,6 per cent to 35,1 per cent during the period under discussion.

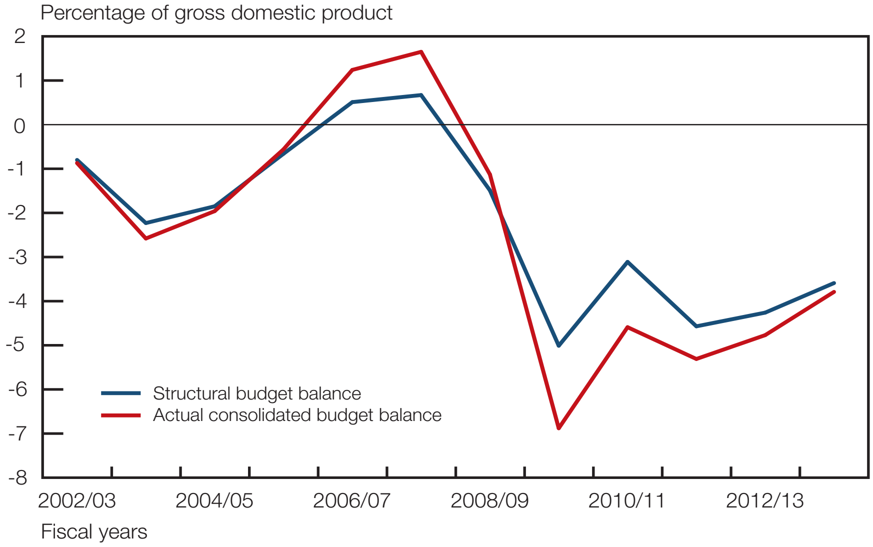
The Budget for fiscal years 2011/12 to 2013/14

Fiscal policy stance

The 2011 National Budget, tabled before Parliament by the Minister of Finance on 23 February 2011, sought to facilitate the intensification of government activities that enhance South Africans' lives and prospects, and allocate funds required for implementing the New Growth Path strategy for economic development. Job creation for the alleviation of unemployment would be government's key focus area over the medium term. The Budget also aimed to maintain macroeconomic stability and support economic growth through a countercyclical fiscal stance which consolidates at a speed that is slightly slower than anticipated earlier on.

Growth in real gross domestic product was projected to reach 3,1 per cent in 2011, rising to 4,4 per cent in 2013. Real investment was expected to expand by 3,9 per cent in 2011 and pick up to a rate of increase of 6,8 per cent in 2013, as the buoyancy of the investment recovery would be an important determinant of future growth. Despite risks to the inflation outlook, inflation was forecast to remain within the target range of 3–6 per cent, moving towards the upper limit of the range in 2013 as the economy strengthens.

Actual consolidated and structural budget balance



Budget Review 2011

Fiscal and monetary policy would continue to work in tandem, with the latter focusing on controlling inflation, whereas fiscal policy would continue to be countercyclical within a sustainable long-term framework. Government intended to continue assisting the Bank in the accumulation of foreign-exchange reserves when market conditions were favourable.

The countercyclical fiscal policy stance adopted two years before the global financial crisis fostered a healthy fiscal position. This created space for government spending to be maintained when the recession set in, despite a sharp decline in revenue. Over the next three years, government spending would continue to grow but at a slower pace than in the recent past. Slower growth in revenue and additional expenditures would result in a higher deficit for fiscal 2011/12 than had been projected in October 2010. However, over the medium-term period the deficit would narrow to a level of 3,8 per cent of estimated gross domestic product by fiscal 2013/14, consistent with restabilising the government debt ratio while conducting a countercyclical fiscal policy.

The 2011 Budget would continue to increase spending on housing, rural development, community services and social assistance grants. Furthermore, expanded access to, and financial assistance for, further education and a range of other initiatives were proposed to expand job opportunities for the youth. All these measures would be undertaken within a sound fiscal framework, but in the context of supporting a vigorous long-term growth path, which would involve continued transformation and commitment of resources.

Following the commitments government had made in the previous Budget, progress was made on several fronts. Savings were accomplished on low-priority categories of spending, releasing over R30 billion to essential services. There would be further enhancement of the Industrial Policy Action Plan. Additional resources were allocated for spending on economic and social infrastructure. A new community-based health-care programme was envisaged as part of the national health insurance initiative, while work on the design and improvement of the social security system continued.

State debt cost was revised downwards to amount to R66,6 billion in fiscal 2010/11. As a proportion of total national government expenditure it was estimated to average 9,3 per cent over the medium-term period. State debt cost as a ratio of gross domestic product was projected to increase from 2,5 per cent in fiscal 2010/11 to 2,9 per cent in fiscal 2013/14.

Fiscal projections: National government[1]

Fiscal years	Revised estimate		Medium-term estimates					
	2010/11		2011/12		2012/13		2013/14	
	R billions	Annual change (per cent)	R billions	Annual change (per cent)	R billions	Annual change (per cent)	R billions	Annual change (per cent)
Expenditure	809,9	8,4	888,9	9,8	968,1	8,9	1 053,0	8,8
State debt cost[2]	66,6	16,5	76,6	15,0	90,8	18,6	104,0	14,6
Current payments	135,3	15,5	147,8	9,2	156,2	5,7	166,9	6,8
Transfers and subsidies	578,3	8,7	648,5	12,1	695,6	7,3	740,7	6,5
Payments for capital assets	8,8	-4,2	11,2	27,1	13,8	23,3	17,5	26,3
Payments for financial assets[3]	20,9		0,8		0,0		0,0	
Contingency reserve and unallocated funds	-		4,1		11,7		23,9	
Expenditure as a ratio of GDP[4]	*30,4%*		*30,5%*		*30,2%*		*29,8%*	
Revenue	666,6	15,0	729,9	9,5	806,4	10,5	904,3	12,1
Revenue as a ratio of GDP	*25,0%*		*25,0%*		*25,2%*		*25,6%*	
Budget balance[5] before borrowing and debt repayment	-143,4		-159,1		-161,7		-148,7	
Balance as a ratio of GDP	*-5,4%*		*-5,5%*		*-5,1%*		*-4,2%*	
Balance as a ratio of GDP: October 2010 MTBPS[6]	*-5,3%*		*-5,0%*		*-4,5%*		*-3,7%*	

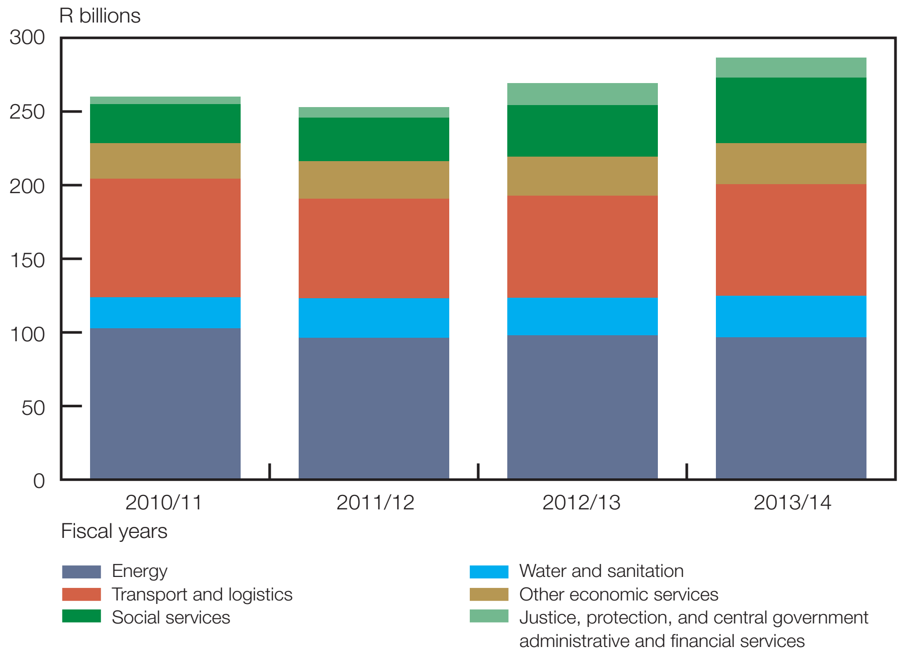
1 Components may not add up to totals due to rounding
2 Includes interest, management cost and the cost of raising loans
3 Consists mainly of lending to public corporations or making equity investments in them for policy purposes. Previously included in transfers and subsidies
4 Gross domestic product
5 Deficit – surplus +
6 *Medium Term Budget Policy Statement 2010*

Government expected that national health insurance (NHI) would be phased in over 14 years. While initial allocations were made in the *Budget Review 2011*, the NHI system would require funding over and above current revenues allocated to public health. Preliminary analysis indicated that the phasing in of a payroll tax (payable by employers), an increase in the VAT rate and a surcharge on individuals' taxable income could be considered for such funding. Announcements about specific funding instruments could be expected in the 2012 Budget.

The financial crisis of 2008 and 2009 led to sharply higher global unemployment. The 2011 Budget funded two initiatives targeted at creating jobs, particularly for young people: a Jobs

Fund to support projects with high employment potential and a youth employment subsidy. The New Growth Path targeted the creation of 5 million jobs over the next ten years. The proposals, building on policies already in place, focused on creating jobs around infrastructure, agriculture, mining, the green economy, tourism, business services and manufacturing.

Public-sector infrastructure expenditure by function



Budget Review 2011

Public-sector infrastructure spending increased from 4,6 per cent of gross domestic product in fiscal 2006/07 to 9,8 per cent of gross domestic product in fiscal 2010/11, and was expected to average 8,4 per cent of gross domestic product over the medium-term period, totalling R809 billion. This would support future economic growth, while contributing directly to current production and income. Expenditure on infrastructure development by function is detailed in the accompanying graph, with energy being the largest single category.

The 2008/09 recession sharply reduced the income available for public expenditure, with nominal tax revenue declining in fiscal 2009/10. Since the middle of 2010, revenues have improved and are expected to track positive real economic growth over the medium term. Recent data suggest a strong recovery in customs duties and VAT receipts during fiscal 2010/11, whereas corporate income tax revenue is lagging behind.

Total national government revenue was projected to increase by 9,5 per cent to amount to R730 billion in fiscal 2011/12. Revenue would rise at an average rate of 10,7 per cent per annum over the three-year budget period, to total R904 billion in fiscal 2013/14.

The 2011 Budget tax proposals are intended to broaden the tax base in support of inclusive growth. Businesses would receive tax relief to support skills development and job creation, particularly for young workers. Various loopholes would be closed and tax equity would be improved by reforming the tax treatment of contributions to medical schemes and retirement funds. A tax on dividends would be implemented, replacing the secondary tax on companies. Consumption-related taxes would be increased, also addressing environmental and health concerns.

Netting the revised national government revenue and expenditure yielded a cash-book deficit before borrowing and debt repayment of R143 billion in fiscal 2010/11. This was R24,2 billion lower than the deficit recorded in the previous fiscal year and slightly higher than the cash-book deficit recorded in the *MTBPS 2010*. The lower deficit can be attributed to a recovery in national government revenue combined with a moderation in the growth of expenditure. As a ratio of gross domestic product, the national government deficit was projected to amount to 5,4 per cent in fiscal 2010/11 before declining to an average of 4,9 per cent over the medium term.

The primary balance, (i.e., revenue net of non-interest expenditure) was projected to amount to a deficit of 2,9 per cent of estimated gross domestic product in fiscal 2010/11. This can be compared with a deficit ratio of 4,5 per cent recorded a year earlier. Primary deficit ratios were expected to decrease over the medium term, bringing the average primary deficit to 2,1 per cent.

Extraordinary payments were expected to amount to R0,8 billion in fiscal 2010/11. These payments consist of losses on the Gold and Foreign Exchange Contingency Reserve Account (GFECRA), revaluation losses on foreign-currency transactions and premiums on bond transactions. Provision was made for a small loss on the GFECRA in fiscal 2011/12.

National government financing

R billions

Item or instrument	Revised estimate	Medium-term estimates		
	2010/11	2011/12	2012/13	2013/14
Deficit	**143,4**	**159,1**	**161,7**	**148,7**
Plus: Extraordinary payments	0,8	0,2	-	-
Cost on revaluation of foreign debt at redemption	0,3	0,2	-2,5	4,9
Less: Extraordinary receipts	3,1	1,4	-	-
Net borrowing requirement	**141,4**	**158,0**	**159,2**	**153,6**
Treasury bills	35,1	22,0	22,0	21,0
Domestic government bonds issued	139,2	135,4	124,2	111,8
Foreign bonds and loans	-1,9	5,2	-6,1	-4,8
Changes in available cash balances*	-31,0	-4,5	19,0	25,5
Total net financing	**141,4**	**158,0**	**159,2**	**153,6**

* Increase – decrease +

The cost on revaluation of foreign loans at maturity was projected to total R0,3 billion in fiscal 2010/11. A total of R3,1 billion in extraordinary receipts were expected in fiscal 2010/11. This mainly consisted of premiums on bond transactions, proceeds from government's liquidation of its investments in the South African Special Risk Association (SASRIA), a special dividend from Telkom and a transfer from the Petroleum Products Equalisation Fund. In fiscal 2011/12, provision was made for the receipt of R50 *million* from SASRIA and R1,3 billion for premiums on bond transactions.

The bulk of the net borrowing requirement would be financed domestically over the medium term. Domestic fixed-income bonds would be the major source of financing followed by Treasury bills. It was foreseen that the appetite for inflation-linked bonds would remain high, with 61 per cent of issuance in the longer-maturity *R202* and *R210* bonds.

There were no issuances of foreign bonds during the first three quarters of fiscal 2010/11. Net redemptions of foreign bonds and loans to the value of R1,9 billion were expected in fiscal 2010/11. Over the medium term, national government intended to borrow US$1 billion a year in global markets to maintain benchmarks in major currencies and meet part of its foreign currency commitments.

National government's available cash balances were projected to increase by R31,0 billion in fiscal 2010/11 but to decline in the outer years of the medium-term projection period.

Gross loan debt of national government was expected to increase from R989 billion to R1,5 *trillion* between fiscal 2010/11 and 2013/14. As a proportion of gross domestic product, it was projected that gross loan debt would increase from 37,1 to 43,1 per cent during the period under discussion.

Consolidated government expenditure was projected to increase from R897 billion in fiscal 2010/11 to R1,2 *trillion* in fiscal 2013/14, as higher state debt costs, wage pressures and growth in social grants continue to claim a greater share of total expenditure. The *Budget Review 2011* provided for an additional non-interest amount of R94,1 billion to augment baseline expenditure over the next three years. Over the medium term, non-interest consolidated expenditure was projected to rise at an average annual rate of 8,0 per cent, compared with the growth rate of 16,8 per cent the previous three years.

Combined social spending (mainly health, education and social welfare) was estimated to amount to R485 billion in fiscal 2010/11 and increase at an average annual rate of 8,4 per cent over the three-year budget period. Expenditure on protection services was estimated to increase from R118 billion in fiscal 2010/11 to R148 billion in fiscal 2013/14. The annual rate of growth in spending on protection services was expected to average 8,0 per cent over the three-year period. Crime reduction remains one of government's top priorities. Over the medium term, additional funds were provided to bring down crime levels, which included a total of R2,1 billion provided for increasing the number of police personnel by 1 660 between fiscal 2012/13 and fiscal 2013/14.

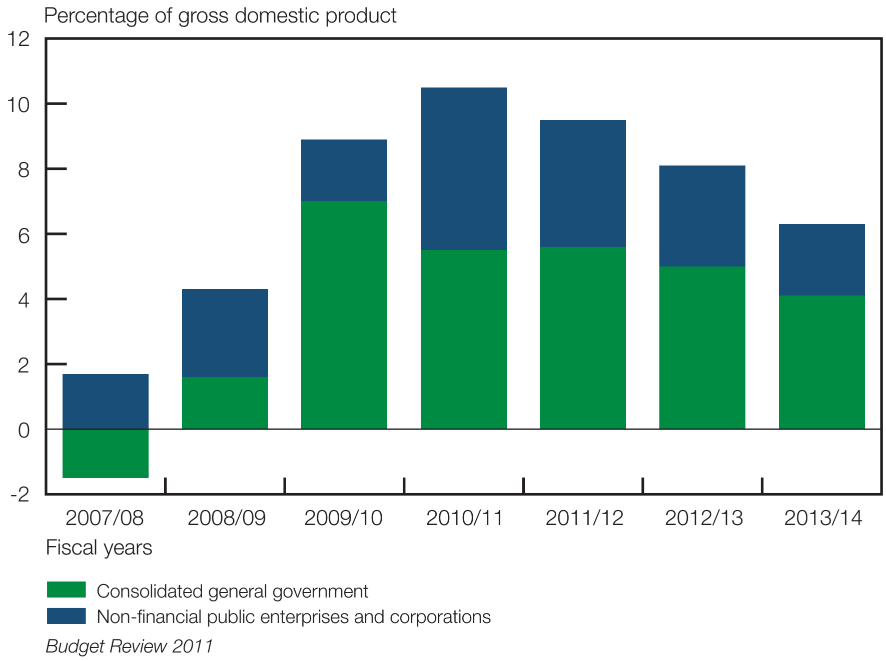
Public-sector borrowing requirement*

R billions

Level of government	Revised estimate	Medium-term estimates		
	2010/11	2011/12	2012/13	2013/14
National government	141,0	157,9	161,7	148,7
Extra-budgetary institutions	8,2	7,2	5,9	3,1
Social security funds	-10,8	-10,4	-11,6	-11,2
Provincial governments	1,6	-1,1	-3,1	-6,0
Local authorities and local enterprises	7,5	9,1	8,2	8,6
General government**	147,5	162,7	161,0	143,2
Percentage of gross domestic product	*5,5%*	*5,6%*	*5,0%*	*4,1%*
Non-financial public enterprises	133,7	113,7	99,1	78,7
Total public sector**	281,2	276,4	260,1	221,9
Percentage of gross domestic product	*10,5%*	*9,5%*	*8,1%*	*6,3%*
Estimated gross domestic product	2 666,9	2 914,9	3 201,3	3 536,0

* Deficit + surplus –
** Calculations may not add up to totals due to rounding

Public-sector borrowing requirement



Budget Review 2011

The public-sector borrowing requirement was budgeted to amount to R281 billion in fiscal 2010/11, decelerating over the medium term to reach R222 billon in fiscal 2013/14. It was projected to reach 10,5 per cent of estimated gross domestic product in fiscal 2010/11, reflecting a positive turnaround following the global economic crisis and increased infrastructure spending by non-financial public enterprises. The borrowing requirement was expected to recede to 6,3 per cent of gross domestic product by fiscal 2013/14, reflecting a cyclical improvement in the consolidated budget balance.

Statement of the Monetary Policy Committee

20 January 2011

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

Since the previous meeting of the Monetary Policy Committee (MPC), there have been more convincing signs that the recovery in the global economy will be sustained. However, growth in the advanced economies is expected to be slow and is subject to a number of downside risks, including the sovereign debt crisis that continues to beset the eurozone. The more promising global growth outlook, as well as the unfavourable weather conditions, has implications for commodity prices, particularly those of food and energy. These pressures are likely to pose an increasing risk to both the global and domestic inflation outlook. Nevertheless, domestic inflation is expected to remain within the target range for the forecast period.

Domestically, the output gap remains negative and gross domestic product (GDP) growth is expected to remain below potential over the next two years. However, there are indications that the outlook for output growth, while hesitant, is somewhat more positive. The recovery in household consumption expenditure appears to be sustained.

The year-on-year inflation rate as measured by the consumer price index (CPI) for all urban areas moderated to 3,5 per cent in December from 3,6 per cent in November 2010. The average inflation rate for 2010 was 4,3 per cent compared with 7,1 per cent in 2009. Food price inflation in December measured 1,4 per cent, unchanged on a month-on-month basis. The main contributor to the inflation outcome remained housing and utilities, primarily electricity, which contributed 1,5 percentage points to the 3,5 per cent outcome. Administered prices excluding petrol increased at a rate of 9,1 per cent in both November and December.

Year-on-year producer price inflation reached a recent peak of 9,4 per cent in June 2010, and has declined moderately since then. In November, the producer price index (PPI) increased by 6,2 per cent, compared with 6,4 per cent the previous month. The impact of the exchange rate on producer prices is still clearly evident, with the prices of imported commodities increasing at a year-on-year rate of 0,5 per cent. Manufactured food prices increased by 0,6 per cent, while agricultural prices declined by 0,3 per cent.

The CPI forecast of the Bank has been revised upwards since the MPC's previous meeting. Nevertheless, the domestic inflation trajectory is still expected to remain within the target range over the entire forecast period to the end of 2012. Inflation is now expected to average 4,6 per cent in 2011 and 5,3 per cent in 2012. The upward adjustment is mainly due to revised assumptions of the international oil price over the forecast period, and we will continue to monitor global inflation trends closely.

The Bank's forecast is similar to the Reuters consensus forecast. In the December survey, the mean forecast of CPI inflation was 4,5 per cent for 2011, 5,4 per cent for 2012 and 5,6 per cent for 2013. These forecasts were slightly higher than those in the November survey. The break-even inflation rates across all maturities also continue to reflect inflation expectations within the target range.

Inflation expectations as reflected in the survey conducted by the Bureau for Economic Research (BER) at Stellenbosch University in the fourth quarter of 2010 continued to trend downwards. For the first time, average expectations for 2011 are within the inflation target band at 5,5 per cent. The expectations of all categories of respondents declined, with both business executives and trade union officials expecting inflation to average 6,0 per cent, while those of the financial analysts declined to 4,5 per cent.

All categories of respondents expect inflation to increase again in 2012 when it is expected to average 6,2 per cent.

The global economic outlook remains uncertain but there appears to be increasing optimism that the recovery, albeit relatively weak, will be sustained. Most forecasts have been revised upwards in recent months but indicate that global growth is expected to be slower in 2011 than in 2010. However, the prospects remain uneven across countries and regions, and a number of risks remain.

Growth in the United States (US) continues to be supported by strong monetary and fiscal intervention, while growth in Japan remains subdued. In the euro area, the recovery is being driven by strong growth in Germany but this is expected to moderate in 2011. In the rest of the euro area, confidence has declined in the wake of the worsening sovereign debt crisis, which remains a major risk to the outlook. Recent co-ordinated measures appear to have stabilised the sovereign debt markets for now, but significant risks remain and a further escalation of the crisis could impact negatively on global growth prospects.

The emerging markets continue to outperform the advanced economies, with strong recoveries in consumption and investment in the major emerging-market economies.

Inflation developments and prospects also appear to reflect the divergent growth trends. Persistent large negative output gaps in the advanced economies have helped to contain inflation pressures, despite rising international oil and food prices. There is still some risk of deflation in the US, although this risk is declining. By contrast, inflation in emerging markets has been increasing, partly as a result of stronger demand pressures but also as a result of the higher weights of energy and food in the consumer price baskets. These trends have resulted in generally tighter monetary policies in emerging markets, but monetary accommodation is expected to persist in most of the major industrialised countries for some time.

The exchange rate of the rand has been relatively volatile since the previous meeting of the MPC, when it was around R7,00 against the US dollar. By early January the rand had appreciated to R6,55, but has since retraced to levels prevailing at the time of the previous meeting. During this period, non-residents became net sellers of rand-denominated bonds as expectations that there would be further interest rate reductions were reversed, but were net buyers of domestic equities.

Factors influencing the exchange rate during this period included developments in the euro/dollar exchange rate, further acceleration in commodity prices and persistent capital flows to emerging markets.

In the absence of general risk aversion, or a tightening of the monetary policy stances in the advanced economies, the rand exchange rate is expected to remain relatively strong. Since the previous meeting of the MPC, the nominal effective exchange rate of the rand depreciated by 0,4 per cent.

During 2010 total direct foreign-exchange reserve accumulation by the Bank and National Treasury amounted to US$7,4 billion, or a spend of just over R53 billion. Despite this, the rand continued to appreciate – 12 per cent against the US dollar during 2010 – and remained strong. Portfolio and foreign direct investment inflows continued, and the net purchases of bonds and equities by non-residents amounted to R89,5 billion in 2010. The Bank will continue to accumulate foreign-exchange reserves as and when possible.

Domestic GDP growth remains subdued, with growth of 2,6 per cent in the third quarter of 2010. Although there are mixed signals about the sustainability of the output recovery, high-frequency data indicate a stronger fourth quarter performance, and forecasts for 2011 have generally been subject to moderate upward revision. The Bank's forecast was also adjusted marginally and growth is now expected to average 3,4 per cent in 2011. The forecast for 2012 is unchanged at 3,6 per cent. The composite leading business cycle indicator of the Bank has been relatively flat in the past few months and declined moderately in October, reflecting the uneven growth prospects.

Gross domestic fixed capital formation is still subdued, having increased by 0,9 per cent in the third quarter of 2010. This rate of investment growth remains too low to impact meaningfully on output growth, and is currently primarily dependent on state-owned enterprises' pipeline commitment to infrastructure, while investment in the manufacturing sector is being constrained by low levels of capacity utilisation. The labour market appears to have stabilised in the third quarter when employment levels were more or less unchanged, although unemployment remains stubbornly high at 25,3 per cent.

The recovery in the manufacturing sector remains hesitant. Manufacturing output increased by 4,6 per cent on a year-on-year basis in November, compared with 2,3 per cent in October. Production of motor vehicles, parts and accessories, in particular, including vehicle exports which increased by 52,8 per cent quarter-on-quarter in the final quarter of 2010, have exhibited robust growth,.

The Kagiso Purchasing Managers Index (PMI) confirms the uncertain outlook. Following a strong improvement in the index in November to a level in excess of the neutral level of 50, it declined again in December, although still indicating an expansion of the sector. The mining sector has also been improving and grew at a year-on-year rate of 9,6 per cent in November. The Rand Merchant Bank (RMB)/BER Business Confidence Indicator remained relatively unchanged throughout 2010, but with a negative outlook.

The recovery in domestic consumption expenditure appears to be sustained. Real final consumption expenditure by households increased at an annualised rate of 5,9 per cent in the third quarter of 2010. Strong expenditure growth was observed in all components of consumption. Real retail trade sales increased at a year-on-year rate of 7,8 per cent in November 2010. New vehicle sales also continued their strong performance, having increased by almost 30 per cent in December. Consumer confidence as reflected in the First National Bank (FNB)/BER Consumer Confidence Index has been at a relatively high level during the past year.

Credit extension maintained its moderate upward trend during 2010. Total loans and advances to the private sector increased by 4,4 per cent in November. Growth over 12 months in mortgage advances has fluctuated around 4,8 per cent since August 2010, reflecting a loss of momentum in the real-estate market. House prices increased somewhat in the first half of 2010, but since then the rate of increase has declined, with some house price indexes indicating that prices have been falling.

Growth in instalment sale and leasing finance, and other loans and advances maintained a positive trend. Within the latter category, growth in credit card advances was positive for the first time since the end of 2008. Bank overdrafts were the only major category that continued to contract, although at a slower rate. Household debt remains high at 78,5 per cent of disposable income.

However, lower interest rates have reduced the ratio of debt-service costs to disposable income to 7,8 per cent, compared with 12,6 per cent in the third quarter of 2008.

Expenditure has been positively affected by growth in real disposable income, lower interest rates and some favourable wealth effects. Share prices on the JSE Limited have reached levels in line with the peaks reached before the onset of the global financial crisis. In 2010 the all-share index increased by 16,1 per cent.

Risks to the inflation outlook emanating from global commodity price increases have become more evident. These risks relate mainly to oil and food price developments. Having fluctuated in the range of US$70–US$80 per barrel for much of 2010, the price of Brent crude oil began to increase in late November and is currently at around US$98 per barrel. The surge in oil prices is due in part to stronger global oil demand and the exceptionally cold weather in the northern hemisphere. These price trends were also affected by US dollar developments, particularly following the announcement of additional quantitative easing by the US Federal Reserve in November.

The domestic petrol price, which has been cushioned, to some extent, by exchange rate developments, has increased by 66 cents per litre since September 2010, and by 11 per cent over the past year.

Since September, the rand exchange rate has offset the petrol price increase by a cumulative 45 cents per litre.

Global food prices have also continued to increase, driven by tight food supplies, changing weather patterns and rising demand in emerging-market economies. To date South Africa has been shielded, to some degree, from these increases by the exchange rate and the bumper maize crop. Domestic maize prices have been increasing since the middle of 2010, but in January 2011 were still about 11 per cent lower than a year ago. By contrast, South Africa is a net importer of wheat, which has increased in price by almost 40 per cent over the past year. Although producer price developments suggest that domestic food price inflation will remain low in the short term, these global developments, unless reversed, will inevitably impact on consumer food price inflation.

Administered prices and wage settlements remain upside risks to the inflation outlook. Although wage increases have moderated slightly over the past months, they are still significantly in excess of the current and expected inflation outcomes. According to Statistics South Africa, the year-on-year rate of increase in average nominal remuneration per worker in the formal non-agricultural sector declined from 15,8 per cent in the second quarter of 2010 to 12,6 per cent in the third quarter. Once labour productivity developments are accounted for, unit labour cost increases amounted to 10,9 per cent and 9,3 per cent in these two quarters respectively. According to Andrew Levy Employment Publications, the average wage settlement in the first nine months of 2010 amounted to 8,3 per cent compared with 9,3 per cent in 2009.

The current level of the repurchase rate is at its lowest level in nominal terms in over 30 years, while the real interest rate is at a level below 1 per cent. This has helped with the recovery in consumption expenditure and should also stimulate domestic investment and growth by reducing the cost of borrowing. However, low interest rates on their own cannot ensure sustainably higher long-run trend growth and employment creation.

The MPC has taken note of the improving growth outlook for the economy, and is of the view that the recovery in domestic consumption expenditure will be sustained. While there are increasing risks to the inflation outlook, they emanate primarily from external cost–push factors, and inflation is expected to remain within the target range until the end of the forecast period.

The MPC has therefore decided to keep the repurchase rate unchanged at 5,5 per cent per annum. At this stage there are no signs of incipient excess demand in the economy, and unless there are significant unexpected changes in the global or domestic outlook, the monetary policy stance is expected to remain relatively stable for some time. The MPC will continue to monitor developments closely and stands ready to act should the need arise.

Statistical tables