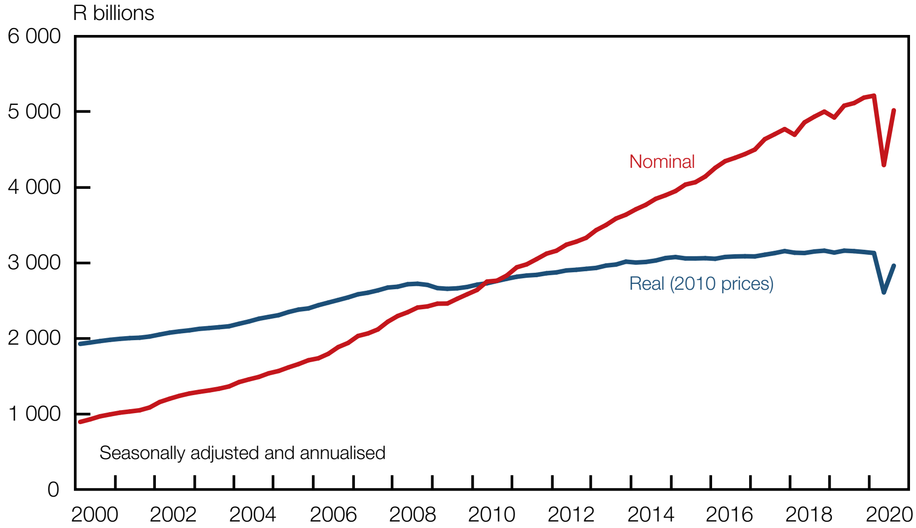
Quarterly Economic Review

Introduction

Domestic economic growth, in both nominal and real terms, rebounded significantly in the third quarter of 2020 with the easing of the coronavirus disease 2019 (COVID-19) lockdown restrictions. This follows the unprecedented contraction in the second quarter at the height of restricted economic activity to curb the spread of COVID-19. South Africa's real gross domestic product (GDP) accordingly increased at an annualised rate of 66.1% in the third quarter of 2020 after the revised contraction of 51.7% in the second quarter – representing both the largest contraction and rebound since quarterly records began in 1960. Despite the strong rebound in the third quarter, real GDP was only at a level similar to that in the first quarter of 2013.

Gross domestic product



Sources: Stats SA and SARB

The turnaround in economic activity was broad-based and underpinned by brisk increases in the real output of the primary, secondary and tertiary sectors. Following a fourth successive quarterly contraction in the second quarter of 2020, the real gross value added (GVA) by the primary sector increased markedly in the third quarter, supported by a significant rebound in the real GVA by the mining sector and a further sizeable increase in real agricultural output. The continued expansion in agricultural output reflected favourable weather conditions as well as the bumper maize and citrus harvests. The rebound in mining production was broad-based and reflected the easing of the lockdown restrictions, supported by higher international commodity prices and increased demand from China, in particular.

The strong rebound in the real output of the secondary sector resulted largely from increased manufacturing production and, to a lesser extent, increased construction activity as well as increased activity in the sector supplying electricity, gas and water. Although the improvement in manufacturing output was evident in all subsectors, food, and in particular beverages, contributed significantly to the increase as restrictions on the sale of alcoholic beverages were lifted in mid-August.

The real GVA by the tertiary sector also rebounded in the third quarter of 2020 but by a slightly smaller magnitude than the contraction in the second quarter. Economic activity increased meaningfully in almost all of the tertiary sectors in the third quarter, with the exception of government and personal services which expanded only slightly. The real output of the commerce sector expanded notably, driven by a strong rebound in the output of the wholesale, retail and motor trade subsectors. The real GVA by the catering and accommodation subsector increased at a slower pace, impacted by continued restrictions on travel and cross-border tourism as most international borders remained closed.

Real gross domestic expenditure (GDE) rebounded from a revised contraction of 42.9% in the second quarter of 2020 to an annualised increase of 23.7% in the third quarter, emulating the recovery in real GDP. Real final consumption expenditure by households rebounded strongly alongside a lesser increase in real gross fixed capital formation, while the de-accumulation of real inventory holdings continued at a much faster pace. Real final consumption expenditure by households and the real net exports of goods and services contributed the most to growth in overall real GDP in the third quarter of 2020.

The rebound in household consumption expenditure in the third quarter of 2020 resulted from sizeable increases in real outlays on durable, semi-durable and non-durable goods, which reflected resurgent demand from a very low base as restrictions on the sale of these goods were lifted. Spending on consumer services recovered at a slower pace, impacted by the remaining restrictions on large social gatherings and international travel, with consumers likely redirecting some of their service-orientated budgets to meet pent-up demand for goods. The turnaround in real expenditure by households was consistent with the rebound in real disposable income in the third quarter of 2020, notwithstanding rising unemployment and low consumer confidence.

Household debt increased in the third quarter of 2020 following an unprecedented decline in the second quarter. However, household debt as a percentage of nominal disposable income decreased from 86.5% in the second quarter of 2020 to 75.7% in the third quarter, as the increase in household disposable income exceeded that in debt. Households' net wealth increased further in the third quarter of 2020, albeit at a slower pace, as the increase in total assets outweighed that in total liabilities. The value of household assets increased despite the FTSE/JSE All-Share Price Index (Alsi) remaining broadly unchanged in the third quarter of 2020 after it recovered notably in the second quarter.

Real gross fixed capital formation also increased in the third quarter of 2020, but by much less than the contraction in the second quarter. Real capital investment by both private and public sector corporations recovered somewhat with the easing of COVID-19 restrictions. Gross fixed capital formation by general government, which was somewhat less affected by the national lockdown restrictions, increased at a slightly slower pace in the third quarter as capital investment in emergency infrastructure increased at a slower rate. Although fixed investment spending increased across most asset classes in the third quarter, the long-term downward trends persisted, with the level of overall real gross fixed capital formation still well below that of a year earlier.

South Africa's national saving rate improved substantially from 11.1% in the second quarter of 2020 to 15.9% in the third quarter. This resulted largely from increased saving by the corporate sector and a slower rate of dissaving by general government. The saving rate of households also increased marginally in the third quarter.

Household-surveyed employment increased by a seasonally adjusted 506 000 in the third quarter of 2020 following a sharp decline of 2.2 million in the second quarter. Total employment was nevertheless still 10.3% below the level of a year earlier as the effects of COVID-19 and the related lockdown restrictions dealt a severe blow to the already weak labour market. Counterintuitively, South Africa's official unemployment rate initially declined notably from 30.1% in the first quarter of 2020 to 23.3% in the second quarter, before escalating to 30.8% in the third quarter. This reflected the movement in the second quarter of a large number of people from the employed and unemployed categories to the inactivity in searching for jobs category – as those people who lost their jobs during the lockdown as well as many of those who were already unemployed were prohibited from actively searching for employment – and subsequently out of inactivity in searching for jobs in the third quarter as the lockdown restrictions were eased.

Growth in the formal non-agricultural nominal remuneration per worker reverted from an increase of 4.4% in the first quarter of 2020 to a decrease of 2.6% in the second quarter – the lowest on record. The combination of COVID-19-induced salary reductions, much lower salary increases, wage freezes as well as substantially lower bonus, overtime and commission payments exerted significant downward pressure on nominal remuneration growth. Labour productivity in the formal non-agricultural sector of the economy contracted by the sharpest rate ever of 11.8% in the second quarter of 2020, while growth in nominal unit labour cost accelerated markedly to 10.3% over the same period. However, the unprecedented contraction in output due to the COVID-19 lockdown restrictions has detracted from the informational content of these macroeconomic indicators.

Headline producer and consumer price inflation both accelerated in recent months from historical lows in May 2020. This resulted largely from the slower pace of decline in fuel prices and as the downward bias of the lockdown-induced imputations of some prices in the consumer price index dissipated. Consumer food price inflation accelerated in October 2020 following the earlier increase in agricultural food prices. Domestic inflationary pressures nevertheless remained fairly muted amid the recessionary conditions.

The value of South Africa's net gold and merchandise exports surged to an all-time high in the third quarter of 2020, along with a more muted increase in merchandise imports as global trade recovered following the easing of COVID-19 lockdown restrictions and the related rebound in economic activity. As a result, South Africa's trade surplus widened significantly to 9.0% – the largest ratio of GDP since the third quarter of 1988. Mining, manufacturing and agricultural exports all increased strongly in the third quarter of 2020, boosted by higher international commodity prices, increased global demand and an improvement in loading rates at domestic ports. The value of merchandise imports increased, although by a much lesser extent than exports, in the third quarter of 2020 and remained well below the level of a year earlier, reflective of weak domestic demand.

The larger trade surplus coincided with a significantly smaller shortfall on the services, income and current transfer account, which resulted largely from a significantly smaller deficit on the income account, as South Africa recorded a first quarterly dividend surplus in almost 25 years. As a consequence, the balance on the current account of the balance of payments switched from a deficit in the second quarter of 2020 to a notable surplus of 5.9% in the third quarter – the largest surplus as a ratio of GDP since the third quarter of 1988.

The net flow of capital on South Africa's financial account of the balance of payments reflected a larger outflow of R38.6 billion in the third quarter of 2020, following a revised outflow of R24.0 billion in the second quarter. On a net basis, direct investment, portfolio investment and reserve assets recorded outflows during the third quarter, while financial derivatives and other investment recorded inflows. Portfolio investment flows largely reflected non-resident net sales of South African equities as well as the acquisition of foreign portfolio assets by South African residents. Other investment inflows largely reflected long-term loans extended to the general government by non-residents to combat the effects of COVID-19. These inflows also boosted the level of South Africa's international reserve assets in the third quarter of 2020.

South Africa's positive net international investment position (IIP) increased significantly in the three months to the end of June 2020, following a substantial increase in the value of foreign assets and a much smaller increase in that of foreign liabilities. The second consecutive large quarterly increase in the market value of South Africa's foreign assets resulted mainly from increases in direct and portfolio investment, following a surge of 20.0% in the United States (US) Standard & Poor's (S&P) 500 Index as well as an increase in the value of resident ownership of dual-listed companies domiciled abroad.

The nominal effective exchange rate (NEER) of the rand decreased significantly during the onset of the COVID-19 pandemic in the first quarter of 2020, but then stabilised during the subsequent two quarters, similar to most other emerging market currencies. The NEER then increased in October and November 2020, supported by improved global sentiment towards emerging market currencies following the release of positive economic statistics in the US and the outcome of the US presidential elections.

Private sector banks' actual daily liquidity requirement varied relatively widely in the third quarter of 2020, with the low of R25.7 billion in July 2020 reflecting a considerable decline in the demand for funding at the weekly main refinancing auctions as private banks experienced periods of surplus liquidity. Although the weekly main refinancing amount on offer was increased from R45.0 billion to R50.0 billion as from 4 November when the South African Reserve Bank (SARB) started to unwind some of the liquidity measures previously implemented, the under-subscription of the weekly main refinancing auctions persisted as banks continued to experience surplus liquidity. Domestic short-term money market interest rates continued to trend gradually lower after the most recent reduction in the repurchase (repo) rate in July 2020.

The robust growth in the broadly defined money supply (M3) during the national lockdown moderated somewhat in recent months, owing to the deposit growth of households levelling off somewhat since July 2020, while that of the corporate sector slowed decisively in October, specifically that of financial companies. By contrast, growth in total loans and advances extended by monetary institutions to the domestic private sector decelerated further in the third quarter of 2020, led by a marked deceleration and then a contraction in loans to companies.

South African government bond yields increased between early June 2020 and early October, reflecting concerns regarding the resurgence of COVID-19 infections globally and a sell-off of emerging market bonds. Subsequently, bond yields declined somewhat to the end of November as the exchange value of the rand appreciated and consumer price inflation remained subdued, even though the *2020 Medium Term Budget Policy Statement (2020 MTBPS)* projected a significantly larger budget deficit and slower debt consolidation. Bond yields increased marginally after the downgrade of South Africa's sovereign credit rating by two rating agencies on 20 November 2020.

The public sector's net issuance of listed bonds in the domestic primary bond market increased by 51.3% year on year to an all-time high of R474 billion in the first 11 months of 2020. This resulted from funding pressures and substantial national government debt issuance due to revenue shortfalls, COVID-19-related spending and the financing of distressed state-owned companies, among other factors. By contrast, private sector companies redeemed bonds over the same period, as funding needs reduced significantly given the weak economic activity due to the national lockdown.

The preliminary non-financial public sector borrowing requirement doubled to R369 billion in the first six months of fiscal 2020/21 compared with the same period of the previous fiscal year. This reflected the significantly larger cash deficits of both national government due to continued revenue shortfalls and the social security funds due to COVID-19 relief payments. In financing the borrowing requirement, the total gross loan debt of national government increased sharply by 20.3% year on year to R3 714 billion (75.2% of GDP) as at 30 September 2020. The *2020 MTBPS* projected total gross loan debt to increase to 81.8% of GDP by the end of fiscal 2020/21, and even further over the medium term to 92.9% of GDP in fiscal 2023/24.

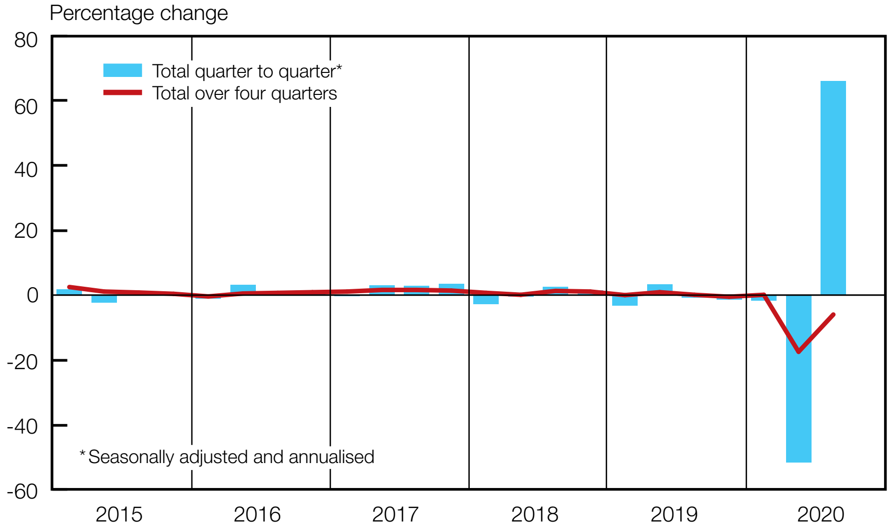
Domestic economic developments

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

Domestic output[1]

In South Africa, real economic growth rebounded significantly in the third quarter of 2020 with the easing of the coronavirus disease 2019 (COVID-19) national lockdown restrictions, following the sharp contraction in the second quarter at the height of restricted economic activity to curb the spread of COVID-19. The marked quarter-to-quarter increase in real economic activity in the third quarter reflected both a revival of economic activity and the low base in the second quarter.

Real gross domestic product



Source: Stats SA

Real *gross domestic product* (GDP) accordingly increased substantially at a seasonally adjusted and annualised rate of 66.1% in the third quarter following the slightly revised contraction of 51.7% in the second quarter – representing both the largest contraction and rebound since quarterly records began in 1960. The turnaround was broad-based and underpinned by brisk increases in the real output of the primary, secondary and tertiary sectors. With the rebound, the contraction in real GDP of 6.0% in the year to the third quarter of 2020 was significantly less than the contraction of 17.5% in the year to the second quarter. However, despite the robust expansion in the third quarter, the average *level* of real output in the first three quarters of 2020 was still 7.9% lower than in the corresponding period in 2019, and real GDP was still at a level last recorded in the first quarter of 2013.

The robust expansion in real economic activity in the third quarter of 2020 was also observed in nominal terms, with a quarter-to-quarter seasonally adjusted, but not annualised, increase of 16.8% in the level of nominal GDP. On a seasonally adjusted and annualised basis, nominal GDP expanded by 86.4% (or R724 billion) in the third quarter of 2020.

Expectations of the contraction in South Africa's real economic growth in 2020 varied from 7.8% in the *2020 Medium Term Budget Policy Statement (2020 MTBPS)* to 8.0% in the International Monetary Fund's (IMF) October 2020 *World Economic Outlook (WEO)*, the same as that of the South African Reserve Bank (SARB) in the November 2020 press statement of the Monetary Policy Committee (MPC).

Real gross domestic product

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

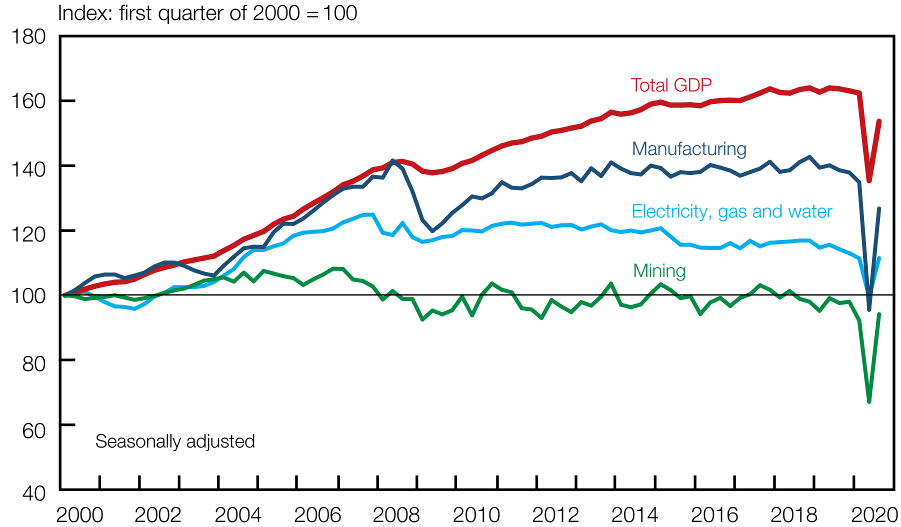
Sector	2019					2020		
	Q1	Q2	Q3	Q4	Year*	Q1	Q2	Q3
Primary sector	-12.3	11.7	-5.7	-0.4	-3.1	-10.4	-57.4	172.9
Agriculture	-16.8	-4.9	-4.5	-7.6	-6.9	35.9	19.6	18.5
Mining	-10.8	17.4	-6.1	1.8	-1.9	-21.5	-72.0	288.3
Secondary sector	-8.0	1.3	-5.0	-2.9	-1.4	-7.5	-72.0	155.6
Manufacturing	-8.8	2.1	-4.4	-1.8	-0.8	-8.5	-74.9	210.2
Construction	-5.3	-2.4	-6.9	-5.9	-3.3	-4.7	-76.5	71.1
Tertiary sector	-0.4	2.9	0.9	-1.0	1.2	1.5	-42.0	37.6
*Non-primary sector***	*-2.1*	*2.5*	*-0.4*	*-1.4*	*0.6*	*-0.5*	*-49.6*	*55.1*
*Non-agricultural sector****	*-2.8*	*3.7*	*-0.8*	*-1.1*	*0.4*	*-2.3*	*-51.7*	*66.1*
Total	-3.2	3.3	-0.8	-1.4	0.2	-1.7	-51.7	66.1

* Percentage change over one year
** The non-primary sector is total GVA excluding agriculture and mining
*** The non-agricultural sector is total GVA excluding agriculture

Source: Stats SA

When excluding the contribution of the generally more volatile primary sector, real output increased by 55.1% in the third quarter of 2020 following a contraction of 49.6% in the second quarter.

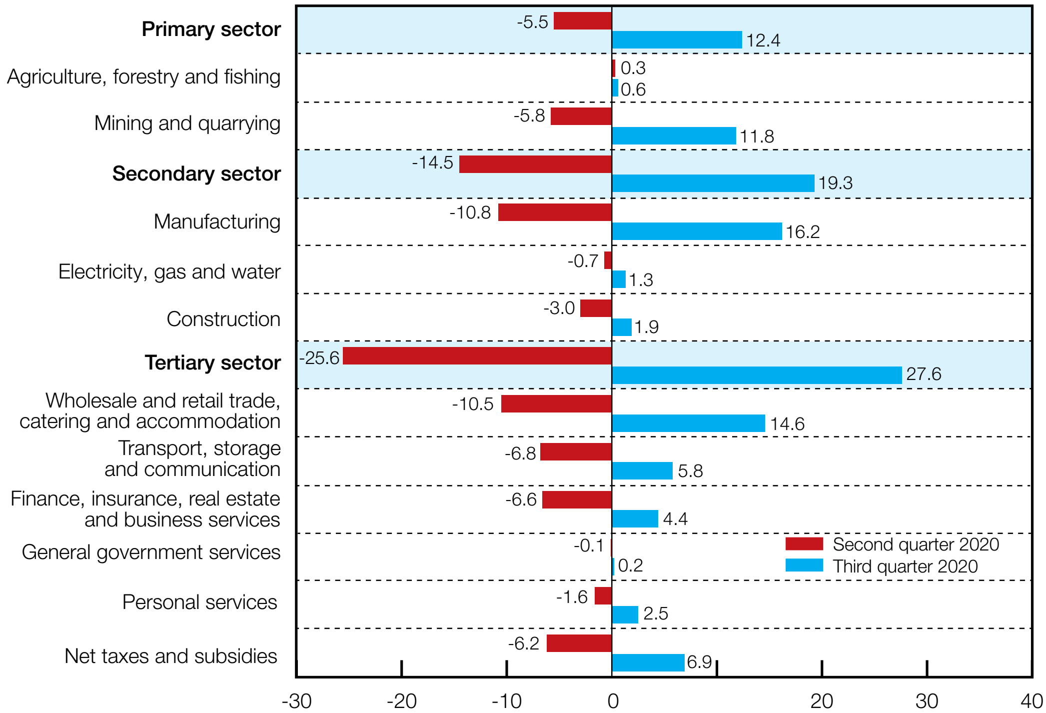
Real gross value added



Source: Stats SA

Following a fourth successive quarterly contraction in the second quarter of 2020, the real gross value added (GVA) by the *primary sector* increased by 172.9% in the third quarter. The marked increase was underpinned by a significant rebound in the real GVA by the mining sector and a further increase in real agricultural output, albeit at a slightly slower pace.

Contributions to growth in real gross domestic product



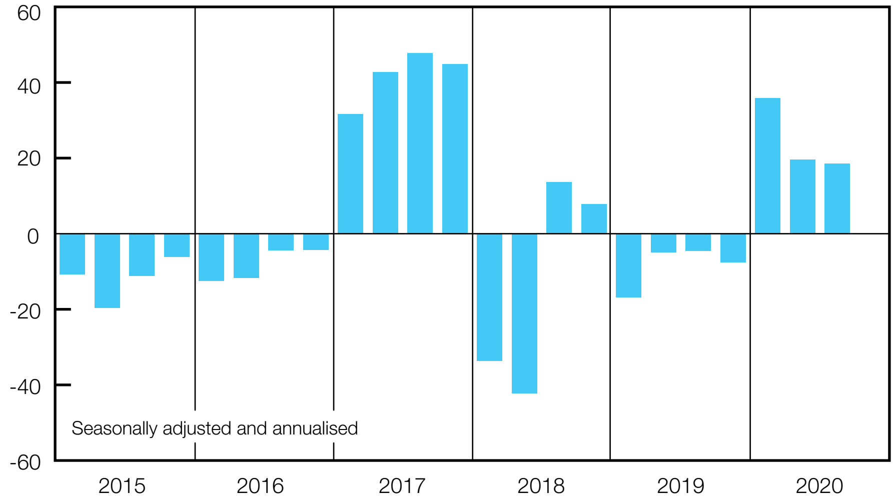
Percentage points

Source: Stats SA

The further increase of 18.5% in the real output of the *agricultural sector* in the third quarter of 2020 followed a revised increase of 19.6% in the second quarter, and marked a third successive quarterly expansion, with the continued expansion reflecting favourable weather conditions as well as the bumper maize and citrus harvests. The average level of real agricultural output was 11.3% higher in the first three quarters of 2020 than in the corresponding period in 2019, following a contraction in the real GVA by the sector in 2019.

Real gross value added by the agricultural sector

Percentage change from quarter to quarter



Source: Stats SA

Commercial maize crop estimates

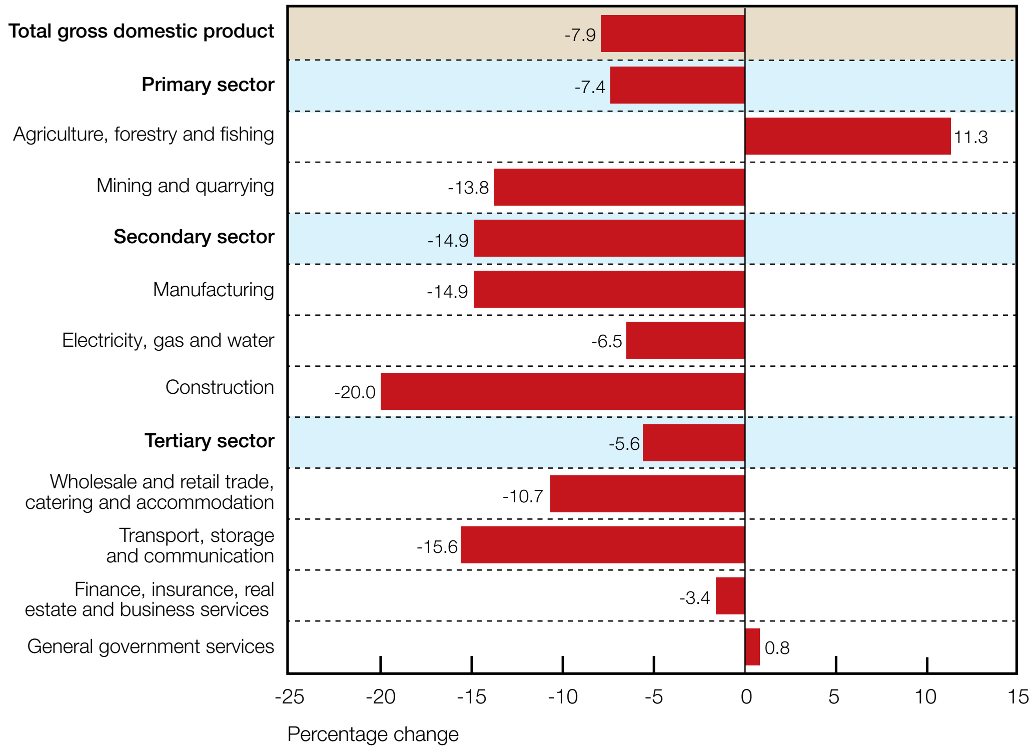
	Crop (million tons)	Area planted (million hectares)
2018/19: final crop	11.3	2.3
2019/20: final production forecast	15.4	2.6

Source: Crop Estimates Committee of the Department of Agriculture, Forestry and Fisheries

The most recent expected commercial maize crop of 15.4 million tons for the 2019/20 season is 36.7% more than the final crop of 2018/19 and the second largest after the peak in 2017. Favourable weather forecasts for the summer rainfall regions, higher agricultural commodity prices and the lower international oil prices incentivised farmers to increase maize plantings in the 2020/21 season to an expected 2.6 million hectares – 13.5% more than in the previous season.

Real gross domestic product

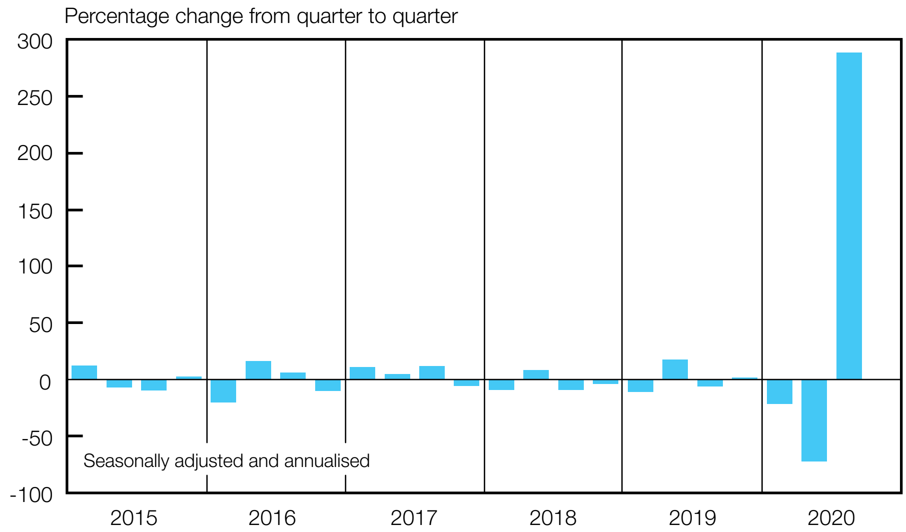
Average level: first three quarters of 2020 compared with the same period of 2019



Source: Stats SA

The expansion in the real GVA by the *mining sector* of 288.3% in the third quarter of 2020 was the strongest of all the sectors and contributed as much as 11.8 percentage points to real GDP growth. The increase was broad-based as production levels of all 12 mineral groups increased, with platinum group metals (PGMs), iron ore, gold, manganese ore and diamonds contributing the most. Mining production was supported by the further easing of the lockdown restrictions to Level 1, a recovery in the automotive industry, higher commodity prices and increased Chinese demand. However, electricity supply disruptions, high operating costs, delays in the return of migrant workers, physical distancing regulations and heightened global uncertainty still weighed on the sector's activity levels. As a result, apart from the previous quarter, the level of real mining GVA in the third quarter of 2020 was at a level last seen in the first quarter of 2012, when production volumes in the mining sector contracted sharply due to domestic electricity supply constraints alongside relatively weaker demand, especially from Asia. The average level of real mining output in the first three quarters of 2020 was 13.8% lower than in the corresponding period in 2019.

Real gross value added by the mining sector

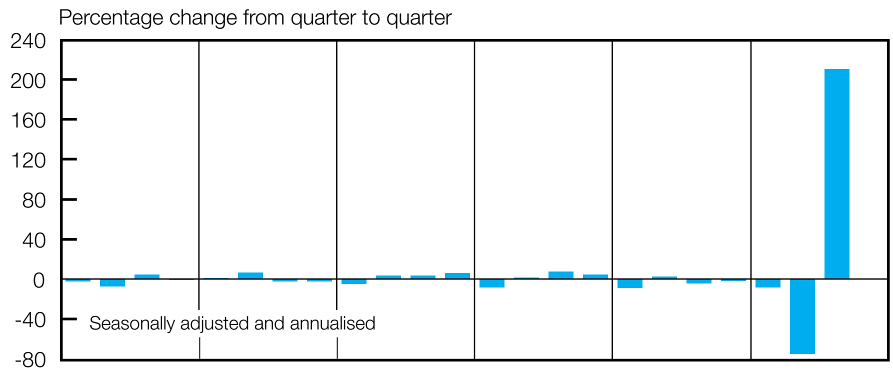


Source: Stats SA

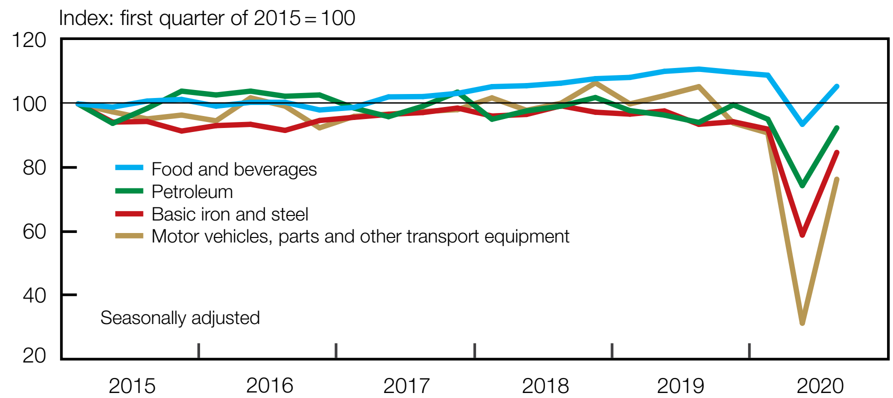
The real GVA by the *secondary sector* grew by a marked 155.6% in the third quarter of 2020, following a contraction of 72.0% in the second quarter. The real output of all three secondary sectors – manufacturing; electricity, gas and water; and construction – increased sharply.

The real GVA by the *manufacturing sector* expanded by a notable 210.2% in the third quarter of 2020 after contracting by 74.9% in the preceding quarter, and contributed the most to overall real GDP growth at 16.2 percentage points.

Real gross value added by the manufacturing sector



Physical volume of manufacturing production: selected subsectors



Source: Stats SA

The broad-based increase in production volumes was particularly evident in the subsectors supplying basic iron and steel, non-ferrous metal and metal products, and machinery; petroleum, chemical, rubber and plastic products; motor vehicles, parts and accessories and other transport equipment; food and beverages; as well as wood and wood products, paper, publishing and printing.

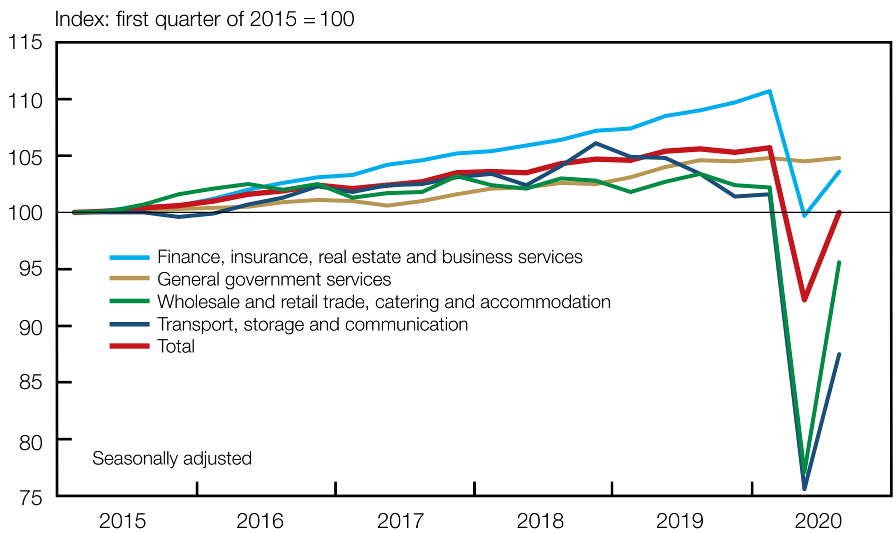
Food, and in particular beverages, contributed significantly to the increase in the real GVA as restrictions on the sale of alcoholic beverages were lifted in mid-August. The sharp and broad-based increase in output was also consistent with the seasonally adjusted utilisation of production capacity in the manufacturing sector which improved from a record low of 60.0% in May 2020 to 73.1% in August, although it was still well below the long-term average of around 81% between 1970 and 2019. Notwithstanding the increase in production, structural impediments, insufficient demand, renewed electricity disruptions and lacklustre fixed investment outlays constrained output in the third quarter to levels below those in the midst of the global financial crisis. The average level of real output of the manufacturing sector was 14.9% lower in the first nine months of 2020 than in the corresponding period in 2019.

Real economic activity in the sector supplying *electricity, gas and water* reverted from a contraction of 36.4% in the second quarter of 2020 to an annualised increase of 58.0% in the third quarter. The significant improvement in electricity production and consumption as well as in water consumption reflected the increase in economic activity, especially in the energy-intensive mining and manufacturing sectors, as well as progress with maintenance at some power stations. Disappointingly, despite the substantial expansion in the third quarter of 2020, the level of the GVA by this sector was still lower than before the electricity supply crisis that started in 2008.

The output of the *construction sector* increased by 71.1% in the third quarter of 2020, following a sharp contraction of 76.5% in the preceding quarter. This was the first increase in nine quarters. Despite the rebounds in civil construction activity as well as in both residential and non-residential building activity, the level of real output in the construction sector in the third quarter of 2020 was still well below the pre-lockdown level. The average level of real GVA by the construction sector mirrored low confidence levels, as output in the first three quarters of 2020 was still 20.0% lower than in the corresponding period in 2019.

The real GVA by the *tertiary sector* rebounded from a revised contraction of 42.0% in the second quarter of 2020 to an expansion of 37.6% in the third quarter – the only major sector that rebounded by less than the decline in the second quarter. Economic activity in almost all of the tertiary sectors picked up meaningfully in the third quarter, with only a marginal increase recorded in general government services.

Real gross value added by the tertiary sector



Source: Stats SA

The output of the *commerce sector* expanded by a robust 137.0% in the third quarter of 2020 from a decline of 67.6% in the second quarter, contributing 14.6 percentage points to overall real GDP growth. Real economic activity in the wholesale, retail and motor trade as well as the catering and accommodation subsectors increased. Higher sales of food, beverages and tobacco; agricultural raw materials and livestock; and other household goods except precious stones supported increased activity in the wholesale trade subsector.

Real retail trade activity was boosted by sales of food and beverages; pharmaceuticals and medical goods, cosmetics and toiletries; household furniture, appliances and equipment; as well as hardware, paint and glass. In addition, new and used vehicle sales increased notably from a very low base amid attractive deals offered by dealers within a low interest rate environment. The GVA by the catering and accommodation subsector was supported by interprovincial travel that was allowed from mid-August, but was still impacted by continued restrictions on travel and cross-border tourism as most international borders remained closed. Despite the marked improvement in economic activity in the commerce sector, subdued business and consumer confidence, income uncertainty, job losses and fewer employment opportunities continued to weigh on the real output of the sector. Consequently, the average level of real GVA by the commerce sector in the first three quarters of 2020 was 10.7% lower than in the corresponding period in 2019.

The real GVA by the *transport, storage and communication services sector* increased by 79.3% in the third quarter of 2020, following a sharp contraction of 69.4% in the second quarter. The improvement was underpinned by increased activity in land and air transport as well as transport support services, as the transportation of all goods was permitted for most of the quarter. Activity in transport services was further bolstered by the lifting of restrictions on interprovincial travel, including air travel within South Africa's borders, from 17 August 2020 when Level 2 of the national lockdown came into effect. However, passenger transportation remained well below pre-COVID-19 levels.

Following a revised contraction of 34.2% in the second quarter of 2020, activity in the *finance, insurance, real estate and business services sector* increased by 16.5% in the third quarter, largely due to increased activity in financial intermediation, insurance and pension funding, real estate and other business services. The average level of real GVA by the sector was 3.4% lower in the first three quarters of 2020 compared with the same period in 2019.

The real GVA by the *general government services sector* increased by 0.9% in the third quarter of 2020 after a decline of 1.0% in the preceding quarter. This reflected an increase in the number of provincial government employees, specifically in healthcare-related jobs and in higher education institutions.

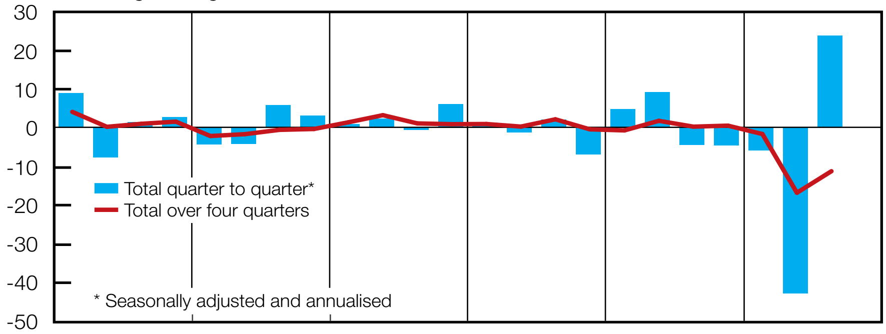
Real gross domestic expenditure[2]

Real *gross domestic expenditure* (GDE) rebounded from a contraction of 42.9% in the second quarter of 2020 to an annualised increase of 23.7% in the third quarter, while real final demand reverted from a contraction of 45.8% to an expansion of 43.5% over the same period, with both mirroring the recovery in real GDP. The real final consumption expenditure by households rebounded strongly, while real gross fixed capital formation recovered, although to a much lesser extent, and real final consumption expenditure by general government increased only slightly. By contrast, real inventory de-accumulation continued at a notably faster pace in the third quarter. Having contracted in two of the first three quarters of 2020, the average *level* of real GDE was 9.7% lower over this period compared with the corresponding period in 2019.

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

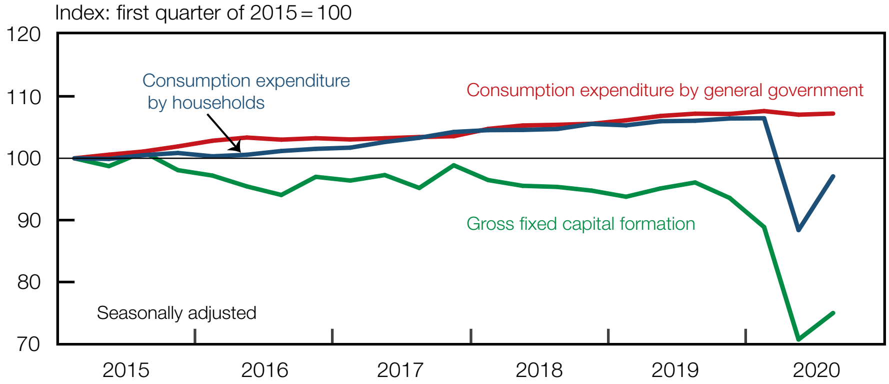
Real gross domestic expenditure

Percentage change



Components of real gross domestic final demand

Index: first quarter of 2015 = 100



Sources: Stats SA and SARB

Real gross domestic expenditure

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

Component	2019					2020		
	Q1	Q2	Q3	Q4	Year[1]	Q1	Q2	Q3
Final consumption expenditure								
Households	-0.9	2.5	0.3	1.4	1.0	0.2	-52.4	69.5
General government	2.2	2.7	1.4	-0.2	1.5	1.8	-2.1	0.7
Gross fixed capital formation	-4.1	5.8	4.1	-10.0	-0.9	-18.6	-59.8	26.5
Domestic final demand[2]	**-0.9**	**3.2**	**1.2**	**-1.2**	**0.8**	**-3.2**	**-45.8**	**43.5**
Change in inventories (R billions)[3]	*-11.7*	*29.4*	*-13.9*	*-40.3*	*-9.1*	*-66.0*	*-48.4*	*-156.2*
Residual[4]	*0.1*	*0.2*	*0.1*	*0.0*	*0.1*	*0.1*	*1.2*	*1.0*
Gross domestic expenditure[5]	**4.7**	**9.1**	**-4.5**	**-4.6**	**0.7**	**-6.0**	**-42.9**	**23.7**

1 Percentage change over one year
2 Comprises final consumption expenditure by households and general government as well as gross fixed capital formation
3 At constant 2010 prices
4 The residual as a percentage of GDP
5 Including the residual

Sources: Stats SA and SARB

With the exception of the change in inventory holdings, all the expenditure components contributed positively to growth in real GDP in the third quarter of 2020. Real final consumption expenditure by households contributed the most, at 43.2 percentage points, reflecting pent-up demand following the easing of the lockdown restrictions. Real net exports contributed a significant 38.3 percentage points to growth in real GDP, supported by a surge in the real exports of goods and services, while real gross fixed capital formation contributed only 5.1 percentage points. By contrast, the real change in inventories subtracted 20.2 percentage points from overall economic growth.

Contributions of expenditure components to growth in real gross domestic product

Percentage points

Component	2019					2020		
	Q1	Q2	Q3	Q4	Year	Q1	Q2	Q3
Final consumption expenditure								
Households	-0.5	1.6	0.2	0.8	0.6	0.1	-33.1	43.2
General government	0.4	0.5	0.3	0.0	0.3	0.4	-0.4	0.2
Gross fixed capital formation	-0.8	1.1	0.8	-2.0	-0.2	-3.8	-11.5	5.1
Change in inventories	5.3	5.3	-5.5	-3.3	-0.1	-3.2	1.8	-20.2
Residual	0.2	0.5	-0.5	-0.2	0.1	0.5	2.6	-0.4
Gross domestic expenditure	**4.6**	**9.0**	**-4.7**	**-4.8**	**0.7**	**-6.1**	**-40.6**	**27.9**
Net exports	-7.8	-5.7	3.9	3.3	-0.6	4.4	-11.2	38.3
Gross domestic product	**-3.2**	**3.3**	**-0.8**	**-1.4**	**0.2**	**-1.7**	**-51.7**	**66.1**

Components may not add up to totals due to rounding off.

Sources: Stats SA and SARB

The real *exports* of goods and services increased by a marked 31.8% in the third quarter of 2020 following a similar contraction in the previous quarter. Mining and manufacturing export volumes rebounded significantly, while agricultural exports increased at a slightly faster pace with the easing of the lockdown restrictions.

Real exports and imports of goods and services

Quarter-to-quarter percentage change*

Component	2020					
	Exports			Imports		
	Percentage of total**	Q2***	Q3***	Percentage of total**	Q2***	Q3***
Total	100.0	-30.0	31.8	100.0	-17.6	-0.4
Mining	45.0	-23.2	28.4	19.9	-14.5	1.2
Of which:						
Mineral products	20.2	-14.5	14.6	14.5	-12.9	0.9
Precious metals including gold, platinum group metals and stones	13.6	-33.4	56.9	1.1	-30.3	43.2
Base metals and articles	11.2	-24.9	21.3	4.4	-16.1	-6.9
Manufacturing	34.6	-35.2	52.9	63.5	-16.5	0.1
Of which:						
Vehicles and transport equipment	12.0	-60.7	111.1	13.1	-55.7	22.4
Machinery and electrical equipment	6.8	-36.6	76.5	25.3	-9.8	4.6
Chemical products	5.5	-7.7	21.3	9.4	7.1	-3.7
Prepared foodstuffs, beverages and tobacco	3.8	-7.9	21.2	2.6	-9.2	-13.6
Agriculture	5.7	6.5	8.3	3.4	5.2	-4.2
Of which:						
Vegetable products	4.4	10.0	7.0	1.5	39.4	-12.4
Services	13.6	-61.4	-1.2	12.3	-34.3	-5.8

* Based on seasonally adjusted and annualised data
** Expressed as a percentage of the total in 2019
*** Not annualised
Components may not add up to totals due to rounding off and the exclusion of unclassified items.

Sources: SARS, Stats SA and SARB

The turnaround in mining exports was broad-based, reflecting increased export volumes of particularly precious metals (including gold, PGMs and stones), base metals and articles thereof as well as mineral products. Robust foreign demand for vehicles and transport equipment; machinery and electrical equipment; chemical products; and prepared foodstuffs, beverages and tobacco underpinned the notable expansion in manufacturing exports. Similarly, the growth in agricultural exports was primarily supported by citrus, wine, maize, nuts, deciduous fruit and sugar cane. By contrast, the total real exports of services continued to decline, albeit at a much slower pace given the sustained prohibition of international travel.

The real *imports* of goods and services receded marginally further by 0.4% (not annualised) in the third quarter of 2020, following a sharp contraction of 17.6% in the second quarter. The real imports of services also declined further, while lower imports of vegetable products weighed down the real value of agricultural imports. Increased import volumes of precious metals (including gold, PGMs and stones) more than fully countered the lower imports of base metals and articles thereof. Manufacturing import volumes increased only marginally as the marked rise in domestic demand for vehicles and transport equipment was almost fully neutralised by lower import volumes of prepared foodstuffs, beverages and tobacco.

Contributions of real exports and imports as well as net exports of goods and services to growth in real gross domestic product

Percentage points

Component	2020					
	Exports		Imports*		Net exports	
	Q2	Q3	Q2	Q3	Q2	Q3
Total	-27.0	37.7	-15.8	-0.5	-11.2	38.3
Mining	-9.5	16.8	-2.8	0.4	-6.7	16.4
Of which:						
Mineral products	-2.6	4.2	-1.9	0.2	-0.7	4.0
Precious metals including gold, platinum group metals and stones	-4.6	9.8	-0.3	0.6	-4.3	9.2
Base metals and articles	-2.3	2.8	-0.6	-0.4	-1.7	3.2
Manufacturing	-10.8	19.9	-9.2	0.1	-1.7	19.8
Of which:						
Vehicles and transport equipment	-6.1	8.3	-6.9	2.3	0.8	6.0
Machinery and electrical equipment	-2.2	5.5	-2.0	1.6	-0.1	3.8
Chemical products	-0.4	2.0	0.6	-0.7	-1.0	2.7
Prepared foodstuffs, beverages and tobacco	-0.3	1.2	-0.2	-0.5	0.0	1.8
Agriculture	0.4	1.0	0.2	-0.3	0.2	1.3
Of which:						
Vegetable products	0.5	0.7	0.5	-0.5	-0.1	1.2
Services	-6.9	-0.1	-3.7	-0.8	-3.3	0.7

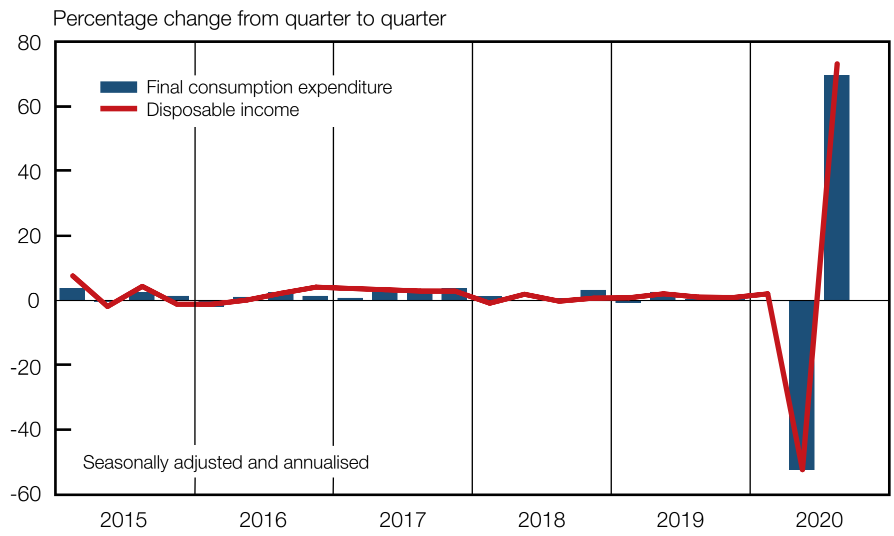
* A positive contribution by imports subtracts from growth and a negative contribution adds to growth.
Components may not add up to totals due to rounding off and the exclusion of unclassified items.

Sources: SARS, Stats SA and SARB

Real *net exports* contributed a notable 38.3 percentage points to real GDP growth in the third quarter of 2020, with real net manufacturing and mining exports contributing 19.8 and 16.4 percentage points respectively. The real net exports of vehicles and transport equipment contributed the most to overall net manufacturing exports, while precious metals (including gold, PGMs and stones) added the most to overall net mining exports. Real net agricultural and services exports also contributed marginally to real GDP growth.

Real *final consumption expenditure by households* expanded by a notable 69.5% in the third quarter of 2020 following a revised contraction of 52.4% in the second quarter. Strong rebounds in real outlays on durable, semi-durable and non-durable goods reflected resurgent demand from a very low base as restrictions on the sales of these goods were lifted. Spending on consumer services recovered at a slower pace, impacted by the remaining lockdown restrictions on other socio-economic activities and international travel. As a result, consumers probably redirected some of their service-orientated budgets to meet pent-up demand for goods. Increased real expenditure by households was consistent with a rise in real disposable income in the third quarter of 2020, despite rising unemployment and low consumer confidence. However, the average level of households' real final consumption expenditure was still 7.0% lower in the first three quarters of 2020 than in the corresponding period in 2019.

Real final consumption expenditure and disposable income of households



Sources: Stats SA and SARB

Real consumer outlays on *durable goods* rebounded by a substantial 275.9% in the third quarter of 2020 following a revised decrease of 71.9% in the second quarter. The increase was evident in all the durable goods categories, with computers and related equipment, furniture and household appliances, personal transport equipment as well as recreational and entertainment goods, in particular, all reflecting the further easing of the lockdown restrictions. Purchases of motor vehicles surged in the third quarter of 2020 as vehicle dealerships returned to normal business operations and as consumers took advantage of the favourable interest rate environment.

Real final consumption expenditure by households

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

Category	2019					2020		
	Q1	Q2	Q3	Q4	Year*	Q1	Q2	Q3
Durable goods..................	-7.2	8.7	2.2	-0.6	0.6	-6.3	-71.9	275.9
Semi-durable goods.........	-11.4	3.7	-1.6	5.6	0.5	-6.4	-87.6	302.2
Non-durable goods	-0.2	2.1	-0.2	0.7	1.1	4.3	-48.7	71.1
Services	2.6	1.3	0.7	1.4	1.2	-0.2	-36.8	23.0
Total................................	-0.9	2.5	0.3	1.4	1.0	0.2	-52.4	69.5

* Percentage change over one year

Source: Stats SA

Reverting from a decline of 87.6% in the second quarter of 2020, real spending on *semi-durable goods* expanded by a substantial 302.2% in the third quarter, as demand for clothing and footwear to a great extent contributed to the biggest quarterly increase on record. Real outlays on all the other semi-durable goods categories also increased markedly, including recreational and entertainment goods; motorcar tyres, parts and accessories; as well as household textiles, furnishings and glassware.

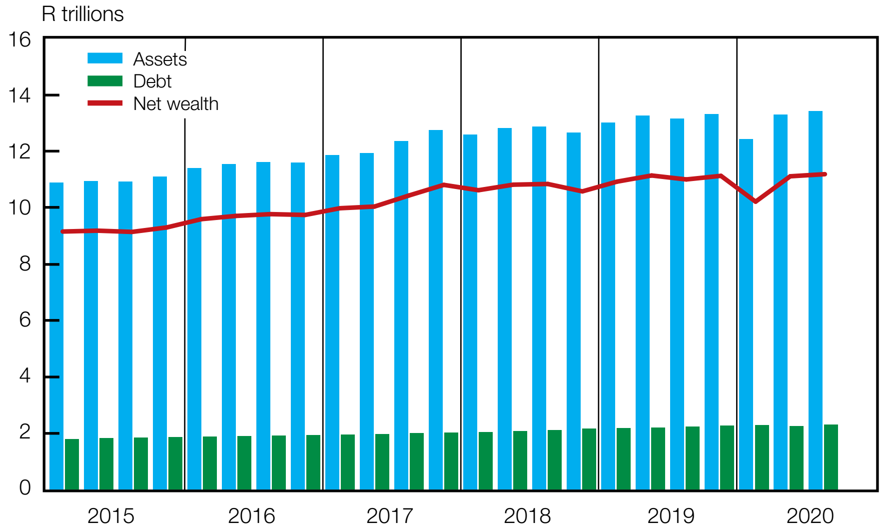
Household consumption expenditure on *non-durable goods* increased by 71.1% in the third quarter of 2020, contributing the most to growth in total final consumption expenditure by households at 26.7 percentage points. This followed a decline of 48.7% in the second quarter. Similar to the other household goods categories, higher real outlays on non-durable goods were broad-based. Expenditure on particularly food, beverages and tobacco products contributed notably, as the sale of these products was permitted again after being restricted during earlier lockdown levels. With motorists allowed to travel between provinces again, the purchase of petroleum products also increased substantially.

Real household expenditure on *services* increased by 23.0% in the third quarter of 2020 after a revised contraction of 36.8% in the second quarter. Consumer spending on all of the services subsectors increased, with transport and communication services recording the fastest growth. Real outlays on rent increased only marginally. The higher expenditure on services contributed 12.3 percentage points to growth in total household final consumption expenditure in the third quarter of 2020.

Household debt increased in the third quarter of 2020 following an unprecedented decline in the second quarter. However, household debt as a percentage of nominal disposable income decreased from 86.5% in the second quarter of 2020 to 75.7% in the third quarter, as the increase in household disposable income exceeded that in household debt. On balance, the ratio of debt-service cost to nominal disposable income declined from 9.5% in the second quarter of 2020 to 7.9% in the third quarter – the lowest since the third quarter of 2006 – reflecting the recent reductions in the prime lending rate while nominal disposable income started to normalise.

Households' net wealth increased further in the third quarter of 2020, albeit at a slower pace, as the increase in total assets outweighed that in total liabilities. Owing to the slower pace of increase in households' net wealth compared to that in nominal disposable income, the ratio of net wealth to nominal disposable income declined from 424% in the second quarter of 2020 to 367% in the third quarter.

Household balance sheet



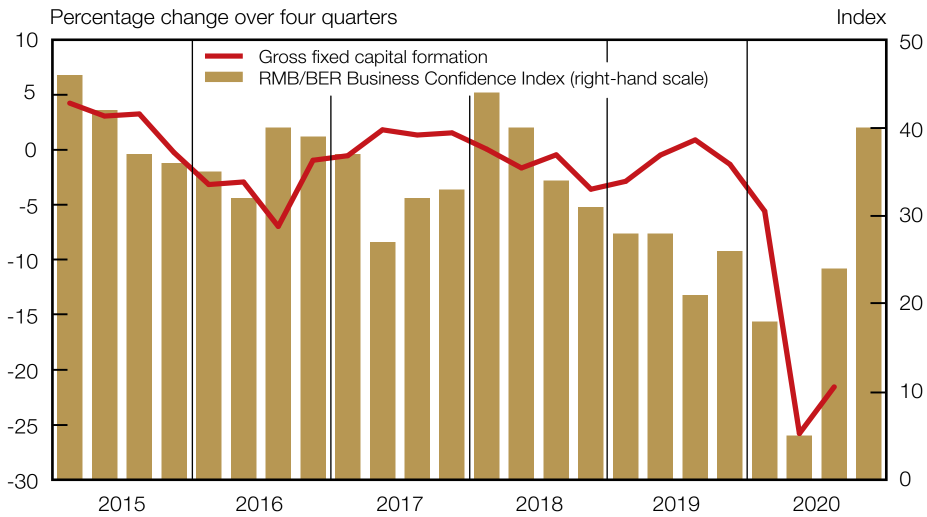
Seasonally adjusted

Source: SARB

Real *final consumption expenditure by general government* increased slightly at an annualised rate of 0.7% in the third quarter of 2020 after contracting by 2.1% in the second quarter. Spending on the real compensation of employees edged slightly higher, in line with an increase in the number of provincial government employees as well as employees in higher education institutions. The moderate expansion in real outlays on non-wage goods and services in the third quarter of 2020 reflected increased spending on health and education. The level of average real spending by general government in the first three quarters of 2020 was 0.5% higher than in the corresponding period in 2019.

Real *gross fixed capital formation* increased by 26.5% in the third quarter of 2020 following a record contraction of 59.8% in the second quarter. Real capital investment by both private and public sector corporations recovered somewhat as COVID-19 restrictions were relaxed. Gross fixed capital formation by general government, which was somewhat less affected by the national lockdown restrictions, advanced at a slightly slower pace in the third quarter as capital investment in emergency infrastructure increased at a slower rate. Nevertheless, amid political uncertainty, weak investor and business confidence, unmet infrastructure needs, periodic electricity constraints and constrained public sector budgets, the average level of real gross fixed capital formation was 17.8% lower in the first three quarters of 2020 than in the corresponding period in 2019. The level of real capital outlays by public corporations was 27.4% lower over this period – the lowest of the three institutional sectors.

Real gross fixed capital formation and business confidence

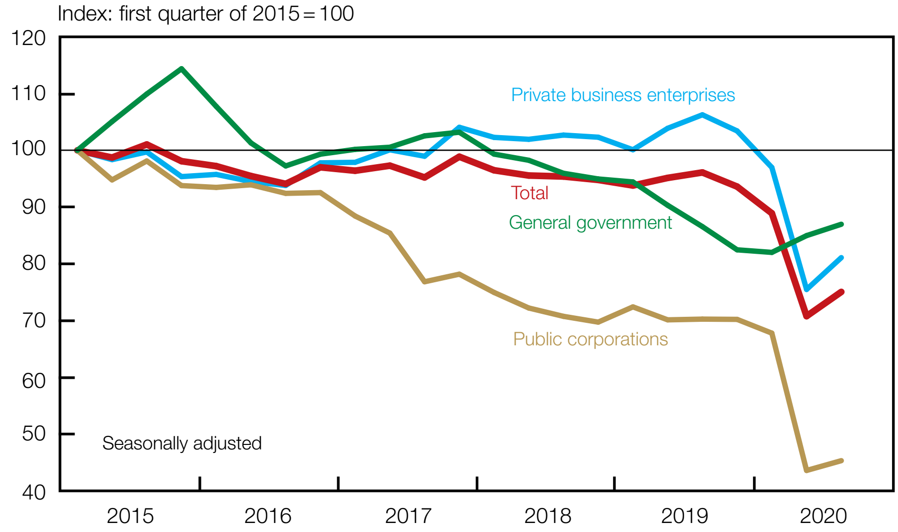


Sources: BER and Stats SA

Real gross fixed capital outlays by *private business enterprises* expanded by 33.2% in the third quarter of 2020, following a record decline of 63.3% in the preceding quarter. The rebound was broad-based, with real capital outlays on construction works as well as on non-residential buildings leading the way. The share of private business enterprises in total nominal gross fixed capital formation increased marginally to 70.1% in the third quarter of 2020 from 68.9% in the second quarter, as the rebound in private fixed capital investment exceeded that by the public sector.

Real gross fixed capital formation by the *public sector* also increased in the third quarter of 2020, supported by increased capital outlays by both public corporations and general government. Real capital spending by *public corporations* expanded by 16.8% in the third quarter of 2020, following a notable decline of 82.9% in the previous quarter. Public corporations invested primarily in transport and electricity generation, particularly in construction works, transport equipment as well as in machinery and equipment. Growth in real capital expenditure by *general government* moderated to 9.8% in the third quarter of 2020 following an increase of 15.2% in the second quarter, as capital expenditure on critical COVID-19-related medical equipment and temporary public health operations increased at a slower pace.

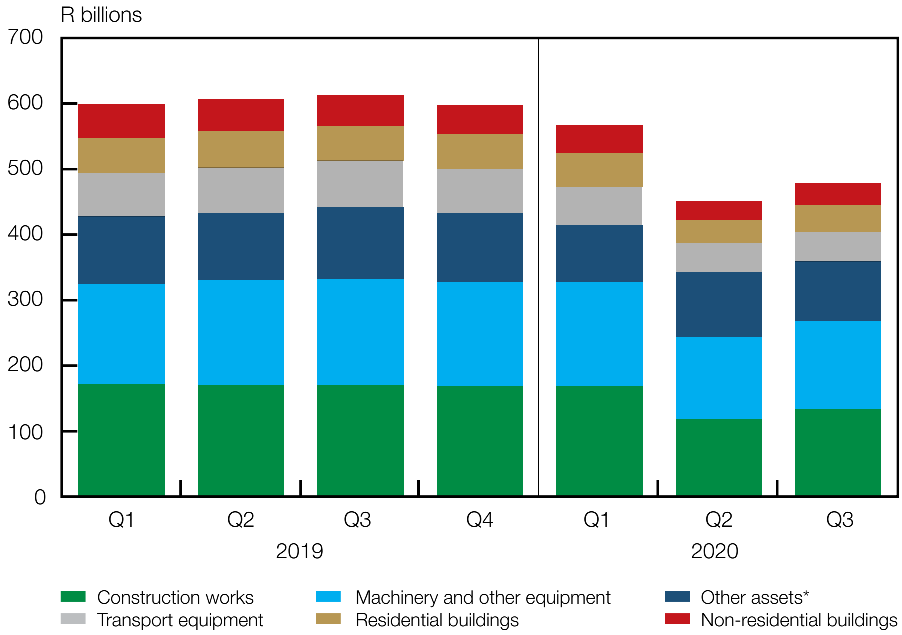
Real gross fixed capital formation by type of organisation



Sources: Stats SA and SARB

Real gross fixed capital expenditure increased across most *asset classes* in the third quarter of 2020, although the long-term downward trends persisted. Evidently, when measured over a year, capital investment in residential and non-residential buildings decreased by 23.5% and 26.3% respectively in the third quarter of 2020. Similarly, real capital investment in transport equipment and in machinery and equipment was, respectively, 36.5% and 17.4% lower in the third quarter of 2020 than in the corresponding period in 2019.

Real gross fixed capital formation by type of asset



* Other assets include information, computer and telecommunications equipment, computer software, research and development, transfer costs, cultivated biological resources, and mineral exploration and evaluation.

Source: Stats SA

Real gross fixed capital formation

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

Sector	2019					2020		
	Q1	Q2	Q3	Q4	Year*	Q1	Q2	Q3
Private business enterprises....	-8.4	16.0	9.5	-10.3	1.1	-22.7	-63.3	33.2
Public corporations................	16.3	-12.0	0.7	-0.3	-1.6	-13.1	-82.9	16.8
General government..............	-2.2	-16.3	-15.6	-17.6	-8.9	-2.2	15.2	9.8
Total......................................	**-4.1**	**5.8**	**4.1**	**-10.0**	**-0.9**	**-18.6**	**-59.8**	**26.5**

* Percentage change over one year

Source: Stats SA

Real *inventory holdings* declined for a fifth successive quarter, decreasing by a record R156 billion (at annualised 2010 prices) in the third quarter of 2020 following a decline of R48 billion in the second quarter. De-stocking continued in most sectors, particularly in trade, mining and manufacturing, as firms used existing stock to satisfy domestic demand following the lockdown along with the strong increase in the net exports of goods.

Gross nominal saving

South Africa's *national saving rate* (gross saving as a percentage of nominal GDP) improved substantially to 15.9% in the third quarter of 2020, from 11.1% in the second quarter. The saving rate of both corporate business enterprises and households increased, while dissaving by general government slowed.

Gross saving by the *corporate sector* as a percentage of nominal GDP increased from 18.8% in the second quarter of 2020 to 22.5% in the third quarter, as operating surpluses improved along with lower tax and dividend payments, after accounting for seasonal variations. Dissaving by *general government* as a percentage of GDP slowed slightly from 9.6% in the second quarter of 2020 to 8.6% in the third quarter, as total seasonally adjusted nominal government expenditure declined by more than revenue collection in the third quarter. Gross saving by the *household sector* as a percentage of GDP increased marginally to 2.0% in the third quarter of 2020 from 1.9% in the second quarter, as the increase in nominal disposable income outweighed that in nominal household consumption expenditure.

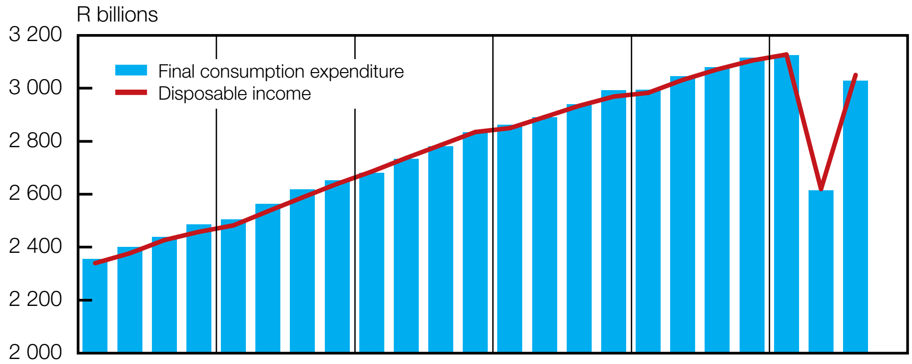
Gross saving as a percentage of gross domestic product

Ratio in per cent at seasonally adjusted annualised rates

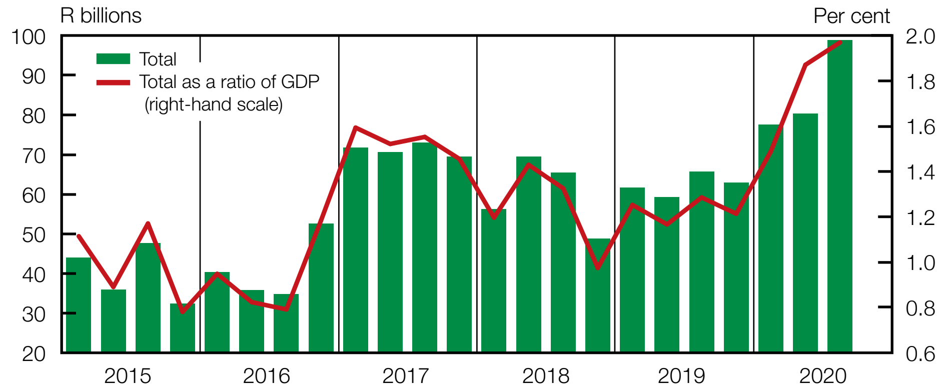
Sector	2019					2020		
	Q1	Q2	Q3	Q4	Year	Q1	Q2	Q3
Corporate........................	13.9	12.8	13.4	13.1	13.3	16.1	18.8	22.5
General government.......	-0.6	0.9	-0.4	0.2	0.0	-1.8	-9.6	-8.6
Household.....................	1.3	1.2	1.3	1.2	1.2	1.5	1.9	2.0
Total..............................	**14.6**	**14.9**	**14.2**	**14.6**	**14.6**	**15.8**	**11.1**	**15.9**

Source: SARB

Nominal final consumption expenditure and disposable income of households



Household gross saving



Seasonally adjusted

Sources: Stats SA and SARB

Box 1 Did the national lockdown distort the composite leading business cycle indicator?

The composite leading business cycle indicator for South Africa, as compiled by the South African Reserve Bank (SARB),[1] is intended to anticipate changes in the direction of aggregate economic activity. This composite leading indicator has a proven track record of shifting direction in advance of a change in the business cycle.[2] Since 1960, turning points in this indicator have occurred, on average, 7 months in advance of business cycle troughs and 13 months in advance of business cycle peaks.[3]

The focus of this box is on the impact of the coronavirus disease 2019 (COVID-19) pandemic, through the national lockdown restrictions, on 2 of the 11 component time series[4] of the leading indicator which displayed counter-intuitive movements. These indicators are the real M1 money supply[5] and the interest rate spread.[6] However, these distortions were not visible in the composite leading business cycle indicator, which attests to the robustness of combining a number of individual leading economic indicators that measure different economic processes in a composite indicator.

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1 The composite leading, coincident and lagging business cycle indicators for South Africa are published monthly by the South African Reserve Bank. See https://www.resbank.co.za/en/home/publications/composite-business-cycle-indicators

2 South Africa's business cycle is measured in terms of the growth cycle definition and therefore represents fluctuations around the long-term trend of overall economic activity.

3 See page S–159 in this edition of the *Quarterly Bulletin* for a chronology of the business cycle phases of South Africa since 1945, which reflect the reference turning points and the duration of the upward and downward phases.

4 For more detail on the most recent revision of the component time series, see 'Box 1: Revision to the composite leading and coincident business cycle indicators', published by the South African Reserve Bank in the June 2015 *Quarterly Bulletin*.

5 The real M1 money supply comprises the nominal value of banknotes and coin in circulation outside the monetary sector as well as cheque, transmission and other demand deposits of the domestic private sector with the monetary sector, deflated with the consumer price index. The six-month smoothed growth rate of this indicator is used as a component of the composite leading business cycle indicator.

6 The interest rate spread is the difference between the yield on 10-year South African rand-denominated government bonds traded in the domestic bond market and the tender rate on 91-day Treasury bills.

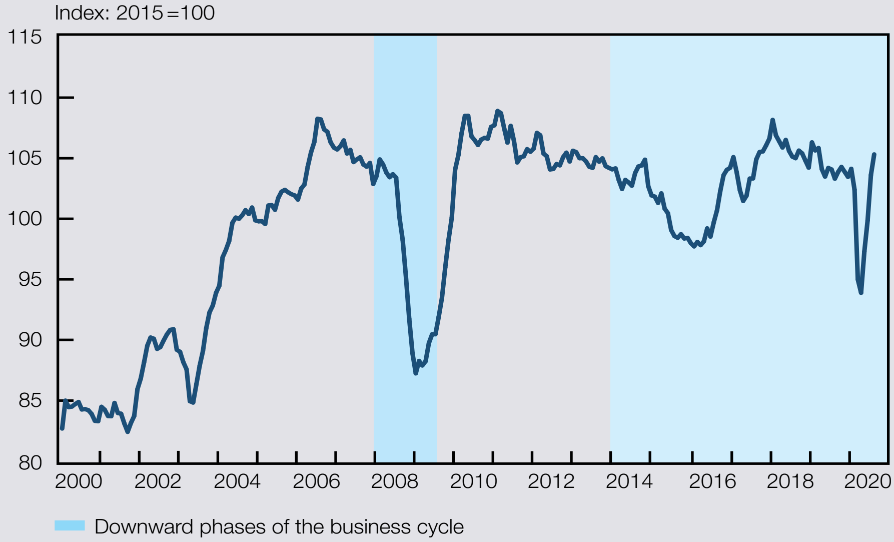
Component time series of the composite leading business cycle indicator

- Commodity price index of South Africa's main export commodities (US dollar)
- Composite leading business cycle indicator of South Africa's major trading-partner countries (percentage change over 12 months)
- Rand Merchant Bank/Bureau for Economic Research (RMB/BER) Business Confidence Index
- BER*: Volume of orders in manufacturing (half weight)
- BER*: Average hours worked per factory worker in manufacturing (half weight)
- Real M1 money supply (deflated with the consumer price index and six-month smoothed growth rate)
- Interest rate spread (yield on 10-year government bonds minus the rate on 91-day Treasury bills)
- Number of building plans approved (flats, townhouses and houses larger than 80 m²)
- Number of new passenger vehicles sold (percentage change over 12 months)
- Job advertisement space in the *Sunday Times* (percentage change over 12 months)
- Gross operating surplus as a percentage of gross domestic product

* Bureau for Economic Research, Stellenbosch University

The composite leading business cycle indicator has trended lower since March 2018 and the prediction of a slowdown in real economic growth was later confirmed by the economic recession which commenced in the third quarter of 2019. However, the leading indicator could not have anticipated the collapse in economic activity in the second quarter of 2020 due to the exogenous nature of the national lockdown brought about by COVID-19, and hence the sharp drop from March to May 2020 rather coincided with the lockdown. This was followed by a rebound up to September 2020 as the lockdown restrictions were gradually lifted.

Composite leading business cycle indicator

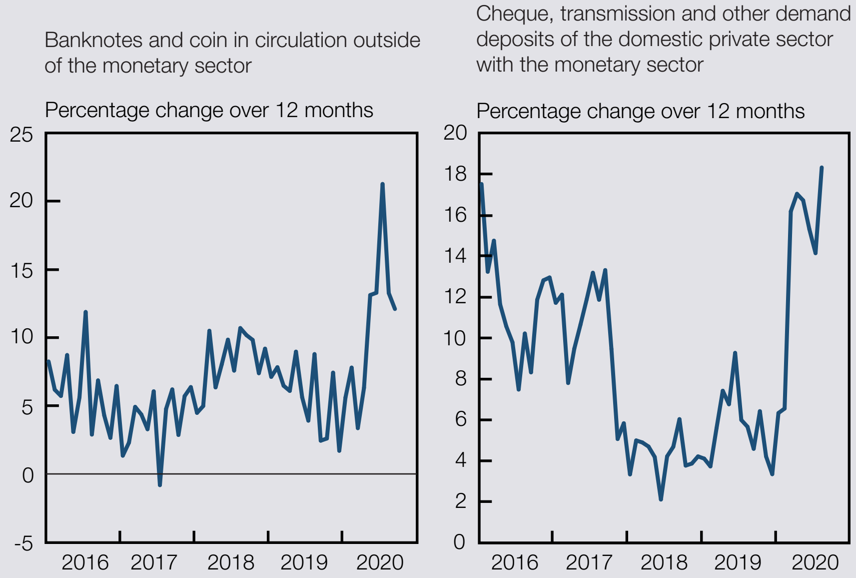


Source: SARB

During the lockdown, both the six-month smoothed growth rate in the real M1 money supply, which accelerated strongly, and the interest rate spread, which widened considerably, behaved counter-intuitively as both of these developments are usually associated with an upward phase of the business cycle.

The COVID-19 shock to the economy distorted the conventional cyclical behaviour of money supply, and during the lockdown, growth in the real M1 money supply accelerated markedly from March 2020, despite the sharp contraction in real economic activity in the second quarter of the year. Strong growth in notes and coin in circulation outside the monetary sector as well as in cheque, transmission and other demand deposits of the domestic private sector with the monetary sector initially reflected consumers' inability to purchase non-essential goods and services. Later on, it reflected both households and companies' continued cautiousness given the uncertainty surrounding COVID-19 as well as expectations of severe job losses and an extended period of weak demand. In addition, support measures such as payment holidays offered by banks as well as enhanced social grant and Unemployment Insurance Fund (UIF) payments also contributed to the increase in real M1 money supply.

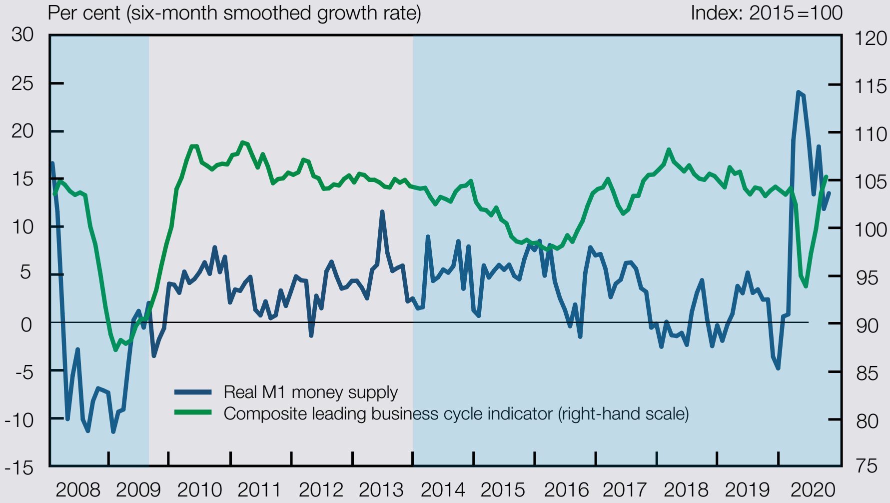
Growth in the components of real M1 money supply



Source: SARB

The demand for money usually moderates during downward phases of the business cycle and starts to increase when the cycle nears a lower turning point, as economic agents require more money for transactional purposes. As the upward phase progresses, the demand for money usually continues to increase as economic activity expands.

Composite leading business cycle indicator and real M1 money supply

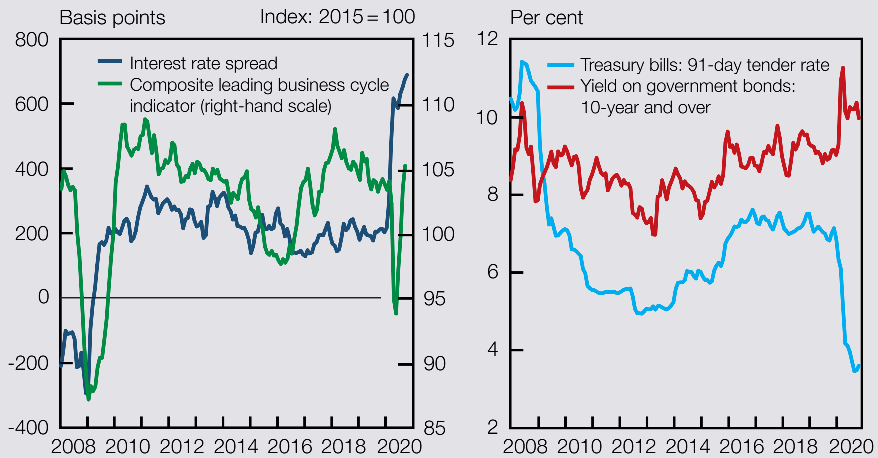


Shaded areas indicate downward phases of the business cycle

Source: SARB

The significant widening in the interest rate spread from February 2020 reflected a marked decline in the tender rate on 91-day Treasury bills (TBs) and a notable increase in the yield on 10-year South African government bonds. This came about as the TB rate followed the repurchase rate lower as the Monetary Policy Committee of the SARB eased monetary policy, whereas bond yields increased as the COVID-19 uncertainty resulted in large-scale non-resident net sales of government bonds, exacerbated by the further deterioration in South Africa's fiscal position.

Composite leading business cycle indicator and the interest rate spread



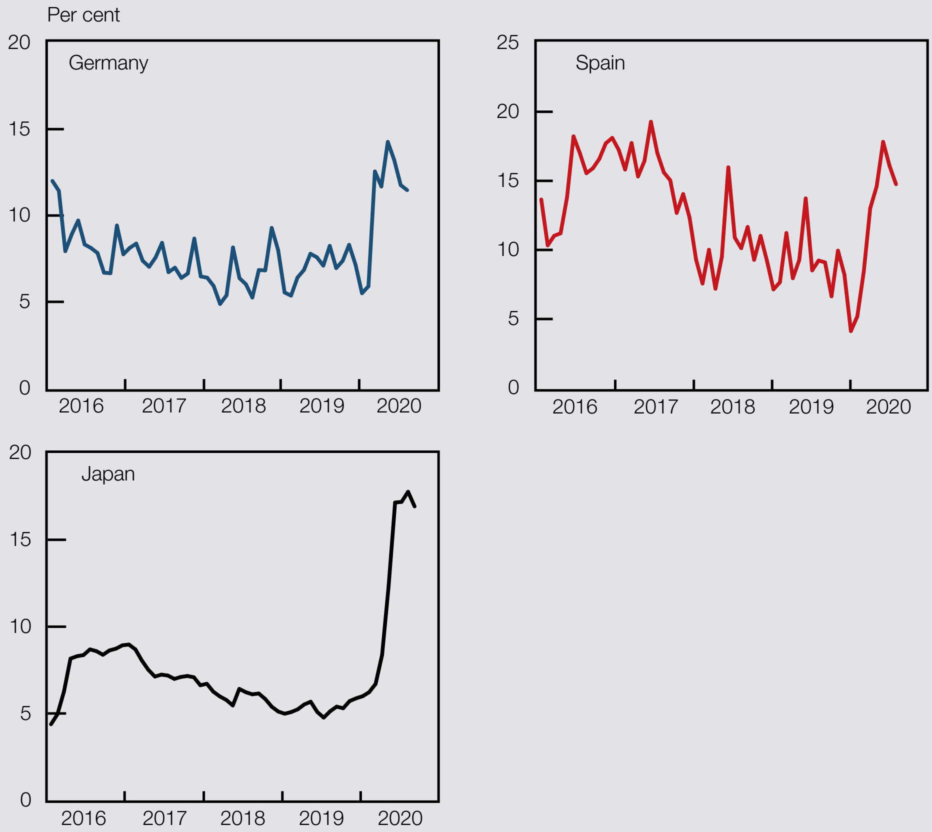
Sources: IRESS, JSE and SARB

A widening in the interest rate spread usually represents either lower short-term interest rates, which reflect an easing in monetary conditions, or an increase in bond yields, which usually points to rising longer-term inflation expectations in line with an acceleration in real economic growth, or a combination of these two factors. By contrast, a narrowing in the interest rate spread points to a slowdown in economic activity. The spread might even become negative, reflecting an inverted yield curve, which could point to an impending economic recession.

An international comparison of growth in real M1 money supply confirms a notable acceleration in this indicator in most countries, similar to that in South Africa. It appears that the combination of stimulus measures and caution resulted in a marked increase in money supply globally, irrespective of the strictness of the global lockdown measures.

Six-month smoothed growth rate of real M1 money supply in selected countries

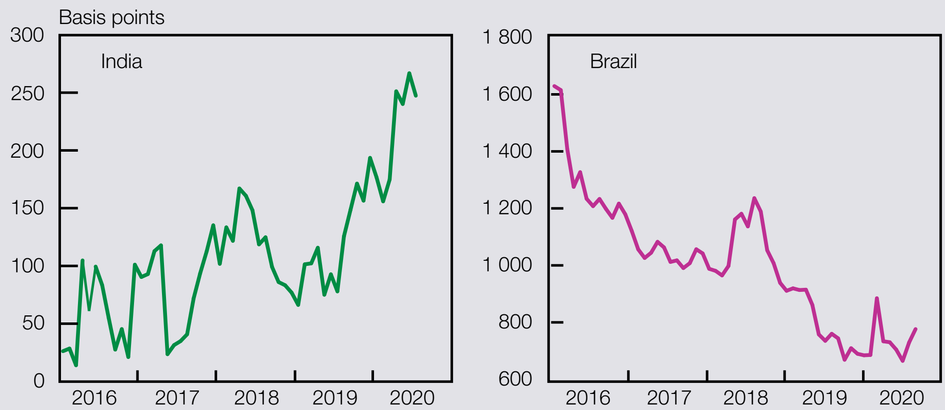
Six-month smoothed growth rate of real M1 money supply in selected countries



Source: Haver Analytics

An international comparison of the interest rate spread of almost all the selected countries reflected a narrowing over the lockdown period, with the exception of India and, to a lesser extent, Brazil where the spread widened, similar to South Africa. This illustrates the difference in the drivers of short-term money market interest rates and bond yields between countries. In the advanced economies, in particular, short-term interest rates were already at historically low levels before the onset of the pandemic, while bond yields decreased as these assets are perceived as low-risk investments during times of global risk aversion, and as continued quantitative easing by major central banks supported demand for such bonds.

The interest rate spread in selected countries



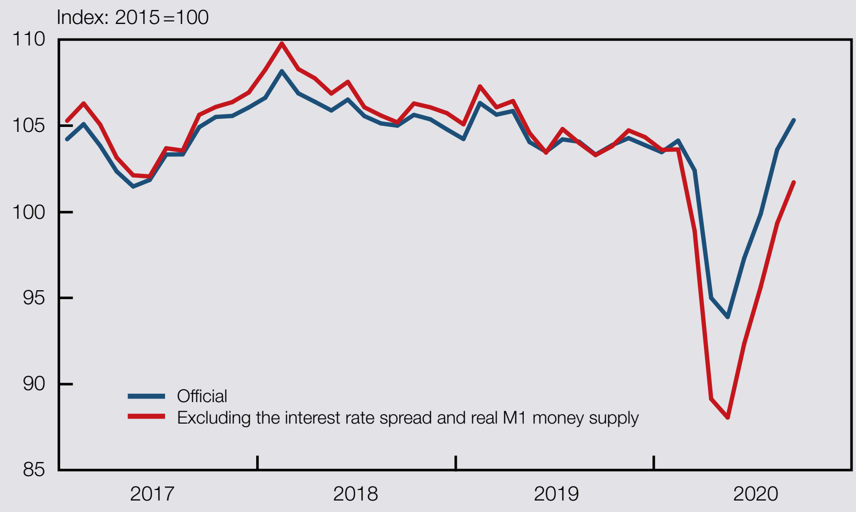
The interest rate spread in selected countries

Source: Haver Analytics

Given the ongoing economic uncertainty following the COVID-19 pandemic, the current narrow interest rate spreads in most countries could be associated with expectations of weak real economic activity. However, in the case of emerging markets such as India, Brazil and South Africa, the widening interest rate spreads are currently behaving in a countercyclical manner and should therefore be interpreted with circumspection.

When excluding the interest rate spread and the real M1 money supply from the composite leading business cycle indicator, the resultant narrower composite leading indicator displays a steeper downward trend from early 2018 to May 2020 and a slightly less pronounced recovery thereafter. Importantly, the turning points in the narrower indicator are exactly the same as those in the officially published composite leading indicator, showing that the countercyclical movement in the two excluded component series did not detract from the leading indicator's ability to indicate cyclical turning points in the economy.

Composite leading business cycle indicator



Source: SARB

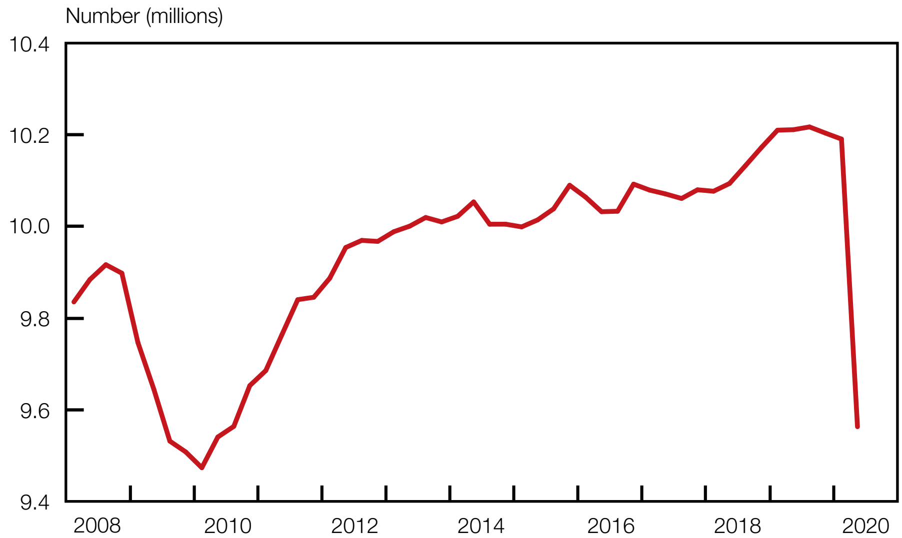
Employment[3]

Enterprise-surveyed[4] *formal non-agricultural employment* decreased by a substantial 630 200 jobs (an annualised -22.5%) in the second quarter of 2020, owing to widespread employment losses across all industries. These job losses coincided with the unprecedented contraction in economic activity amid the COVID-19 pandemic and associated lockdown restrictions to contain the spread of the virus, and lowered the level of employment to an estimated 9.56 million – the lowest level since the second quarter of 2010 in the aftermath of the global financial crisis. While the economy has since been reopened in a phased approach, the severity of the COVID-19 pandemic will likely imply job losses even after the complete lifting of all lockdown restrictions.

3 Unless stated to the contrary, the *Quarterly Employment Statistics (QES)* data reported in this section are seasonally adjusted.

4 This is according to Stats SA's *QES* survey.

Formal non-agricultural employment

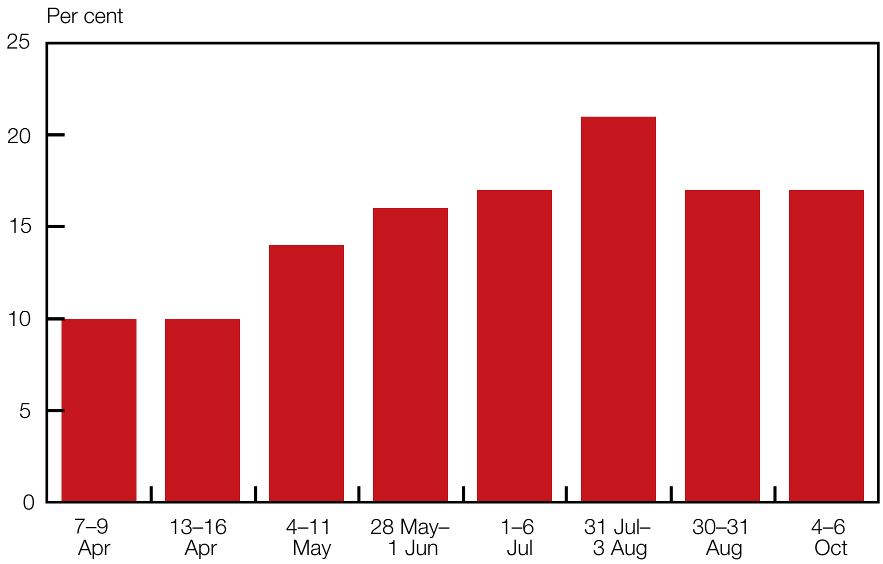


Sources: Stats SA and SARB

5 See 'The COVID-19 pandemic's financial impact on South African consumers' of 20 October 2020, available at https://content.transunion.com/v/financial-hardship-report-sa-wave-eight

The impact of COVID-19 on households is evident from a TransUnion[5] report, which shows that 77% of respondents continued to be negatively impacted financially, despite the easing of the lockdown restrictions. While consumers' concern regarding their ability to pay accounts and service debt remained high at 86%, confidence to make future payments had increased, and slightly fewer consumers reported using savings or borrowing to supplement their cash flow. Although the pace of increase in the percentage of respondents who indicated that they had lost their jobs in subsequent waves of the survey had lost momentum, businesses still continued to feel the strain of the lockdown restrictions as well as lower consumer demand.

Proportion of respondents indicating job losses in 2020



Source: TransUnion

Public sector employment decreased by an annualised 10.9% in the second quarter of 2020, as the start of the nationwide lockdown at the end of March coincided with the financial year-end of various government institutions, which resulted in the non-renewal of some contracts. Employment decreased at all levels of the public sector, with the largest year-on-year declines occurring in local governments, other public sector enterprises as well as public transport, storage and communication services. The latter two sectors reflected job shedding by ailing state-owned companies (SOCs) amid the constrained fiscal environment, while job losses in the former sector resulted mainly from the suspension of the Expanded Public Works Programme (EPWP) during the national lockdown period. The expectation of a notable increase in healthcare-related jobs following the outbreak of the COVID-19 pandemic did not materialise in the second quarter, as the majority of these workers were only contracted at the end of July 2020.

The lockdown-induced disruption to economic activity impacted *private sector employment* much more, resulting in a decrease of 564 900 jobs in the second quarter of 2020 – its lowest employment level since the first quarter of 2005. A notable 406 600 of these jobs were lost in the services sectors, which account for more than 70% of private sector employment. The magnitude of the declines in terms of the number of jobs lost, from the most to the least severe across the sectors, ranged from trade, catering and accommodation services to finance, insurance, real estate and business services and community, social and personal services, followed by transport, storage and communication services. The job losses in these services sectors were more than double those recorded in the goods-producing sectors, where employment levels had already been contracting for a number of years to multi-decade lows.

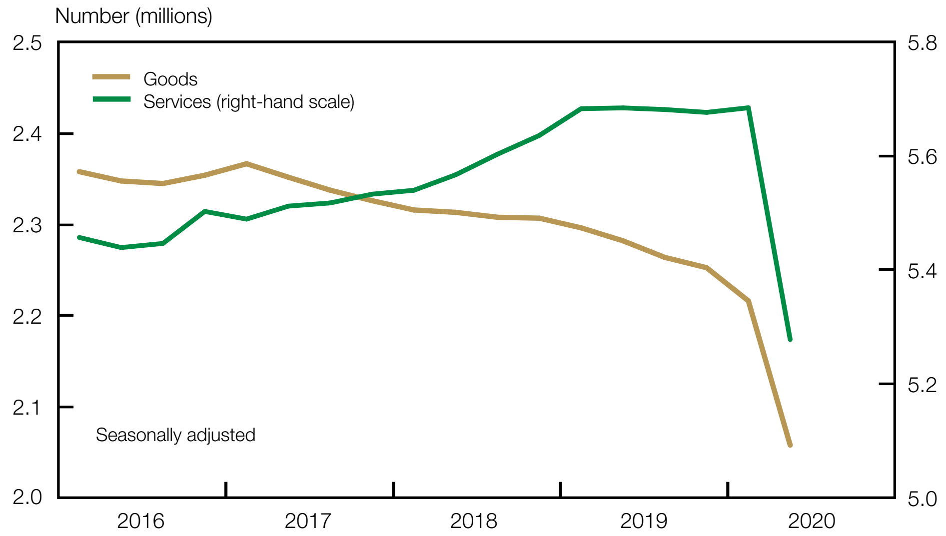
Enterprise-surveyed formal non-agricultural employment*

Sector	Change over one quarter: Q2 2020		Change over four quarters to Q2 2020	
	Number	Per cent annualised	Number	Per cent
Total mining	-10 000	-8.4	-12 700	-2.8
Gold mining	-600	-2.6	-2 500	-2.6
Other mining	-9 400	-9.8	-10 200	-2.8
Manufacturing	-73 800	-22.5	-100 000	-8.2
Construction	-74 400	-43.4	-111 400	-18.7
Total goods-producing	*-158 200*	*-25.6*	*-224 100*	*-9.8*
Trade, catering and accommodation services	-181 400	-28.3	-180 700	-7.9
Transport, storage and communication services	-31 800	-28.4	-28 600	-7.3
Finance, insurance, real estate and business services	-139 300	-21.7	-139 200	-5.9
Community, social and personal services	-54 200	-28.9	-57 900	-8.7
Total services	*-406 600*	*-25.7*	*-406 400*	*-7.2*
Private sector	-564 900	-25.7	-630 500	-7.9
National departments	-4 500	-3.8	-6 600	-1.4
Provinces	-19 400	-6.9	12 700	1.2
Local governments	-19 500	-20.2	-4 200	-1.2
Transport, storage and communication services	-5 900	-21.2	-7 400	-7.1
Other public sector enterprises, including electricity and IEC**	-16 000	-21.4	-35 400	-12.1
Public sector	-65 300	-10.9	-40 900	-1.8
Grand total	-630 200	-22.5	-671 400	-6.6

* Seasonally adjusted. Components may not add up to totals due to rounding off.
** Electoral Commission of South Africa

Sources: Stats SA and SARB

Formal private sector employment



Sources: Stats SA and SARB

The *mining sector* registered the least employment losses among the goods-producing sectors in the second quarter of 2020, despite the sharp contraction in the real value added by the sector over this period due to the closure of most mining operations, subdued global demand as well as supply-chain disruptions. Mining companies also continued to benefit from higher international commodity prices and the earlier depreciation in the exchange value of the rand. PGM prices increased notably and the gold price benefitted from concerns about the pandemic and ongoing global trade tensions.

The *manufacturing sector* shed a further 73 800 jobs in the second quarter of 2020, consistent with suppressed demand, output and sentiment. Subsequently, manufacturing business confidence[6] rose from an all-time low of 6 index points in the second quarter of 2020 to 22 index points in the third quarter, after the sector came to a near standstill in April during the strictest lockdown level. The Bureau for Economic Research (BER) noted that many businesses were either forced to close or experienced a dearth in turnover and squeezed profit margins during the lockdown which, coupled with significant idle capacity, had negative implications for investment spending and employment. Of concern is that an increase in employment could be impeded when the economy recovers, as businesses have restructured to operate with fewer labour resources.

6 As measured by the Bureau for Economic Research's (BER) Absa Manufacturing Survey.

Employment in the construction sector decreased by 74 400 jobs in the second quarter of 2020, extending the already substantial job losses registered since the third quarter of 2018. Subsequently, the *First National Bank (FNB)/BER Civil Confidence Index* increased to only 11 index points in the third quarter of 2020, a still low level from the lockdown-low of 5 index points in the second quarter. This suggests continued suppressed activity despite the easing of the lockdown restrictions, as the outlook for new projects has weakened confidence over the short term.

After falling to an all-time low of 4 index points in the second quarter of 2020, the *FNB/BER Building Confidence Index* rebounded to 24 index points in the third quarter. This surge was underpinned by a sharp increase in the confidence of hardware retailers and building material manufacturers, likely supported by increased renovations during the extended lockdown period. Despite the improvement, the survey suggests that activity and profitability remained weak. FNB expects this outlook to continue over the short term in light of weak order books and muted growth in the building project pipeline.

The COVID-19 labour market shock was particularly evident in the private services sectors of the economy, which employ many lower-skilled workers, often in lower-earning jobs and on flexible employment contracts. According to the International Labour Organization (ILO), these jobs also have weaker protection and a higher possibility of substitution by home production or mechanisation. The *finance, insurance, real estate and business services sector* shed an estimated 139 300 jobs in the second quarter of 2020, largely due to substantial employment losses registered in the business services not elsewhere classified subsector. This subsector alone contributed about 20% to the decline in total services sector employment, as the majority of these workers are employed on limited and unspecified duration contracts.

Similarly, the *trade, catering and accommodation services sector* lost around 181 400 jobs in the second quarter of 2020. Notable job shedding took place in the retail trade as well as the hotel and restaurant subsectors, as the initial hard lockdown, together with the effect of the prolonged period of travel restrictions, severely impacted the hospitality industry and reduced retail clientele. After plunging to a 29-year low of 11 index points in the second quarter of 2020, the increase in retailer confidence[7] to 36 index points in the third quarter mostly reflected optimism related to the ability to trade again. However, business conditions across the entire retail sector were affected by the weak domestic economic environment, which necessitated a reconfiguration of business models. Retailers are not expecting a material improvement in conditions in the short term as the weakness in household balance sheets, labour market uncertainty and muted consumer confidence weigh on consumer spending.

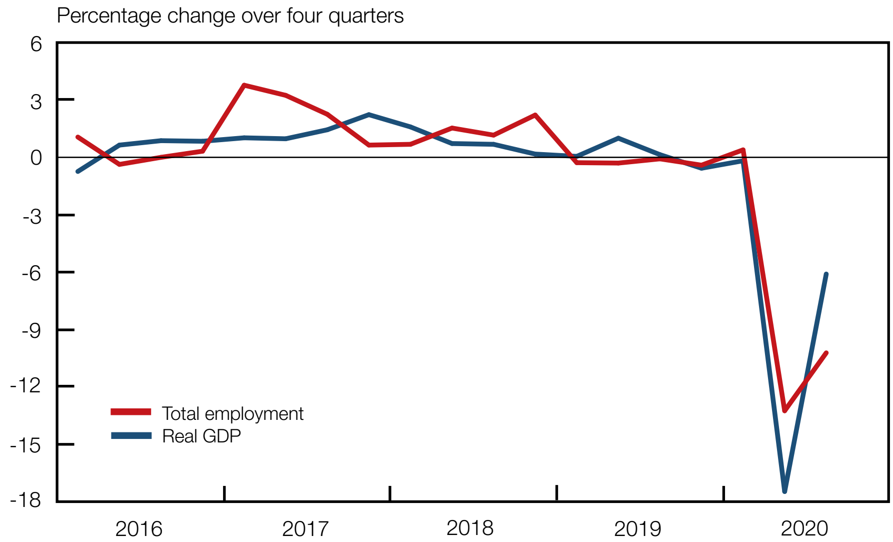
Following a sharp seasonally adjusted decline of 2.2 million (-13.4%) in the second quarter of 2020, household-surveyed employment increased by 506 000 (3.6%) in the third quarter. At approximately 14.69 million in the third quarter of 2020, total employment was still 1.6 million (10.3%) below the level of a year earlier.[8] This reflected the marked contraction in real GDP

7 As measured by the BER's Retail Survey.

8 Stats SA noted that the response rate of the *QLFS* was 57.6% for the third quarter of 2020 compared with 57.1% in the second quarter and 87.7% in the first quarter. Furthermore, given the change in the survey mode of collection (telephonic instead of face to face) and with estimates not based on a full sample, a comparison with previous quarters should be made with caution. http://www.statssa.gov.za/publications/P0211/P02113rdQuarter2020.pdf

during the second quarter, as the effects of COVID-19 and subsequent lockdown restrictions dealt a severe blow to the already weak labour market. Job losses were recorded in all four main household-surveyed subsectors in the year to the second quarter of 2020. In the third quarter of 2020, the level of formal non-agricultural employment was still 900 000 below that of a year earlier, with informal sector employment 539 000 lower, employment by private households 165 000 lower and agricultural employment 72 000 lower. Moreover, significant year-on-year job losses occurred among workers with unspecified employment contracts (942 000), followed by those with contracts of a limited duration (239 000) and those with contracts of a permanent nature (235 000) in the third quarter of 2020.

Household-surveyed employment and economic activity



Sources: Stats SA and SARB

Household-surveyed employment by industry* (number, thousands)

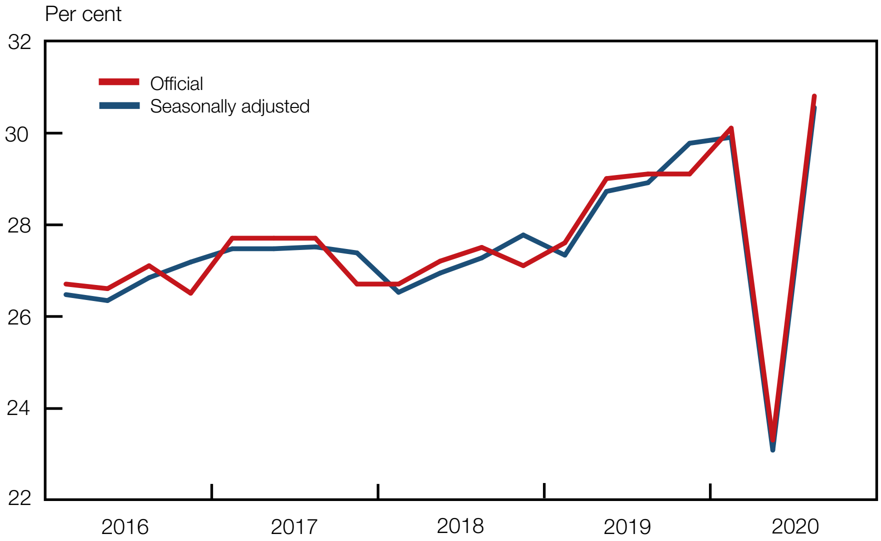
	Share of total employed Q3 2020	Seasonally adjusted			Not seasonally adjusted		
		Q3 2020	Change over one quarter Q3 2020		Q3 2020	Change over four quarters Q3 2020	
	Per cent	Number	Number	Per cent	Number	Number	Per cent
Agriculture	5.6	803	13	1.6	808	-72	-8.2
Mining	2.6	417	44	11.8	419	0	0.0
Manufacturing	10.3	1 477	22	1.5	1 460	-300	-17.0
Electricity, gas and water supply	0.8	97	-13	-11.8	90	-43	-32.3
Construction	7.6	1 073	-1	-0.1	1 080	-259	-19.3
Trade, catering and accommodation services	20.9	2 992	40	1.4	3 008	-400	-11.7
Transport, storage and communication services	6.3	878	-11	-1.2	878	-97	-9.9
Finance, insurance, real estate and business services	16.0	2 430	174	7.7	2 434	-58	-2.3
Community, social and personal services	22.9	3 391	153	4.7	3 381	-298	-8.1
Private households	7.1	1 129	128	12.8	1 121	-165	-12.8
Total employed	100.0	14 687	549	3.9	14 679	-1 692	-10.3

* Some totals may not add up due to rounding off.

Source: Stats SA

Despite the sharp decline in employment, the number of officially unemployed persons decreased markedly by 2.8 million in the second quarter of 2020 and by 2.4 million (-35.3%) from a year earlier, bringing the number of officially unemployed persons to a multi-year low of 4.3 million. This resulted in a significant decline in South Africa's official unemployment rate to 23.3% in the second quarter of 2020, from 30.1% in the first quarter (and by 29.0% a year earlier). This outcome reflected classification and measurement challenges related to the national lockdown. Statistics South Africa (Stats SA) followed the ILO guidelines which resulted in a marked decrease in measured unemployment in South Africa as the COVID-19 lockdown restrictions hindered mobility, with those who had lost their jobs not being able to search for new jobs and those who were unemployed also not being able to actively search for a job. However, as the lockdown restrictions eased and job searches resumed, the number of officially unemployed persons increased by 2.2 million (51.6%) in the third quarter of 2020, and decreased by 201 000 (-3.0%) from a year earlier, bringing the official number of unemployed persons to 6.5 million. This resulted in a significant reversal in South Africa's official unemployment rate from 23.3% in the second quarter of 2020 to 30.8% in the third quarter (and from 29.1% a year earlier). The seasonally adjusted unemployment rate also increased sharply, from 23.1% in the second quarter of 2020 to 30.6% in the third quarter.

Unemployment rate



Sources: Stats SA and SARB

The number of discouraged work seekers increased by 330 000 (13.6%) between the second and third quarter of 2020, but fell by about 97 000 (-3.5%) in the year to the third quarter. Unique to the second quarter of 2020 is the 'other not economically active' category, which increased significantly by 5.3 million people (42.4%), and is the main reason for the technical bias in the unemployment rate. All job losers as well as the unemployed who did not satisfy the 'active job search' criteria were classified under this category. The outcome of a large increase in the not economically active population, which resulted in a technical decline in the official unemployment rate in the second quarter of 2020, was observed globally. However, in the third quarter of 2020 about 2.5 million people moved out of the 'other not economically active' category and back into the labour force as they were allowed to search for jobs.

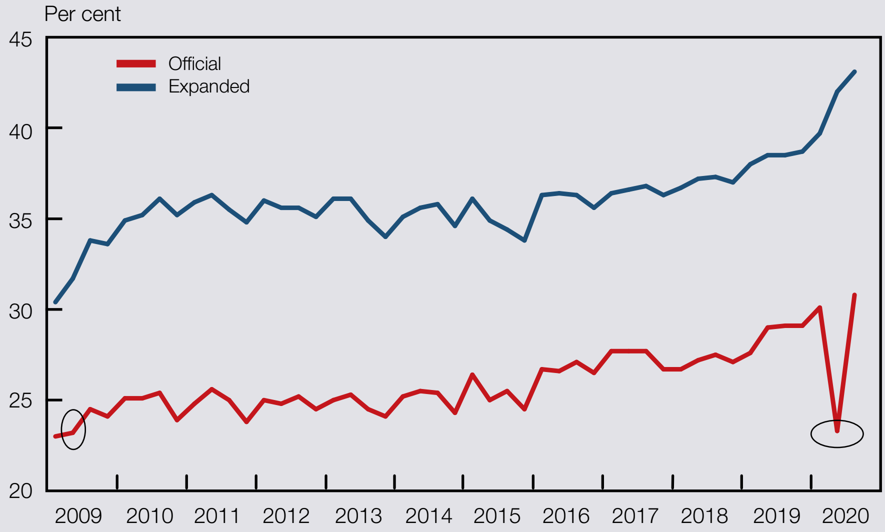
Box 2 Why did South Africa's unemployment rate decline sharply in the second quarter of 2020?

South Africa's official unemployment rate declined substantially to 23.3% in the second quarter of 2020 from a record high of 30.1% in the first quarter. The surprising second-quarter outcome represented the lowest unemployment rate since the second quarter of 2009 and was counter-intuitive, given the marked contraction in real economic activity on account of the coronavirus disease 2019 (COVID-19) outbreak and the subsequent decrease of 2.2 million employed persons. The official unemployment rate then increased sharply to 30.8% in the third quarter of 2020, above its pre-COVID level, as lockdown restrictions eased.

The sharp fall in the official unemployment rate in the second quarter was a temporary anomaly, reflective of the national lockdown that impeded people's ability to actively search for work, together with a number of classification and measurement challenges encountered by Statistics South Africa (Stats SA) when conducting the second-quarter 2020 Quarterly Labour Force Survey[1] (QLFS). International comparisons reveal similar movements in the official unemployment rate of most countries to that of South Africa during the second quarter of 2020, although the timing of the full impact differed.

South Africa's expanded unemployment rate, which includes discouraged work seekers and those who did not actively search for work, on the contrary increased from 39.7% in the first quarter of 2020 to 42.0% in the second quarter, indicating more accurately the level of unemployment at the time. The expanded unemployment rate then increased even further to a new high of 43.1% in the third quarter of 2020.

Unemployment rate



Source: Stats SA

Stats SA's methodology for the calculation of the official unemployment rate adheres to the International Labour Organization (ILO) guidelines[2] and measures the portion of the labour force[3] that is unemployed. The unemployed portion is measured as all persons aged 15 to 64 years who were not employed in the reference week of the survey; who actively looked for work or tried to start a business in the four weeks preceding the survey interview; who were available to begin working or to start a business in the reference week; or who had not actively looked for work in the past four weeks, but had a job or business to start at a definite date in the future for which they were available.[4] The official unemployment rate is calculated as:

$$\textit{Official unemployment rate} = \frac{\textit{Total unemployment}}{\textit{Total labour force}} \times 100$$

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1 Stats SA noted that the response rate of the QLFS was 57.1% for the second quarter of 2020 compared with 87.7% for the first quarter. Furthermore, given the change in the survey mode of collection (telephonic instead of face to face) and with estimates not based on a full sample, a comparison with previous quarters should be made with caution. See page 20 in Stats SA's statistical release PO211 'Quarterly Labour Force Survey'. http://www.statssa.gov.za/publications/P0211/P02113rdQuarter2020.pdf

2 See https://ilostat.ilo.org/resources/concepts-and-definitions/#standards

3 The labour force equals the total number of employed and unemployed persons.

4 See page 24 in Stats SA's statistical release PO211 'Quarterly Labour Force Survey Quarter 2: 2020'. http://www.statssa.gov.za/publications/P0211/P02112ndQuarter2020.pdf

Quarterly Labour Force Survey statistics

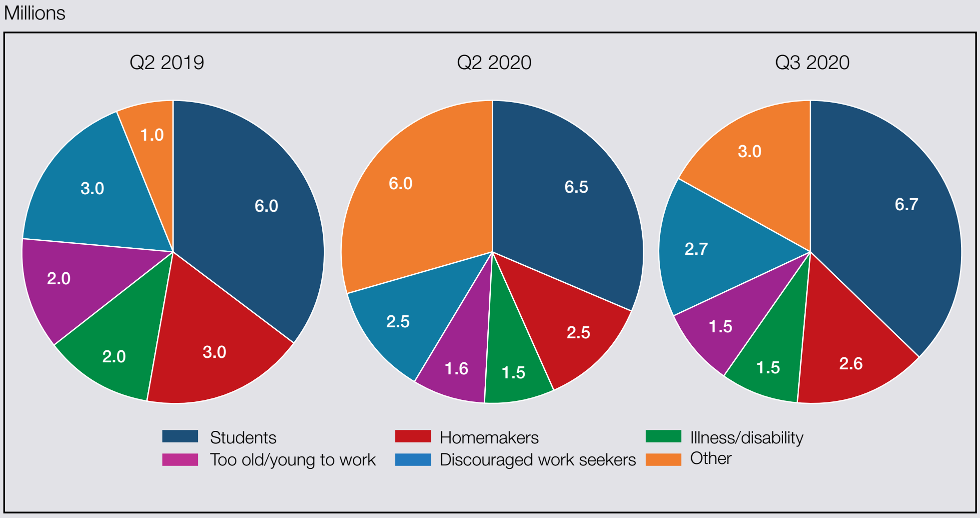
	Number (thousands)				Quarter-to-quarter change			
					Number		Per cent	
	Sep 2019	Mar 2020	Jun 2020	Sep 2020	Jun 2020	Sep 2020	Jun 2020	Sep 2020
a. Total employed	16 375	16 383	14 148	14 691	-2 253	543	-13.6	3.8
b. Total unemployed (official definition)	6 734	7 070	4 295	6 533	-2 775	2 238	-39.3	52.1
c. Total labour force (a+b)	23 109	23 452	18 433	21 224	-5 019	2 791	-21.4	15.1
d. Total not economically active	15 474	15 422	20 578	17 944	5 156	-2 634	33.4	-12.8
e. Population 15–64 years (c+d)	38 582	38 874	39 021	39 167	147	146	0.4	0.4
f. Official unemployment rate[1] (b/c)*100	29.1%	30.1%	23.3%	30.8%	–	–	–	–
g. Discouraged	2 855	2 918	2 471	2 696	-447	225	-15.3	9.1
h. Other reasons for not searching for work	820	929	6 041	2 995	5 112	-3 046	550.3	-50.4
i. Expanded unemployment rate[2]	38.5%	39.7%	42.0%	43.1%	–	–	–	–

1 Stats SA follows the ILO definition of calculating the official unemployment rate, which is internationally comparable.
2 The expanded unemployment rate is calculated by Stats SA's own in-house formula and is not internationally comparable.

Source: Stats SA

From the first to the second quarter of 2020, both the number of employed and unemployed persons decreased markedly. The decline in the number of employed persons largely reflected job losses as a result of the sharp contraction in real economic activity, while the decline in the number of unemployed persons reflected the inability to actively search for employment due to the lockdown restrictions. With these people prevented from being active in the labour market, they were classified as not economically active due to 'other' reasons. Stats SA noted that almost all of these people indicated 'national lockdown' as their main reason for inactivity. Apart from the 'other' category, which was the major driver of inactivity in the second quarter of 2020, not economically active persons also include students, homemakers, ill or disabled people, those who are either too old or too young to work, as well as discouraged work seekers. The marked increase in the 'other' category in the second quarter of 2020 was partially reversed in the third quarter, as people were again able to search for jobs. This resulted in a sharp decline in the total not economically active category in the third quarter, with the majority of those people moving to the unemployed category.

Characteristics of the not economically active population



Source: Stats SA

Although lowering the official unemployment rate in the second quarter of 2020, the marked increase in the number of not economically active persons contributed to the increase in the expanded unemployment rate. Expanded unemployment[5] is measured as all persons aged 15 to 64 years who were not employed in the reference week of the survey; and who were available to work but did not look for work either because they were discouraged from looking for work, or did not look for work for reasons other[6] than discouragement.

$$\textit{Expanded unemployment rate} = \frac{\textit{Total unemployed + discouraged work seekers + other reasons for not searching}}{\textit{(Total labour force + discouraged work seekers + other reasons for not searching)}} \times 100$$

The phenomenon of a large increase in the not economically active population and a concomitant decrease in unemployment was not unique to South Africa, and was also observed globally, with the exception of Canada and the United States (US). The ILO[7] noted that unemployment decreased as the lockdowns led to both a substantial increase in job losses and inactivity in searching for jobs. Similar to Stats SA, the ILO also cautioned that changes in unemployment in the second quarter of 2020 could be misleading. The ILO indicated that earlier crises show that reinstating or activating inactive people into employment is even more difficult than re-employing the unemployed, which suggests that the labour market recovery could be very slow and protracted.

The different outcome in the US and Canada is due to persons on temporary lay-off being considered as not attached to their job, and therefore classified as unemployed.[8] According to the Organisation for Economic Co-operation and Development[9] (OECD), people are classified as unemployed if they fulfil the criteria of being available and actively searching for a job, which is in line with the ILO definition. However, the OECD emphasised that, following COVID-19, many countries have somewhat adjusted their calculation of the unemployment rate.

The US Bureau of Labor Statistics[10] (BLS) noted that in March 2020, people who were laid off due to pandemic-related closures were specifically classified as 'unemployed on temporary lay-off' without further testing for their return to their job. Moreover, people who were absent from work during the entire reference week were not included in this category but were misclassified[11] as 'employed but not at work'. In Canada, persons on temporary lay-off were also classified as unemployed if they had a date of return or provided an indication that they would be re-called by their employers. By contrast, Eurostat[12] indicated that in Europe, those temporarily laid off were still classified as employed but not at work if they had already worked at their current job before being laid off and were expected to return after the period of absence.

In the second quarter of 2020, the number of unemployed persons decreased and the number of not economically active persons increased substantially in many countries, although the timing of the full impact differed, based on similar methodological treatments of both unemployment and inactivity. This resulted in a decline in the official unemployment rate of most countries, with the US and Canada the notable exceptions.

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5 See page 12 in Stats SA's statistical release PO211 'Quarterly Labour Force Survey Quarter 3: 2020'. http://www.statssa.gov.za/publications/P0211/P02113rdQuarter2020.pdf

6 The number of people indicating other reasons for not searching for employment is derived by Stats SA, and is calculated as expanded unemployment minus official unemployment minus discouraged work seekers.

7 International Labour Organization, 'ILO Monitor: COVID-19 and the world of work', sixth edition, 23 September 2020. https://www.ilo.org/global/topics/coronavirus/impacts-and-responses/WCMS_755910/lang--en/index.htm

8 In the US, those temporarily laid off are classified as unemployed, unless they have an expected future date to return to work or otherwise fulfil the active job-search criteria.

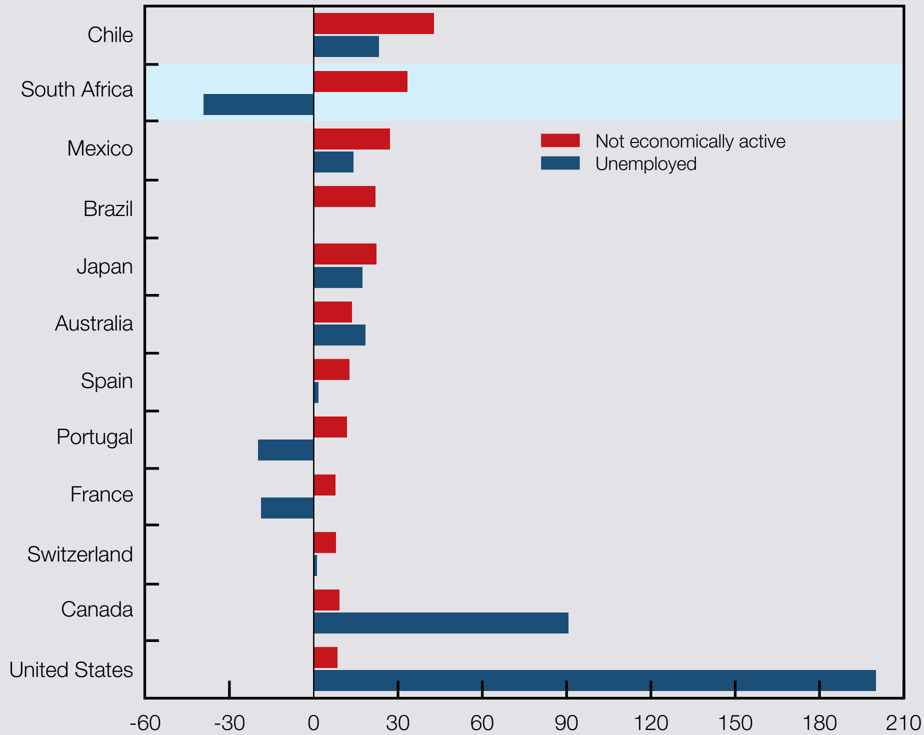
9 OECD News Release, 'Unemployment rates', July 2020. https://www.oecd.org/sdd/labour-stats/publicationsdocuments/newsrelease/

10 US Bureau of Labor Statistics, 'Frequently asked questions: The impact of the coronavirus (COVID-19) pandemic on the employment situation for March 2020', 3 April 2020. https://www.bls.gov/cps/employment-situation-covid19-faq-march-2020.pdf

11 The BLS added that previous misclassifications in the US data occurred with federal workers in both the 2013 and 2019 partial federal government shutdowns.

12 European Commission, Eurostat, 'EU Labour Force Survey Explanatory Notes (to be applied from 2016Q1 onwards)', March 2016. https://ec.europa.eu/eurostat/documents/1978984/6037342/EU-LFS-explanatory-notes-from-2016-onwards.pdf

Quarterly change in the unemployed and not economically active population in the second quarter of 2020 in selected countries



Per cent

Sources: ILO and Stats SA

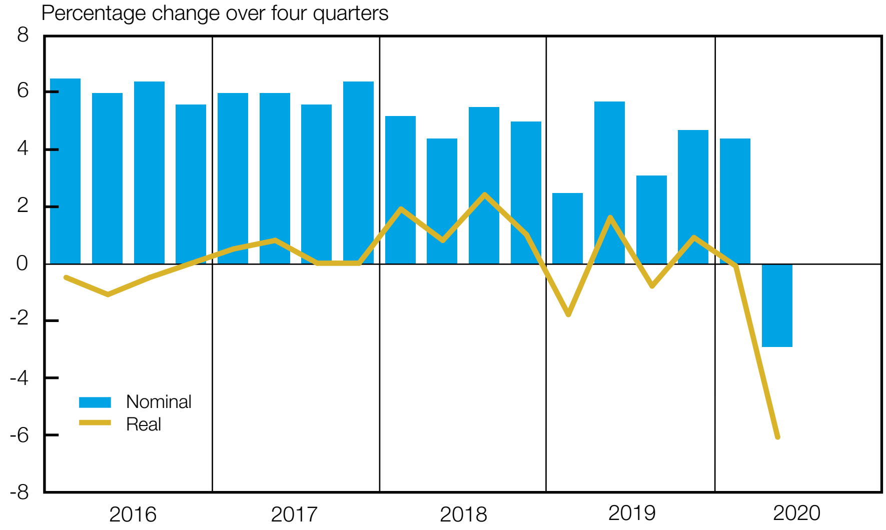
The expanded unemployment rate is probably a more realistic indicator of labour market conditions given the inactivity during the national lockdown. In South Africa, as well as in other countries, the official unemployment rate could rise sharply as survey collection methods are restored and as people are allowed to actively search for jobs following the lifting of the lockdown restrictions. This was already evident in the third quarter of 2020 with the substantial movement from inactivity to unemployment.

Labour cost and productivity

The year-on-year rate of change in *formal non-agricultural nominal remuneration per worker* reverted from an increase of 4.4% in the first quarter of 2020 to a decrease of 2.6% in the second quarter – the lowest on record. The combination of COVID-19-induced salary reductions, much lower salary increases, wage freezes as well as significantly lower bonus, overtime and commission payments exerted significant downward pressure on nominal remuneration growth. In addition, the pace of decrease in real wages per worker accelerated notably from 0.1% in the first quarter of 2020 to a 37-year high of 6.4% in the second quarter.

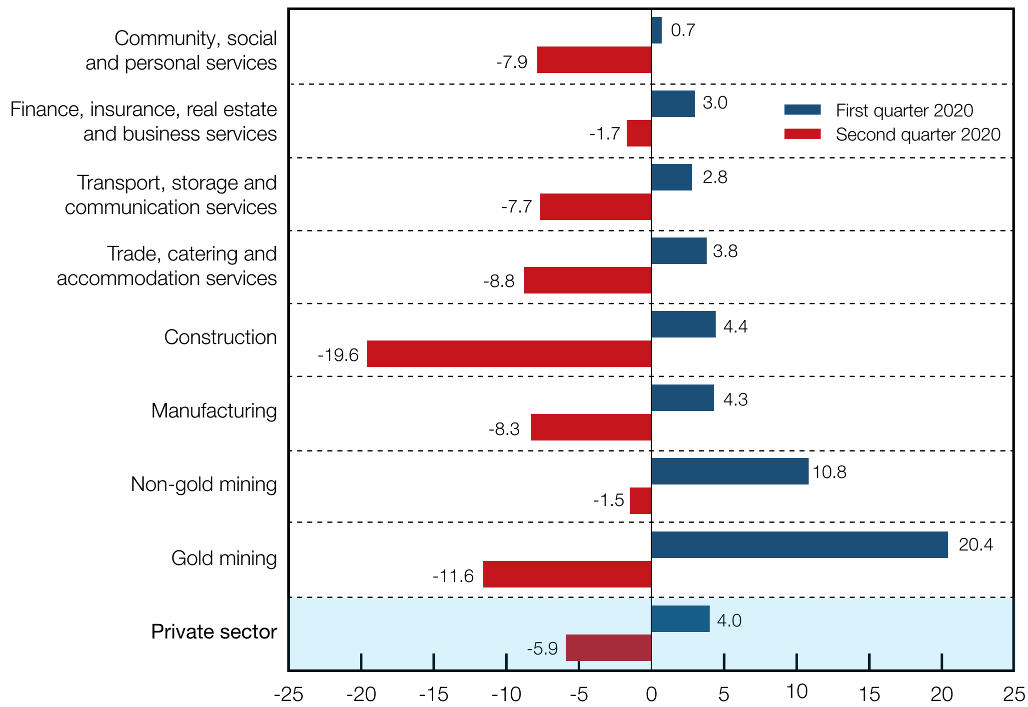
The rate of increase in *nominal remuneration per private sector worker* decelerated sharply from 4.0% in the first quarter of 2020 to a historic low of -5.9% in the second quarter due to a broad-based decrease in basic salaries and wages across all private subsectors, as well as lower bonus and overtime payments. In real terms, private sector remuneration per worker decreased by a substantial 9.5% in the second quarter of 2020 from a year earlier.

Formal non-agricultural remuneration per worker



Sources: Stats SA and SARB

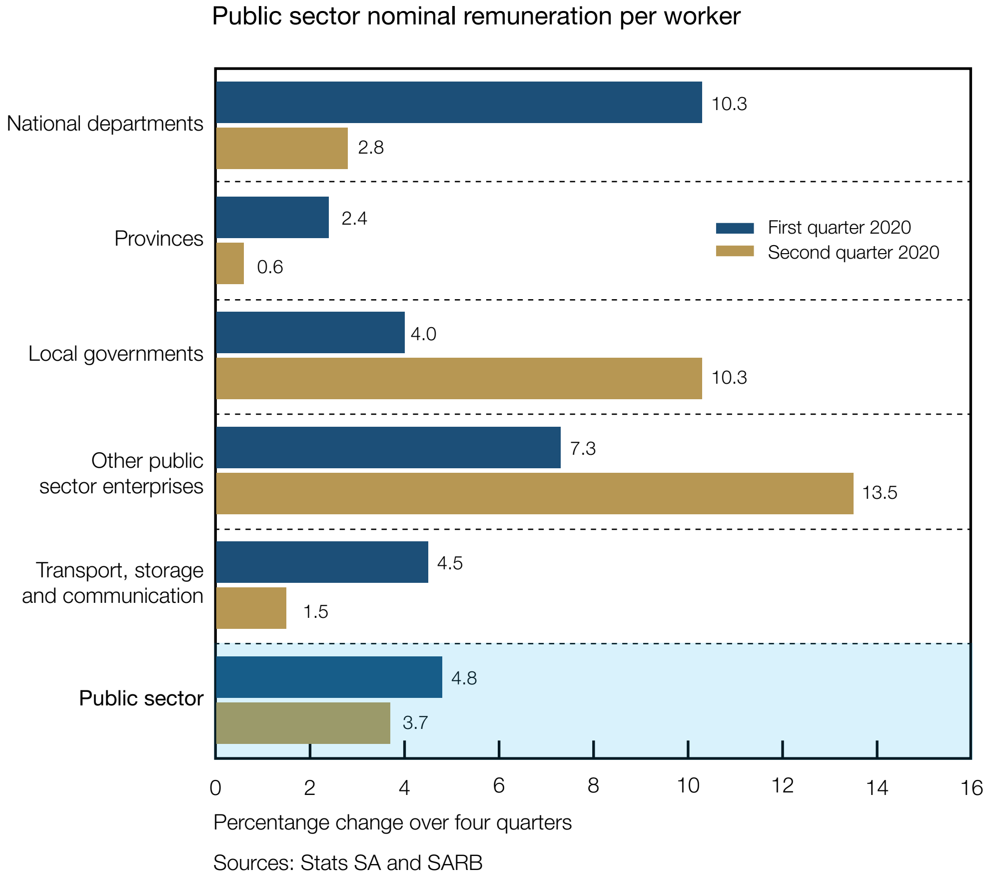
Private sector nominal remuneration per worker



Percentange change over four quarters

Sources: Stats SA and SARB

In stark contrast, *public sector remuneration growth per worker* only slowed from 4.8% in the first quarter of 2020 to 3.7% in the second quarter. Wage growth per worker was weighed down by the non-implementation of the annual public sector wage increase in 2020 to curb the government wage bill, particularly at national departments and provinces. By contrast, wage growth per worker accelerated notably at local governments and other public sector enterprises, likely due to the temporary suspension of the EPWP during the national lockdown, which substantially reduced the number of employees in these two tiers of government.

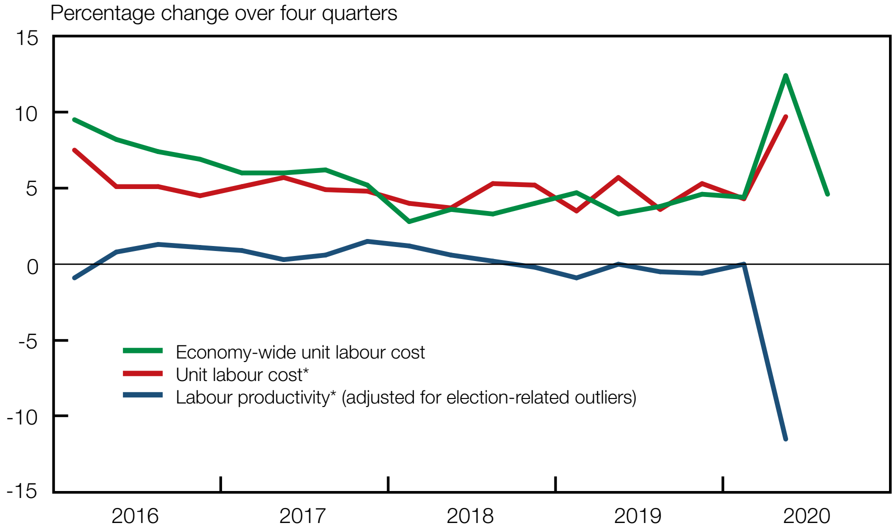


According to Andrew Levy Employment Publications, the *average wage settlement rate in collective bargaining agreements* decreased further to 6.3% in the first nine months of 2020 – the lowest rate since the first quarter of 2007. This is well below the 6.8% recorded in the corresponding period of 2019 and the average of 6.7% for 2019 as a whole. Likewise, the *number of workdays lost due to industrial action* fell notably to a 12-year low of 35 000 in the first nine months of 2020 compared with 1.2 million in the corresponding period of 2019, as many wage negotiations were deferred following the outbreak of the pandemic. However, the gradual reopening of the economy could potentially result in a rise in labour disputes due to the financial strain placed on employers and employees, as well as some employers reneging on existing wage agreements.

Labour productivity in the formal non-agricultural sector of the economy contracted by the sharpest rate ever of 11.8% in the second quarter of 2020, as the unprecedented contraction in output outweighed the decrease in employment on a year-on-year basis. Conversely, growth in *nominal unit labour cost* in the formal non-agricultural sector accelerated markedly from 4.3% to 10.3% from the first to the second quarter of 2020, as total remuneration contracted at a much slower pace than output. This was the highest year-on-year rate of increase since the second quarter of 2010. Economy-wide unit labour cost growth moderated notably from a 27-year high of 12.4% in the second quarter of 2020 to 4.6% in the third quarter, as the rebound in output outweighed that in the compensation of employees on a year-on-year basis.

The data distortions due to COVID-19 have detracted from the informational content of some economic indicators, such as labour productivity and unit labour cost, which currently reflect the exogenous nature of the pandemic rather than the true stance of the economy, and should therefore be treated with circumspection. These indicators superficially suggest that labour market conditions are becoming much tighter, which usually only occurs late in a business cycle expansion. However, this outcome is not consistent with the actual stance of the labour market at present, which is characterised by notable job losses and falling wages.

Labour productivity and nominal unit labour cost



* Formal non-agricultural sector

Sources: Stats SA and SARB

Prices[9]

Headline producer and consumer price inflation both accelerated somewhat from historical lows in May 2020, which resulted from a marked decrease in fuel prices in the wake of the COVID-19 pandemic. Headline producer price inflation accelerated from a 10-year low of 0.4% in May 2020 to a seven-month high of 2.7% in October, driven by an acceleration in the pace of increase in the prices of food and tobacco products, rubber and plastic products, as well as motor vehicles, while coal and petroleum prices declined at a slower pace. Headline consumer price inflation accelerated from a 16-year low of 2.1% in May 2020 to 3.3% in October as the year-on-year pace of decline in fuel prices moderated notably and as the downward bias of the lockdown-induced imputations of some prices in the consumer price index (CPI) dissipated.[10] The quickening in consumer price inflation in October 2020 resulted from an acceleration in food and non-alcoholic beverage price inflation and, to a lesser extent, also in vehicle, alcoholic beverages and tobacco as well as recreation and culture product price inflation.

Producer price inflation for intermediate manufactured goods accelerated gradually to 3.5% in October 2020. Despite this being the highest inflation rate since June 2019, the acceleration was not broad-based, with many intermediate manufacturing categories remaining in deflation.

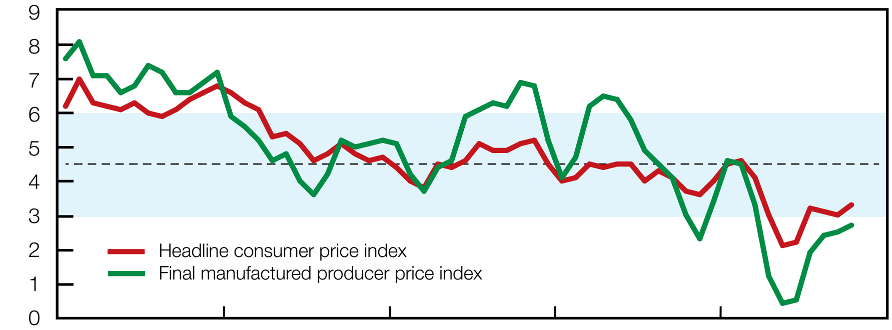
After reaching a four-month low in June 2020, producer price inflation for agricultural, forestry and fishery products quickened to 10.8% in October, led by higher agricultural product prices. Producer price inflation for mining products has remained elevated throughout 2020, and accelerated anew from 26.0% in June 2020 to 36.4% in September, before moderating again to 29.5% in October. Although coal and gas prices continued to decrease, gold and other metal ores as well as non-ferrous metal ores price inflation accelerated markedly in October. Producer price inflation of electricity and water decelerated for four consecutive months to 4.3% in September 2020, before accelerating to 7.7% in October. Although water price inflation remained unchanged at 7.4% for a fourth successive month, electricity price inflation slowed to a multi-year low of 3.9% in September 2020, before accelerating to 7.7% in October as the annual price increases were implemented after being delayed in response to COVID-19.

9 Unless stated to the contrary, all rates mentioned in this section reflect year-on-year changes.

10 For a more thorough discussion of the impact of the national lockdown on the compilation of the CPI, see 'Box 3: Methodological changes to the compilation of the consumer price index in response to the COVID-19 lockdown' in the September 2020 edition of the *Quarterly Bulletin*, available at https://www.resbank.co.za/en/home/publications/publication-detail-pages/boxes/2020/10330

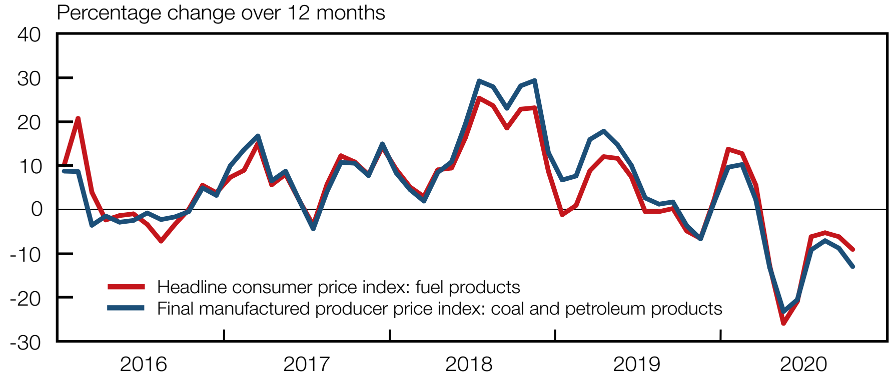
Headline producer and consumer prices

Percentage change over 12 months



Producer and consumer fuel prices

Percentage change over 12 months



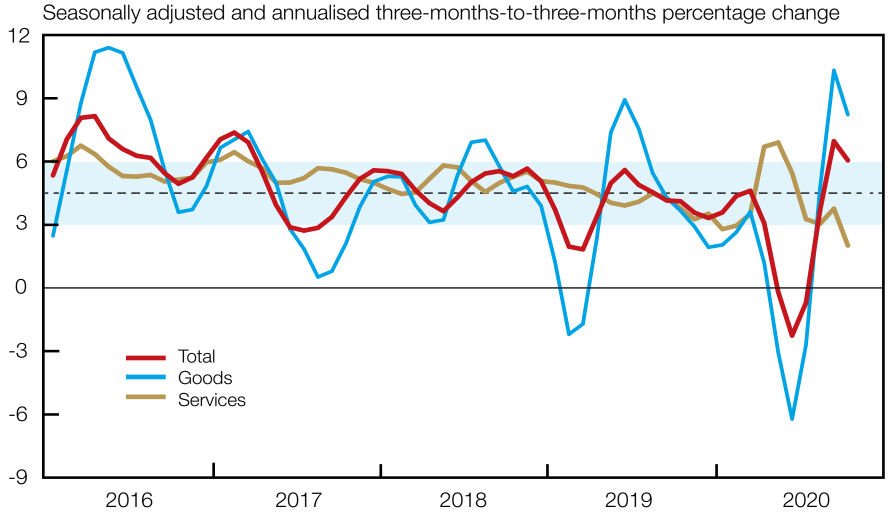
---- Midpoint of the inflation target range (4.5%)

Source: Stats SA

The deceleration in year-on-year headline consumer price inflation to a historical low of 2.1% in May 2020 is consistent with the loss of short-term momentum as measured by the seasonally adjusted and annualised three-months-to-three-months percentage change. This rate of increase then accelerated apace to 7.0% in September as the short-term momentum in consumer goods price inflation accelerated to 10.3%, driven by an increase in fuel prices from very low levels and as the downward bias of the price imputations by Stats SA dissipated. Subsequently, the short-term pace of increase in both consumer goods and services prices moderated in October 2020, as especially fuel and rental price inflation slowed further.

Headline consumer price index

Seasonally adjusted and annualised three-months-to-three-months percentage change



---- Midpoint of the inflation target range (4.5%)

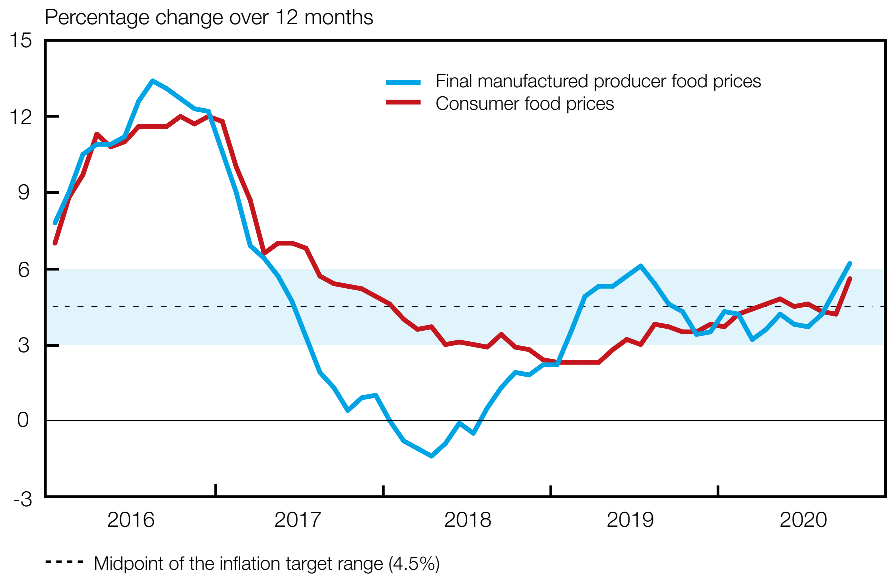
Sources: Stats SA and SARB

Consumer goods prices, on average, remained unchanged in the year to May 2020 despite a decrease in fuel prices, which caused non-durable goods price inflation to moderate meaningfully to -0.2% over this period. Both semi-durable and durable goods price inflation remained fairly muted in 2020, despite the marked depreciation in the exchange value of the rand in the first quarter. Non-durable and semi-durable goods price inflation remained below the lower limit of the inflation target range of 3.0% for seven consecutive months up to October 2020, indicating benign inflationary pressures amid weak consumer demand and muted exchange rate pass-through in the current recessionary environment. However, durable goods price inflation accelerated somewhat to 3.7% in October 2020 due to the high import content of these goods, in particular new motor vehicles and parts thereof, which reflects exchange rate movements. Consumer goods price inflation accelerated to 2.6% in October 2020 as food price inflation in particular quickened.

*Consumer services price inflatio*n moderated steadily over the three years to June 2020, to 3.7% – its lowest rate in 14 years. Price inflation in the housing and utilities category, with a combined weight of almost 40% in the consumer services price basket, decelerated substantially following unusually low rental price inflation. Inflation in domestic worker wages also moderated to its lowest level in 23 years when it slowed to 3.5% in September 2020, likely impacted by the financial strain experienced by many households due to COVID-19. Inflation in restaurant and hotel services prices slowed further to its lowest level since the inception of the classification of individual consumption by purpose (COICOP) classification in January 2008, and amounted to -0.5% in September 2020 and -0.3% in October. Hotel services prices in particular decreased for 10 consecutive months up to September 2020, reflecting the impact of the international and domestic travel restrictions on the accommodation industry. Consumer services price inflation remained fairly benign at 3.8% in September and October 2020.

Producer and consumer food price inflation remained relatively benign throughout most of 2020. However, following 18 months of deflation, agricultural producer food prices started to increase, with price inflation accelerating to as much as 12.7% in the year to October 2020, as especially cereals and other crops as well as live animal price inflation quickened. Manufactured producer food price inflation was more subdued at around 4% during the eight months up to August 2020, before accelerating to 6.2% in October following a quickening in the two highest weighted individual categories, namely meat and meat products as well as bakery products, in response to the earlier price increases in agricultural producer food prices. By contrast, consumer food price inflation oscillated at around 4.5% during the first nine months of 2020, before accelerating to 5.6% in October as prices increased at a faster pace in all nine food categories.

Final manufactured producer and consumer food price index



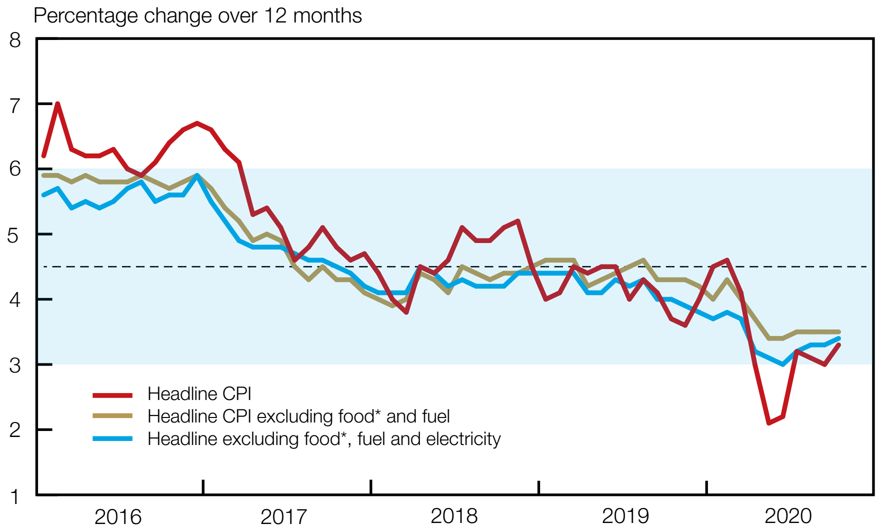
Source: Stats SA

US dollar-denominated international food prices edged higher in recent months, with the year-on-year rate of increase in the international food price index of the United Nations' Food and Agriculture Organization (FAO) accelerating to a seven-month high of 6.0% in October on account of firmer demand, especially from China, and a weaker US dollar. When expressed in rand terms, the year-on-year increase in FAO international food prices accelerated even more to 17.0% in October 2020, following the earlier depreciation in the exchange value of the rand. Concerns over production prospects in the southern hemisphere as well as dry conditions in parts of Europe led to an increase in wheat prices, which resulted in the pace of increase in FAO international cereals prices, in US dollar terms, accelerating markedly from 6.9% in August 2020 to 16.6% in October. Consequently, the year-on-year rate of increase in the FAO international cereals price index, in rand terms, also accelerated noticeably from an already high 21.7% in August 2020 to 28.8% in October.

The acceleration in international food and cereals price inflation, in rand terms, could eventually impact domestic food prices. This, together with the recent acceleration in agricultural producer food price inflation, could exert upward pressure on especially bread and cereals prices at the consumer level, which is the second highest weighted product group within the consumer food price basket. Although South Africa is a net importer of wheat, the expected increase in domestic wheat production of 40% in the 2020/21 production season, according to the Crop Estimates Committee of the Department of Agriculture, Forestry and Fisheries, could mitigate price pressures somewhat.

Underlying inflationary pressures receded to a multi-year low in June 2020, reflecting muted price pressures amid the domestic recessionary conditions, which impeded the ability of businesses to pass on price increases to consumers. When subtracting the impact of food, non-alcoholic beverages and fuel prices from headline consumer price inflation, the resultant measure of underlying inflation moderated to 3.4% in May 2020 before accelerating marginally to 3.5% in July, and remained at this level up to October. The SARB's preferred measure of core inflation (also excluding electricity prices) has remained below the midpoint of the inflation target range for 30 successive months, and at 3.0% in June 2020 was the lowest since March 2011 due to a combination of weak demand and the impact of price imputations by Stats SA. Subsequently, core inflation accelerated to 3.4% in October 2020 as especially alcoholic beverages and tobacco as well as new vehicle price inflation quickened, reflecting the lifting of the lockdown restrictions and the dissipation of price imputations for these products.

Headline and underlying measures of consumer prices



---- Midpoint of the inflation target range (4.5%)

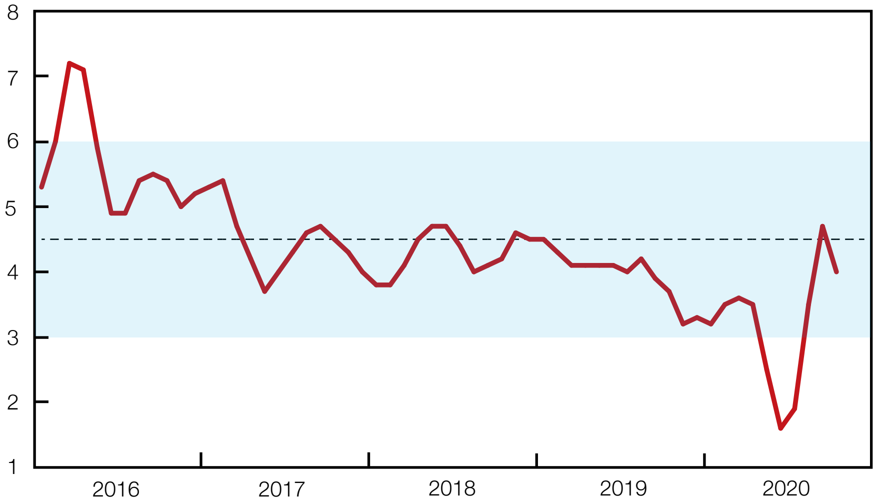
* Food includes non-alcoholic beverages

Source: Stats SA

Core inflation's seasonally adjusted and annualised short-term pace of increase consistently decelerated from a peak value of 7.2% in March 2016 to below the lower level of the inflation target range of 3.0% in May 2020, before moderating further to a recent trough of 1.6% in June as a result of the lockdown-induced price imputations. Thereafter, this measure accelerated again to 4.7% in September before slowing again to 4.0% in October.

Headline consumer price index excluding food*, fuel and electricity

Seasonally adjusted and annualised three-months-to-three-months percentage change



---- Midpoint of the inflation target range (4.5%)

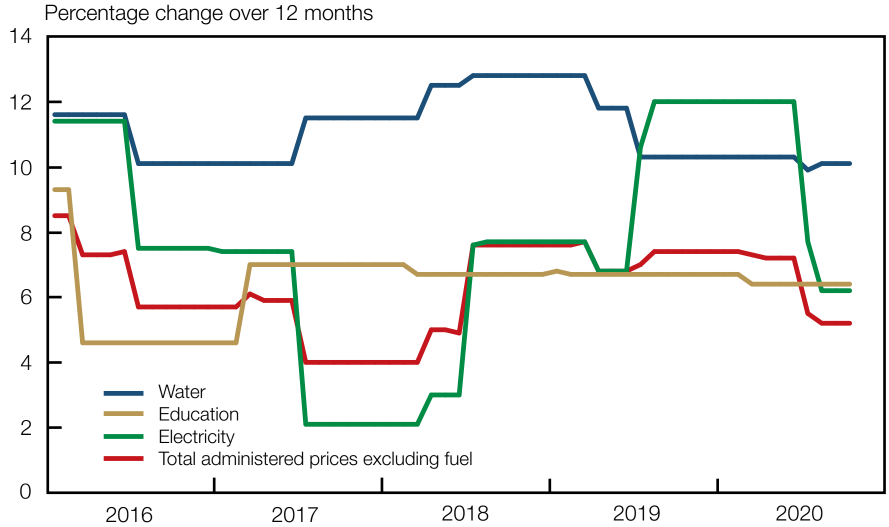
* Food includes non-alcoholic beverages

Sources: Stats SA and SARB

Changes in *administered prices* switched from a year-on-year increase of 9.2% in January 2020 to a decrease of 3.1% in May, and mirrored the marked deceleration in fuel price inflation from 13.7% to -25.9% over the same period. Administered price inflation then accelerated slightly to 0.9% in October as fuel prices decreased at a slower pace. However, when excluding fuel prices, administered price inflation decelerated from 7.2% in June 2020 to 5.5% in July, and subsequently to 5.2% in the three months to October. When also excluding electricity prices, administered price inflation moderated from 5.3% in January 2020 to 4.6% in September and October.

Administered price index

Percentage change over 12 months



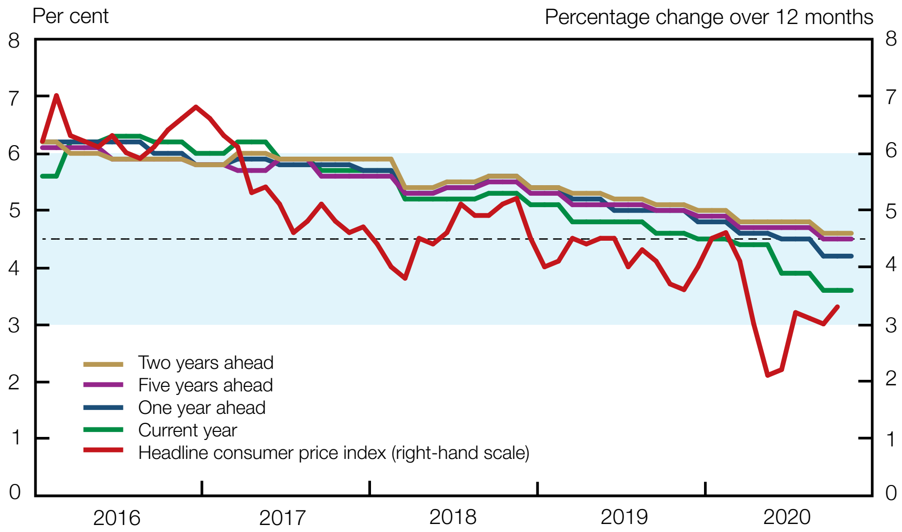
Source: Stats SA

These two measures of underlying administered price inflation have essentially moved sideways since July 2019, emphasising the impact of fuel price changes on the overall index, with fuel comprising 28.63% of the total weight of the administered price basket. The recent slowdown in these two measures of underlying administered price inflation resulted from a moderation in electricity price inflation and municipal assessment rates. The administered prices of water, electricity and education, with a combined weight of almost 45% in the administered price basket, have all increased at rates well above the upper limit of the inflation target range of 6% since at least mid-2018.

11 Inflation expectations as measured by the *Survey of Inflation Expectations,* conducted by the BER in the third quarter of 2020.

Average inflation expectations[11] declined further for all forecast years to a new 15-year low in the third quarter of 2020. Expectations declined to 3.6% for 2020 (3.9% previously), 4.2% for 2021 (4.5% previously) and 4.6% for 2022 (4.8% previously).

Inflation expectations and headline consumer price index



---- Midpoint of the inflation target range (4.5%)

Source: Stats SA

The inflation expectations of all three respondent groups declined further over all of the forecast horizons in the third quarter of 2020 relative to the previous quarter's survey, except for financial analysts whose 2020 forecast remained unchanged. The inflation expectations of business representatives remained notably higher for all surveyed horizons compared to financial analysts and trade union representatives, indicative of higher non-wage inflation expectations, since all three respondent groups have muted wage inflation expectations for 2020 and 2021.

Headline consumer price inflation expectations

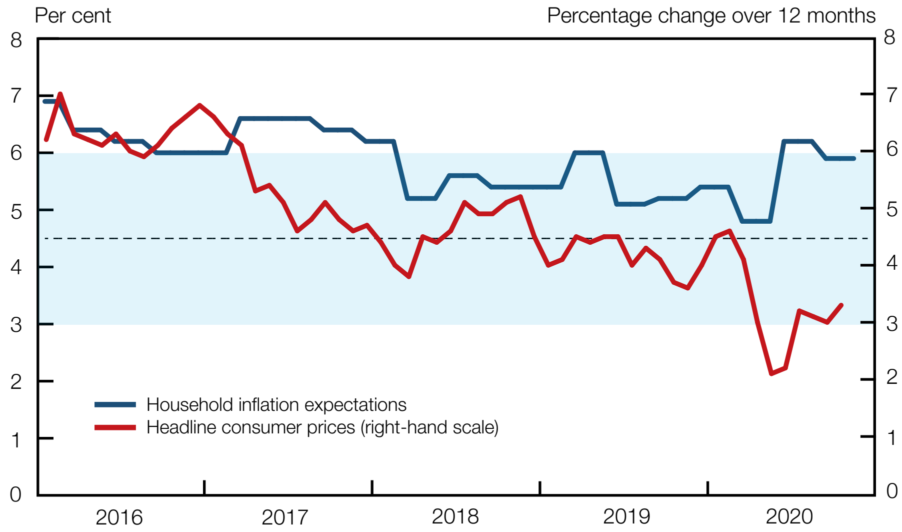
Per cent, as surveyed in the third quarter of 2020

Average inflation expected for:	Financial analysts	Business representatives	Trade union representatives	All surveyed participants
2020	3.2	4.1	3.4	3.6
2021	4.0	4.7	4.0	4.2
2022	4.4	5.2	4.4	4.6
The next five years	4.4	4.9	4.2	4.5

Source: BER

Average five-years-ahead inflation expectations declined further to 4.5% in the third quarter of 2020 from 4.7% in the second quarter. The decline could be attributed to financial analysts and business representatives lowering their forecasts to 4.4% (4.6% previously) and 4.9% (5.2% previously) respectively. The five-year expectations of trade union representatives remained unchanged at 4.2% in the third quarter of 2020.

Household inflation expectations and headline consumer price index



---- Midpoint of the inflation target range (4.5%)

Sources: BER and Stats SA

After increasing notably from 4.8% in the first quarter of 2020 to 6.2% in the second quarter, *household inflation expectations* retreated somewhat to 5.9% in the third quarter. Household inflation expectations continue to remain close to the upper end of the inflation target range and stand in sharp contrast to those of the other respondent groups and actual measured inflation outcomes.

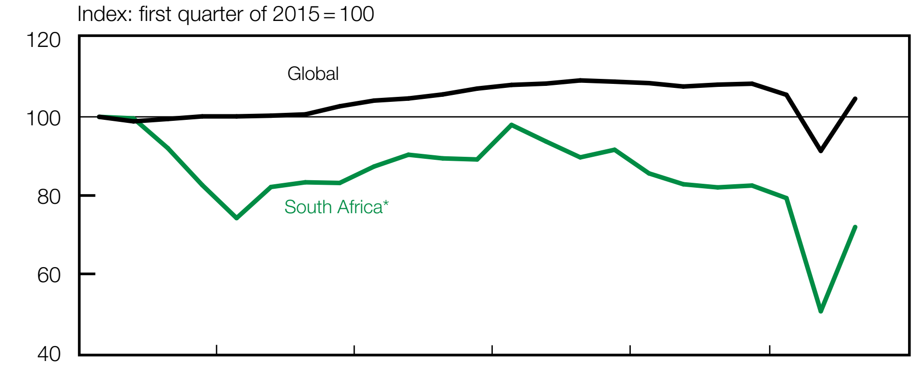
External economic accounts

Current account[12]

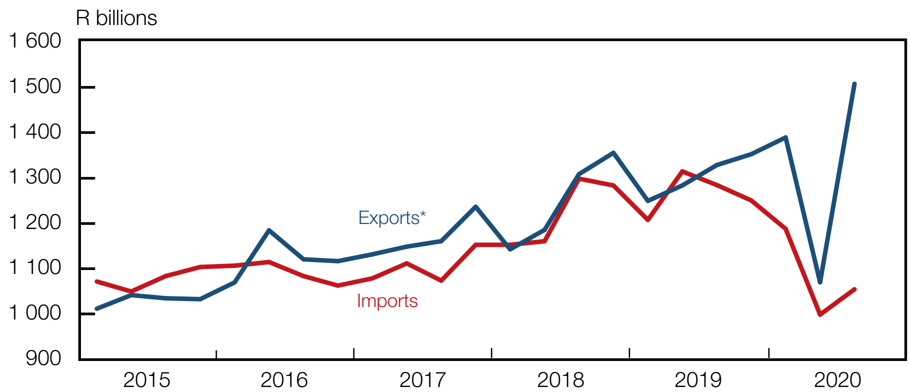
12 Unless stated to the contrary, the current account transaction flows referred to in this section are all seasonally adjusted and annualised.

South Africa's export volumes bounced back in the third quarter of 2020, in step with global trade volumes, following the easing of COVID-19 lockdown restrictions and the related rebound in economic activity. In South Africa, the value of net gold and merchandise exports surged to an all-time high in the third quarter of 2020, along with a more muted increase in merchandise imports.

Volume of merchandise exports



Value of merchandise exports and imports



* Including gold
Seasonally adjusted and annualised

Sources: CPB Netherlands Bureau for Economic Policy Analysis, Stats SA and SARB

As a result, South Africa's trade surplus widened to a sizeable R454 billion in the third quarter of 2020 from R71.4 billion in the second quarter – and to the largest ratio of GDP of 9.0% since the third quarter of 1988. The significantly higher value of exports reflected a marked increase in volumes and a lesser increase in prices, while the increase in the value of imports was driven by prices.

The large trade surplus coincided with a significantly smaller shortfall on the services, income and current transfer account. Hence, the balance on the current account of the balance of payments switched from a deficit of R124 billion in the second quarter of 2020 to a surplus of R297 billion in the third quarter – and to the largest ratio of GDP of 5.9% since the third quarter of 1988.

Current account of the balance of payments

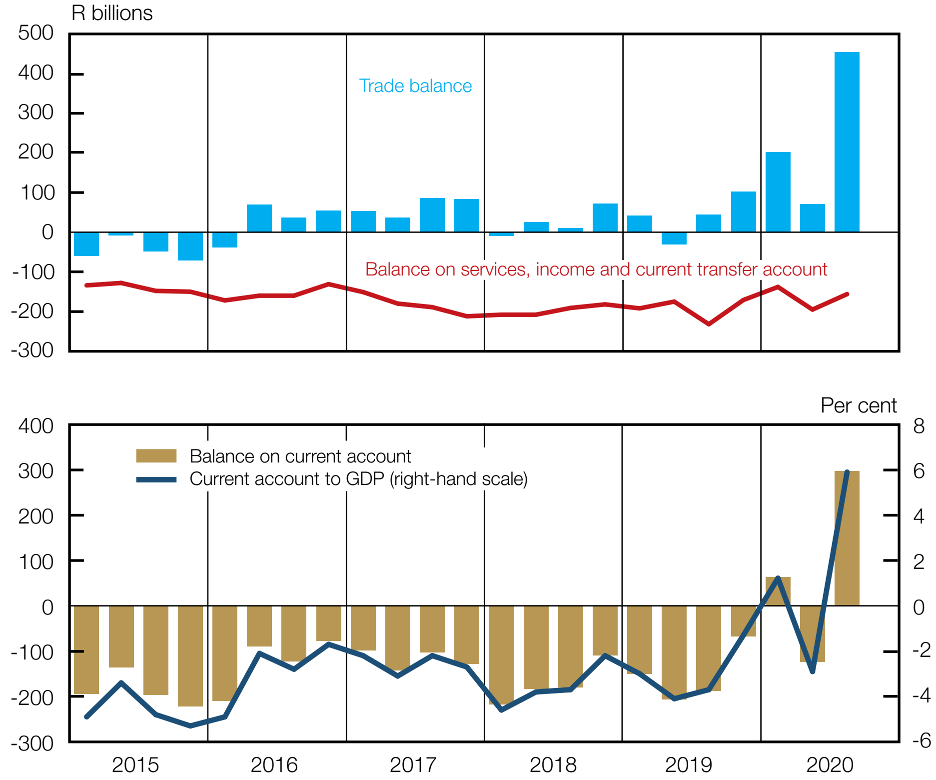
R billions, seasonally adjusted and annualised

	2019			2020		
	Q3	Q4	Year	Q1	Q2	Q3
Merchandise exports	1 258	1 260	1 236	1 292	990	1 379
Net gold exports	70	93	67	97	79	129
Merchandise imports	-1 284	-1 250	-1 264	- 1 187	-998	-1 054
Trade balance	44	102	39	202	71	454
Net service, income and current transfer payments	-232	-171	-192	-138	-195	-156
Balance on current account	-188	-68	-153	63	-124	297
As a percentage of gross domestic product						
Trade balance	0.9	2.0	0.8	3.9	1.7	9.0
Services balance	-0.2	-0.3	-0.3	-0.1	-1.3	-1.1
Income balance	-3.6	-2.3	-2.8	-1.8	-2.4	-1.1
Current transfer balance	-0.7	-0.7	-0.7	-0.7	-0.8	-1.0
Balance on current account	-3.7	-1.3	-3.0	1.2	-2.9	5.9

Components may not add up to totals due to rounding off.

Sources: Stats SA and SARB

Current account of the balance of payments

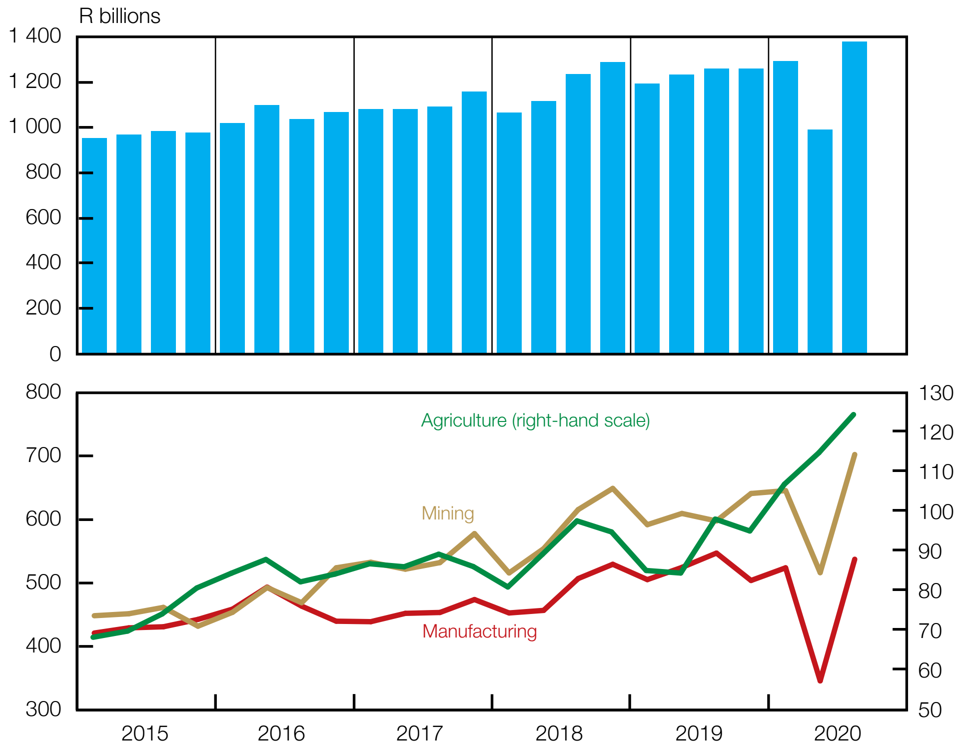


Seasonally adjusted and annualised

Sources: Stats SA and SARB

The value of merchandise exports increased by a significant 39.2% in the third quarter of 2020, boosted by a rebound in global trade and higher international commodity prices. South Africa was able to benefit from the increase in global demand and the recovery in domestic mining and manufacturing production in the third quarter of 2020.

Value of merchandise exports*



* Excluding gold
Seasonally adjusted and annualised
Sources: Stats SA and SARB

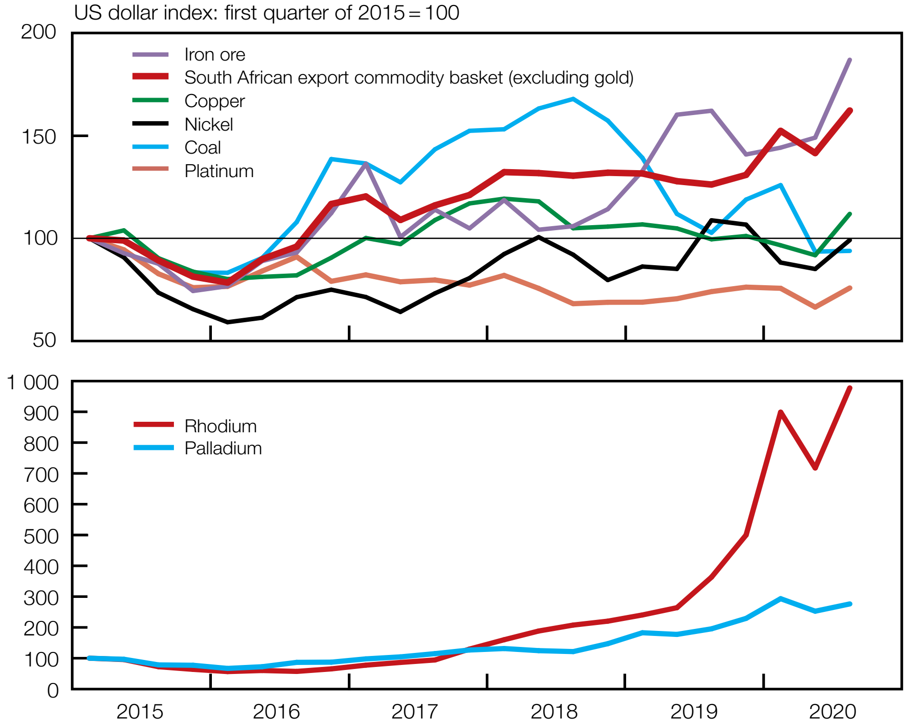
The broad-based rebound in manufacturing exports was supported by significant increases in especially vehicles and transport equipment as well as machinery and electrical equipment, and also chemical products. An increase in domestic vehicle production satisfied foreign demand as major export destinations exited their lockdowns together with government incentives, which supported vehicle sales. This is reflected by the surge in the number of vehicles exported, from around 32 000 in the second quarter of 2020 to about 76 000 in the third quarter (not seasonally adjusted or annualised), according to the National Association of Automobile Manufacturers of South Africa (NAAMSA). At the same time, the higher exports of machinery and electrical equipment largely reflected a marked increase in demand for catalytic converters on account of stricter vehicle emission standards, in especially European and North American countries. Over the same period, increased demand for diagnostic and laboratory reagents contributed to the exports of chemical products.

The value of all the subcategories of mining exports, in particular PGMs, increased strongly in the third quarter of 2020. This reflected the post-lockdown increase in international commodity prices that was driven by the recovery in global demand, and which was satisfied by the better utilisation of production capacity and an improvement in loading rates at domestic ports. The volume of bulk exports handled at the Saldanha Iron Ore Terminal and the Richards Bay Coal Terminal increased by about 30% and 18% respectively in the third quarter (not seasonally adjusted or annualised), according to the National Ports Authority. The surge in exported mineral products was driven by iron ore, coal, manganese and chromium. Over the same period, agricultural exports advanced further as the citrus harvesting season reached its peak.

The upward trend in the US dollar price of a basket of domestically produced non-gold export commodities, which was briefly interrupted by a decrease of 7.1% in the second quarter of 2020, continued with an increase of 14.7% in the third quarter as most prices increased at double-digit rates. The prices of copper, iron ore and nickel were supported by, among other factors, improved global manufacturing activity, while that of palladium and rhodium were buoyed by surging demand amid stringent environmental regulations, especially in Europe and China, as well as by supply concerns, mainly in South Africa.

International prices of selected South African export commodities

US dollar index: first quarter of 2015 = 100

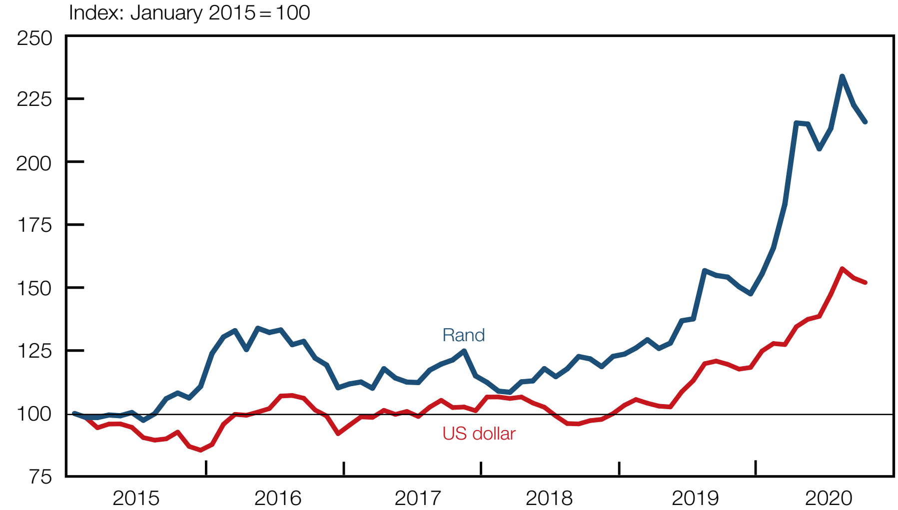


Sources: Afriforesight, World Bank and SARB

The pace of increase in the rand price of international commodities in the third quarter of 2020 was moderated by the appreciation in the exchange value of the rand. Nevertheless, the rand price of total merchandise exports increased by 4.5% in the third quarter of 2020 together with an increase of 33.3% in volumes.

Gold price

Index: January 2015 = 100



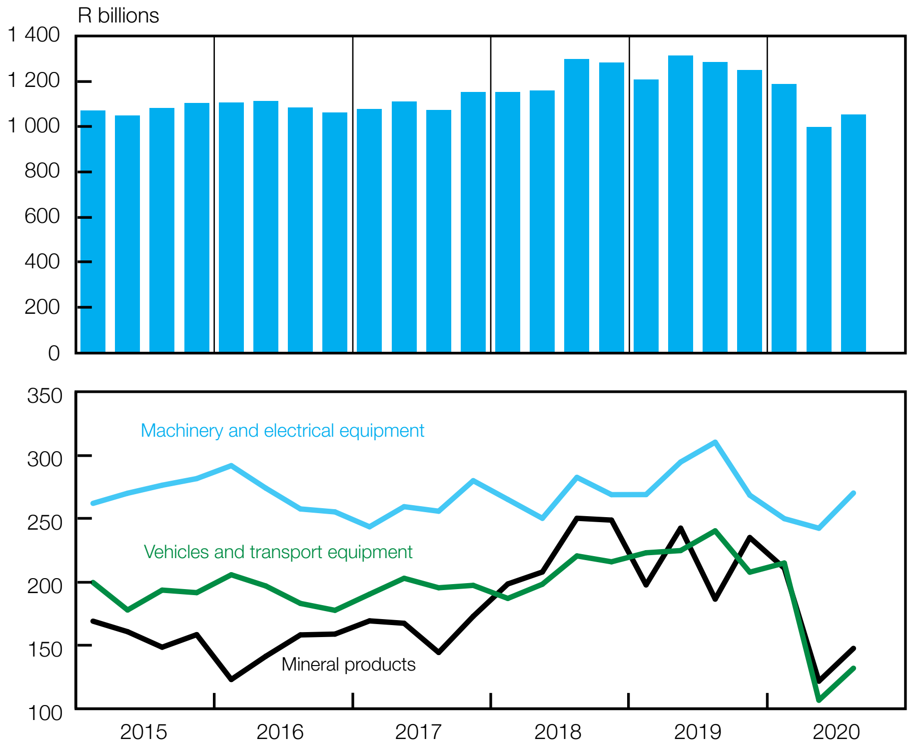
Sources: Reuters and SARB

The average US dollar price of gold on the London market increased further to an all-time high in August 2020, supported by sustained demand. The gold price then decreased somewhat in September as the US dollar strengthened and demand weakened.

The average realised rand price of net gold exports only increased by 4.5% in the third quarter of 2020 as the increase in the US dollar price was moderated by an appreciation in the exchange value of the rand. The increase in the rand price of gold, which coincided with a strong increase in the volume of net gold exports, supported an increase of 62.5% in the value of net gold exports in the third quarter.

Following four consecutive quarterly declines, the value of merchandise imports increased somewhat in the third quarter of 2020, supported by both mining and manufacturing. However, imports still contracted by 14.9% in the first three quarters of 2020 compared with the corresponding period of 2019, reflective of weak domestic demand. The increase in mining imports largely reflected mineral products, particularly refined petroleum. This included more imports of distillate fuel and petrol as domestic suppliers replenished stocks due to higher domestic demand with the easing of the lockdown restrictions.

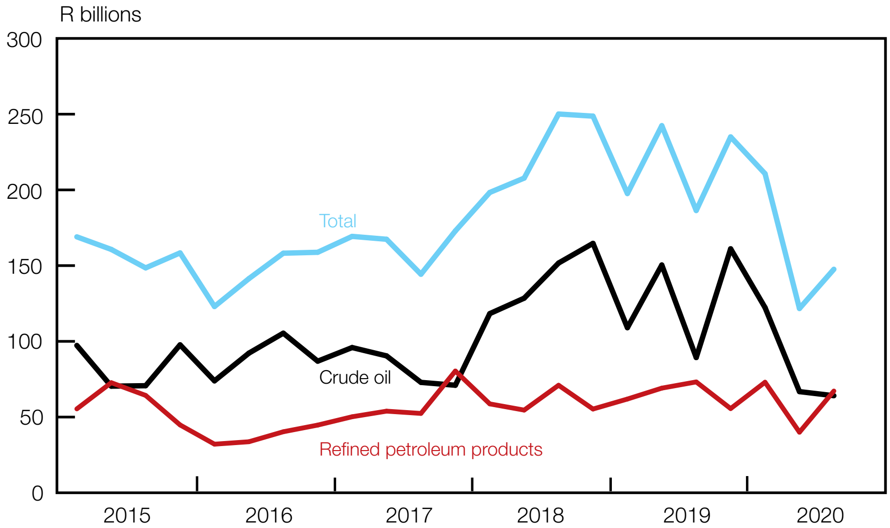
Value of merchandise imports



Seasonally adjusted and annualised
Sources: Stats SA and SARB

By contrast, the value of imported crude oil contracted for a third consecutive quarter in the third quarter of 2020. The number of imported barrels of crude oil fell by 28.9% in the third quarter as some refineries still had stock available after operations were halted during the second quarter under lockdown. The contraction in volumes outweighed the sharp rise in the average realised rand price of imported crude oil to around R750 per barrel in the third quarter.

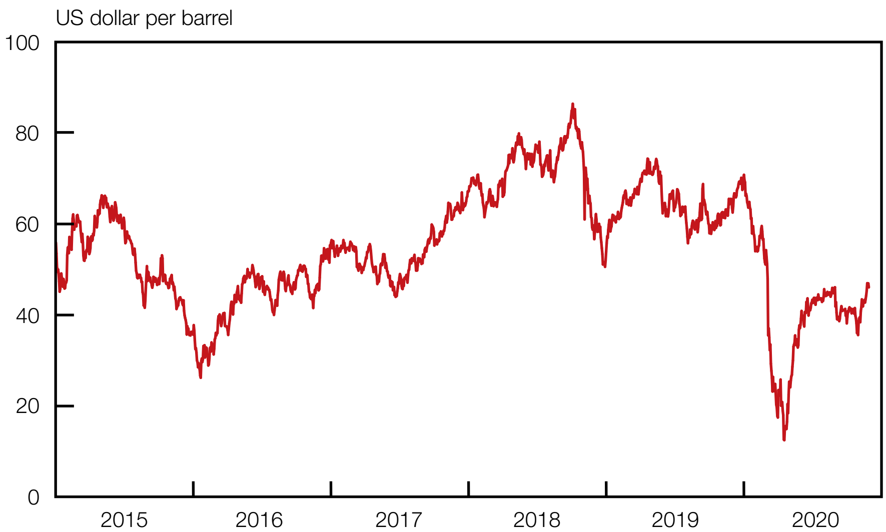
Value of mineral imports



Seasonally adjusted and annualised
Sources: Stats SA and SARB

After the sharp decline in the demand for crude oil during the global lockdowns, the international price increased in July and August 2020 as surpluses diminished. The spot price of Brent crude oil then declined again in September amid a revival of COVID-19 infections globally, which raised concerns about the outlook for global oil demand. The reinstatement of lockdowns in some countries, especially in Europe, together with a growing oversupply and the gradual return of Libyan production, among other factors, suppressed prices. The spot price of Brent crude oil dropped further to an average of US$40.12 per barrel in October 2020 before increasing to US$46.05 at the end of November.

Brent crude oil price



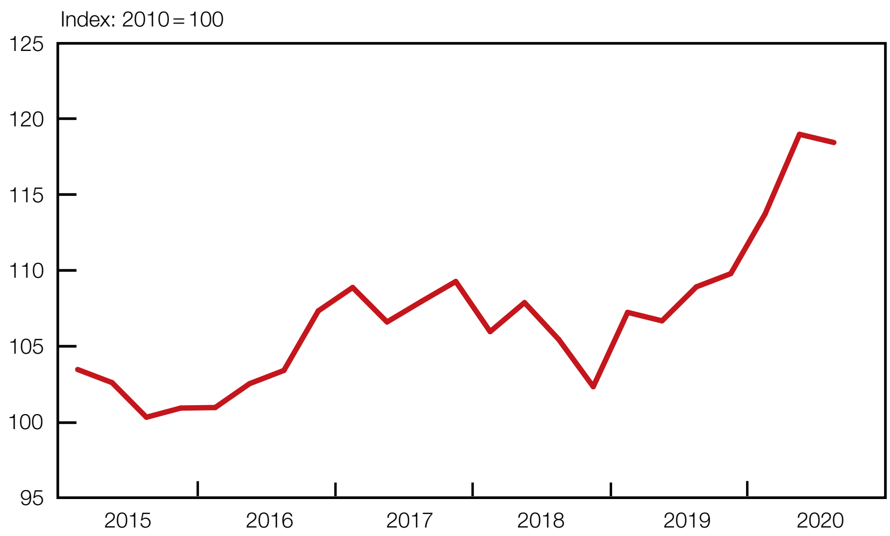
Sources: Reuters and SARB

The value of manufacturing imports was buoyed by the increased imports of automotive equipment components as well as machinery and electrical equipment in the third quarter of 2020. The latter included three large steam generators, which were the first of six generators purchased by Eskom and will be used to replace the existing generators at the Koeberg nuclear power station.

The broadly sideways movement in the volume of merchandise imports in the third quarter of 2020 resulted in a decrease in the import penetration ratio – that is, real merchandise imports as a ratio of GDE – from 24.8% in the second quarter of 2020 to 23.5% in the third quarter. Over the same period, the appreciation in the average quarterly exchange value of the rand was not enough to counter the substantial increase in international crude oil prices.

Following four consecutive quarterly improvements, South Africa's terms of trade deteriorated slightly in the third quarter of 2020 as the rand price of imported goods and services increased more than that of exports.

Terms of trade*



* Including gold

Sources: Stats SA and SARB

Box 3 Unpacking South Africa's terms of trade[1]

The terms of trade[2] is an important macroeconomic aggregate that measures a country's purchasing power of exports relative to imports from the relationship between the relative prices of exports and imports. Changes in the terms of trade associate an increase with an improvement[3] and a decrease with a deterioration. An improvement in the terms of trade implies that, for the same amount of exports, more imports can be purchased. This box presents the methodology underlying the compilation of South Africa's terms of trade, discusses the drivers of its recent improvement, and compares its evolution during the global financial crisis (GFC) with that during the coronavirus disease 2019 (COVID-19) pandemic.

The South African Reserve Bank's (SARB) methodology for compiling South Africa's terms of trade for goods and services is based on derived aggregate export and import price deflators, which are part of Statistics South Africa's (Stats SA) estimation of the gross domestic product (GDP) and gross domestic expenditure (GDE) statistics.[4] Stats SA uses both price and unit value indices (UVIs) as deflators to derive the imports and exports of goods and services at constant prices. As deflators, UVIs are used for homogeneous imports and exports; domestic producer price indices (PPIs) for heterogeneous exports; exchange rate-adjusted foreign PPIs where import price indices for goods are not available; and exchange rate-adjusted foreign consumer

1 This box relates to the statistics on South Africa's terms of trade on pages S–85 and S–153 of this edition of the *Quarterly Bulletin* and the South African Reserve Bank's quarterly statistical press release, 'Balance of payments: current account of the balance of payments', available at https://www.resbank.co.za/en/home/publications/quarterly-bulletin1/current-account-release

2 'Terms of trade' is calculated as the ratio of a country's export prices to import prices.

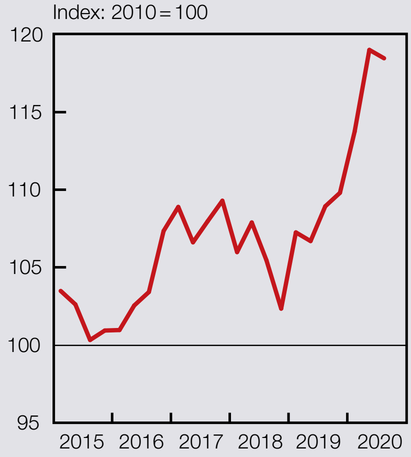
3 An improvement in the terms of trade could, among other things, reflect an increase in export prices concomitant with either unchanged or lower import prices; a smaller decline in export prices than in import prices; unchanged export prices with a related decrease in import prices; and export prices increasing at a faster pace than import prices.

4 See paragraph 3.5.5 'Constant price estimates – deflators' on pages 74 to 76 of Statistics South Africa's 'Expenditure on gross domestic product: sources and methods', available at http://www.statssa.gov.za/publications/P0441/Expenditure_on_GDP_Sources_and_Methods.pdf

price indices (CPIs) for imported services. For example, UVIs are used for imported petroleum products and motor vehicles as well as for the exports of certain mineral products such as iron ore, coal, manganese, copper and platinum group metals.[5]

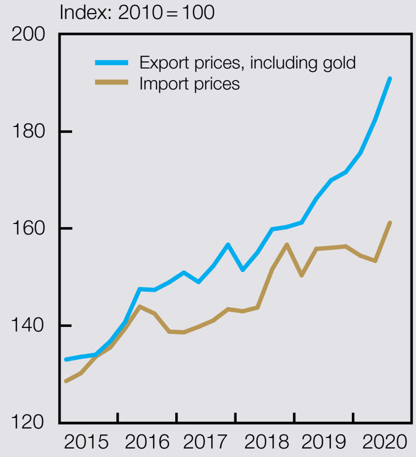
South Africa's terms of trade, as calculated from the aggregate export and import price deflators, which are derived from the aggregated nominal and constant export and import values, improved uninterrupted from the third quarter of 2019 to the second quarter of 2020. This reflected a sustained increase in the price of exports of goods and services, while that of imports at first remained broadly unchanged before declining more recently. In the third quarter of 2020, the price of imports of goods and services increased more than that of exports, resulting in a slight deterioration in the terms of trade.

South Africa's terms of trade of goods and services, including gold



Source: SARB

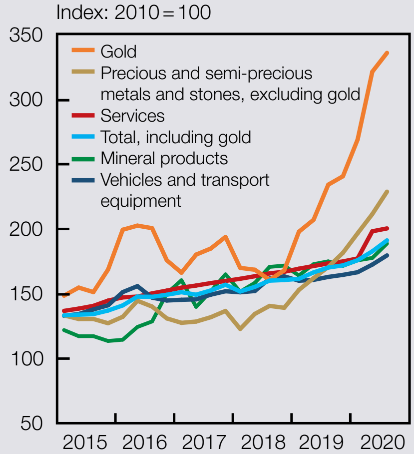
South Africa's export and import prices



Source: Stats SA

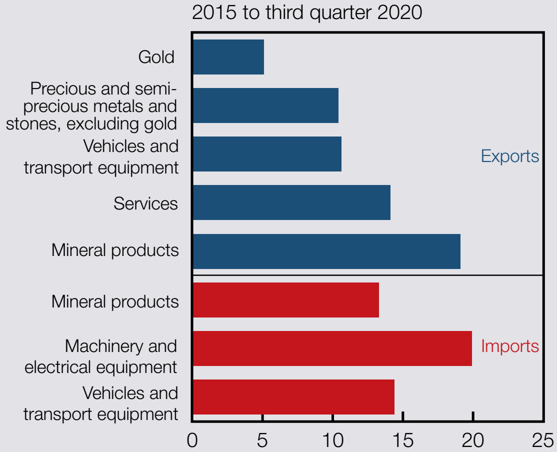
The increase in export prices was mainly driven by higher prices of gold; precious and semi-precious metals and stones, in particular rhodium and palladium; iron ore, as part of minerals; and also, to a lesser extent, vehicles and transport equipment as well as services. Up to the third quarter of 2020, the export price of gold had almost doubled from the first quarter of 2018, while that of precious and semi-precious metals and stones had increased by 86.5% and that of vehicles and transport equipment had increased by 18.9%. The overall export price was also boosted by these products' relative weights in the export price index.

Export prices of goods and services



Sources: Stats SA and SARB

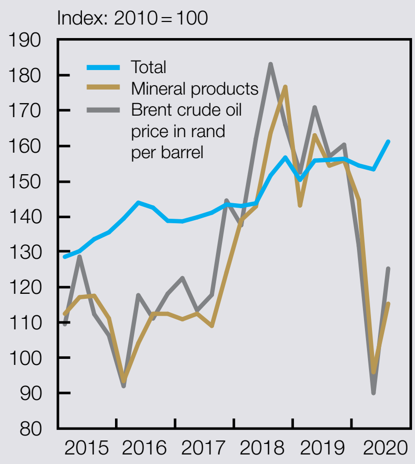
Weight in export and import price indices



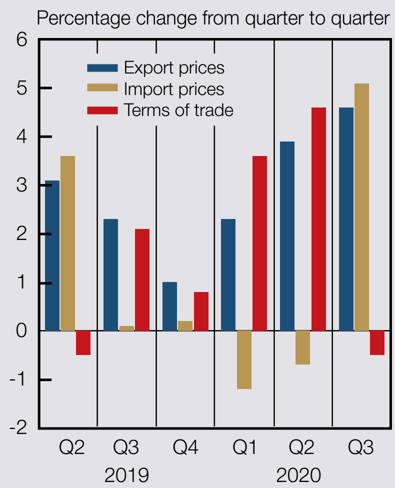
5 For more detail on the variety of deflators available, see Stats SA's 'Expenditure on gross domestic product: sources and methods', available at http://www.statssa.gov.za/publications/P0441/Expenditure_on_GDP_Sources_and_Methods.pdf

Import prices moved broadly sideways for most of 2019 before declining somewhat thereafter. This decline reflected lower mineral product prices, in particular that of crude oil, as the demand for oil shrunk in response to the COVID-19-related lockdowns globally. Changes in the prices of imported machinery and electrical equipment as well as vehicles and transport equipment also affected total import prices due to their relative weights in the index.

Import prices of goods and services



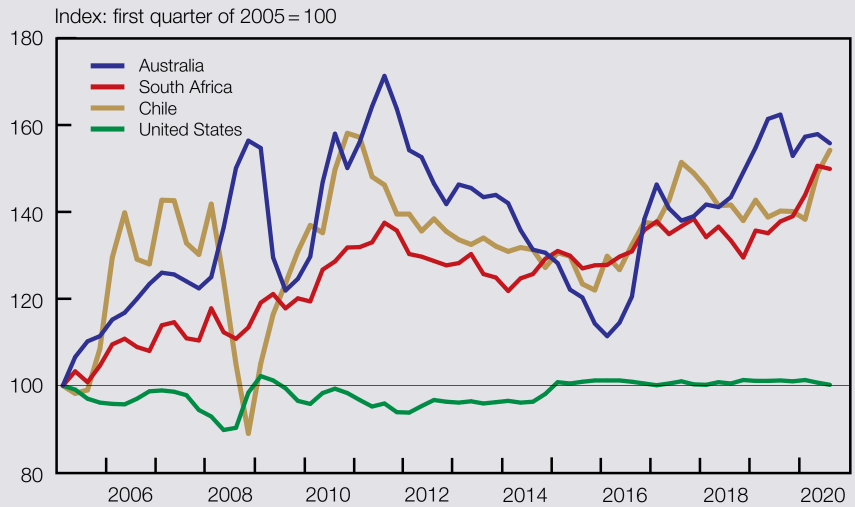
Drivers of the terms of trade



Sources: Reuters, Stats SA and SARB

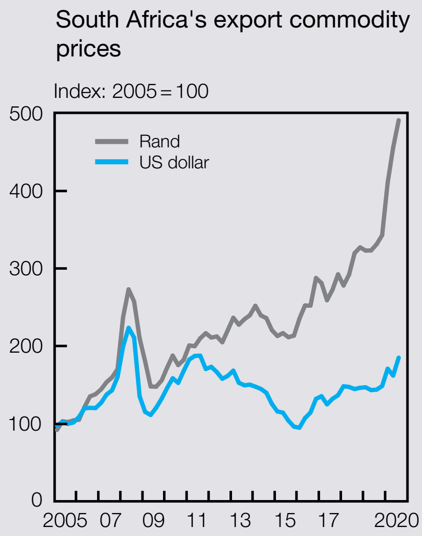
The drivers of South Africa's terms of trade differed during both the COVID-19 lockdown and the GFC, and are related to developments in the exchange value of the rand and international commodity prices. A comparison of the terms of trade of selected countries reflects the impact of volatility in international commodity prices and changes in the trends of such prices on commodity-exporting countries relative to that of countries with diversified exports.

Terms of trade of selected countries

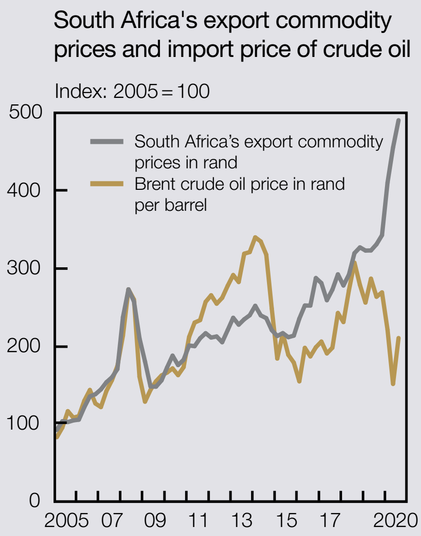


Sources: Haver Analytics, Stats SA and SARB

The decline in South Africa's export commodity prices in US dollar terms during the GFC was somewhat softened by the depreciation in the exchange value of the rand at the time. This contrasts with an increase in export commodity prices in US dollar terms during COVID-19, together with a significant depreciation in the exchange value of the rand, which boosted the rand price of South African exports.



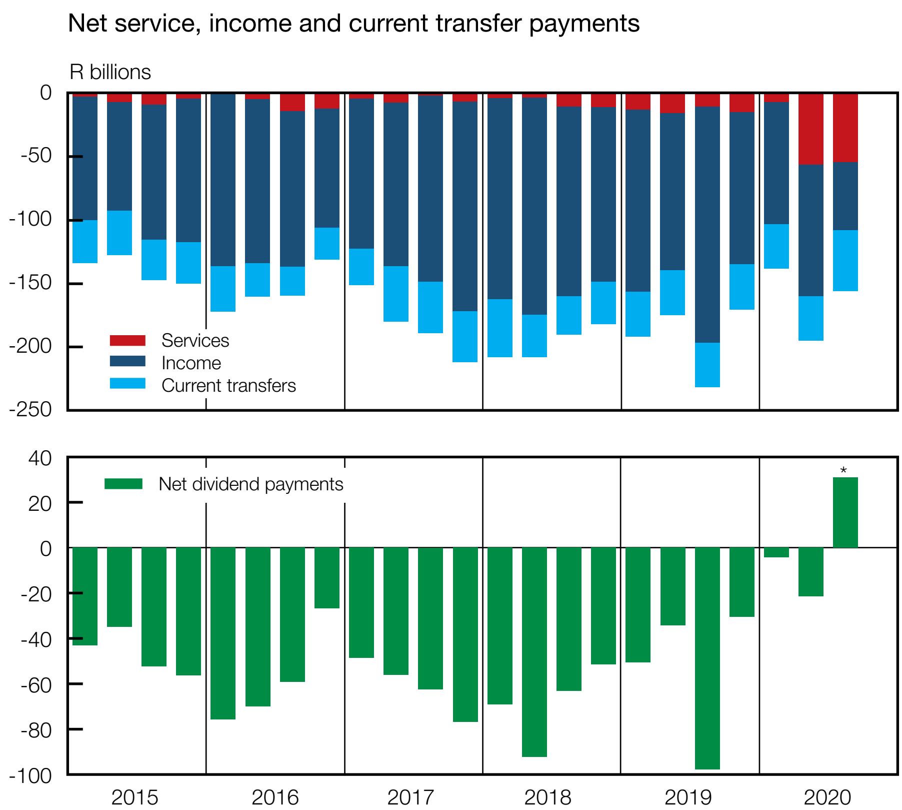
Sources: Afriforesight, Reuters, World Bank and SARB



Sources: Reuters and SARB

The interplay between export and import prices also differed between the COVID-19 and the GFC episodes. The realised rand price of imported crude oil declined noticeably during both episodes, while the decline in South African export commodity prices in rand terms during the GFC sharply contrasts an increase during COVID-19.

The shortfall on the services, income and current transfer account decreased meaningfully to R156 billion in the third quarter of 2020 from R195 billion in the second quarter. As a percentage of GDP, the deficit narrowed to 3.1%, from 4.5% over the same period. The lower deficit can be ascribed to a significantly smaller deficit on the income account and a slightly smaller services deficit, partially countered by larger net current transfer payments.



* Net dividend receipts
Seasonally adjusted and annualised
Source: SARB

Net services payments decreased slightly in the third quarter of 2020 from the high level established in the second quarter, as the unusual circumstances brought about by the COVID-19 restrictions continued to severely impact travel and passenger transportation. Despite international borders remaining officially closed during the third quarter of 2020, both gross travel receipts and gross travel payments increased slightly as border traffic, particularly to and from South Africa's neighbouring countries, picked up somewhat. As such, net travel receipts remained almost unchanged at the extremely low second-quarter levels. Consistent with the minor increase in gross travel payments, gross passenger transportation payments also increased slightly. Compared with the third quarter of 2019, gross receipts for total services contracted by almost 60%, while gross payments for total services contracted by just more than 37%.

The deficit on the income account decreased noticeably in the third quarter of 2020, to only 1.1% of GDP. This compares with an average quarterly income deficit of 2.7% of GDP since 2015. The narrowing in the deficit was brought about by a rare occurrence, namely a dividend surplus (net dividend receipts) – the first quarterly dividend surplus in almost 25 years. Although both gross dividend receipts and gross dividend payments contracted in the third quarter, the magnitude of the decline in gross dividend payments was considerably more pronounced at just more than 62%. This was a direct consequence of the recent severe adverse economic conditions experienced by most domestic companies, mainly as a result of COVID-19's impact on operations, as well as future uncertainties. Net interest payments increased slightly as gross interest payments increased slightly more than gross interest receipts, preventing the deficit on the income account from decreasing further.

Net current transfer payments increased in the third quarter of 2020 as gross current transfer payments advanced, while gross current transfer receipts contracted from a relatively high base in the second quarter.

Financial account

The net flow of capital on South Africa's financial account of the balance of payments (excluding unrecorded transactions) recorded a larger outflow of R38.6 billion in the third quarter of 2020, following a revised outflow of R24.0 billion in the second quarter. The revision of transactions in financial derivative assets in the first and second quarter of 2020 resulted in net outflows of capital in the financial account. On a net basis, direct investment, portfolio investment and

Net financial transactions

R billions

	2019			2020		
	Q3	Q4	Year	Q1	Q2	Q3
Change in liabilities						
Direct investment	17.3	10.5	66.8	29.0	17.4	-16.5
Portfolio investment	40.2	9.3	88.0	-97.6	-54.8	-28.8
Financial derivatives	-37.9	-50.8	-163.2	-73.7	-116.1	-78.6
Other investment	0.9	-42.0	-10.2	52.0	-34.5	40.7
Change in assets						
Direct investment	-21.6	-12.4	-45.1	-9.2	18.9	-8.5
Portfolio investment	34.7	8.7	43.0	79.6	41.7	-19.9
Financial derivatives	34.8	52.3	159.0	69.0	107.2	85.2
Other investment	83.0	24.6	5.4	-93.4	-25.9	3.1
Reserve assets	-77.2	9.9	-25.4	42.2	22.1	-15.2
Total identified financial transactions*	74.3	10.1	118.5	-2.1	-24.0	-38.6
As a percentage of gross domestic product	*5.7*	*0.8*	*2.3*	*-0.2*	*-2.2*	*-3.0*

* Excluding unrecorded transactions. Components may not add up to totals due to rounding off.
Inflow + outflow -

Source: SARB

reserve assets recorded outflows during the third quarter, while financial derivatives and other investment recorded inflows. Net financial account outflows as a ratio of GDP increased from 2.2% in the second quarter of 2020 to 3.0% in the third quarter.

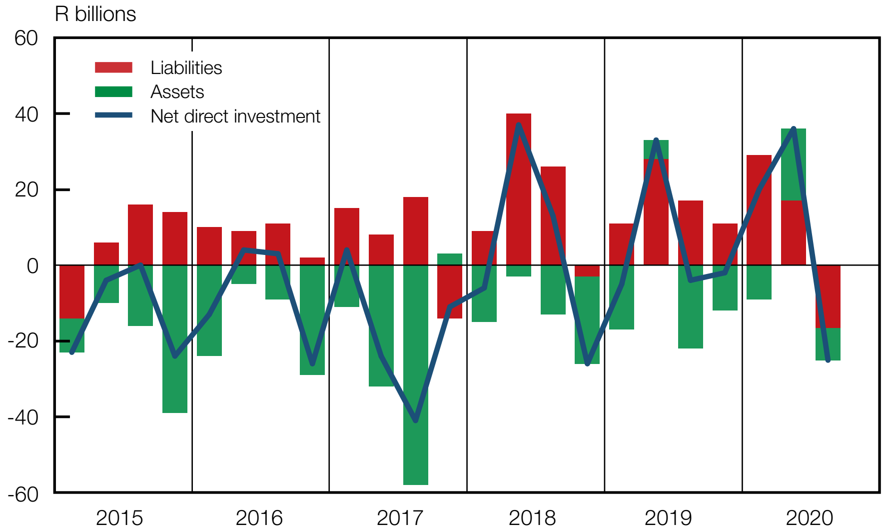
Foreign-owned assets in South Africa

South Africa's direct investment liabilities decreased by R16.5 billion in the third quarter of 2020 following an increase of R17.4 billion in the second quarter, as domestic subsidiaries repaid loans to foreign parent companies.

Portfolio investment liabilities recorded a reduced outflow of R28.8 billion in the third quarter of 2020 following an outflow of R54.8 billion in the second quarter, as non-residents' net sales of domestic equity securities outweighed net purchases of domestic debt securities. Non-residents purchased debt securities to the value of R8.0 billion in the third quarter of 2020 following notable net sales of R41.7 billion in the preceding quarter, while net sales of equities increased to R36.9 billion, from R13.1 billion over the same period.

Other investment liabilities switched to an inflow of R40.7 billion in the third quarter of 2020 from a revised outflow of R34.5 billion in the second quarter, as non-residents extended long-term loans to the general government. The financial assistance acquired by government to combat the effects of COVID-19 was in the form of a US$4.3 billion loan from the International Monetary Fund (IMF) and a US$1 billion loan from the New Development Bank.

Direct investment flows



Source: SARB

South African-owned assets abroad

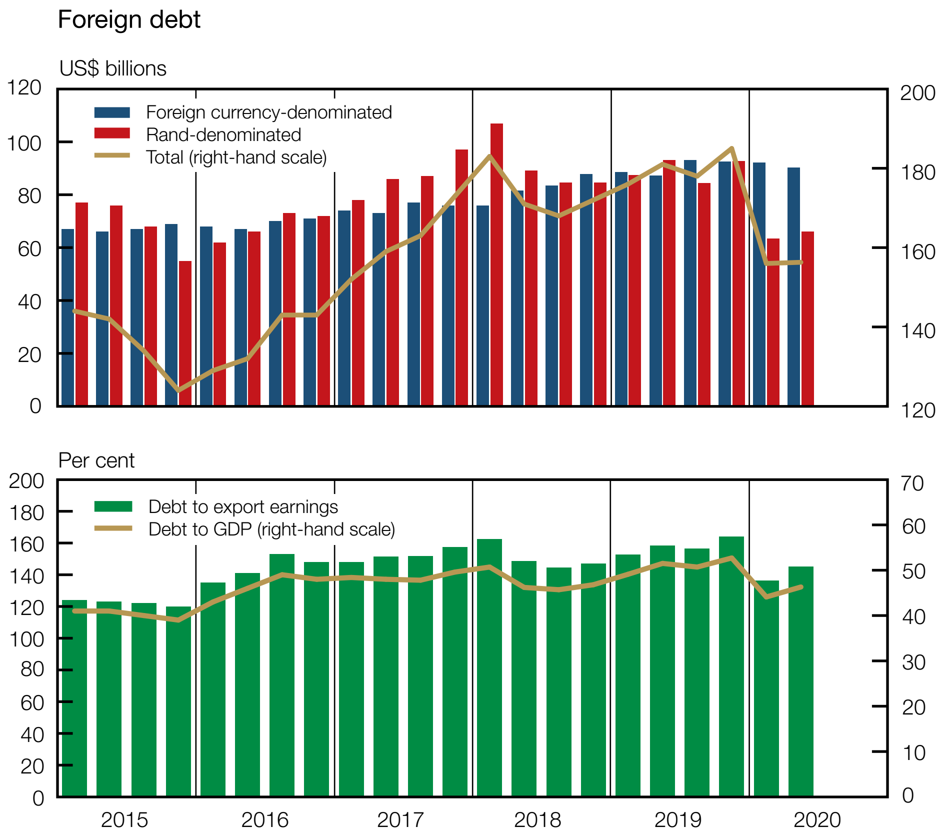
South Africa's direct investment assets increased by R8.5 billion in the third quarter of 2020, following a decrease of R18.9 billion in the second quarter. The outflow reflected domestic parent companies extending mainly short-term loans to non-resident subsidiaries.

South African residents acquired foreign portfolio assets of R19.9 billion in the third quarter of 2020, following the disposal of R41.7 billion in the second quarter. This outflow occurred mainly as a result of the domestic banking and non-banking private sectors' purchases of foreign debt securities, despite the disposal of foreign equity securities by the domestic non-banking private sector.

Other investment assets switched to an inflow of R3.1 billion in the third quarter of 2020, from an outflow of R25.9 billion in the second quarter. The inflow was mainly the result of the domestic banking sector repatriating deposits from non-resident banks, which was partly countered by the domestic private non-banking sector extending short-term loans to non-residents.

Foreign debt

South Africa's total external debt increased marginally from US$155.6 billion at the end of March 2020 to US$156.3 billion at the end of June. However, in rand terms, total external debt decreased from R2 798 billion at the end of March 2020 to R2 710 billion at the end of June as the exchange value of the rand appreciated against the US dollar.



Source: SARB

Foreign currency-denominated external debt decreased from US$92.1 billion at the end of March 2020 to US$90.3 billion at the end of June. The decrease was due to a decline in loans and deposits of the private banking sector as well as the redemption of South African government foreign currency-denominated international debt of US$500 million and ¥30 billion respectively during the second quarter of 2020.

Rand-denominated external debt, expressed in US dollars, increased from US$63.5 billion at the end of March 2020 to US$66.0 billion at the end of June. The increase was mainly due to an increase in the market value of non-resident bond holdings as well as an increase in the US dollar value of rand-denominated external debt following the appreciation in the exchange value of the rand over the period. This was partly offset by net sales of domestic rand-denominated bonds by non-residents.

South Africa's total external debt as a ratio of GDP increased from 44.1% at the end of March 2020 to 46.3% at the end of June. Likewise, the ratio of external debt to export earnings increased from 136.4% to 145.0 % over the same period.

Foreign debt of South Africa

US$ billions at end of period

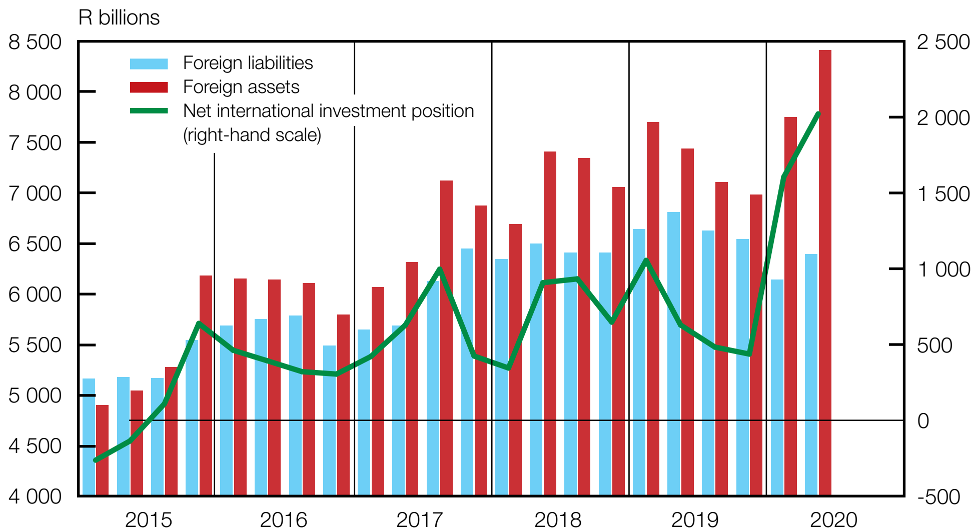
	2019				2020	
	Q1	Q2	Q3	Q4	Q1	Q2
Foreign currency-denominated debt.................	**88.5**	**87.4**	**93.2**	**92.6**	**92.1**	**90.3**
Debt securities	30.7	29.0	33.5	33.5	32.2	31.4
Other...	57.8	58.4	59.7	59.1	59.9	58.9
Public sector	10.5	10.4	10.9	10.3	10.5	10.9
Monetary sector	17.9	18.0	17.8	18.7	19.7	17.5
Non-monetary private sector	29.4	30.0	31.0	30.0	29.7	30.5
Rand-denominated debt..................................	**87.5**	**93.2**	**84.5**	**92.8**	**63.5**	**66.0**
Debt securities...	50.4	55.1	50.0	57.6	36.9	38.9
Other	37.1	38.1	34.5	35.2	26.6	27.1
Total foreign debt	**176.0**	**180.6**	**177.7**	**185.4**	**155.6**	**156.3**
As a percentage of gross domestic product....	*49.1*	*51.5*	*50.7*	*52.7*	*44.1*	*46.3*
As a percentage of total export earnings	*152.7*	*158.5*	*156.4*	*164.0*	*136.4*	*145.0*

Source: SARB

International investment position

South Africa's positive net international investment position (IIP) increased significantly from a revised R1 604 billion at the end of March 2020 to R2 022 billion at the end of June. This reflected a substantial increase in foreign assets and a much smaller increase in foreign liabilities. Similar to the first quarter of 2020, divergent movements in the prices of different financial instruments again contributed to the significant increase in the positive net IIP in the second quarter.

South Africa's international investment position



Source: SARB

The market value of South Africa's foreign assets (outward investment) increased substantially by 8.6% in the second quarter of 2020, from a revised R7 748 billion at the end of March 2020 to R8 415 billion at the end of June, following an increase of 11.0% in the first quarter. Foreign assets increased in all functional categories in the second quarter, except for financial derivatives and reserve assets. Direct investment increased mainly as a result of the valuation effects of an increase in the share price of a large dual-listed company with a primary listing abroad. Foreign portfolio investment assets increased, mainly due to an increase of 20.0% in the US Standard & Poor's (S&P) 500 Index as well as an increase in the value of resident ownership of dual-listed companies domiciled abroad, along with an increase in the share prices of those companies. The increase in other investment assets resulted mainly from an increase in resident banks' short-term loans under repurchase agreements to non-residents, while reserve assets decreased due to the valuation effect of the appreciation in the exchange value of the rand.

The market value of South Africa's foreign liabilities (inward investment) increased by 4.1% in the second quarter of 2020, from a revised R6 144 billion at the end of March 2020 to R6 393 billion at the end of June 2020, following a decline of 6.1% in the first quarter. The increase in foreign liabilities reflected a significant increase in portfolio investment, while all of the other categories recorded declines. The value of direct investment liabilities declined marginally despite an increase of 22.2% in the FTSE/JSE All-Share Price Index (Alsi) in the second quarter of 2020, as net asset values of non-listed companies declined due to the impact of the COVID-19 lockdown restrictions. Portfolio investment liabilities increased as the notable increase in the Alsi resulted in the higher valuation of foreign shareholding of domestic shares, notwithstanding the national government's redemption of international debt of US$500 million and ¥30 billion during the second quarter of 2020. The decrease in other investment liabilities was mainly due to the repayment of short-term loans by the domestic banking sector as well as lower non-resident deposits at domestic banks.

As a ratio of South Africa's annual GDP, foreign assets increased from 150.5% at the end of March 2020 to 169.6% at the end of June, while foreign liabilities increased from 119.3% to 128.9% over the same period. This resulted in an increase in the positive net IIP to 40.7% of GDP at the end of June 2020.

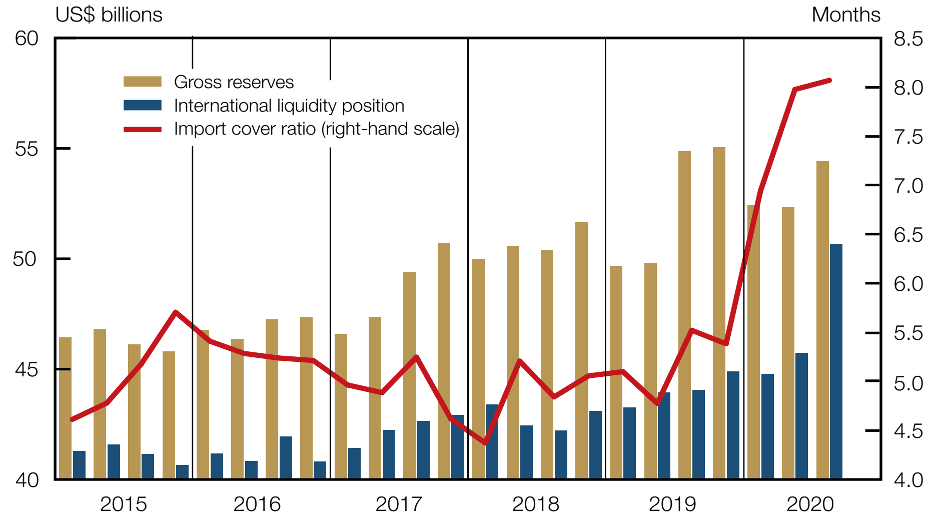
International reserves and liquidity

South Africa's international reserve assets increased by R15.2 billion in the third quarter of 2020 following three successive quarters of decrease.

Measured in US dollar terms, the value of South Africa's gross gold and other foreign reserves (i.e. the international reserves of the SARB before accounting for reserves-related liabilities) increased from US$52.3 billion at the end of June 2020 to US$54.4 billion at the end of September, mainly reflecting proceeds from foreign borrowings received on behalf of government. The country's gross gold and other foreign reserves then decreased to US$53.8 billion at the end of November. South Africa's international liquidity position[13] increased from US$45.7 billion at the end of June 2020 to US$50.7 billion at the end of September, and further to US$51.3 billion at the end of November.

13 This is calculated as the SARB's gross gold and foreign reserves minus foreign currency-denominated liabilities against both domestic and foreign counterparties plus/minus the forward position in foreign currency.

International reserves



Source: SARB

The level of import cover (i.e. the value of gross international reserves relative to the value of merchandise imports, as well as services and income payments) increased slightly from 8.0 months at the end of June 2020 to 8.1 months at the end of September.

Exchange rates[14]

Following the significant decrease in the nominal effective exchange rate (NEER) of the rand during the onset of the COVID-19 pandemic in the first quarter of 2020, it stabilised during subsequent quarters. A similar trend was observed among most other emerging market currencies. The NEER decreased by 0.3% in the third quarter of 2020 following an increase of 2.7% in the second quarter.

14 Unless stated to the contrary, all percentage changes in this section are based on the end of the period.

Exchange rates of the rand

Percentage change

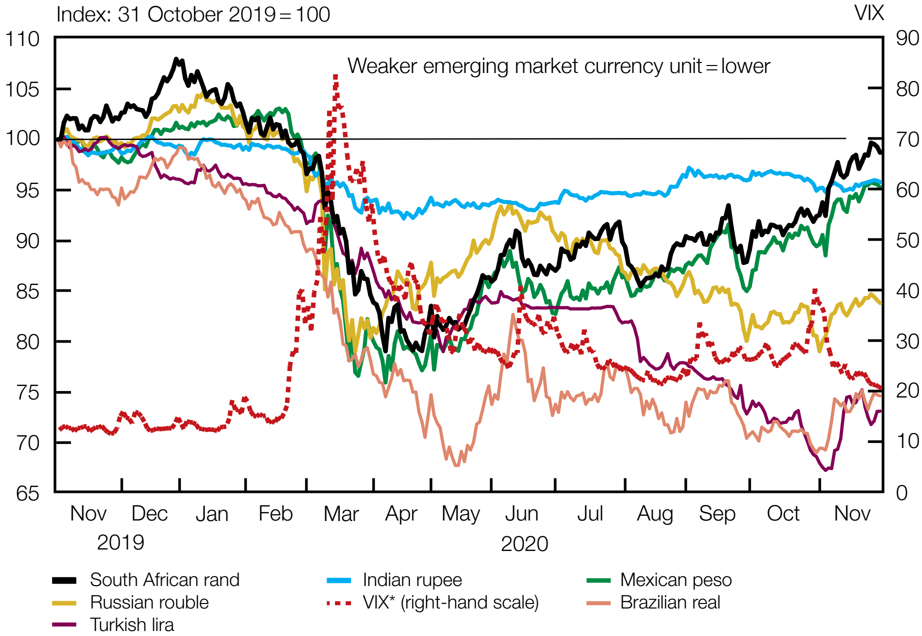
	31 Dec 2019 to 31 Mar 2020	31 Mar 2020 to 30 Jun 2020	30 Jun 2020 to 30 Sep 2020	30 Sep 2020 to 30 Nov 2020
Weighted average*	-19.3	2.7	-0.3	8.3
Euro	-20.4	1.7	-2.0	8.4
US dollar	-21.9	3.8	2.4	10.7
Chinese yuan	-20.5	3.5	-1.4	7.0
British pound	-16.9	4.2	-1.9	6.5
Japanese yen	-22.2	3.2	0.5	9.2

* Trade-weighted exchange rate against a basket of 20 currencies (nominal effective exchange rate)
Depreciation – appreciation +

Source: SARB

In July 2020, the NEER decreased slightly by 0.3% amid the release of less favourable domestic economic indicators. However, the NEER increased by 0.7% in August, buoyed by improved risk sentiment towards emerging market financial assets and a weakening US dollar amid political developments ahead of the US presidential elections in November.

Emerging market currencies against the US dollar



* The Volatility Index (VIX) is a real-time index that represents the market's expectation of 30-day forward-looking volatility derived from the S&P 500 Index options and was developed by the Chicago Board Options Exchange (CBOE). The VIX provides a measure of market risk and investor sentiment.

Sources: Bloomberg, Reuters and SARB

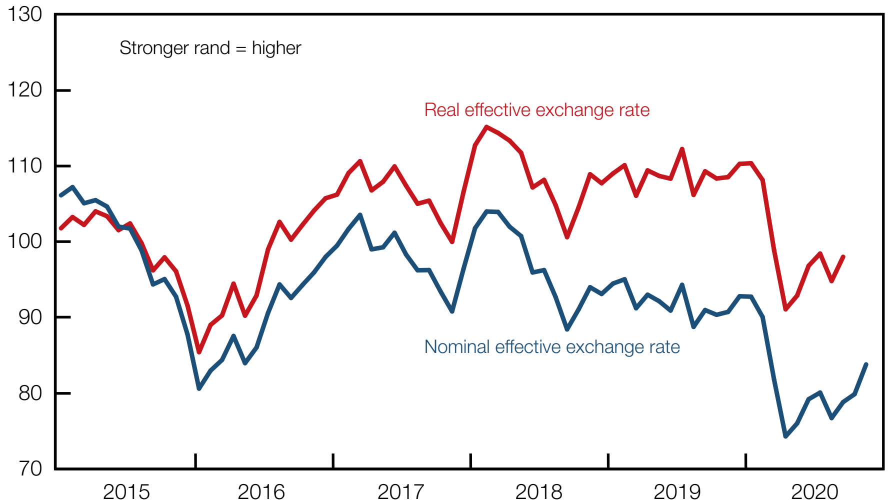
Financial market sentiment also improved as a result of the continued easing of COVID-19 lockdown restrictions domestically in mid-August. The resurgence of trade tensions between China and the US towards the end of September 2020 weighed on emerging market currencies, and the NEER accordingly decreased again by 0.8% in September.

The NEER subsequently increased by 3.3% in October 2020 as global sentiment towards emerging market currencies improved in light of the release of positive economic statistics in the US. However, the rand depreciated towards the end of October following the release of the *2020 MTBPS*, which highlighted renewed concerns about South Africa's fiscal and sovereign debt positions. The NEER appreciated substantially in the days following the outcome of the US presidential elections.

Although volatility in global financial markets has subsided somewhat and some emerging market currencies have strengthened thus far during the second half of 2020, it is noteworthy that the rand has performed relatively well compared to other emerging market currencies, despite South Africa's non-investment grade sovereign credit rating, closely following the trend in the Mexican peso. From a low of R19.08 against the US dollar in early April 2020, the rand appreciated by 24.8% to R15.28 against the US dollar by the end of November. Apart from the Mexican peso, the rand outperformed some emerging market currencies such as the Brazilian real, Turkish lira and Russian rouble.

Effective exchange rates of the rand

Index: 2015 = 100



Source: SARB

The real effective exchange rate (REER) of the rand decreased by a notable 16.4% from January 2019 to April 2020, reflecting improved competitiveness for domestic producers in foreign markets over this period. This decrease resulted mainly from the sharp depreciation in the exchange value of the rand at the onset of the COVID-19 pandemic and associated lockdown restrictions at the end of March 2020. The REER increased by 7.6% between April 2020 and November 2020, along with the gradual easing of domestic COVID-19 lockdown restrictions and an appreciation in the exchange value of the rand.

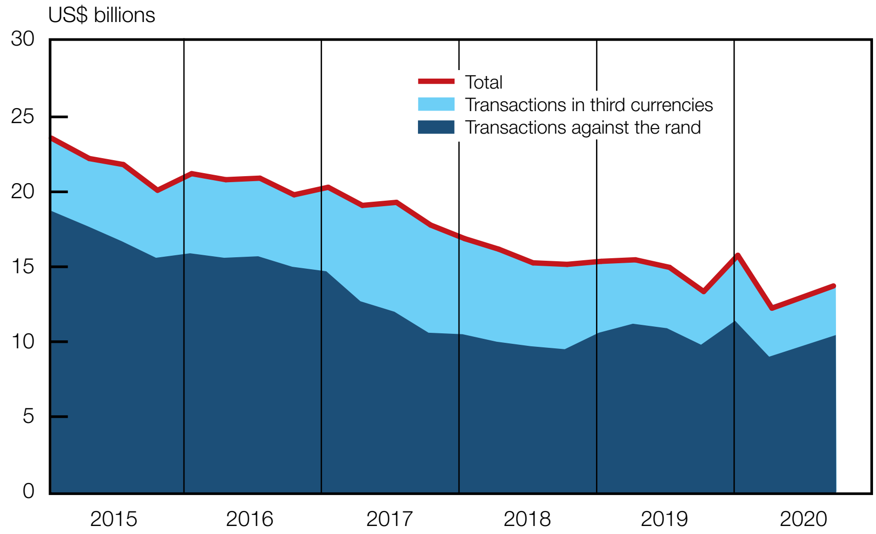
Turnover in the South African foreign exchange market

The net average daily turnover[15] in the South African foreign exchange (FX) market increased from US$12.3 billion in the second quarter of 2020 to US$13.3 billion in the third quarter, or by 7.5%, following a significant decrease of 21.9% in the first quarter due to the impact of COVID-19. The increase in net turnover during the third quarter mainly resulted from FX transactions against the rand, which increased from US$9.0 billion in the second quarter of 2020 to US$9.8 billion

15 This is calculated as the daily average of all new foreign exchange transactions concluded during a specified period, adjusted for local interbank double counting.

in the third quarter, or by 9.6%. The easing of domestic lockdown restrictions, together with improved global sentiment, spurred activity in FX transactions. By contrast, transactions in third currencies remained unchanged at US$3.4 billion over the same period.

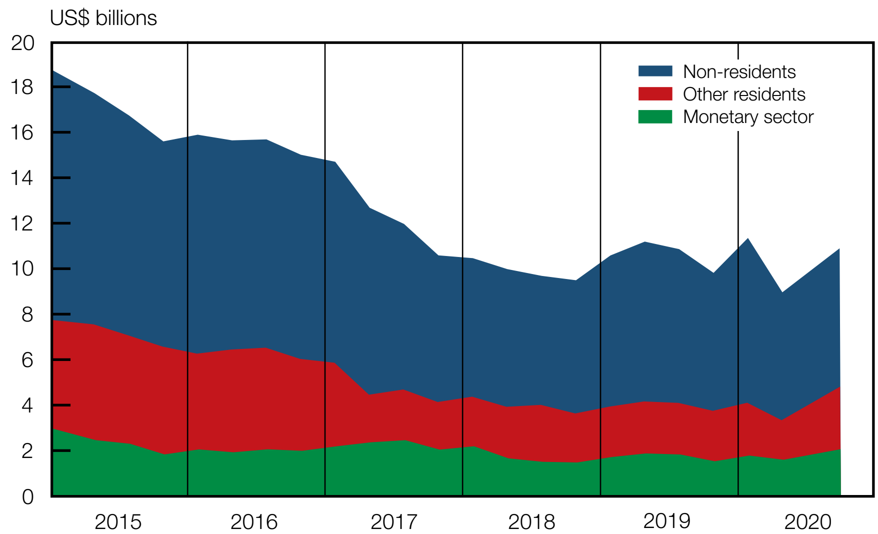
Net average daily turnover in the South African foreign exchange market



Source: SARB

Although non-resident participation in the rand market has been the largest contributor to turnover, it was severely affected by COVID-19. Average non-resident participation of US$7.2 billion in the first quarter of 2020 declined to US$5.6 billion in the second quarter – the lowest since 2018. However, non-resident participation increased to US$6.1 billion in the third quarter as most economies started to emerge from the impact of the COVID-19 lockdown and as various stimulus measures reinforced confidence. In addition, monetary sector transactions in the rand market increased from US$1.7 billion in the second quarter of 2020 to US$2.1 billion in the third quarter. Similarly, FX transactions against the rand with resident counterparties increased from US$1.7 billion to US$2.6 billion over the same period.

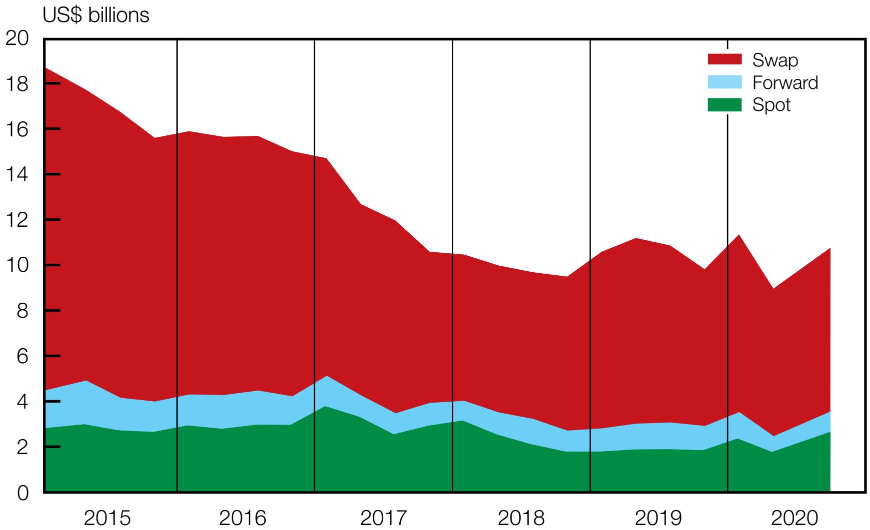
Composition of net average daily turnover in the South African foreign exchange market against the rand, by counterparty



Source: SARB

The composition of the net average daily turnover in the South African FX market against the rand is dominated by swap transactions, which increased from US$6.5 billion in the second quarter of 2020 to US$7.2 billion in the third quarter, or by 11.1%. Forward transactions increased from US$0.7 billion in the second quarter of 2020 to US$0.9 billion in the third quarter, or by 29.4%. Likewise, spot transactions increased by a notable 49.5%, from US$1.8 billion to US$2.7 billion over the same period, reflecting the more stable exchange value of the rand.

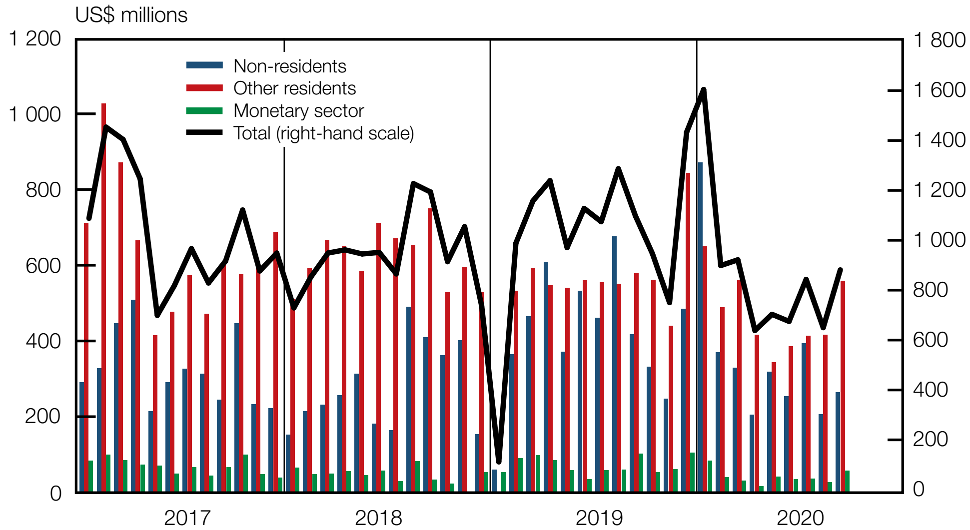
Composition of net average daily turnover in the South African foreign exchange market against the rand, by instrument



Source: SARB

As forward transactions were severely impacted by COVID-19, rand transactions in the forward market showed a significant decline in non-resident participation during the latter part of the first quarter of 2020, a trend which continued in the second quarter. Non-resident participation averaged only US$0.3 billion in both the second and third quarter of 2020, down from US$0.5 billion in the first quarter. Meanwhile, monetary sector participation in the forward market remained stable in 2020, averaging less than US$0.1 billion in both the second and third quarter of 2020.

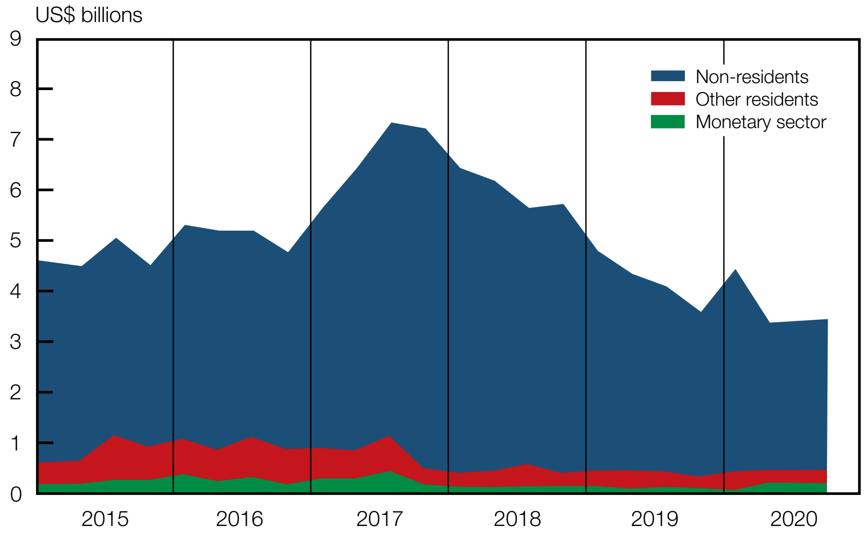
Composition of net average daily turnover of forward transactions in the South African foreign exchange market against the rand, by counterparty



Source: SARB

From mid-2017, transactions in third currencies decreased consistently, and declined sharply during the height of the COVID-19 pandemic in the first quarter of 2020. Transactions in third currencies are mainly driven by non-resident participation, which subsequently increased from an average of US$2.9 billion in the second quarter of 2020 to US$3.0 billion in the third quarter, or by 2.4%. Resident participation also increased slightly by 6.0%, from US$0.2 billion to US$0.3 billion over the same period, while monetary sector participation declined by 5.5% to average US$0.2 billion in the third quarter of 2020.

Composition of net average daily turnover in the South African foreign exchange market in third currencies, by counterparty



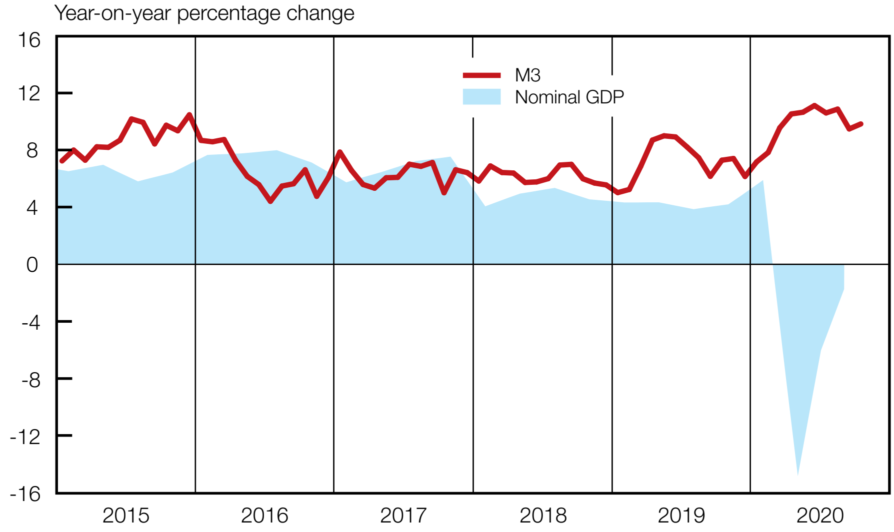
Source: SARB

Monetary developments, interest rates and financial markets

Money supply

The robust growth in the broadly defined money supply (M3) during the national lockdown moderated somewhat in recent months, while the gap between the pace of increase in M3 and economic activity has closed, following the rebound in growth in *nominal* GDP in the third quarter of 2020. The deposit growth of households has levelled off somewhat since July 2020, while that of the corporate sector diverged, with growth in the deposits of non-financial companies remaining robust and that of financial companies slowing sharply up to October. The declining trend in M3 growth was also evident in the quarter-to-quarter seasonally adjusted and annualised rate of increase, which decelerated significantly from 27.1% in the second quarter of 2020 to 5.9% in the third quarter. Consequently, the income velocity of M3 rebounded from its all-time low of 1.05 in the second quarter of 2020 to 1.21 in the third quarter, alongside the rebound in nominal GDP.

Money supply and gross domestic product

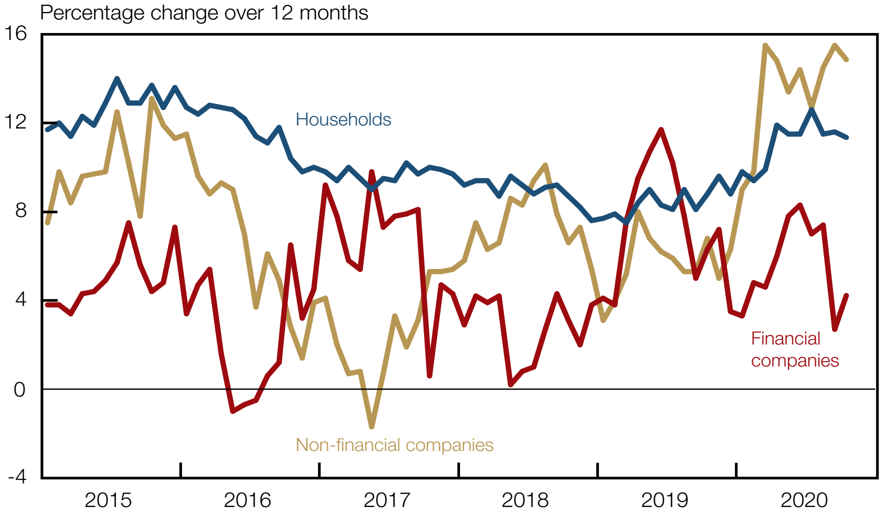


Sources: Stats SA and SARB

Year-on-year growth in M3 accelerated from 7.2% in January 2020 to a high of 11.1% in June amid the strict national lockdown, which initially limited spending to the purchasing of basic necessities, before moderating to 9.8% in October alongside the easing of restrictions. Growth in household deposits, initially boosted by the reduction in consumption expenditure during the lockdown, moderated from 12.6% in July 2020 to 11.3% in October as spending normalised somewhat. Similarly, growth in the deposit holdings of the corporate sector moderated from 10.9% in June 2020 to 9.0% in October, led by the marked slowdown in the deposit growth of financial companies.

While the easing of the lockdown restrictions benefitted the deposit growth of non-financial companies, the contemporaneously low interest rate environment prompted financial companies to seek out alternative financial assets. The lifting of some lockdown restrictions, which ignited economic activity and boosted cash flow, contributed to an acceleration in the deposit growth of non-financial companies, from 12.7% in July to 15.5% in September, before moderating somewhat to 14.9% in October. By contrast, growth in the deposit holdings of financial companies decelerated significantly from a high of 8.3% in June 2020 to a low of 2.7% in September and 4.2% in October, amid the low rate of return on bank deposits. Withdrawals were recorded by, among others, fund managers as well as money market and other unit trusts.

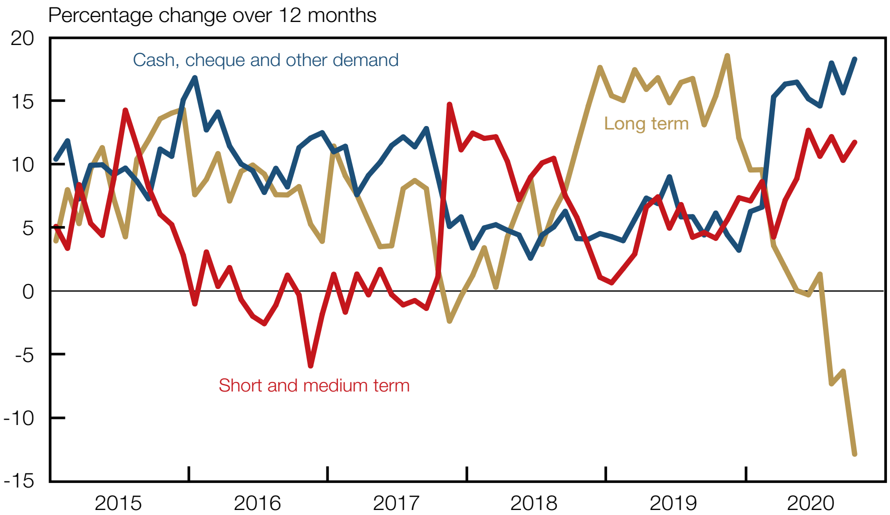
Deposit holdings of households and companies



Source: SARB

Maturity preferences continued to diverge in the highly uncertain economic environment, with depositors favouring liquid and short- to medium-term deposits. Year-on-year growth in cash, cheque and other demand deposits accelerated sharply to a high of 18.3% in October 2020. Growth in short- and medium-term deposits also accelerated briskly from a low of 4.3% in March 2020 to 12.7% in June, but then retraced somewhat to 11.7% in October. The shift away from long-term deposits was probably influenced by the progressive decline in interest rates to extraordinary low levels during the course of 2020. Long-term deposits contracted significantly by 12.9% in October.

Deposits by maturity

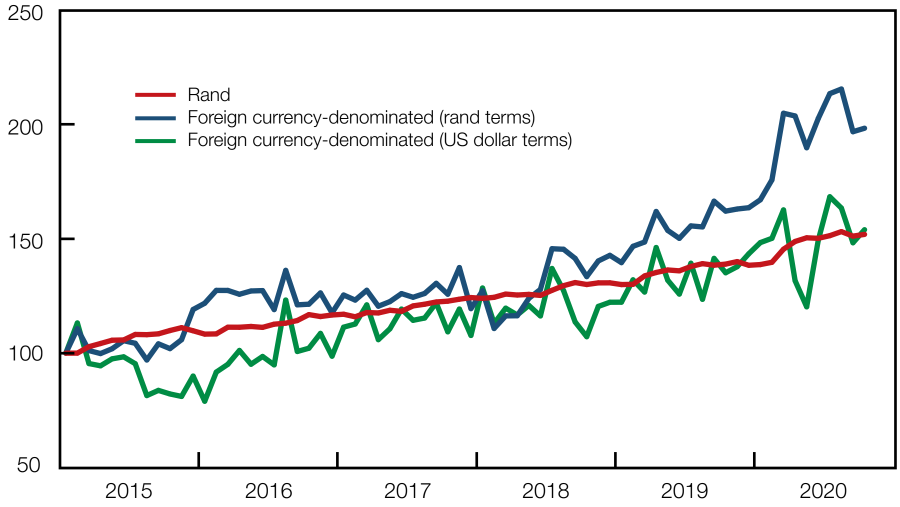


Source: SARB

The value of foreign currency-denominated deposits increased significantly from December 2019 to March 2020, following the marked depreciation in the exchange value of the rand triggered by the COVID-19 pandemic. In July 2020, the value of foreign currency-denominated deposits reached an all-time high when National Treasury increased its foreign currency deposits at the SARB, following loans received from the IMF and the New Development Bank. The value of foreign currency-denominated deposits has since decreased again, owing to withdrawals and the appreciation of the exchange value of the rand. Nonetheless, the value of foreign currency-denominated deposits accounted for only 3.4% of total M3 in October 2020, down from a recent high of 3.7% in July.

Money supply

Index: January 2015 = 100



Source: SARB

Reflective of changes in spending and investment behaviour in the current extraordinary environment, total M3 deposit holdings increased by only R21.3 billion in the third quarter of 2020, following increases of R214 billion in the first quarter and R125 billion in the second quarter of the year at the height of the COVID-19 crisis. The household sector contributed R39.6 billion to the increase in M3 in the third quarter of 2020, compared with an increase of R66.1 billion in the second quarter. The deposit holdings of the corporate sector contracted by R18.3 billion in the third quarter, as that of financial companies decreased by R65.3 billion and that of non-financial companies increased by R47.0 billion.

M3 holdings of households and companies

	Year-on-year change (R billions)					Percentage of total M3 deposit holdings*
	2019		2020			
	Q3	Q4	Q1	Q2	Q3	
Households	34.5	21.2	27.0	66.1	39.6	35.9
Companies: Total	40.1	-24.9	187.4	59.2	-18.3	64.1
Of which: Financial	9.9	-63.3	89.4	76.7	-65.3	34.2
Non-financial	30.3	38.4	98.0	-17.5	47.0	29.9
Total M3 deposits	74.6	-3.7	214.4	125.2	21.3	100.0

* Expressed as a percentage of the total outstanding balance as at September 2020

Source: SARB

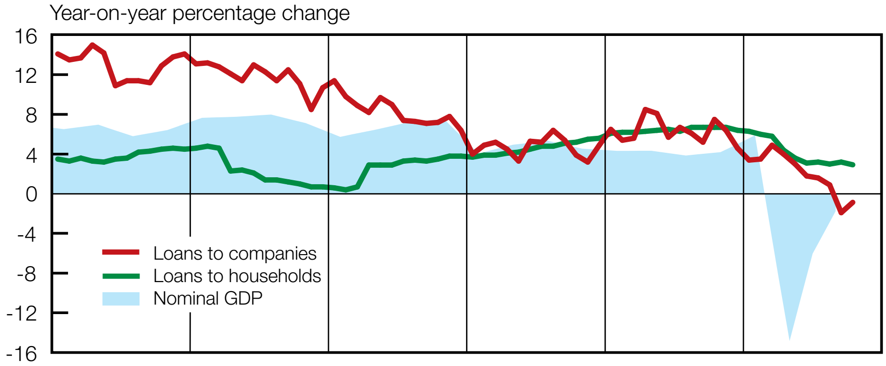
Statistically, the counterparts to the increase in M3 of R21.3 billion in the third quarter of 2020 consisted of an increase of R43.5 billion in net foreign assets of the monetary sector, while decreases of R38.4 billion in claims against the domestic private sector and R23.7 billion in net credit extended to the government sector[16] moderated the increase in M3. Net other assets (a contra-entry absorbing changes in foreign assets, among other factors) increased by R40.0 billion.

16 This is the difference between government deposits and banks' claims on government (mainly holdings of government securities).

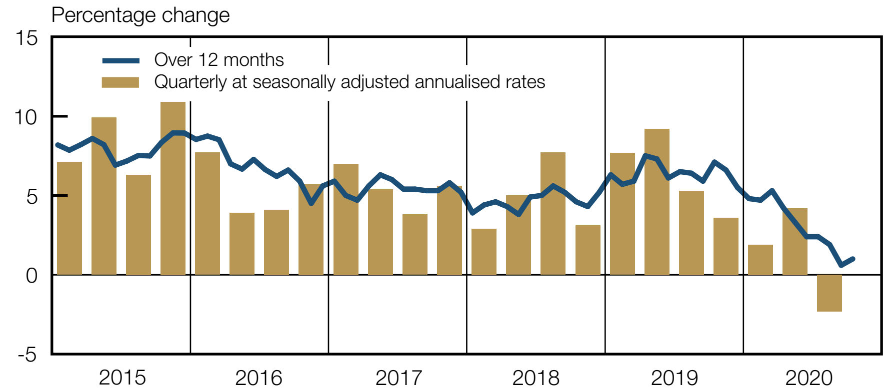
Credit extension

Growth in total loans and advances extended by monetary institutions to the domestic private sector decelerated further in the third quarter of 2020, led by a marked deceleration and then a contraction in loans to companies. The year-on-year growth in total loans and advances decelerated sharply from a high of 5.3% in March 2020 to 0.6% in September – the lowest growth rate since April 2010 – before accelerating slightly to 1.0% in October.

Bank loans and gross domestic product



Total loans and advances to the private sector

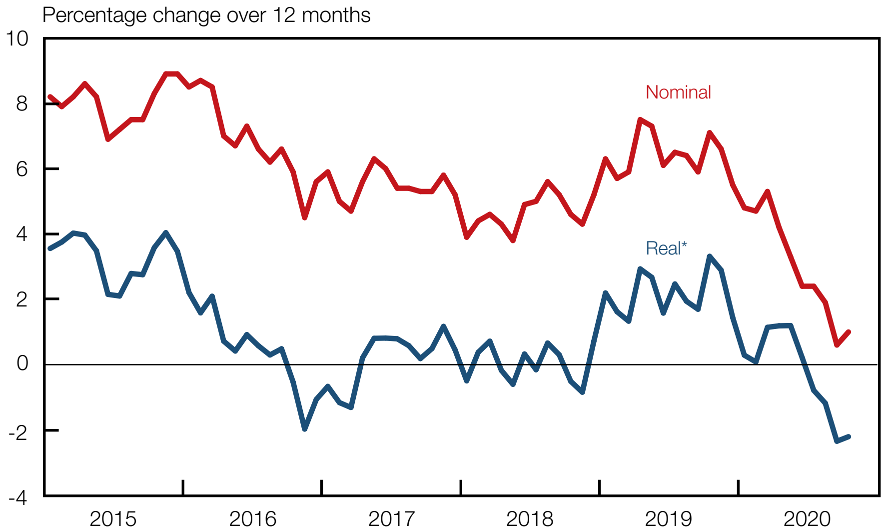


Sources: Stats SA and SARB

The weak credit extension was also visible in the quarter-to-quarter seasonally adjusted and annualised growth in total loans and advances to the domestic private sector, which fell to -2.3% in the third quarter of 2020, down from a recent high of 4.2% in the second quarter. This was the first quarterly contraction in credit extension since the fourth quarter of 2009 in the aftermath of the global financial crisis. Total loans and advances as a percentage of GDP decreased from 83.4% in the second quarter of 2020 to 71.0% in the third quarter, largely due to the marked increase in nominal GDP. In real terms, credit growth slowed from a recent high of 3.3% in October 2019 to -2.2% in October 2020. The corporate sector was the main driver of the decline in credit extension, while the household sector's demand for credit also petered out but remained positive.

The contraction of 1.9% in credit extension to companies in September 2020 – the first contraction since August 2010 – moderated to 0.9% in October. The steady decline in corporate demand for bank funding was the result of, among other factors, slowing demand for credit from non-financial corporates in the mining, mineral and telecommunications industries as well as some SOCs.

Total loans and advances



* Deflated with the consumer price index
Source: SARB

Growth in credit extension to households moderated from a recent high of 6.7% in October 2019 to 3.0% in August 2020 and remained weak at 2.9% in October. It is likely that the slowdown initially resulted from limited spending during the stricter lockdown levels from April to June 2020, which was later exacerbated by reduced creditworthiness due to the impact of subsequent income and job losses. Demand for bank funding has since remained muted, despite the continued gradual relaxation of lockdown restrictions.

Credit extended to households and companies

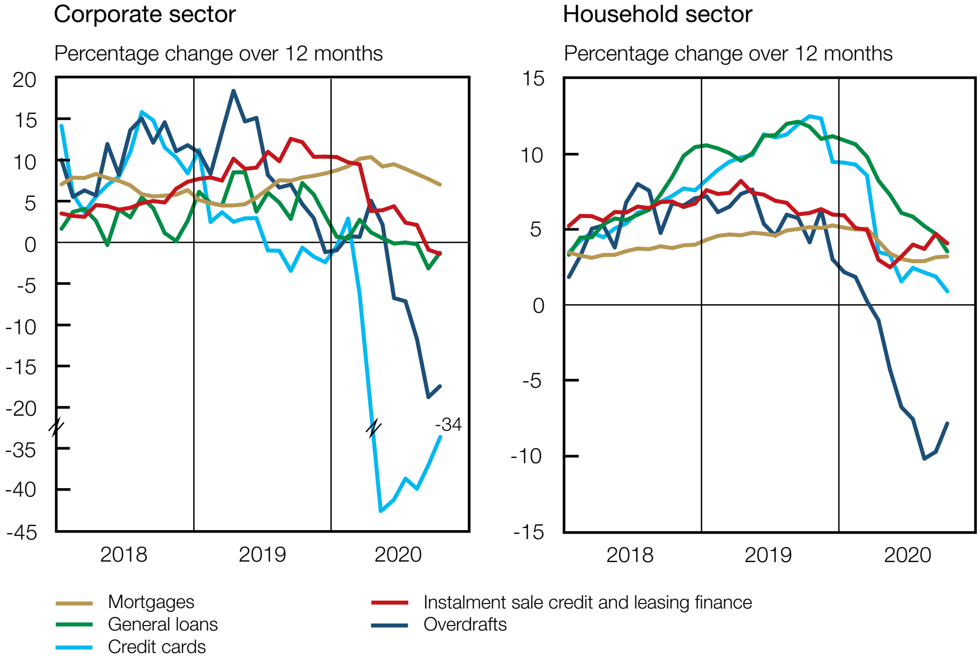
	Year-on-year change (R billions)					Percentage of total loans and advances*
	2019	2020				
	Q3	Q4	Q1	Q2	Q3	
Households	23.9	28.8	24.0	-24.1	25.8	49.8
Companies: Total	23.2	-6.0	58.8	-43.8	-42.8	50.2
Of which: Financial	-0.9	8.7	-12.0	12.3	35.2	12.0
Non-financial	24.2	-14.7	70.8	-56.2	-78.1	38.2
Total bank loans and advances	47.1	22.7	82.8	-68.0	-17.1	100.0

* Expressed as a percentage of the total outstanding balance as at September 2020

Source: SARB

Credit extension to the corporate sector contracted by R42.8 billion in the third quarter of 2020, the second consecutive large quarterly decrease. Overdrafts decreased by a significant R31.3 billion in the third quarter of 2020, while general loans – the corporate sector's most preferred category of credit – declined by R17.5 billion, less than the decrease of R38.8 billion in the second quarter. Various industries returned to full production in the third quarter under eased lockdown restrictions, and some companies in mining and resources, among others, resorted to the repayment of loans entered into before or during the COVID-19-induced lockdown. Credit extension to non-financial companies contracted by a notable R78.1 billion in the third quarter following a contraction of R56.2 billion in the previous quarter. By contrast, credit extension to financial companies expanded by R12.3 billion in the second quarter of 2020 and by a further R35.2 billion in the third quarter.

Selected loans and advances



Source: SARB

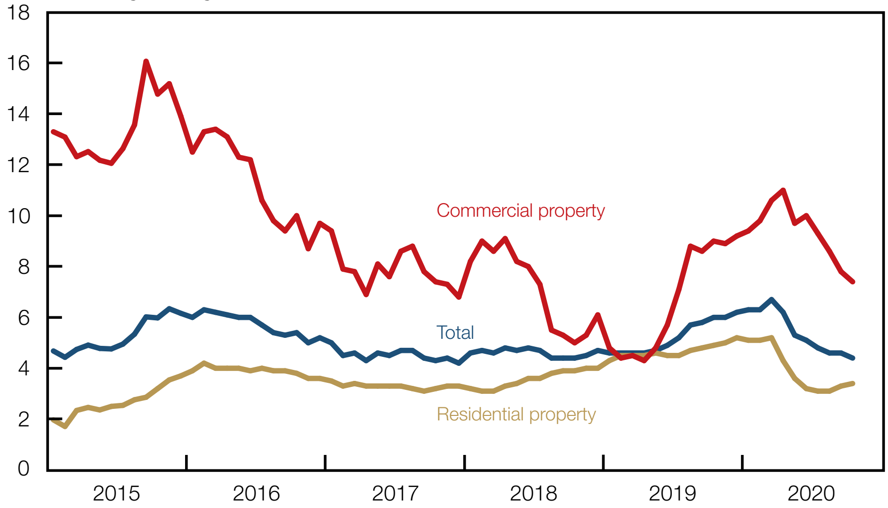
Growth in general loans to companies slowed from 3.2% in December 2019 to -3.1% in September 2020, and then improved slightly to -1.3% in October. The pace of increase in overdrafts to companies recovered briefly from December 2019 to April 2020, before contracting by as much as 17.4% in the year to October. Year-on-year growth in credit card advances, which constitutes only 0.3% of loans to companies, fell to a low of -42.8% in May 2020 before improving slightly to -34.1% in October. The sharp contraction in these two credit categories likely reflects the extent to which the lockdown has impeded operations. Furthermore, the repayment of loans by companies, which currently exceeds their take-up of new loans, reflects the avoidance of undue exposure to debt in the current uncertain economic environment.

The moderation in *credit extension to the household sector* has been relatively broad-based thus far in 2020, amid uncertainty brought about by the COVID-19 pandemic as well as the impact of income and employment losses on households' ability to borrow. Year-on-year growth in general loans to households decelerated from a recent high of 12.1% in September 2019 to 3.5% in October 2020. Growth in credit card advances also slowed sharply from 12.5% in October 2019 to 0.9% in October 2020, while the utilisation of overdrafts contracted by 7.8% in October 2020 even though it was up from the low in August. Growth in instalment sale credit rebounded somewhat from a low of 2.5% in May 2020 to 4.1% in October as vehicle sales improved with the easing of the lockdown restrictions.

Growth in *mortgage advances* started the year on an upbeat note as it accelerated to 6.7% in March 2020 before tapering off to 4.6% in September, alongside the effects of the national lockdown. Since the easing of the lockdown restrictions, growth in mortgage advances on residential property has displayed a moderate recovery, while that on commercial property continued to slow. Growth in mortgage advances on residential property accelerated marginally from a recent low of 3.1% in July 2020 to 3.4% in October, as the sharp decrease in the cost of borrowing probably boosted the demand for property, although a backlog in property registrations may still have been dampening growth in mortgages. Growth in mortgage advances on commercial property remained relatively lively, although it moderated from a recent high of 11.0% in April 2020 to 7.4% in October.

Mortgage advances

Percentage change over 12 months



Source: SARB

Growth in *instalment sale credit and leasing finance*, mainly used to finance the purchases of new and used vehicles, continued to moderate to a recent low of 2.2% in October 2020 as vehicle sales had not yet returned to pre-lockdown levels. Consumer preferences may be shifting towards the used vehicle market in the current constrained financial environment, while the new work-from-home milieu may also be supressing the demand for vehicles somewhat.

Growth in bank credit by economic sector

Percentage change over four quarters

Economic sector	2019		2020			Percentage of total credit extension*
	Q3	Q4	Q1	Q2	Q3	
Households	7.8	7.6	6.6	3.7	2.5	35.3
Finance and insurance	-5.4	-7.2	8.7	2.8	3.7	16.4
Real estate	10.9	8.0	12.6	9.9	6.1	11.7
Wholesale and retail trade	0.3	-7.3	-0.1	4.1	-3.1	4.8
Manufacturing	5.2	0.1	10.7	7.6	-2.7	4.1
Business services	-1.9	-4.1	11.1	6.7	10.2	3.4
Transport, storage and communication	4.8	3.1	5.7	3.9	3.0	3.1
Electricity, gas and water	9.8	10.4	3.5	1.2	2.3	2.4
Agriculture, forestry and fishing	-4.4	-7.5	12.4	8.8	20.8	2.3
Mining and quarrying	1.0	-6.5	4.2	33.2	-6.1	1.5
Construction	2.3	5.7	6.4	10.5	12.0	0.9
Community, social, personal services and other	-3.1	7.6	-3.0	12.3	16.2	14.1
Total	**2.9**	**2.8**	**6.4**	**6.2**	**4.9**	**100.0**

* Expressed as a percentage of the total outstanding balance as at September 2020

Source: SARB

Despite the gradual resumption of operations by most industries after the lifting of the initial strict lockdown regulations, growth in overall credit extension remained weak, as companies seemed to be avoiding excessive exposure to debt in the uncertain economic environment. Nonetheless, some sectors still experienced double-digit growth rates, notably agriculture, community and social services as well as construction and business services. In particular, growth in credit extension to the agricultural sector accelerated strongly in the third quarter of 2020, amid the apex of the harvesting season. Credit demand by manufacturing, wholesale and retail trade as well as mining and quarrying contracted again in the third quarter of 2020, probably reflective of the protracted weak economic conditions. The finance and insurance as well as the electricity, gas and water sector recorded positive, but relatively modest, increases in credit extension over this period.

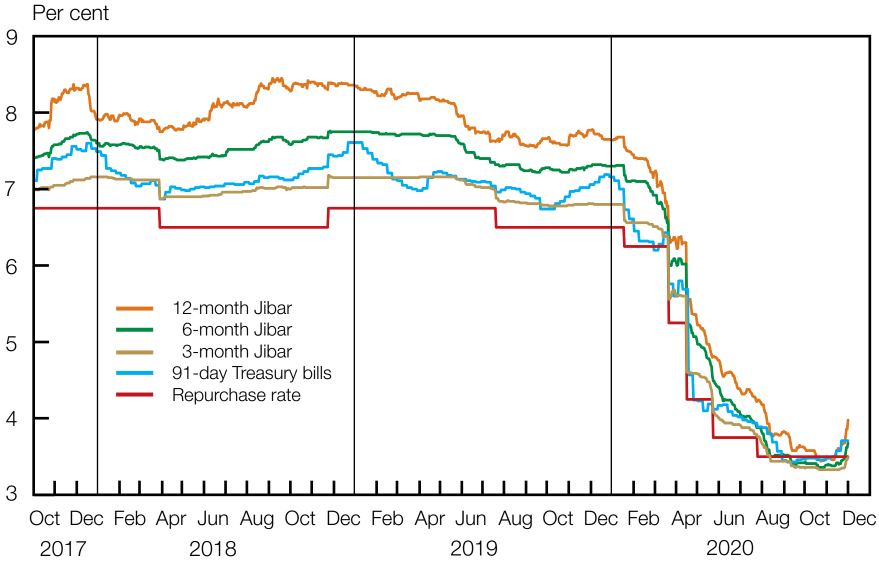
Interest rates and yields

The SARB's Monetary Policy Committee (MPC) decided to keep the repurchase (repo) rate unchanged at 3.50% at both the September and November 2020 meetings, having assessed the overall risks to the inflation outlook to be relatively balanced over the medium term. Following the most recent reduction in the repo rate in July 2020, domestic short-term interest rates generally continued lower, except for occasional interruptions when the exchange value of the rand depreciated. Money market conditions were also moderately affected by a projected wider fiscal deficit in the *2020 MTBPS* in late October.

The 3-month Johannesburg Interbank Average Rate (Jibar) declined from 3.79% on 23 July 2020, prior to the 25 basis point reduction in the repo rate, to 3.33% on 20 October, where it remained for an extended period before increasing slightly to 3.49% at the end of November. The 6-month Jibar followed a similar trajectory, initially decreasing by 52 basis points from 3.88% on 23 July 2020 to 3.36% on 19 October, before increasing moderately to 3.68% on 30 November. The 12-month Jibar averaged 3.94% in the third quarter of 2020, down from an average of 5.12% in the second quarter, and declined even further to a low of 3.44% on 22 October. However, the rate then increased to 3.98% on 30 November.

The tender rate on 91-day Treasury bills (TBs) decreased by 56 basis points, from 4.02% on 1 July 2020 to 3.46% in late October, alongside continued broad-based investor demand for short-term instruments. Subsequently, the rate on 91-day TBs increased only moderately to 3.71% in late November, despite the steeper debt trajectory announced in the *2020 MTBPS*.

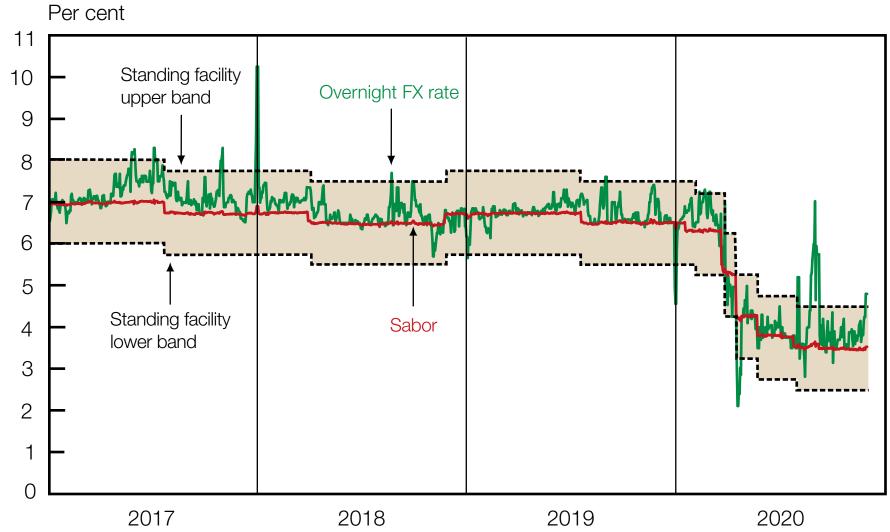
Money market rates



Source: SARB

In recent months, the market for interbank lending occasionally reflected relatively constrained liquidity conditions. Although the South African Benchmark Overnight Rate (Sabor) remained well within the standing facility limits, the overnight FX rate occasionally exceeded the upper standing facility limit due to a shortage of liquidity in the FX forward market. The Sabor remained closely aligned to the repo rate and has been averaging 3.55% since the lowering of the policy rate in July. By contrast, the overnight FX rate displayed much more volatility, initially increasing sharply by 327 basis points, from 3.75% on 10 July 2020 to 7.02% on 31 August, temporarily exceeding the upper limit of the standing facility range due to a brief liquidity shortage in the FX forward market towards month-end. However, the overnight FX rate quickly normalised to fluctuate within a narrower range as liquidity conditions in the FX forward market eased. On balance, the overnight FX rate fluctuated around an average of 4.13% in the third quarter of 2020, similar to the average of 4.09% in the second quarter. In October and November, the overnight FX rate fluctuated around an average of 3.83%, with a low of 3.15% on 1 October and a high of 4.80% on 30 November.

Benchmark overnight rates

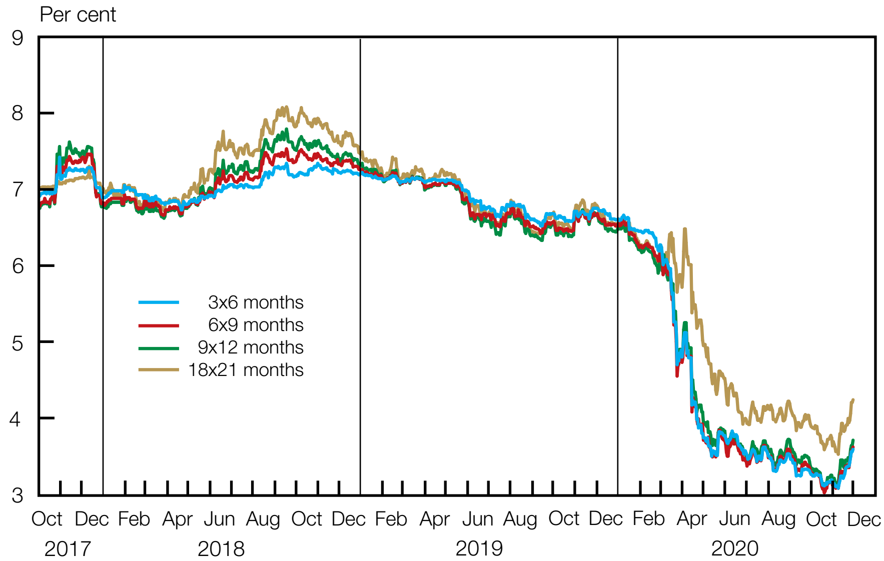


Source: SARB

Rates on forward rate agreements (FRAs) generally trended lower in the third quarter of 2020, occasionally interrupted by fluctuations in the exchange value of the rand. The downward trend in FRA rates across the maturity spectrum was also supported by the relatively benign inflation outcomes in recent months, leading to expectations that the policy rate will remain low in the coming months. For example, the 3x6-month FRA declined by 43 basis points from 3.53% on 29 August 2020 to as low as 3.08% on 9 November, before edging higher to 3.59% on 30 November. Longer-term FRAs declined even more sharply, with the 9x12-month FRA decreasing by 64 basis points from 3.72% on 28 August to 3.08% on 19 October, before it fluctuated higher to 3.71% at the end of November despite the recent appreciation in the exchange value of the rand.

Private sector banks' deposit and lending rates have decreased alongside the lower repo rate thus far in 2020. The prime lending rate has remained at 7.00%, having followed the most recent reduction in the policy interest rate in July, while the weighted-average flexible rate charged by banks on mortgage advances decreased by 26 basis points from 6.89% in June to 6.63% in October. Although the weighted-average overdraft rate also declined to 7.86% in October 2020, it continued to exceed the prime lending rate. Deposit rates offered by banks also adjusted lower, with the weighted-average interest rate on call deposits decreasing from 3.95% in June 2020 to 3.62% in October. At the same time, banks offered an average of 5.06% on 12-month fixed deposits, while the interest rate on cheque accounts declined to only 1.46%. Similarly, the interest rate offered on one-month notice deposits decreased from 3.94% in June to 3.61% in October.

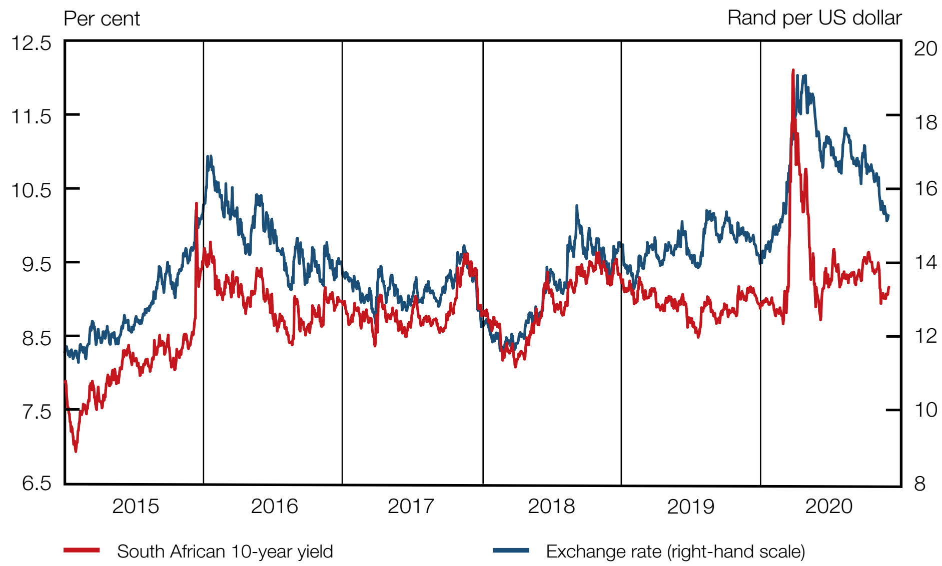
Forward rate agreements



Source: SARB

The *yield on 10-year South African rand-denominated government bonds* issued and traded in the domestic market increased by 92 basis points, from 8.72% on 3 June 2020 to 9.64% on 7 October. This reflected concerns regarding the resurgence of COVID-19 infections globally and a sell-off of emerging market bonds. Subsequently, the 10-year South African government bond yield declined by 47 basis points to 9.17% on 30 November as the exchange value of the rand appreciated and consumer price inflation remained subdued, even though the *2020 MTBPS* projected a significantly larger budget deficit and slower debt consolidation. The bond yield increased marginally after South Africa's sovereign credit rating was downgraded by two rating agencies on 20 November 2020.

Government bond yield and the exchange rate



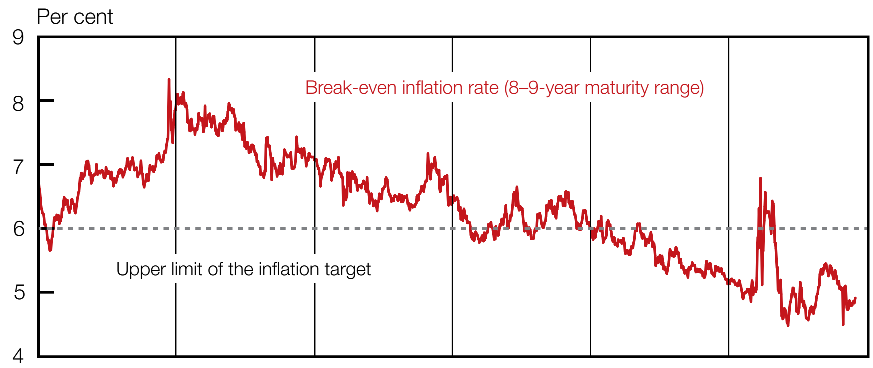
Sources: IRESS, JSE and SARB

The *break-even inflation rate* in the 8–9-year maturity range[17] breached the 6% upper limit of the inflation target range in March and April 2020. This reflected a sudden spike in both the nominal yield on conventional bonds and the real yield on inflation-linked bonds, brought about by uncertainty as to the impact of the COVID-19 pandemic on real economic activity and the financial markets as well as the increase in South Africa's risk premium and concomitant

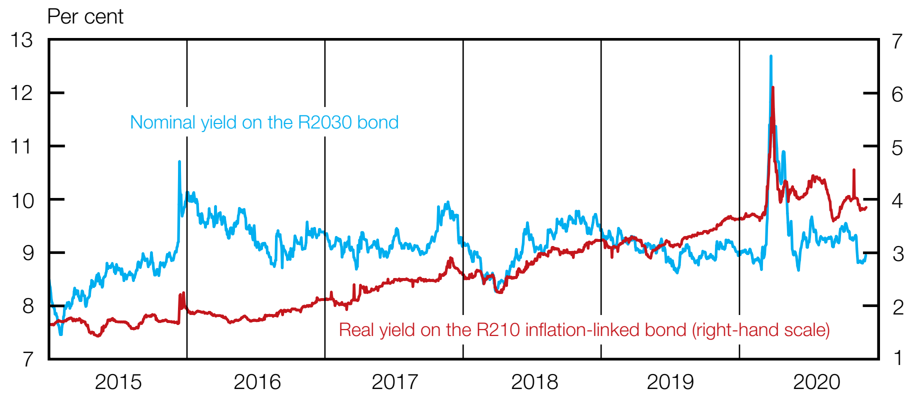
17 The break-even inflation rate in the 8–9-year maturity range was calculated as the difference between the nominal yield on the R2030 conventional bond and the real yield on the R210 inflation-linked bond.

non-resident net sales of bonds. The break-even inflation rate then fell sharply from 6.43% on 23 April 2020 to 4.91% on 30 November as real bond yields declined to a lesser extent than nominal yields, as the exchange value of the rand appreciated and inflation remained subdued.

Break-even inflation rate



Government bond yields



Sources: IRESS, JSE and SARB

The *yield curve* changed from 3 June 2020 to 7 October as short-term yields declined somewhat while the slope steepened and the level shifted higher beyond five years. These changes, among other factors, reflected renewed risk aversion and concerns regarding the deteriorating domestic fiscal position. Subsequently, the level of the yield curve decreased across almost all maturities to 30 November, except at the short end. The yield gap,[18] which had initially widened from 701 basis points on 3 June 2020 to 831 basis points on 7 October, narrowed again to 766 basis points on 30 November.

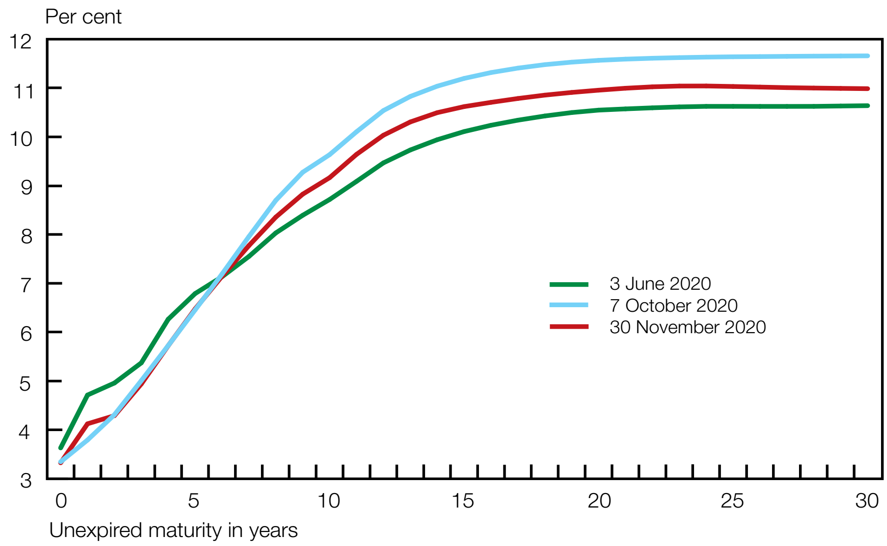
The yield spread between emerging market US dollar-denominated bonds and US government bonds, as measured by the JPMorgan Emerging Markets Bond Index Plus (EMBI+),[19] narrowed from a high of 543 basis points in March 2020 at the height of the COVID-19 pandemic to 363 basis points in November as investor sentiment improved with the easing of the lockdown restrictions and the resumption of economic activity. Similarly, South Africa's *sovereign risk premium*[20] in the five-year maturity range narrowed markedly from an average of 579 basis points in April 2020 to 294 basis points in November.

18 The yield gap is measured as the difference between yields at the extreme long and short ends of the yield curve.

19 The EMBI+ measures the total returns on US dollar-denominated debt instruments of emerging market economies.

20 This is the differential between the yield on South African government US dollar-denominated bonds and that on US dollar-denominated bonds of the US government.

Yield curve



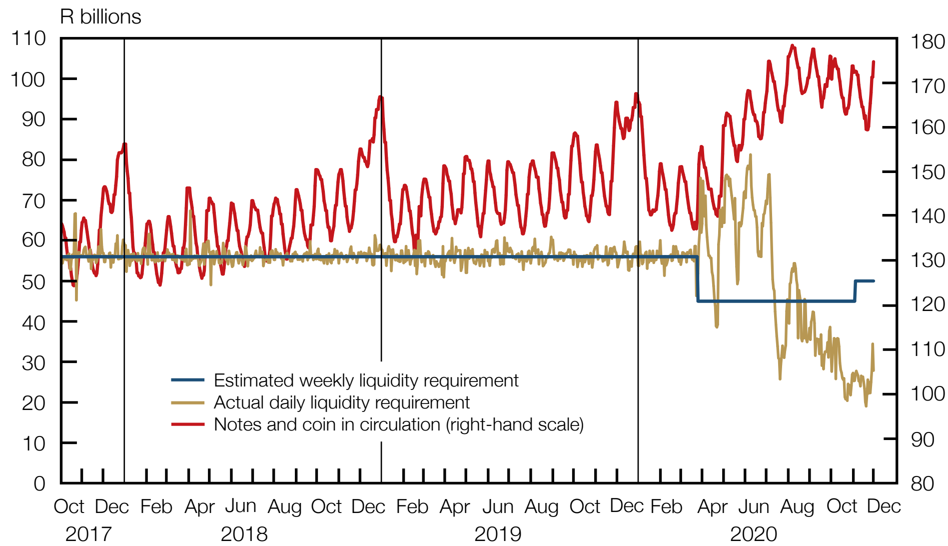
Sources: IRESS and JSE

Money market

Private sector banks' actual daily liquidity requirement varied relatively widely in the third quarter of 2020, fluctuating between a low of R25.7 billion and a high of R76.3 billion, while averaging R41.1 billion. The low of R25.7 billion in July 2020 reflected a considerable decline in the demand for funding at the weekly main refinancing auctions, as private banks experienced more frequent periods of surplus liquidity. Nonetheless, at that point the weekly main refinancing amount on offer was kept fixed at R45.0 billion after it was reduced from R56.0 billion in March 2020. Subsequently, the weekly main refinancing amount was increased to R50.0 billion as from 4 November when the SARB started to unwind some of the liquidity measures previously implemented. In October and November 2020, the actual daily liquidity requirement of private sector banks fluctuated between a low of R19.0 billion and a high of R36.3 billion, indicating that the under-subscription of the weekly main refinancing auctions continued with banks experiencing an extended period of surplus liquidity.

The total accommodation to banks reached a high of R101 billion in March 2020, but subsequently declined significantly to R54.1 billion in July and further to R33.2 billion in October, as demand for cash at the weekly main refinancing auctions declined and longer-term refinancing matured.

Liquidity requirement

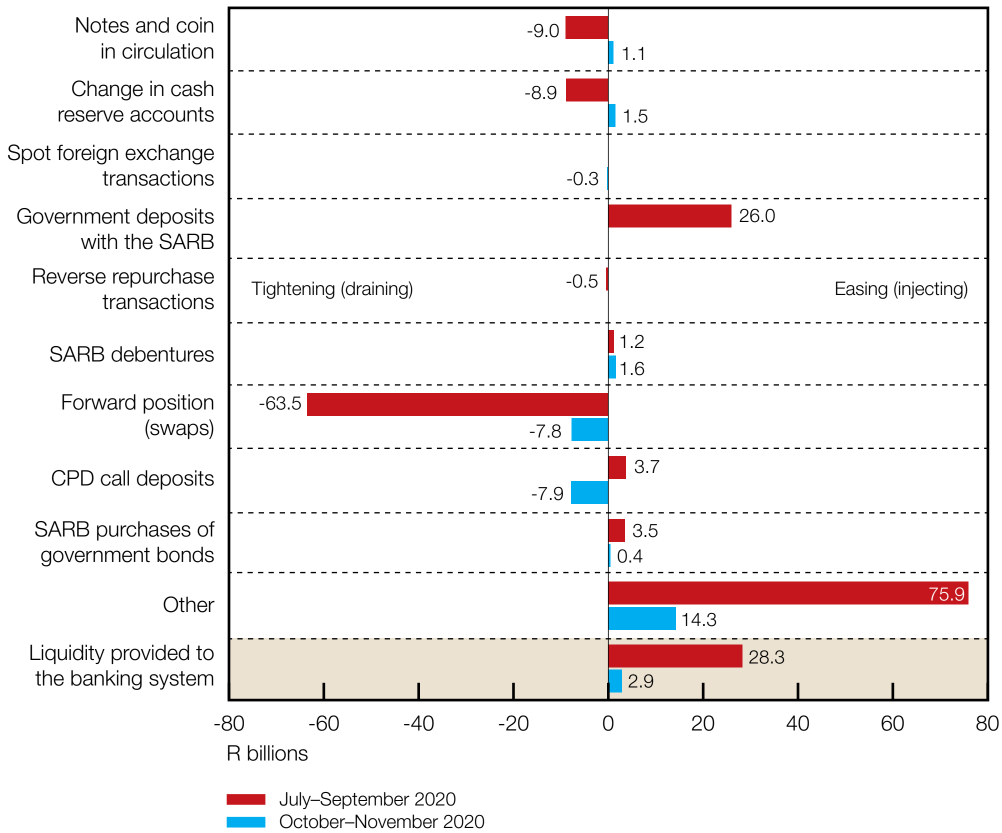


Source: SARB

The net effect of the factors influencing market conditions expanded liquidity in the money market by R27.1 billion in the second quarter of 2020 and by a further R28.3 billion in the third quarter. An increase in notes and coin in circulation outside the SARB tightened money market liquidity by R9.0 billion in the third quarter, with private banks' required cash reserve deposits also adding R8.9 billion to the contraction in liquidity. In addition, the SARB entered into FX swap transactions to the total value of R63.5 billion, mainly to neutralise funds from loans received on behalf of National Treasury from the IMF and the New Development Bank, as reflected in the 'other' category. These movements were partially offset by National Treasury withdrawing R26.0 billion from the National Treasury Sterilisation Deposit Account at the SARB for short-term bridging finance purposes. The Corporation for Public Deposits (CPD) decreased deposits at the SARB by R3.7 billion to assist National Treasury with its month-end liquidity obligations.

In October and November 2020, liquidity once again increased by R2.9 billion. This included a decrease in the required cash reserve deposits of private sector banks of R1.5 billion, an increase in CPD deposits with the SARB of R7.9 billion and the maturing of SARB debentures of R1.6 billion.

Factors influencing money market liquidity conditions



Source: SARB

From January to November 2020, capital redemption and coupon interest payments of R155 billion were effected from government's tax and loan accounts. Of this amount, R1.8 billion accrued to the SARB's portfolio of government bonds.

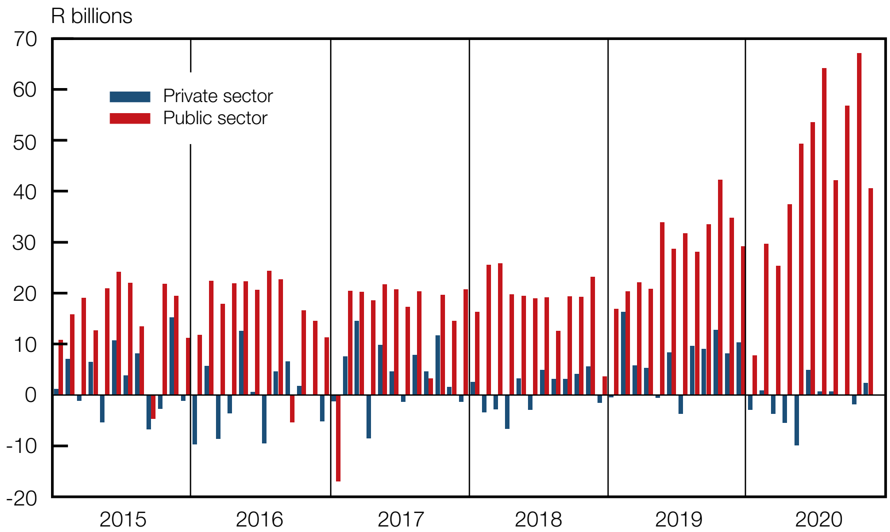
Bond market

The public sector's[21] net issuance of listed bonds in the *domestic primary bond market* increased by 51.3% year on year to an all-time high of R474 billion in the first 11 months of 2020. This reflected revenue shortfalls, COVID-19-related spending and the financing of distressed SOCs, among other factors, which continued to contribute to funding pressures and substantial national government debt issuance.

21 The public sector includes national and local governments as well as public corporations.

By contrast, private sector companies redeemed bonds to the net amount of R14.2 billion during the 11 months to November 2020, as opposed to the net issuance of R70.8 billion during the same period of 2019. Private sector companies' reduced funding needs in 2020 resulted from the weak economic activity due to the national lockdown. The total value of all JSE-listed debt securities in issue of R3.9 trillion at the end of November 2020 was 14.8% more than a year earlier.

Net issues in the domestic primary bond market



Source: JSE

The *value of turnover* in the domestic secondary bond market has remained relatively subdued thus far in 2020 alongside wide swings in bond yields. The daily average turnover of R140 billion in the first 11 months of 2020 was 7.1% lower than in the corresponding period of 2019.

The increase in the value of rand-denominated bonds in issue in the *European bond market* in the 11 months to November 2020 contrasted the decline in the *Uridashi bond market*. In total, the net issuance of rand-denominated debt more than tripled during this period to R25.0 billion from a year earlier. The larger yield differential contributed to increased demand for rand-denominated bonds issued in international markets.

Rand-denominated bonds issued in international bond markets, January to November 2020

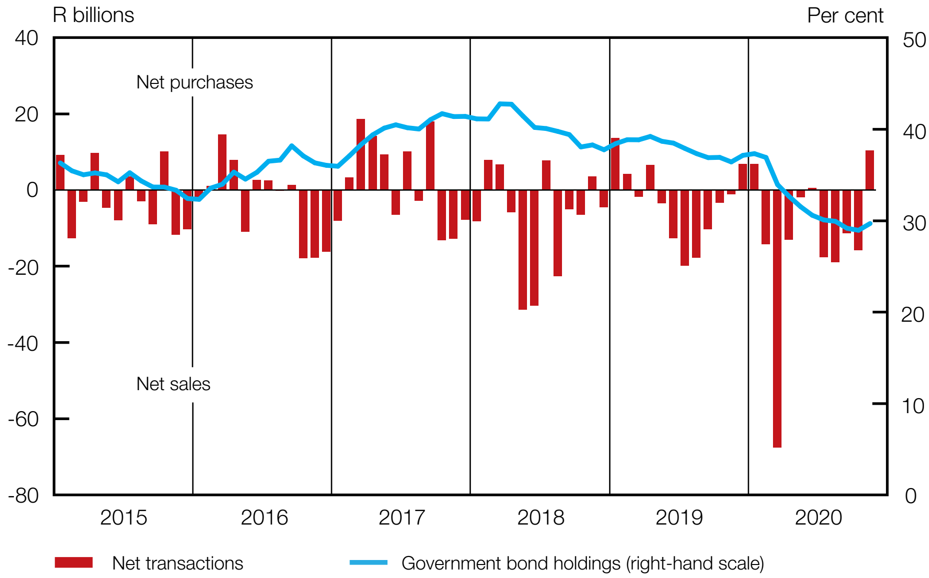
R millions

	Eurorand		Uridashi		Total	
	2019	2020	2019	2020	2019	2020
Issues	39 968	39 431	1 055	464	41 023	39 895
Redemptions	24 095	11 049	8 887	3 798	32 982	14 847
Net	15 873	28 382	-7 832	-3 334	8 041	25 048

Source: Bloomberg

Non-residents continued to be net sellers of domestic debt securities in 2020, according to JSE data. Net sales of R14.4 billion in the second quarter of 2020 was followed by a further R47.9 billion in the third quarter and R5.5 billion in October and November. This contributed to record-high cumulative net sales of R143 billion in the first 11 months of 2020 compared with net sales of R45.9 billion in the same period of 2019. Non-resident net sales reflected the general sell-off of emerging market bonds and, in particular, concern over South Africa's fiscal position. As a result, the share of non-residents' holdings of government bonds declined to 29.0% at the end of October 2020 – the lowest level since December 2011.

Non-residents' net transactions in the domestic bond market



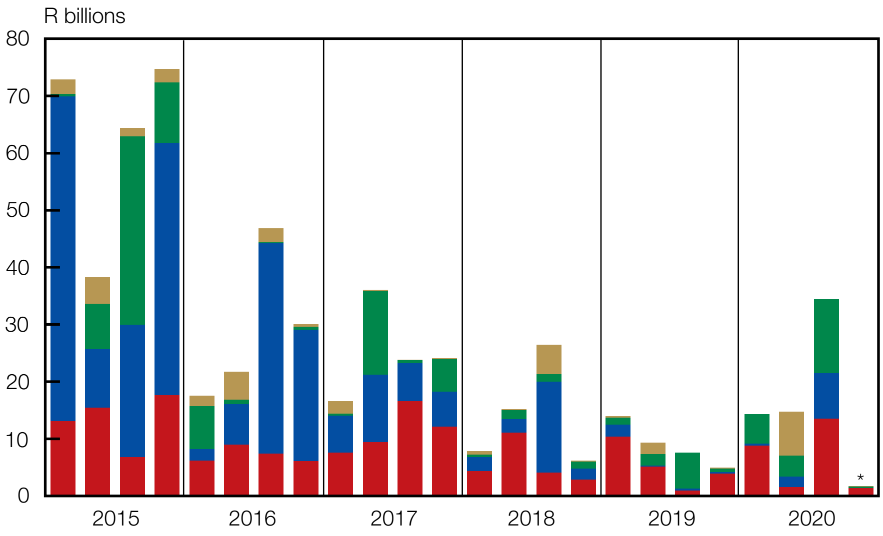
Sources: JSE and National Treasury

Share market

Equity capital raised by companies listed on the JSE in the domestic and international primary share markets of R65.2 billion in the first 11 months of 2020 was nearly double that in the same period of 2019. Despite more de-listings than new listings, this reflected a need for funding due to the impact of COVID-19 on real economic activity and, in particular, changes to capital structures to reduce debt and increase liquidity. In September 2020, a primary-listed mining company and a secondary-listed financial company contributed the most to the total value of shares issued. The mining company issued shares for cash to the value of R12.5 billion to fund the redemption of US dollar-denominated convertible bonds to reduce debt, while the real estate and investment trust raised capital through a rights issue, also in the amount of R12.5 billion, to reduce indebtedness and to increase liquidity. Thus far in 2020, companies in the financial sector have contributed the most to the total value of shares issued at 38.6%, followed by companies in the resources sector at 33.5%.

The *value of turnover* in the secondary share market of the JSE remained elevated, with a daily average turnover of R23.3 billion in the first 11 months of 2020, which was 12.4% more than in the same period of 2019. Turnover surged on higher share volumes, reflective of the increased uncertainty due to the effects of the COVID-19 pandemic. The market capitalisation of all shares listed on the JSE increased from a low of R14.5 trillion in March 2020 to R17.2 trillion in August, before declining to R15.8 trillion in October, reflecting share price movements. Subsequently, market capitalisation again increased to R17.4 trillion in November.

Equity capital raised on the JSE by sector

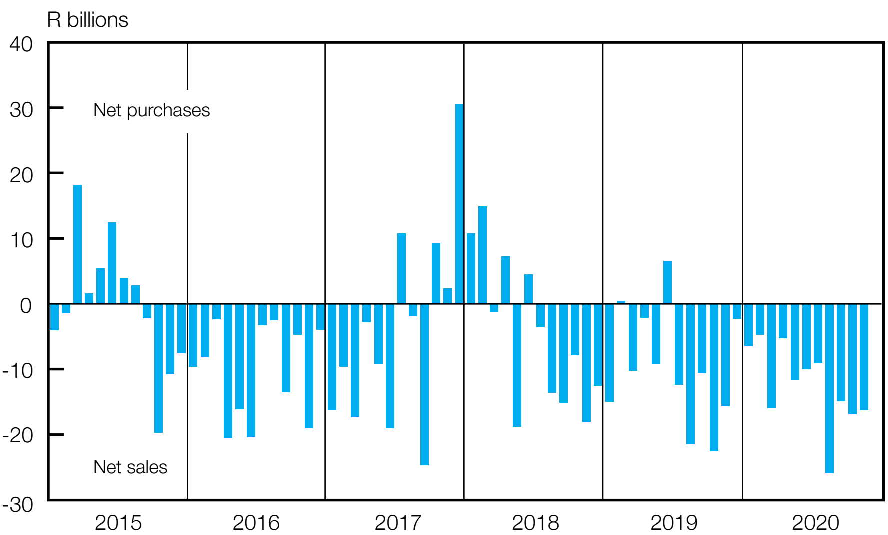


* October and November

Source: JSE

Non-residents' net sales of domestic-listed shares of R54.0 billion in the first half of 2020 was followed by net sales of R49.8 billion in the third quarter and R33.1 billion in October and November, as reported by the JSE. The persistent net sales, among other factors, reflected concerns over the prospects for a recovery in economic activity as well as the deteriorating fiscal position. Non-residents' record-high cumulative net sales of R137 billion in the 11 months to November 2020 exceeded the R112 billion in the corresponding period of 2019.

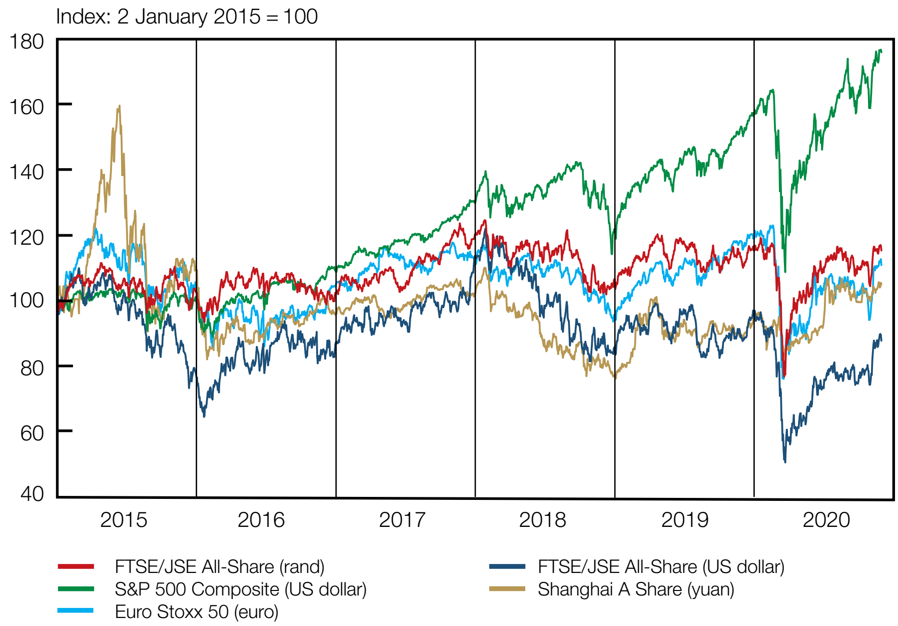
Non-residents' net transactions in the domestic share market



Source: JSE

The *share prices* of JSE-listed companies rebounded by 22.2% in the second quarter of 2020 and then remained broadly unchanged in the third quarter of 2020, with the FTSE/JSE All-Share Price Index (Alsi) ending the third quarter 0.2% lower. Thereafter, the Alsi declined by 4.8% to 51 685 index points at the end of October as it followed global equity markets. Global equity markets were weighed down by uncertainty around the US presidential elections, the lack of agreement on US fiscal stimulus as well as negative sentiment following rising COVID-19 infections in the US and Europe, and the subsequent reintroduction of lockdown measures in some European countries. The Alsi then increased again to 57 092 index points on 30 November, as global equity markets were buoyed by the outcome of the US elections as well as optimism about a possible COVID-19 vaccine. Gains in domestic share prices were more noticeable in the financial and resources sectors, with increases of 17.0% and 10.9% respectively in November 2020, followed by an increase of 7.9% in share prices of companies in the industrial sector.

Share prices



Sources: IRESS, JSE and SARB

The overall historical *price-earnings ratio* of ordinary shares listed on the JSE increased from a recent low of 13.8 in March 2020 to 42.2 in November, as total earnings declined sharply while share prices increased.

Market for exchange-traded derivatives

Following the brief decline in *domestic maize prices* from April to May 2020, the spot price of white maize contracts listed on the JSE Commodity Derivatives Market increased noticeably by 50.2%, from R2 356 per ton on 27 May 2020 to R3 539 per ton on 30 November. Similarly, the spot price of yellow maize increased by 39.3%, from R2 488 per ton to R3 467 per ton over the same period. These sharp increases were mainly driven by higher international maize prices and growing global demand, despite global supplies remaining elevated.

By contrast, the spot price of *domestic wheat contracts* declined from an all-time high of R6 900 per ton on 24 July 2020 to R4 835 per ton on 30 November, despite a marked increase in international wheat prices. This reflected the appreciation in the exchange value of the rand and expectations of the largest wheat harvest in 19 years. Favourable winter rains in the Western Cape and generally improved moisture levels in other winter crop growing areas of South Africa led to the further upward revision of the harvest estimate. In September 2020, the wheat import tariff was increased from R516.6 per ton to R832.1 per ton, but was then lowered again to R544.2 per ton in November.

Grain prices

Sources: JSE and International Grains Council

Turnover in equity derivatives decreased in the first 11 months of 2020 compared with the corresponding period of 2019, amid volatility in the underlying share market. Similarly, turnover in currency derivatives also declined over the same period.

Derivatives turnover on the JSE, January to November 2020

Type of derivative	Value (R billions)	Change over one year (per cent)
Equity	4 911	-15
Warrants	2	71
Commodity	846	11
Interest rate	1 325	7
Currency	971	-2

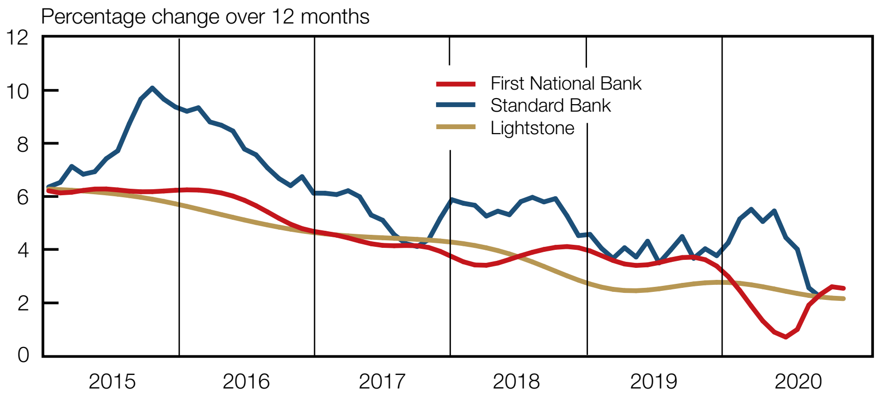
Source: JSE

Real estate market

Growth in domestic residential property prices continued to slow during 2020, as reflected in the year-on-year rates of increase in nominal house prices which varied between 2.2% and 2.6% across the different price indicators in October 2020. The muted growth in residential property prices continued to be a reflection of the protracted period of weak economic growth, high unemployment and constrained growth in household disposable income, which were exacerbated by the effects of the COVID-19 pandemic. Encouragingly, the average time that residential properties remained on the market[22] declined from 14.1 weeks in the second quarter of 2020 to 10.6 weeks in the third quarter – the lowest since the third quarter of 2007. This was largely attributable to the historically low interest rate environment and lower transfer duties, which improved affordability and boosted the demand for lower- to mid-priced properties, as well as a change in housing needs due to the pandemic.

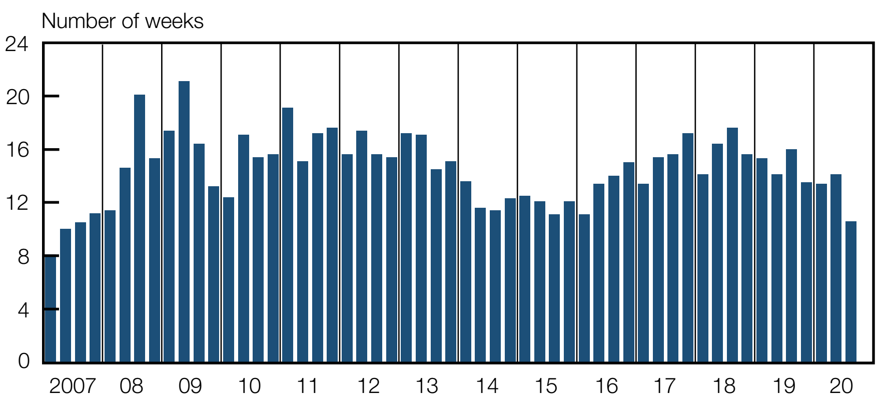
22 From the third quarter of 2020, the First National Bank Home Buying Estate Agent Survey, which shows the average number of weeks that residential properties remained on the market, also includes affordable lower-priced properties valued below R500 000.

Nominal house prices



Sources: First National Bank, Lightstone and Standard Bank

Average time residential properties remain on the market

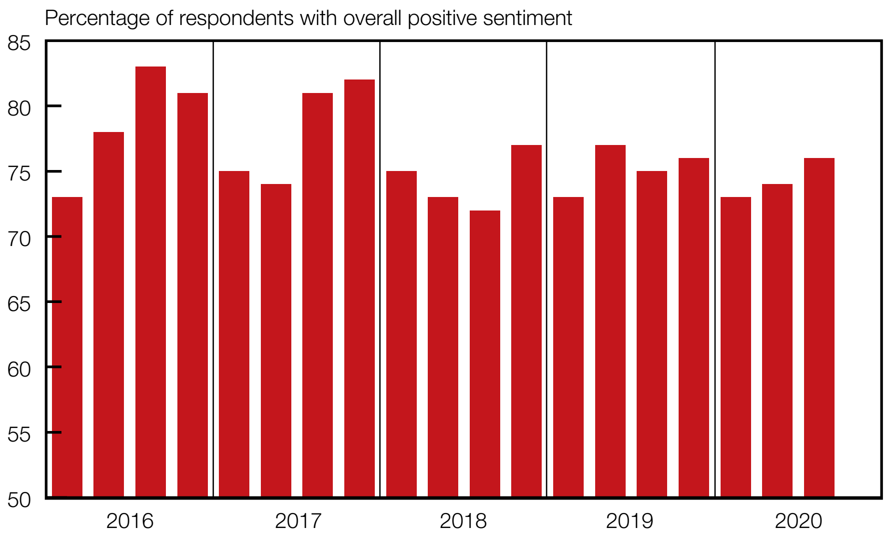


Source: First National Bank

23 The HSI measures consumer sentiment among South Africans with regard to the buying, selling, investing, renting and renovating of residential property as well as property market conditions in general.

Despite the subdued growth in house prices, activity in the residential property market is expected to improve in line with the higher confidence displayed by the Absa Homeowner Sentiment Index (HSI).[23] The HSI increased further from 74% in the second quarter of 2020 to 76% in the third quarter, indicating improved sentiment in the South African property market despite the prevailing weak economic conditions.

Homeowner Sentiment Index for the residential property market



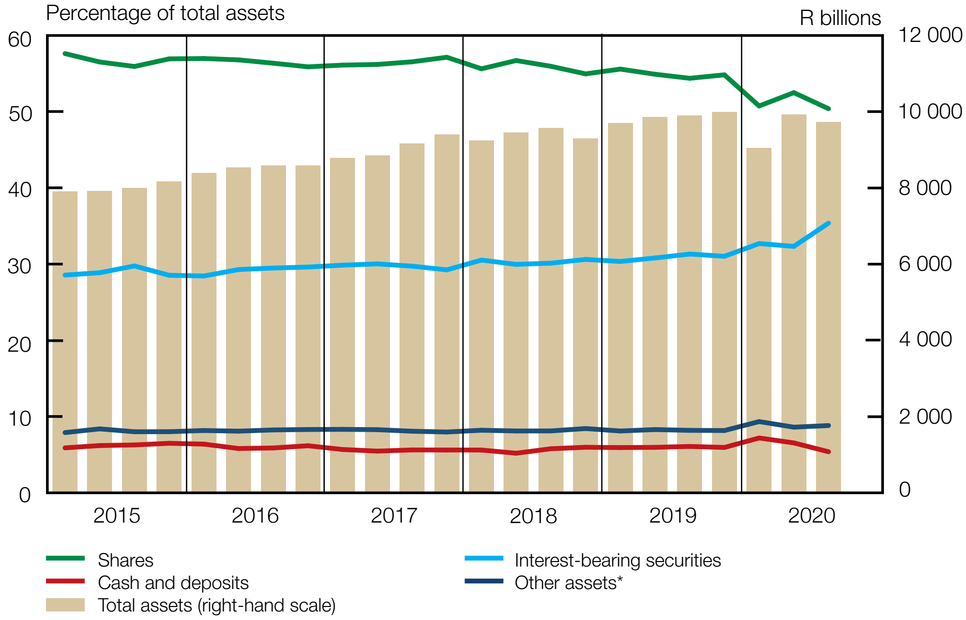
Source: Absa

Non-bank financial intermediaries[24]

The balance sheet of non-bank financial institutions contracted in the third quarter of 2020, in line with the decline in financial asset prices. The consolidated assets of these institutions declined by 2.0% from the second quarter of 2020 to R9.7 trillion in the third quarter. The balance sheets of insurance companies increased marginally by 1.0% over this period. By contrast, the asset base of finance companies and the PIC declined by 1.3% and 0.4% respectively in the third quarter of 2020. On a year-on-year basis, the total assets of non-bank financial institutions declined by 1.7% in the third quarter of 2020.

24 These consist of unit trusts, the Public Investment Corporation, long- and short-term insurance companies, public and private pension funds, participation bond schemes, finance companies and non-monetary public financial corporations.

Total assets of non-bank financial institutions



* Other assets include non-financial assets, accounts receivable, financial derivatives, loans and insurance technical reserves

Source: SARB

Equity holdings fell by 2.1 percentage points from the second quarter of 2020 to 50.4% of total assets in the third quarter. There is some scope for these institutions to reallocate funds to equities, as the current holding is 3.2 percentage points below the 10-year average. The holding of equities by insurers increased slightly by 0.8% from the second quarter of 2020 to the third quarter, while that of the PIC declined. The holding of interest-bearing securities by non-bank financial institutions increased by 3.1 percentage points to 35.4% of total assets in the third quarter of 2020. Relatively high bond yields and muted inflation might encourage the further movement of funds to interest-bearing securities.

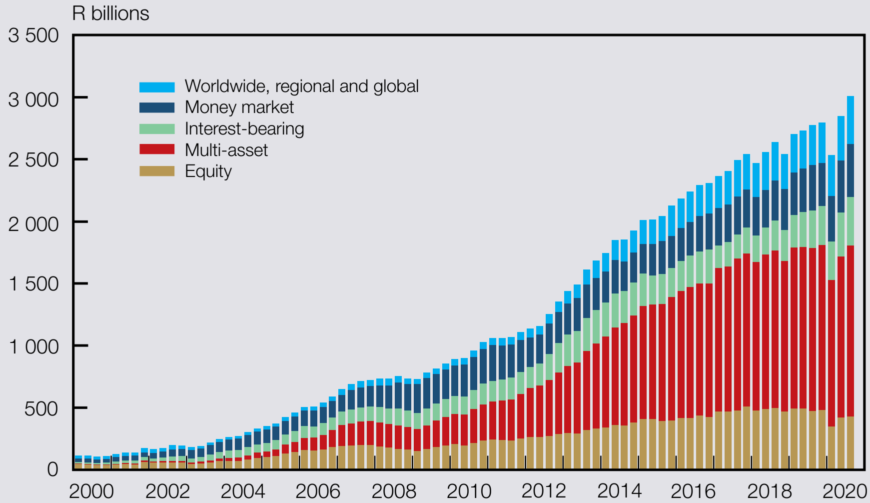
The exposure of non-bank financial institutions to cash and deposits declined in the third quarter of 2020. The holding of cash and deposits as a percentage of total assets declined by 1.2 percentage points from the second quarter of 2020 to 5.4% in the third quarter, against the backdrop of lower interest rates. The value of loans extended by these institutions remained unchanged at 5.0% of total assets over the same period. Consistent with weak consumer demand and reduced creditworthiness, credit extended by finance companies declined by 1.2% from the second quarter of 2020 to the third quarter.

Box 4 Unpacking unit trust statistics[1]

Unit trusts are collective investment schemes[2] which pool investors'[3] funds. Unit trusts can be classified into different types of funds[4] with diverse asset allocation[5] mandates to provide for investors' needs. This box introduces some of the different dimensions of unit trust statistics and highlights some of the broad trends in these statistics.

An analysis of the total assets of unit trusts by type of fund[6] shows the dominance of multi-asset funds, which render well-diversified portfolios, and accounted for 45.9% of total assets in the third quarter of 2020. By contrast, equity funds only accounted for 14.2% of total assets in the third quarter of 2020. The contribution by money market funds averaged 21.8% from the first quarter of 2000 to date, but declined gradually to 14.1% in the third quarter of 2020, while that of interest-bearing funds averaged 14.8% over the same period.

Allocation of total assets by type of unit trust



Source: SARB

The total assets[7] of unit trusts grew from a quarterly average of only R111 billion in 2000 to R2.6 trillion in the third quarter of 2020. The analysis indicates average exposures to equity of 50.7%, interest-bearing securities[8] of 35.9%, and cash and deposits[9] of 12.2% as from the first quarter of 2000 to the third quarter of 2020. Equity holdings peaked at 58% in the fourth quarter of 2015, with declines during both the global financial crisis and the current coronavirus disease 2019 (COVID-19) pandemic.

Foreign assets[10] accounted for 31.5% of total assets at the end of the third quarter of 2020, and domestic intra-industry assets, which are excluded from the above measure of total assets, increased from about R1.5 billion in the final quarter of 2000 to R368 billion in the third quarter of 2020.

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1 This box relates to the statistics of unit trusts on page S–36 in this edition of the *Quarterly Bulletin*, as revised from 1996, with the presentation aligned to the South African Reserve Bank's newly introduced unit trust survey, which expands on financial instruments and institutional sector counterparties.

2 Collective investment schemes were established in terms of the Collective Investment Schemes Control Act 45 of 2002. In addition to unit trusts, collective investment schemes also include participation bond schemes and hedge funds as well as other forms of funds. See https://www.gov.za/documents/collective-investment-schemes-control-act

3 Investors in unit trusts include all institutional sectors. Individuals form part of the household sector, while the financial sector is demarcated into banks and non-bank financial institutions, with the latter including pension funds, insurance companies, trust companies and unit trusts (fund of funds). Non-financial corporations, both public and private, also invest in unit trusts.

4 Unit trusts can broadly be classified as equity funds, multi-asset funds, interest-bearing funds (excluding money market funds), money market funds, worldwide funds, as well as regional and global funds.

5 The broad asset allocation categories are cash and deposits; interest-bearing securities issued by the private, public and foreign sectors; equity; and other assets such as accounts receivable and financial derivatives.

6 Domestic intra-industry assets such as fund of funds are included here in total assets.

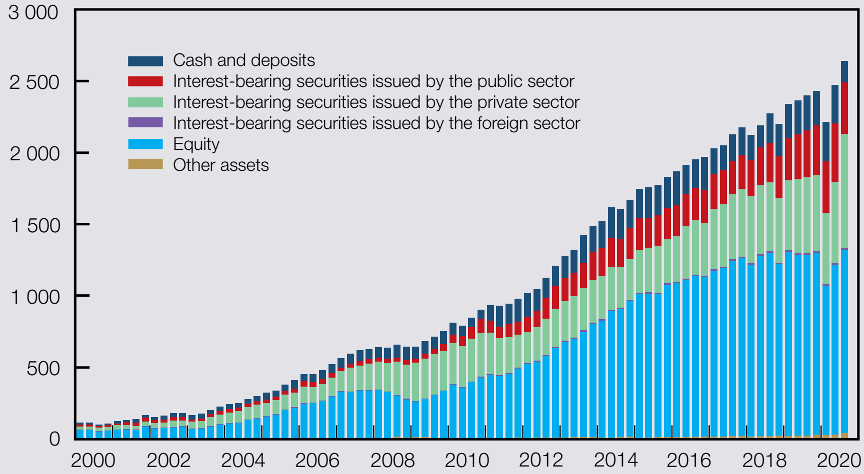
7 Total assets exclude domestic intra-industry assets.

8 Interest-bearing securities include bonds and money market instruments issued by the domestic public sector (national and local governments as well as state-owned companies), the domestic private sector and the foreign sector.

9 Cash and deposits comprise transferable and other deposits with banks.

10 Foreign assets are financial instruments issued by non-residents.

Asset allocation of total assets*



* Total assets, excluding domestic intra-industry assets

Source: SARB

Domestic and foreign assets as at the end of September 2020

R billions

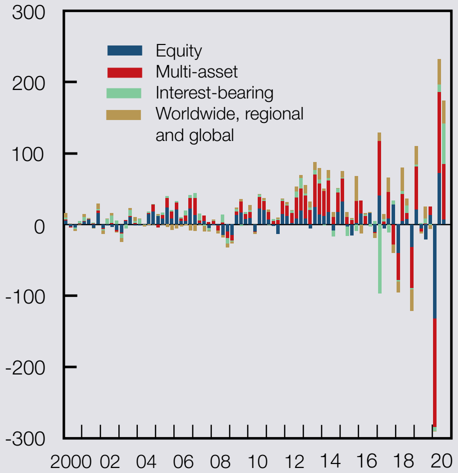
Financial asset	Domestic issuers	Foreign issuers
Cash and deposits	115	34
Interest-bearing securities	1 155	17
Equity	497	777*
Other assets	42	2

* Foreign equity includes secondary listings on the JSE Limited

Source: SARB

Revaluations[11] indicated that the changes in the prices of underlying financial assets contributed substantially to the growth in the total assets of unit trusts. According to this calculation, revaluations accounted for R1.5 trillion of the current outstanding value of total assets of R3.0 trillion. It is also evident how price movements in the underlying assets affect flows to unit trusts and asset classes with different lags.

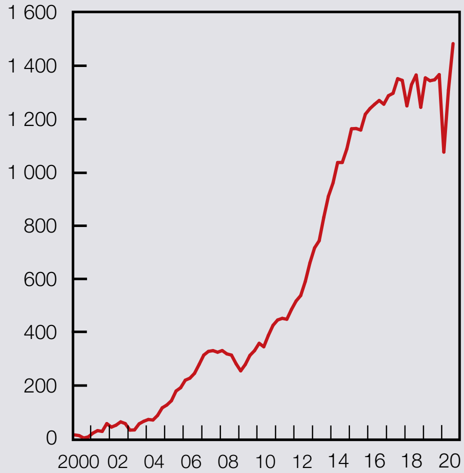
Revaluations* per type of unit trust



* Revaluations calculated as the change in total assets minus net flows

Source: SARB

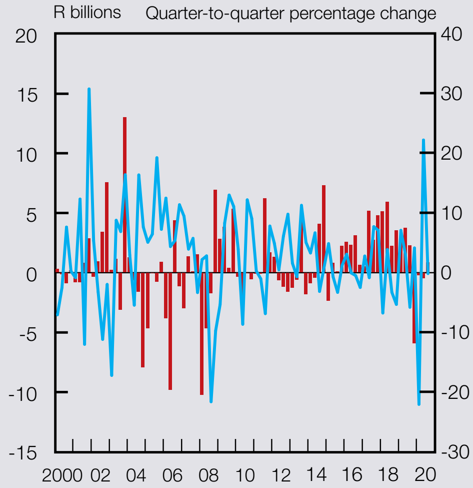
Cumulative revaluations*



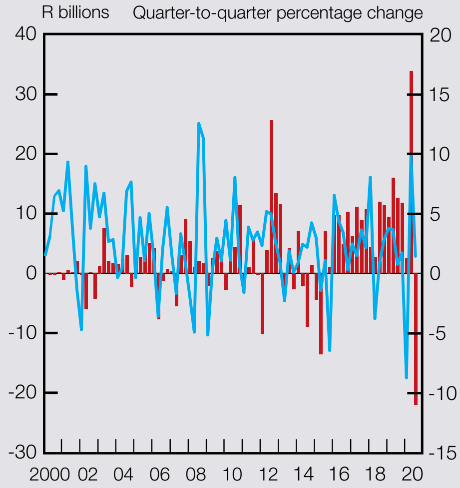
* Excluding money market funds

11 Revaluations are calculated as the change in total assets minus net flows.

Net equity flows and movements in equity prices



Net interest-bearing security flows and movements in bond prices



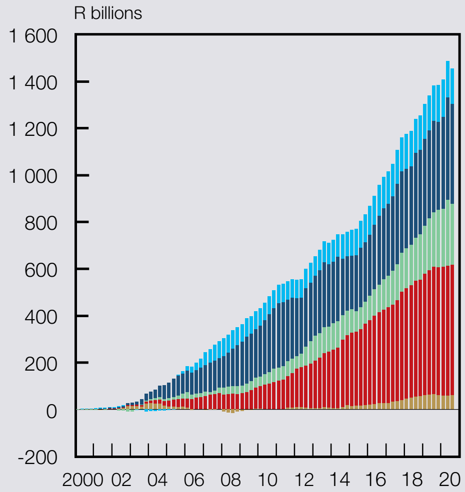
Net equity flows
All-Share Price Index (right-hand scale)

Net interest-bearing security flows
All Bond Index (right-hand scale)

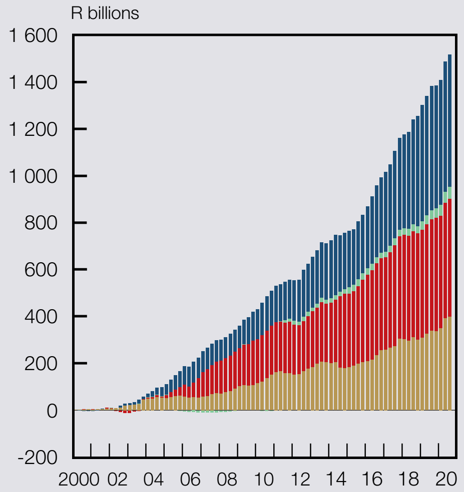
Sources: JSE and SARB

The cumulative net flows per type of unit trust clearly show a preference for multi-asset funds and an increase in flows to funds that invest in interest-bearing securities as well as to money market funds. It is also evident that, in terms of net flows from investors, non-bank financial institutions currently dominate, followed by companies in the 'other' category[12] and households.

Cumulative net flows by type of unit trust



Cumulative net flows by investors' institutional sector



Equity
Interest-bearing
Worldwide, regional and global
Multi-asset
Money market

Households
Banks
Other
Non-bank financial institutions

Source: SARB

These net flows combined with revaluations render the different institutional sector holdings of net assets[13] in unit trusts. The household sector dominated the investor universe in 2000 but the investor landscape has subsequently changed, and in the third quarter of 2020 non-bank financial institutions accounted for 70.2% of net assets followed by households at 22.1%, with the remaining sectors accounting for 7.7%.

12 The 'other' category includes private and public non-financial corporations, local government and non-residents.

13 Net assets equal total assets, including domestic intra-industry assets, minus total liabilities, such as financial derivatives and distributable income.

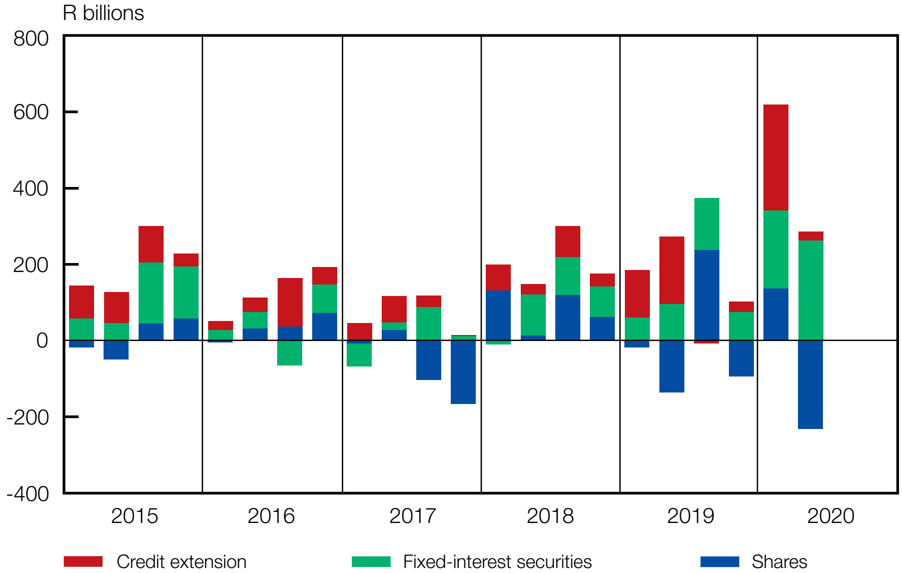
Flow of funds

The global economy recovered partially in the second quarter of 2020 after grinding to a near halt in the first quarter, as most countries imposed restrictions on social and economic activity to curb the spread of COVID-19. South Africa's net borrowing from the *rest of the world* of R13.4 billion in the second quarter of 2020 was slightly more than the R8.1 billion in the first quarter. Net flows through deposits with the domestic banking sector reverted from an inflow of R44.0 billion in the first quarter of 2020 to an outflow of R29.0 billion in the second quarter due to the repatriation of deposits by foreigners. Non-residents' net sales of long-term government bonds of R43.5 billion (including the redemption of foreign securities of R7.6 billion) in the second quarter of 2020 reflected the further deterioration of the domestic fiscal position and South Africa's subsequent exclusion from the World Government Bond Index. Net purchases of domestic shares by non-residents of R4.0 billion in the first quarter of 2020 reverted to net sales of R11.1 billion in the second quarter. Loans extended to the domestic sector, mainly private non-financial corporate business enterprises, increased by R44.2 billion in the second quarter, whereas the domestic banking sector repaid loans. South Africa's gold and foreign reserves declined by R42.2 billion and R22.1 billion in the first and second quarter of 2020 respectively.

Financial intermediation[25] flows decreased in the second quarter of 2020 along with the unprecedented contraction in economic activity. Net purchases of fixed-interest securities by financial intermediaries, mostly non-bank financial institutions, amounted to R263 billion in the second quarter of 2020 compared with R204 billion in the first quarter. Intermediation through shares reverted from net purchases of R137 billion in the first quarter of 2020 to net sales of R231 billion in the second quarter. The extension of bank loans and advances switched from an increase of R199 billion to a decline of R35.4 billion over the same period. However, mortgage loans increased by R6.7 billion in the second quarter, with most extended to private non-financial corporate business enterprises. The general concern about the spread of COVID-19 as well as the loss of income and earnings hampered the creditworthiness of both households and non-financial corporate business enterprises. In the second quarter of 2020, banks sourced funds through deposits of R158 billion, insurers and retirement funds through interest in retirement and life funds of R43.0 billion, and other financial institutions sourced R72.2 billion mainly through the sale of units in collective investment schemes.

25 Financial intermediaries comprise the monetary authority, banks and non-bank financial institutions (excluding the PIC).

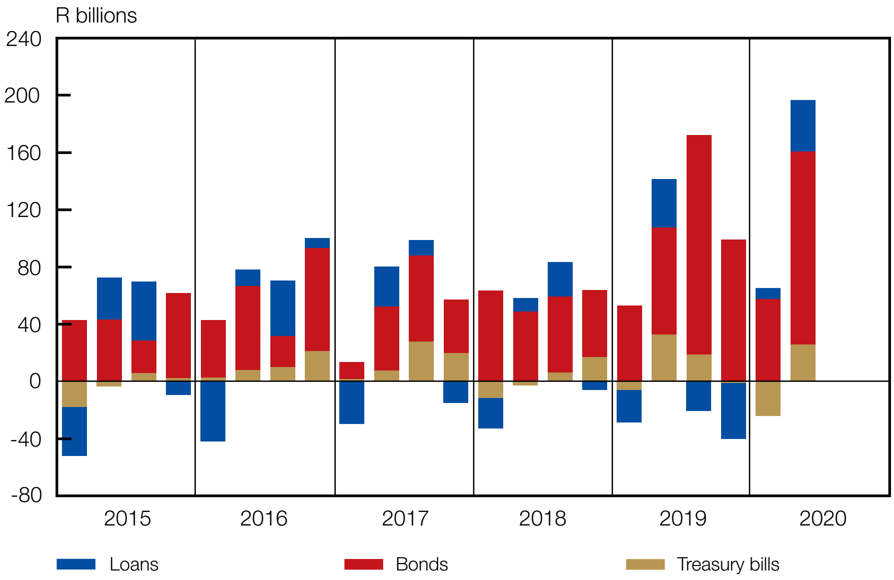
Net acquisition of financial assets through selected instruments by financial intermediaries



Source: SARB

The *Supplementary Budget Review* released in June 2020 highlighted, among other things, the need for sizeable loans from various international financial institutions to enable the fiscal response to the COVID-19 pandemic. Government also indicated that it would continue to raise funds in the domestic financial market amid much lower revenue collection due to the marked contraction in economic activity which had eroded the tax base. *General government's* net borrowing requirement, which increased sharply from R94.4 billion in the first quarter of 2020 to R143 billion in the second quarter, was mainly financed in the domestic financial markets through considerable net issuances of R135 billion in bonds and R25.6 billion in TBs. The banking sector was the counterparty to R37.6 billion of the TB issuances. In addition, the government sector sourced R36.0 billion through loans, mainly from the CPD, while deposit holdings increased by R81.1 billion in the second quarter of 2020.

General government's main sources of funding



Source: SARB

Capital spending by *non-financial corporate business enterprises* declined by 12.4% from the first quarter of 2020 to the second quarter, and net issuances of securities by public sector non-financial corporations amounted to only R2.8 billion – mostly held by banks. Non-financial corporate business enterprises increased their deposit holdings by only R15.5 billion as business activity was severely constrained by the lockdown regulations in the second quarter of 2020. Gross saving by non-financial corporate business enterprises declined and their financial surplus receded to R38.1 billion over the period. In addition, credit extended to non-financial corporate business enterprises increased by R97.6 billion in the second quarter of 2020, mainly from the foreign sector, as these enterprises reduced their demand for credit from domestic banks.

The sharp contraction in economic activity due to the COVID-19 lockdown adversely affected the *household sector's* finances in the second quarter of 2020. The total compensation of employees fell sharply due to job losses, while some employees had to accept a reduction in remuneration as the earnings of businesses came under severe pressure. Despite the easing of lockdown restrictions, with some retail outlets resuming operations in the second quarter of 2020, households were reluctant to spend or to incur more debt, which resulted in increased savings and a net surplus position of R56.1 billion. The surplus funds were channelled to deposits of R60.3 billion, up from R31.9 billion in the first quarter. However, contributions to retirement and life funds of R54.3 billion in the first quarter of 2020 decreased to R20.7 billion in the second quarter due to the implementation of relief measures, which included the suspension of pension contributions to mitigate the impact of the pandemic. Despite the interest rate reductions in the second quarter of 2020, households were reluctant to borrow given the highly uncertain economic environment, with loans incurred by this sector declining by R62.1 billion.

Public finance[26]

Non-financial public sector borrowing requirement[27]

The *non-financial public sector borrowing requirement* increased significantly by 100% year on year to R369 billion in the first six months (April–September 2020) of fiscal 2020/21. This reflected the significantly larger borrowing requirement of the consolidated general government, owing to the higher deficits of national government and the social security funds. The larger deficit of national government could be attributed to higher intergovernmental transfers to other levels of general government of R484 billion (53.2% of total expenditure) over the period. Following the COVID-19 relief measures, the cash balances of social security funds switched from a surplus in the first six months of fiscal 2019/20 to a deficit of R40.8 billion in the first six months of fiscal 2020/21. All other spheres of general government recorded cash surpluses in the period under review. Non-financial public enterprises and corporations, or state-owned companies (SOCs), recorded a lower deficit over the same period.

26 Unless stated to the contrary, the year-on-year rates of increase in this section compare April–September 2020 to April–September 2019. Data for both periods are unaudited and preliminary.

27 The non-financial public sector borrowing requirement is calculated as the cash deficit/surplus of the consolidated general government as well as non-financial public enterprises and corporations.

Non-financial public sector borrowing requirement

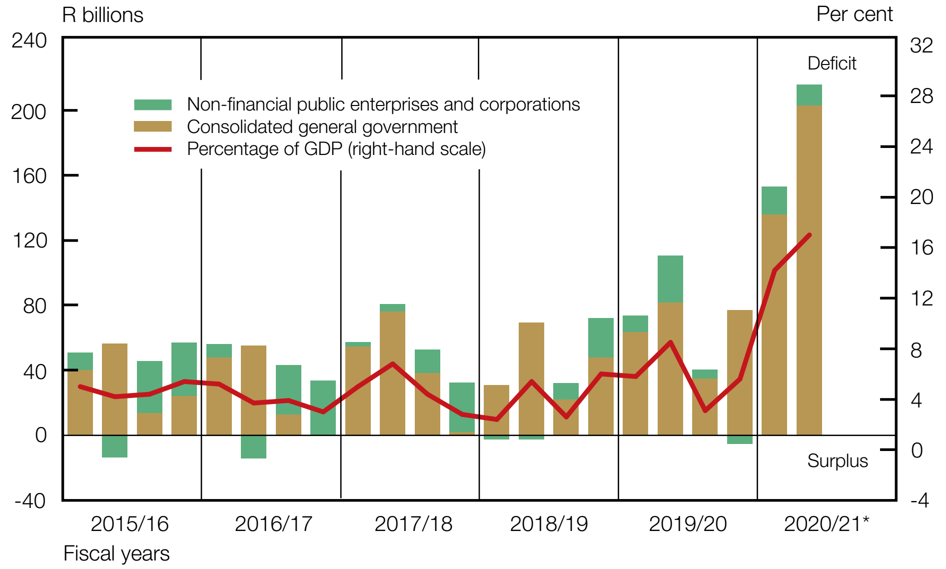
R billions

Level of government	Apr–Sep 2019*	Apr–Sep 2020*
Consolidated general government	145.2	338.8
National government	196.8	370.8
Extra-budgetary institutions	-20.0	-33.8
Social security funds	-15.0	40.8
Provincial governments	-15.2	-29.7
Local governments	-1.4	-9.4
Non-financial public enterprises and corporations	39.1	30.2
Total**	**184.3**	**368.9**
As a percentage of gross domestic product	*7.2*	*15.7*

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

Sources: National Treasury, Stats SA and SARB

Non-financial public sector borrowing requirement

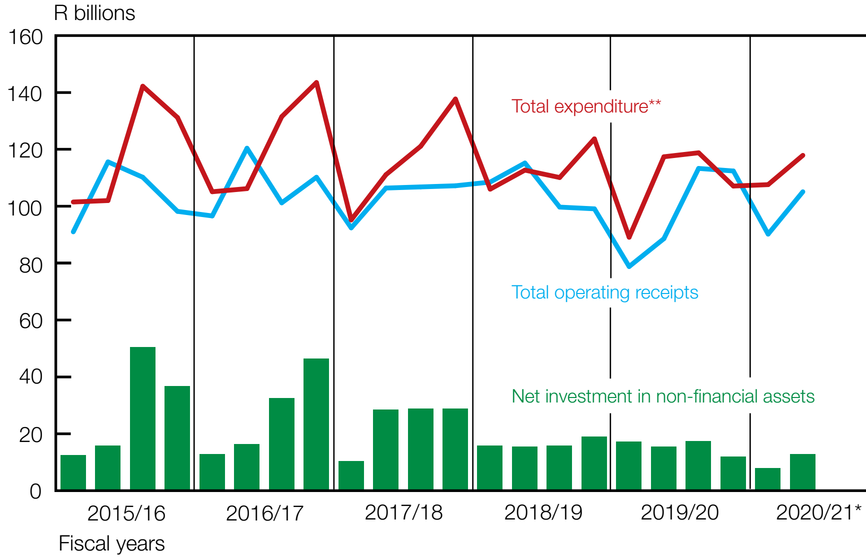


* April–September 2020

Sources: National Treasury, Stats SA and SARB

The preliminary cash deficit of the *non-financial SOCs* of R30.2 billion in the first six months of fiscal 2020/21 was R8.9 billion less than in the same period of the previous fiscal year. Over this period, total cash receipts from operating activities increased by 16.7% to R195 billion, while total expenditure, inclusive of both operating cash payments and net investment in non-financial assets, rose by 9.2% to R225 billion. The increase in total expenditure reflected higher current expenditure, with interest payments being one of the main drivers. By contrast, net investment in non-financial assets contracted during the period under review, marked by a contraction in infrastructure spending by major non-financial SOCs amid constrained borrowing capacity and COVID-19 challenges.

Financial activities of non-financial public enterprises and corporations



* April–September 2020
** Including both operating cash payments and investment in non-financial assets
Source: SARB

The non-financial public sector borrowing requirement as a ratio of GDP increased notably to 15.7% in the first six months of fiscal 2020/21 from 7.2% in the same period of the previous fiscal year. This was largely due to the contraction in nominal GDP on account of the national lockdown.

Box 5 The *2020 Medium Term Budget Policy Statement*[1]

The *2020 Medium Term Budget Policy Statement (2020 MTBPS)* sets out government's strategy for economic recovery and fiscal consolidation amid the impact of the coronavirus disease (COVID-19) pandemic and the related nationwide lockdown on domestic economic activity and public finances. The expected outcomes of the *2020 MTBPS* are accelerated broad-based economic growth and a return to fiscal sustainability through the narrowing of the budget deficit, stabilising debt to gross domestic product (GDP), and realigning the composition of spending from consumption to investment, which will be achieved with the support from structural reforms.

Amid significant uncertainty, the *2020 MTBPS* revised annual growth in real GDP for the current year to an even larger contraction of 7.8% compared to 7.2% projected in the *2020 Supplementary Budget Review*. These expected sharp contractions contrast projected growth of 0.9% in the *2020 Budget Review*, and South Africa is now expected to only return to an expansion in real GDP in 2021. Although consumer price inflation (CPI) is currently close to the lower end of the 3–6% target range, it is expected to fluctuate around the 4.5% midpoint over the medium term, given the moderation of inflation expectations.

The impact of the COVID-19 pandemic and government's response are clearly visible in the macroeconomic projections of both the *2020 Supplementary Budget Review* and the subsequent *2020 MTBPS*.

Macroeconomic projections[1, 2]

Percentage

	2019[3]	2020			2021			2022			2023	
	Outcome	Medium-term estimates[4]										
	MTBPS	Budget	Supplementary Budget	*MTBPS*	Budget	Supplementary Budget	*MTBPS*	Budget	Supplementary Budget	*MTBPS*	Supplementary Budget	*MTBPS*
Real GDP growth	0.2	0.9	-7.2	-7.8	1.3	2.6	3.3	1.6	1.5	1.7	1.5	1.5
CPI	4.1	4.5	3.0	3.2	4.6	3.9	4.1	4.6	4.3	4.4	4.5	4.5
Current account balance (as a percentage of GDP)	-3.0	-3.4	…	-0.8	-3.5	…	-1.6	-3.7	…	-2.0	…	-2.7
GDP at current prices (R billions)	5 078	5 359	4 900	4 885	5 676	5 228	5 240	6 035	5 536	5 553	5 873	5 877

1 Projections of the *2020 Budget Review, 2020 Supplementary Budget Review* and *2020 Medium Term Budget Policy Statement*
2 Calendar years
3 *2020 MTBPS*
4 *2020 Budget Review, 2020 Supplementary Budget Review* and *2020 MTBPS*
… denotes not available

Source: National Treasury

These revised macroeconomic projections are subject to significant risks given the backdrop of high and rising debt-service costs, much lower public infrastructure investment spending, and the deterioration of the public sector's balance sheet as state-owned companies (SOCs) and municipalities continue to struggle financially. These developments informed the review of the fiscal framework which hinges on a reduction in government's wage bill and the revenue proposals.

1 The *2020 Medium Term Budget Policy Statement (2020 MTBPS)* was presented to Parliament by the Minister of Finance on 28 October 2020.

Fiscal framework*

R billions/percentage of GDP

	2019/20**	2020/21		2021/22		2022/23		2023/24
	Outcome	Medium-term estimates***						
		Budget	*MTBPS*	Budget	*MTBPS*	Budget	*MTBPS*	*MTBPS*
Total consolidated revenue	1 518	1 584	1 277	1 683	1 458	1 791	1 596	1 706
Total consolidated expenditure	1 849	1 954	2 038	2 040	1 994	2 141	2 080	2 139
Of which: Debt-service cost	204.8	229.3	233.0	258.5	271.8	290.1	317.6	353.1
*Primary deficit*****	*-140.3*	*-138.7*	*-474.8*	*-107.9*	*-265.7*	*-69.2*	*-169.0*	*-84.4*
Percentage of GDP	*-2.7*	*-2.6*	*-9.8*	*-1.9*	*-5.0*	*-1.1*	*-3.0*	*-1.4*
Consolidated budget deficit (fiscal balance)...............................	-330.6	-370.5	-761.1	-357.5	-535.9	-349.7	-483.9	-433.4
Percentage of GDP	*-6.4*	*-6.8*	*-15.7*	*-6.2*	*-10.1*	*-5.7*	*-8.6*	*-7.3*
Gross loan debt (national government)	*3 261*	*3 562*	*3 974*	*3 978*	*4 552*	*4 384*	*5 071*	*5 536*
Percentage of GDP	*63.3*	*65.6*	*81.8*	*69.1*	*85.6*	*71.6*	*90.1*	*92.9*

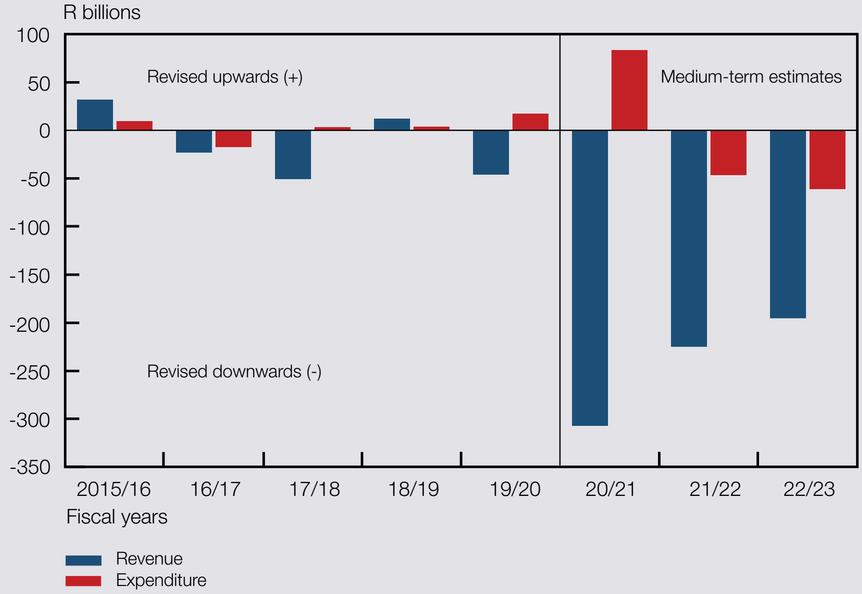
* Fiscal years
** *2020 MTBPS*
*** *2020 Budget Review* and *2020 MTBPS*
**** Main Budget

Source: National Treasury

The *2020 MTBPS* projected consolidated government revenue to be 19.4% less at R1 277 billion in fiscal 2020/21 compared with the February 2020 Budget. This contraction in revenue reflects the revised economic growth projections and expected underperformance of all major tax categories. The estimated gross tax revenue for fiscal 2020/21 of R1 113 billion is R8.7 billion less than projected in the *2020 Supplementary Budget Review,* and R313 billion less than the February 2020 Budget. Revenue proposals, such as tax increases as well as improved tax collection and administration, are vital to deliver the expected revenue of R1 706 billion in fiscal 2023/34, amid the effect of the decline in remuneration on personal income tax and that of lower consumption on value-added tax and import duties.

Revisions to consolidated government revenue and expenditure*

R billions



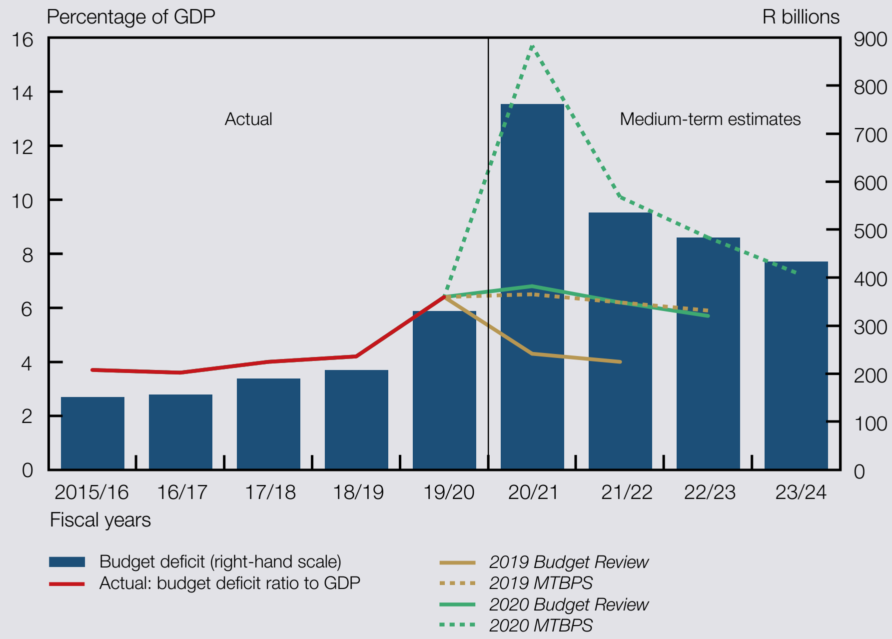
* Budget Review to MTBPS

Source: National Treasury

The projected consolidated government expenditure of R1 954 billion for fiscal 2020/21 in the *2020 Budget Review* was revised higher to R2 038 billion in the *2020 MTBPS*. Expenditure was revised lower in the subsequent two fiscal years, in line with government's commitment to narrowing the fiscal deficit to stabilise debt.

The *2020 MTBPS'* consolidated government budget deficit of 15.7% of GDP for fiscal 2020/21 is significantly higher than the original 6.8% projected in the *2020 Budget Review*, but is expected to decline to 7.3% over the medium term.

Consolidated government budget deficit



Source: National Treasury

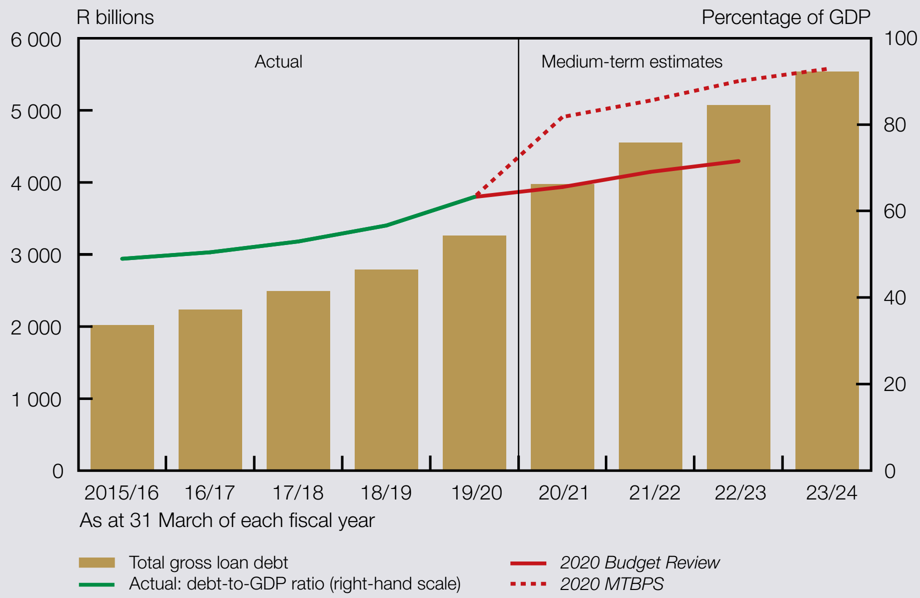
Fiscal sustainability requires the *2020 MTBPS* to achieve a primary surplus by fiscal 2025/26. This will necessitate a large reduction in non-interest spending of R300 billion over the next three years, most of which will have to come from the wage bill, with the share of compensation of employees to total spending decreasing from 32.7% as estimated in the *2020 Budget Review* to 31.3% over the medium term. Also, consistent with the aim of shifting spending from consumption to investment, payments for capital assets are expected to grow by more than inflation, increasing from R88.9 billion in fiscal 2020/21 to R112 billion in fiscal 2023/24, at an annual average rate of 7.8%.

Debt-service cost is the fastest growing component of spending, given the increase in national government debt. Interest payments are expected to increase from R233 billion (12.9% of total expenditure) in the current fiscal year to R353 billion (18.3% of expenditure) in fiscal 2023/24, or 5.9% of GDP.

The gross borrowing requirement – the sum of the budget deficit and maturing loans – increased by R342 billion to R775 billion for fiscal 2020/21 compared to the February 2020 Budget. Government revised its financing strategy, as outlined in the *2020 Supplementary Budget Review*, and will now access its sterilisation and foreign currency deposits at the South African Reserve Bank and obtain loans from international finance institutions, while continuing to increase its borrowing in the domestic money and bond markets.

National government's gross loan debt, which was originally projected at R3 562 billion (65.6% of GDP) for fiscal 2020/21 in the *2020 Budget Review*, was revised higher to R3 974 billion (81.8% of GDP) in June, and remained unchanged in the *2020 MTBPS.* However, gross loan debt is expected to increase to R5 536 billion (92.9% of GDP) in fiscal 2023/24, before stabilising at 95.3% of GDP in 2025/26.

National government gross loan debt



Source: National Treasury

The fiscal framework projections remain at risk from contingent liabilities related to SOCs, uncertainty about the domestic economic recovery, a possible second wave of COVID-19 infections as well as the implementation of expenditure reduction measures, in particular the wage bill.

Budget comparable analysis of national government finance

National government expenditure continued to increase while revenue contracted, resulting in a R177 billion year-on-year increase in the cash book deficit to R367 billion in the first six months of fiscal 2020/21 (April–September 2020). The significantly larger cash book deficit was mainly financed in the domestic financial markets through the net issuance of TBs and government bonds, which contributed to a further increase in national government's gross loan debt to R3 714 billion as at 30 September 2020.

National government revenue contracted by a sizeable 18.7% year on year to R510 billion in April–September 2020, as revenue collection of all tax categories decreased. The underperformance in revenue continued to mirror, among other things, the adverse effects of the COVID-19 lockdown that was imposed in an already weak economy. Revenue at 21.7% of GDP in April–September 2020 was lower than the 24.5% recorded in the same period a year earlier. The February 2020 Budget projected national government revenue of R1 398 billion for fiscal 2020/21 as a whole. In June, this was revised lower to R1 100 billion in the *2020 Supplementary Budget Review* and in October it was revised slightly further down to R1 098 billion in the *2020 MTBPS.*

National government finances

	Actual Apr–Sep 2019		Actual Apr–Sep 2020		Originally budgeted[1] Fiscal 2020/21		Revised estimates			
							Fiscal 2020/21[2]		Fiscal 2020/21[3]	
	R billions	Percentage change[4]	R billions	Percentage change[4]	R billions	Percentage change[5]	R billions	Percentage change[6]	R billions	Percentage change[6]
Revenue	627	4.5	510	-18.7	1 398	4.1	1 100	-18.2	1 098	-18.3
Percentage of GDP ...	*24.5*		21.7		*25.8*		22.6		22.6	
Expenditure	817	12.2	877	7.3	1 766	4.5	1 809	7.0	1 806	6.9
Percentage of GDP ...	*32.0*		37.4		*32.5*		*37.2*		37.2	
Cash book balance[7] ...	-190		-367		-368		-710		-708	
Percentage of GDP ...	-7.4		-15.6		*-6.8*		*-14.6*		-14.6	
Primary balance[8]	-90.6		-251		-139		-473		*-475*	
Percentage of GDP ...	-3.5		-10.7		*-2.6*		*-9.7*		-9.8	
Gross loan debt[9].........	3 087	14.3	3 714	20.3	3 562	9.2	3 974	21.9	3 974	21.9
Percentage of GDP ...	61.4		75.2		65.6		81.8		81.8	

1 *2020 Budget Review*
2 *2020 Supplementary Budget Review*
3 *2020 MTBPS*
4 Year-on-year percentage change: actual outcome on previous year's actual outcome
5 Year-on-year percentage change: budgeted on previous year's actual outcome
6 Year-on-year percentage change: revised estimates on previous year's actual outcome
7 Cash book deficit – surplus +
8 Cash book deficit – surplus + (excluding interest payments)
9 As at 30 September for rand values

Sources: National Treasury, SARS and Stats SA

Revenue from taxes on income, profits and capital gains contracted by 15.8% year on year to R308 billion (60.3% of total revenue) in April–September 2020. This contraction resulted mainly from lower personal income tax (PIT) collections of R219 billion and corporate income tax (CIT) collections of R76.9 billion, which declined by 12.0% and 24.8% respectively. The underperformance in PIT occurred primarily on account of lower pay-as-you-earn (PAYE) receipts following significant job losses. The significant contraction in CIT resulted mostly from lower provisional payments, particularly from the finance, manufacturing as well as the wholesale and retail trade sectors as a result of the COVID-19 lockdown measures. The February 2020 Budget's projected revenue from taxes on income, profits and capital gains of R814 billion for fiscal 2020/21 as a whole was revised lower to R631 billion in the *2020 Supplementary Budget Review.*

In the first six months of fiscal 2020/21, revenue from taxes on goods and services of R182 billion (35.7% of total revenue) contracted by a significant 20.4% year on year. This was mainly on account of year-on-year declines in excise duties, the general fuel levy and net value-added tax (VAT) receipts, which declined by 64.4%, 16.3% and 15.0% respectively over the period. Lower revenue collections in this tax category reflected tax relief deferrals and a decline in the sales of goods and services along with subdued consumer demand, as well as the prohibition of trade related to alcoholic beverages and tobacco, which was subsequently relaxed under Level 1[28] of the COVID-19 lockdown restrictions. The February 2020 Budget's projected revenue from taxes on goods and services of R514 billion for fiscal 2020/21 as a whole was revised lower to R417 billion in the *2020 Supplementary Budget Review*.

28 Most activities were allowed to resume as from 21 September 2020, given that precautions and health guidelines were followed at all times.

National government revenue in fiscal 2020/21[1]

Revenue source	Originally budgeted[2] Fiscal 2020/21		Revised estimates[3] Fiscal 2020/21		Actual Apr–Sep 2020	
	R billions	Percentage change[4]	R billions	Percentage change[5]	R billions	Percentage change[6]
Taxes on income, profits and capital gains	813.6	5.3	631.4	-18.3	307.7	-15.8
Of which: Income tax on individuals	546.8	3.3	455.5	-13.9	219.3	-12.0
Income tax on companies	230.2	7.1	154.6	-28.1	76.9	-24.8
Payroll taxes	19.4	5.0	11.3	-38.9	2.9	-66.7
Taxes on property..	17.5	9.6	14.2	-11.2	7.1	-4.2
Taxes on goods and services	514.0	4.5	417.4	-15.2	182.0	-20.4
Of which: Value-added tax (VAT) net	360.6	4.0	301.3	-13.1	136.4	-15.0
Domestic	421.7	5.6	360.5	-9.7	182.1	-6.7
Imports	193.0	7.2	149.8	-16.7	64.4	-22.6
Refunds................................	-254.1	9.3	-209.0	-10.1	-110.0	-6.7
General fuel levy.........................	85.2	6.3	64.9	-19.0	32.3	-16.3
Excise duties..............................	56.0	4.9	41.6	-22.1	8.4	-64.4
Taxes on international trade and transactions.	60.6	7.7	46.9	-16.7	18.8	-26.0
Of which: Import duties	59.5	7.2	45.8	-17.4	17.7	-29.0
Other revenue[7]	36.2	-5.5	41.7	9.0	23.3	38.2
Less: SACU[8] payments	63.4	26.1	63.4	26.1	31.7	26.1
Total revenue	1 398.0	4.1	1 100.0	-18.2	510.1	-18.7

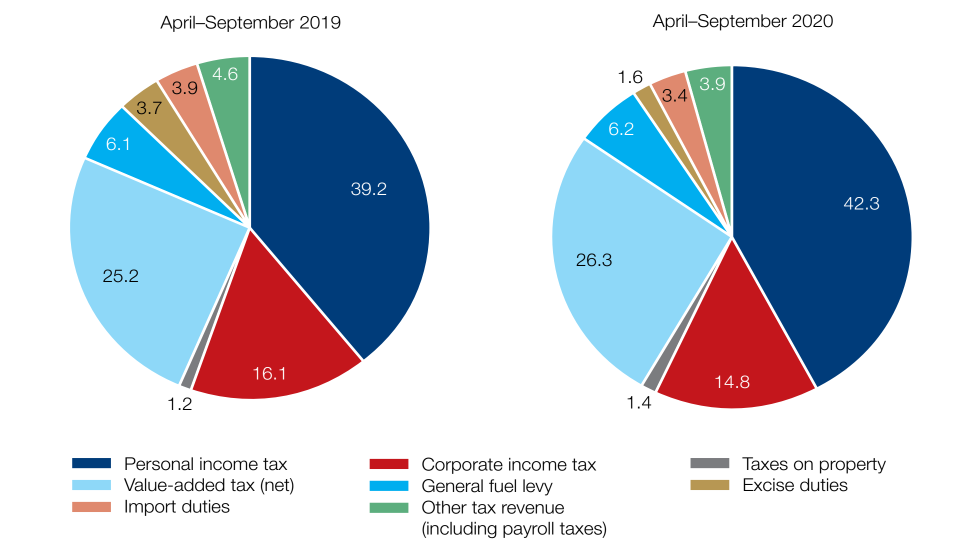
1 Components may not add up to totals due to rounding off and the exclusion of unclassified items.
2 *2020 Budget Review*
3 *2020 Supplementary Budget Review*
4 Year-on-year percentage change: budgeted on previous year's actual outcome
5 Year-on-year percentage change: revised estimates on previous year's actual outcome
6 Year-on-year percentage change: actual outcome on previous year's actual outcome
7 Including non-tax revenue and extraordinary receipts
8 Southern African Customs Union

Sources: National Treasury and SARS

Income from taxes on international trade and transactions decreased sharply by 26.0% year on year to R18.8 billion in the first half of fiscal 2020/21. This resulted mainly from a notable contraction in the imports of key contributing products, such as vehicles as well as electrical and other machinery, as COVID-19 regulations severely constrained international trade.

Composition of national government tax revenue

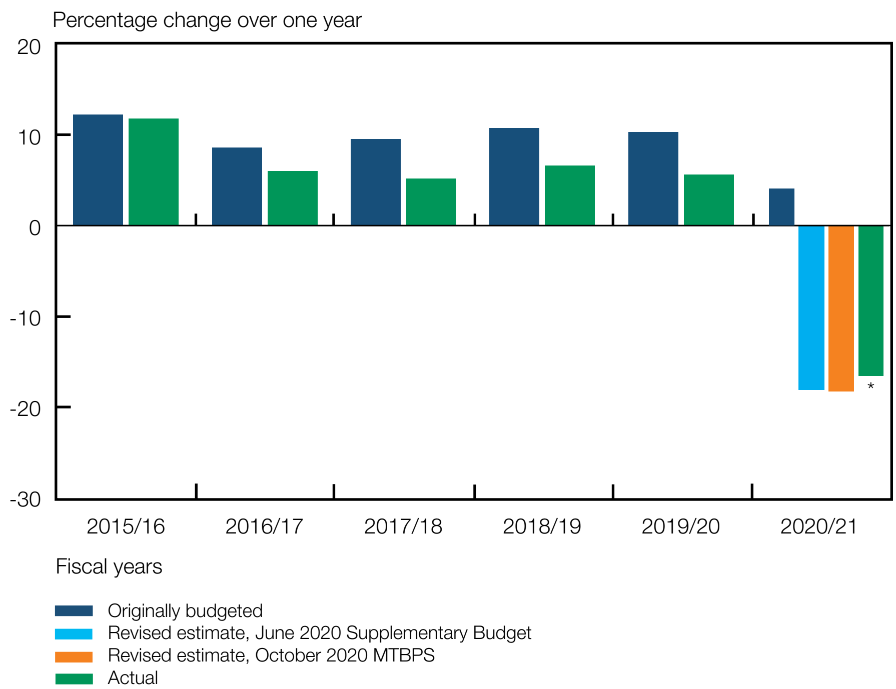
Per cent



Source: SARS

Other revenue, which includes non-tax revenue and extraordinary receipts, increased significantly by 38.2% year on year to R23.3 billion in the first six months of fiscal 2020/21. The February 2020 Budget had earmarked R63.4 billion as transfers to the Southern African Customs Union (SACU) for fiscal 2020/21 as a whole. Of this amount, R31.7 billion was transferred in two equal instalments in April and July 2020.

Revenue of national government



* April–October 2020

Sources: National Treasury, SARS and SARB

In the first seven months of fiscal 2020/21, total revenue collected contracted by 16.6% year on year to R593 billion as all tax categories continued to underperform following the prolonged weakness in economic activity amid the global COVID-19 pandemic.

National government expenditure increased by 7.3% year on year to R877 billion in April–September 2020, largely reflecting higher voted expenditure, interest payments on government debt (debt-service cost) as well as equitable share transfers to provinces. As a ratio of GDP, national government expenditure of 37.4% in April–September 2020 was higher than the 32.0% recorded in the same period a year earlier. Total expenditure of R1 766 billion for fiscal 2020/21 was originally envisaged in the February 2020 Budget, but was subsequently revised upwards to R1 809 billion in the *2020 Supplementary Budget Review* and R1 806 billion in the *2020 MTBPS,* largely on account of COVID-19-related stimulus measures.

Total voted expenditure by national government departments of R480 billion (54.8% of total expenditure) – comprising transfers and subsidies, current payments, and payments for capital and financial assets – increased by 6.8% year on year. Transfers and subsidies of R343 billion increased notably by 10.5% year on year, representing increased transfers to the departments of Social Development, Higher Education and Training, Cooperative Governance, Transport and Health, among others. By contrast, current payments contracted marginally by 0.5% year on year to R113 billion. Payments for financial assets of R20.1 billion in the first half of fiscal 2020/21 included the recapitalisation of some SOCs, such as South African Airways (R10.2 billion), Eskom (R6.0 billion) and the Land and Agricultural Development Bank of South Africa (R3.0 billion).

National government expenditure in fiscal 2020/21[1]

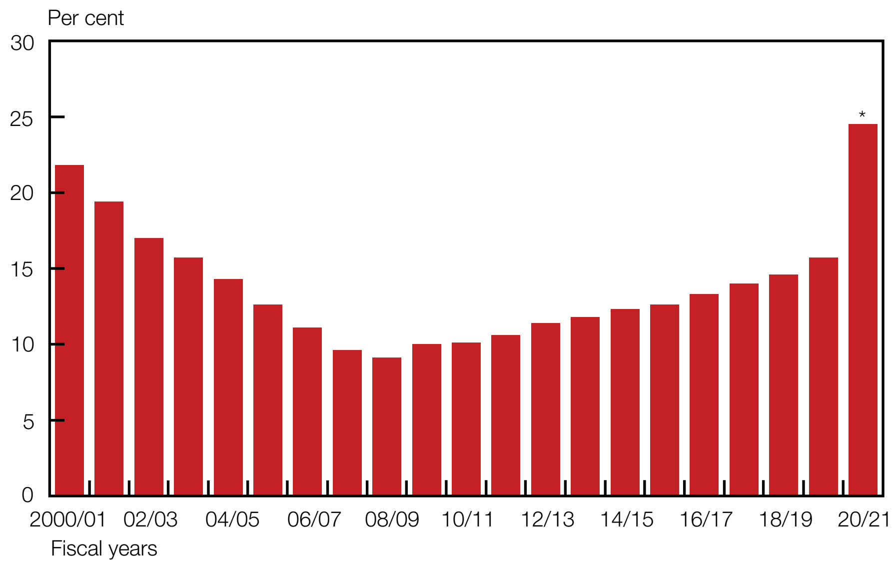
Expenditure item	Originally budgeted[2] Fiscal 2020/21		Revised estimates[3] Fiscal 2020/21		Actual Apr–Sep 2020	
	R billions	Percentage change[4]	R billions	Percentage change[5]	R billions	Percentage change[6]
Voted expenditure	963.1	2.0	987.7	4.6	480.2	6.8
Of which: Transfers and subsidies	644.0	2.8	663.9	6.0	343.3	10.5
Current payments	261.3	8.3	262.8	8.9	113.3	-0.5
Payments for capital assets	15.3	30.8	15.5	32.3	3.5	-10.7
Payments for financial assets	42.5	-33.9	45.5	-29.2	20.1	-5.0
Statutory amounts[7]	802.9	7.6	821.5	10.1	396.8	7.9
Of which: Provincial equitable share	538.5	6.5	538.5	6.5	269.2	6.5
Interest on debt	229.2	12.0	236.3	15.5	116.3	16.9
General fuel levy	14.0	6.5	14.0	6.5	4.7	6.5
Total expenditure	1 766.0	4.5	1809.2	7.1	877.0	7.3

1 Components may not add up to totals due to rounding off and the exclusion of unclassified items.
2 *2020 Budget Review*
3 *2020 Supplementary Budget Review*
4 Year-on-year percentage change: budgeted on previous year's actual outcome
5 Year-on-year percentage change: revised estimates on previous year's actual outcome
6 Year-on-year percentage change: actual outcome on previous year's actual outcome
7 Including extraordinary payments

Source: National Treasury

Interest paid on national government debt (debt-service cost) increased briskly by 16.9% year on year to R116 billion in April–September 2020, absorbing 23.9% of total net tax revenue. This increase was in line with the spiralling stock of national government debt. The February 2020 Budget projected debt-service costs of R229 billion for fiscal 2020/21 as a whole. This was revised to R236 billion and R233 billion in the *2020 Supplementary Budget Review* and the *2020 MTBPS* respectively.

National government debt-service cost as a ratio of total tax revenue



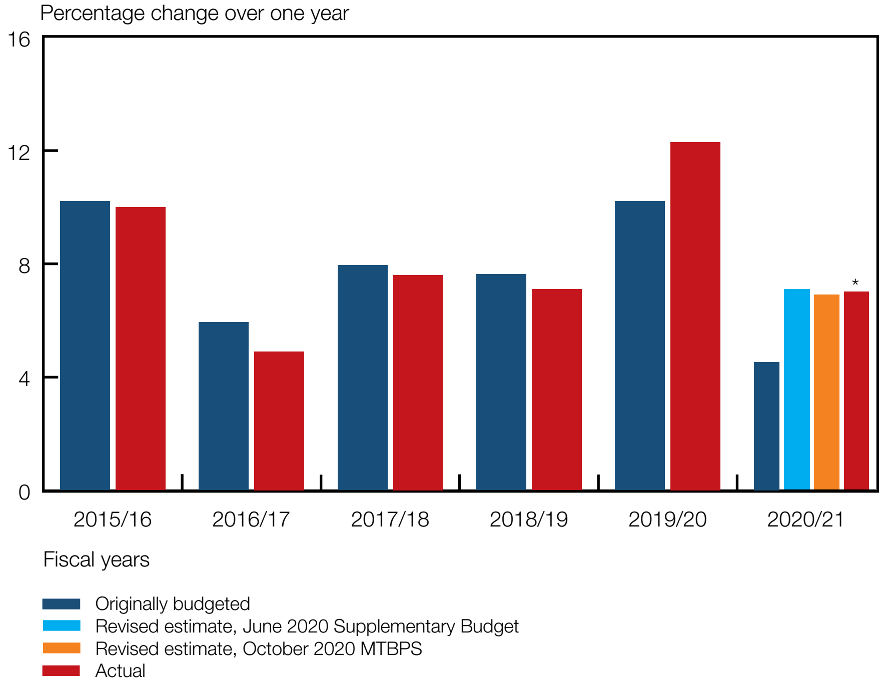
* April–September 2020

Sources: National Treasury, SARS and SARB

Statutory equitable share transfer payments by national government to provinces – the main source of provincial government revenue – increased by 6.5% year on year to R269 billion in April–September 2020. The February 2020 Budget allocated R538 billion for fiscal 2020/21 as equitable share transfers to provinces as well as R14.0 billion to metropolitan municipalities as a share of the general fuel levy. In August 2020, the first instalment of R4.7 billion was transferred to metropolitan municipalities.

In the first seven months of fiscal 2020/21, total expenditure increased at a year-on-year rate of 7.0% to R1 010 billion. This could largely be attributed to COVID-19-related spending, support provided to some SOCs as well as higher debt-service cost.

Expenditure by national government



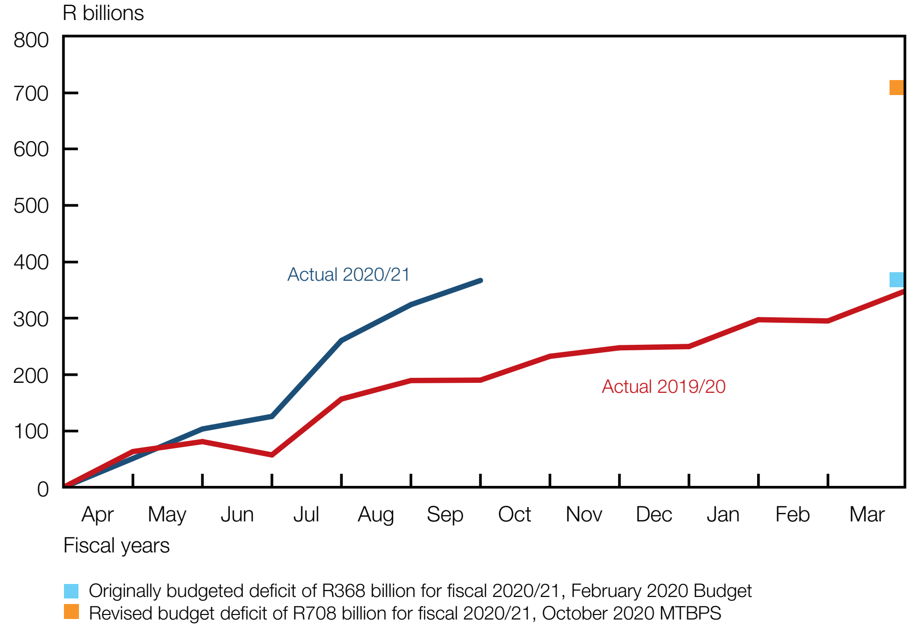
* April–October 2020

Sources: National Treasury, SARS and SARB

National government's total revenue and expenditure for the period April–September 2020 resulted in a cumulative cash book deficit of R367 billion, which was R177 billion more compared with April–September 2019. The originally envisaged cash book deficit of R368 billion for fiscal 2020/21 in the February 2020 Budget was revised upwards by almost double in both the *2020 Supplementary Budget Review* and the *2020 MTBPS*, to R710 billion and R708 billion respectively. These revisions reflected the projected shortfalls in tax revenue due to the sharp contraction in economic activity and higher spending as a result of the COVID-19 pandemic.

In the first seven months of fiscal 2020/21, the net outcome of national government's revenue and expenditure yielded a cash book deficit of R417 billion, which was R184 billion more than a year earlier.

Cumulative deficit of national government



Sources: National Treasury, SARS and SARB

29 The primary deficit is the cash book deficit excluding interest payments.

The primary deficit[29] of national government more than doubled to R251 billion in April–September 2020 from R90.6 billion recorded in the same period a year earlier. As a ratio of GDP, the primary deficit increased sharply from 3.5% in the first six months of fiscal 2019/20 to 10.7% in the corresponding period of fiscal 2020/21. The February 2020 Budget projected a primary deficit for national government of R139 billion (2.6% of GDP) for fiscal 2020/21. However, this was revised significantly higher in both the *2020 Supplementary Budget Review* and the *2020 MTBPS* to R473 billion (9.7% of GDP) and R475 billion (9.8% of GDP) respectively.

National government financing

R billions

Item or instrument	Actual Apr–Sep 2019	Actual Apr–Sep 2020	Originally budgeted[1] Fiscal 2020/21	Revised estimates[2] Fiscal 2020/21
Cash book deficit	190.1	366.9	368.0	709.7
Cash flow deficit[3]	207.1	390.8	...	...
Plus: Cost/profit on revaluation of foreign debt at redemption[4]	11.4	6.5	4.3	6.7
Accrual adjustments	26.7	45.8	...	...
Net borrowing requirement	191.8	351.5	372.3	716.4
Treasury bills and short-term loans[5]	63.8	86.9	48.0	146.0
Domestic bonds[5]	123.5	248.7	285.2	410.0
Foreign bonds and loans[5]	61.5	79.0	21.3	117.2
Change in available cash balances[6]	-57.0	-63.0	17.7	43.2
Total net financing[7]	191.8	351.5	372.3	716.4

1 *2020 Budget Review*
2 *2020 Supplementary Budget Review*
3 The cash flow deficit includes extraordinary receipts and payments, and differs from the cash book deficit.
4 Cost + profit –
5 Net issuance + net redemption –
6 Increase – decrease +
7 Components may not add up to totals due to rounding off.
... denotes not available

Sources: National Treasury and SARB

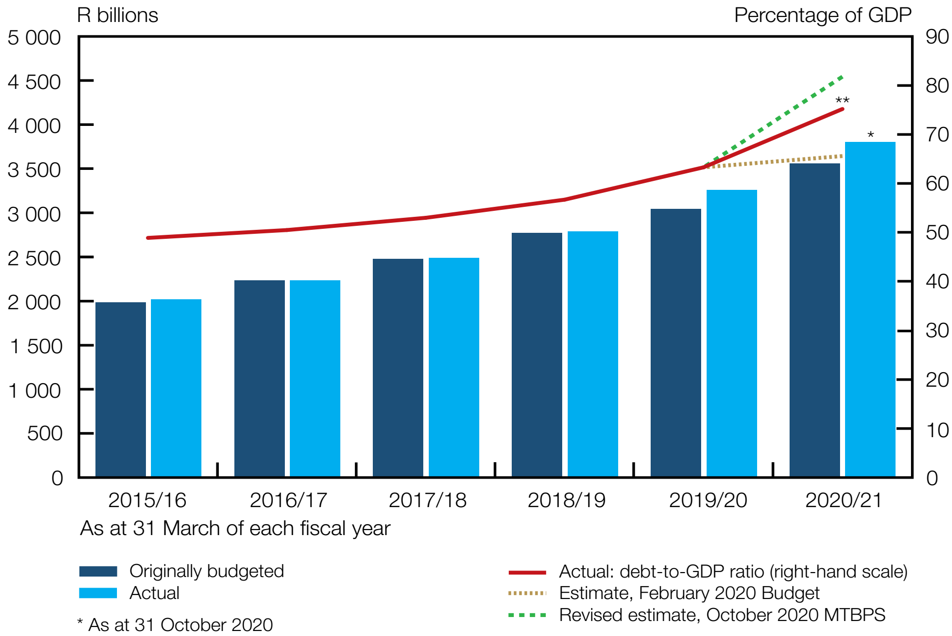
National government's cash flow deficit increased by R184 billion year on year to R391 billion in the first half of fiscal 2020/21. After taking the cost of revaluation of foreign debt at redemption and accrual adjustments into account, the net borrowing requirement[30] increased significantly from R192 billion in April–September 2019 to R352 billion a year later – an increase of R160 billion.

The higher net borrowing requirement of national government in the first half of fiscal 2020/21 was financed primarily in the domestic financial markets through the net issuance of domestic long-term government bonds. Government's net issuance of TBs, domestic long-term government bonds and short-term loans from the CPD amounted to R86.9 billion in April–September 2020, while the net issuance of domestic government bonds was R249 billion. The net issuance of foreign bonds and loans was R79.0 billion over this period. The funding activities of national government increased the overall available cash balances by R63.0 billion in the first six months of fiscal 2020/21.

The total gross loan debt of national government increased significantly by R627 billion, or 20.3% year on year, raising the outstanding balance to R3 714 billion (75.2% of GDP) as at 30 September 2020. This upsurge reflected a rise in the outstanding balance of both domestic and foreign currency-denominated debt, with domestic debt accounting for 88.1% of the total. However, the outstanding balance of foreign currency-denominated debt increased at a faster pace than domestic debt (i.e. 24.3% as opposed to 19.8%).

In February 2020 national government's gross loan debt was initially budgeted to amount to R3 562 billion (65.6% of GDP) at the end of fiscal 2020/21. The *2020 Supplementary Budget Review*, however, revised gross loan debt significantly higher to R3 974 billion (81.8% of GDP), in line with an anticipated higher deficit and an associated increase in financing needs. Even though the forecast for total gross loan debt remained unchanged in the *2020 MTBPS*, domestic debt was revised higher while foreign debt was revised lower. Gross loan debt was projected to increase further over the medium term to reach R5 536 billion (92.9% of GDP) in fiscal 2023/24. The projections of rising debt were mainly associated with the persistent widening of the budget deficit as well as fluctuations in interest rates, inflation and exchange rates.

Gross loan debt of national government



* As at 31 October 2020
** As at 30 September 2020

Sources: National Treasury, Stats SA and SARB

The domestic debt of national government (marketable and non-marketable) increased to R3 273 billion as at 30 September 2020, or R541 billion more compared with the same period a year earlier, with the marked increase largely resulting from the higher net issuance of domestic

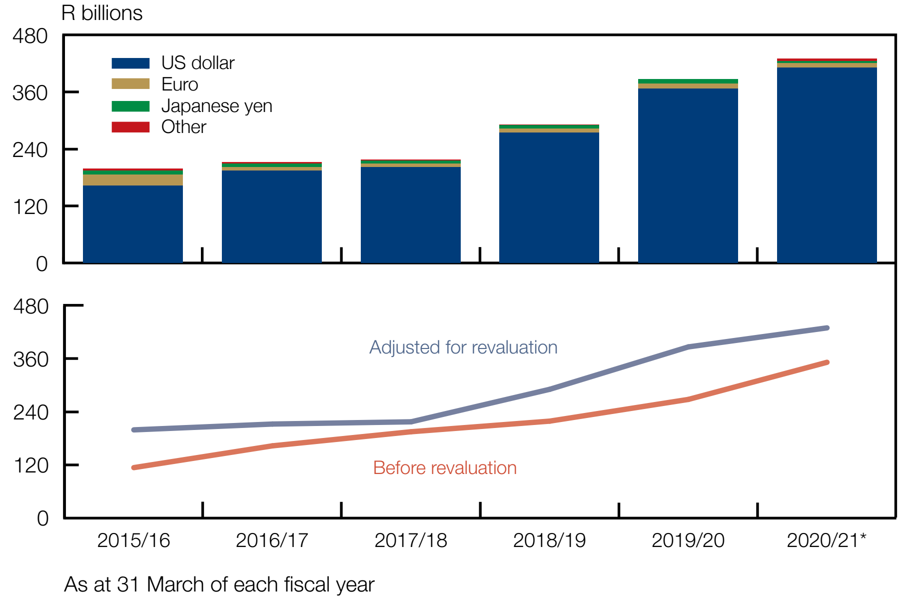
30 The net borrowing requirement is calculated as the cash flow deficit after accounting for the revaluation of foreign debt at redemption and accrual adjustments.

marketable debt. Domestic marketable debt (marketable bonds and TBs) increased to R3 216 billion as at 30 September 2020, or R526 billion more compared with the same period a year earlier, and accounted for 98.3% of total domestic debt. Although the outstanding amount of domestic non-marketable debt (short-term loans from the CPD and other debt) accounted for less than 2% of total domestic debt, such debt increased at a faster rate of 37.4% compared with marketable debt, which increased by 19.5% in the year to 30 September 2020. The *2020 Supplementary Budget Review* revised total domestic debt for fiscal 2020/21 higher to R3 476 billion compared with R3 227 billion originally estimated in the February 2020 Budget. The *2020 MTBPS* added a further R21.7 billion, projecting domestic debt of R3 498 billion for fiscal 2020/21.

National government's total foreign currency-denominated debt (marketable and non-marketable) of R441 billion as at 30 September 2020 was R86.0 billion more compared with the same period in the previous fiscal year. This increase could largely be attributed to a rise in non-marketable foreign debt and unfavourable exchange rate revaluation effects, as the domestic currency continued to lose ground against the other major international trading currencies.

Non-marketable foreign debt increased significantly from R1.3 billion (0.4% of total foreign debt) as at 30 September 2019 to a notable R89.0 billion (20.2% of total foreign debt) a year later. This increase reflected foreign borrowing to the value of US$5.3 billion (R86.9 billion) during July 2020 in response to the COVID-19 pandemic. The *2020 MTBPS* revised foreign currency-denominated debt lower to R476 billion compared with the earlier upward revision to R498 billion in the June 2020 Supplementary Budget. This compares to the original estimate of R334 billion in the February 2020 Budget.

Foreign currency-denominated debt of national government



* As at 31 October 2020

Sources: National Treasury and SARB

Before taking revaluation effects into account, foreign debt increased from R281 billion to R347 billion between 30 September 2019 and 30 September 2020, largely reflecting borrowing in July 2020. After accounting for revaluation effects, foreign currency-denominated debt amounted to R441 billion (a revaluation of R93.1 billion) as at 30 September 2020. National government's foreign debt is denominated in three currencies – the US dollar, euro and Japanese yen. The US dollar-denominated debt represents 96.7% of total foreign debt, with the balance shared between the euro and the Japanese yen. The average outstanding maturity of foreign marketable bonds increased from 162 months as at 30 September 2019 to 168 months a year later.

Abbreviations

Alsi	All-Share Price Index
BER	Bureau for Economic Research
BLS	Bureau of Labor Statistics
CIT	corporate income tax
COVID-19	coronavirus disease 2019
CPD	Corporation for Public Deposits
CPI	consumer price index
CURCAP	current and capital account
EMBI+	Emerging Markets Bond Index Plus
EPWP	Expanded Public Works Programme
FAO	Food and Agriculture Organization
FBSAA	financial balance sheet and accumulation account
FRA	forward rate agreement
FX	foreign exchange
GDE	gross domestic expenditure
GDP	gross domestic product
GFC	global financial crisis
GVA	gross value added
HIS	Homeowner Sentiment Index
ICT	information and communications technology
IEA	integrated economic accounts
IIP	international investment position
ILO	International Labour Organization
IMF	International Monetary Fund
Jibar	Johannesburg Interbank Average Rate
JSE	JSE Limited
MFI	monetary financial institution
MTBPS	*Medium Term Budget Policy Statement*
NEER	nominal effective exchange rate
NFBSAA	non-financial balance sheet and accumulation account
NPISHs	non-profit institutions serving households
OECD	Organisation for Economic Co-operation and Development
PGM	platinum group metal
PIC	Public Investment Corporation
PIT	personal income tax
PPI	producer price index
QES	*Quarterly Employment Statistics*
QLFS	*Quarterly Labour Force Survey*
REER	real effective exchange rate
repo	repurchase (rate)
RMB	Rand Merchant Bank
ROW	rest of the world
S&P	Standard & Poor's
Sabor	South African Benchmark Overnight Rate
SACU	Southern African Customs Union
SARB	South African Reserve Bank
SARS	South African Revenue Service
SNA	*System of National Accounts*
SOC	state-owned company
Stats SA	Statistics South Africa
TB	Treasury bill
US	United States
UVI	unit value index
VAT	value-added tax
VIX	Volatility Index