



Reality Check

A review of the local economy, May 2009

By Tendani Mantshimuli, consumer economist, Liberty Life

Economic figures show that the economy is still in dire straits as South Africa faces a recession. The global outlook is even bleaker. However, against this negative backdrop some positive signs have started to emerge.

Economic figures look bleak

There's no doubt that there's still cause for concern about the direction the South African economy is headed.

GDP continues to weaken

High frequency indicators like manufacturing and mining production, as well as retail sales and vehicle sales, point to a continuation in the contraction of gross domestic product (GDP) from the last quarter of 2008 into the first quarter of this year. A decline in GDP in the first quarter of 2009 would mean that the country is technically in a recession.

Global growth revised downward

Internationally, the International Monetary Fund (IMF) has revised down its forecast for global growth for 2009 from a marginal increase of 0.5% in its January *World Economic Outlook (WEO)* to a decline of 1.3% in the April *WEO*. The decline in global growth partly reflects weakness in demand as consumer confidence remains low. This has negative implications for our balance of payments as it means exports will remain under pressure which does not help our current account deficit.

Business failure and job losses

Here at home the unfortunate side effect of weak domestic growth has been the failure of some businesses. Statistics SA has reported a substantial increase in company liquidations during the first quarter of this year compared to the same period last year. The pressures that businesses are facing have led to an increase in retrenchments or reduced in working hours. During the first quarter of 2009, 88 000 people lost their jobs in the formal sector of the economy. Companies have also scaled down or put on hold their fixed investment expenditure projects. This is the grim reality that businesses face.

Light at the end of the tunnel

It's not all gloom and doom, there are some signs of life that are evident in the economy.

Interest rates fall

Interest rates have come down by a cumulative 350 basis points since December 2008 with more cuts envisaged in the coming Monetary Policy Council (MPC) meetings. This has reduced the cost of repaying debt for consumers and will ease the pressure on their disposable income.

For example, a household with a R500 000 bond would be paying approximately R1450 less a month on interest repayments.

This is the most aggressive easing cycle we've seen so far that has in a short space of time unwound the prolonged tightening cycle we had, which is good for the consumer. The lessons of the past two years should however not be forgotten: even when interest rates are low, never borrow more than you'll be able to repay when interest rates inevitably rise again.

Household debt declines

There is some comfort in the fact that household debt has been coming down with households actually taking up less debt. Growth in credit extension to the private sector has dropped from a high of 27.5% in October 2006 to 8.5% in March 2009.

Inflation improves marginally

Inflation is somewhat sticky but the trend is downward. In its latest MPC statement the Reserve Bank indicated that inflation is forecast to fall below the upper 6 per cent of the target band by the third quarter of this year. Though very volatile, we've see a recent strengthening of the exchange rate of the rand which is good for food inflation and might also mitigate the increase in the oil prices.

Peaceful elections

Barring the Western Cape spat, the peaceful change of government administration bodes well for the country and investor confidence. There was general acceptance of the new cabinet appointments across a broad sector of the society. This is probably mainly because there is no indication that the new administration's policies will be a big departure from those the government supported since 1994. Also, the restructuring of government has shifted emphasis to efficiency and service delivery.

Wages higher, but electricity too

Andrew Levy's Wage Settlement Survey Interim Report for Quarter 1, 2009, reports that wage settlements were 10.2% which is above the average first quarter inflation rate of about 8.4%. This means that workers were somewhat compensated for a loss in purchasing power. However, the expected increase in electricity prices will to some extent offset the gains that consumers would have on their disposable income.