Industrial Development Corporation

Your partner in development finance

Economic Overview

Recent developments in the global and South African economies

June 2013

Department of Research and Information

HIGHLIGHTS

The global economy continues to be characterised by a multi-speed recovery, with growth still relatively tepid on average. In the advanced world, levels of economic activity continue to stagnate or contract in several countries, whilst the recovery momentum appears to be gaining a firmer footing in the USA. A number of sizeable emerging and developing economies, in turn, have experienced a slowdown in broad economic activity.

Global manufacturing output remains under immense pressure due to subdued demand and competitive pressures on the production front. This has been evidenced by sharp declines in international trade volumes in recent months. Weak demand from Europe continues to affect export-led economies such as China's, in turn impacting adversely on industrial production. Decelerating fixed investment activity as this Asian giant refocuses on stimulating internal demand, has also resulted in softer global commodity prices.

Current economic developments and the near term outlook are generally unfavourable for job creation in a world facing a substantially larger unemployment challenge. Recent data indicates that most countries are struggling to create new jobs or at least recover those lost since the onset of the recession in 2008-09.

Projections for Africa's economic growth in 2013-14 remain favourable. Rising activity levels in mining and oil, agriculture and service sectors should support the expected average annual growth rate of just over 5% over this period. Despite some noticeable progress on a number of socio-economic factors over the years, the continent still faces several challenges, key amongst these being high levels of unemployment and poverty. This has raised concerns over the inclusiveness and sustainability of the solid growth experienced over the years.

South Africa's economy continues to be negatively affected by global trading conditions, with adverse home-grown factors aggravating its performance in recent times. Harsh recessionary conditions in the Eurozone are having a particularly detrimental effect on the local manufacturing sector, specifically its export-oriented segments. Combined with subdued growth elsewhere in the world and competitive challenges on the local front, such developments are stifling prospects for a meaningful industrial recovery.

Real GDP growth measured a disappointing 0.9% in the first quarter of 2013, dragged downward by a sharp contraction in manufacturing output. Despite positive contributions by a number of services sectors, such rates of expansion were also quite subdued. The rate of growth for the domestic economy is expected to be rather sluggish in 2013 as a whole since global growth remains generally sub-optimal and demand conditions are still particularly dire in several industrialised economies.

Business confidence, although having improved from recent lows, is still at a "neutral" level. Major underlying factors include weak demand domestically and abroad, and uncertainty over future prospects, with the trading and operating environments faced by the local manufacturing and mining sectors being particularly challenging. The leading business cycle indicator, in turn, dipped slightly in March 2013 after having reached a 2-year high in February, thus reflecting yet difficult economic conditions.

The mining sector reported a strong rebound in output, as a number of its sub-sectors recorded robust growth in the opening three months of 2013. The solid 6.1% expansion in output levels were underpinned by a 31.4% rise in gold production, assisted by substantial increases in production by a number of smaller mining segments, including copper, manganese and chrome. Higher output levels in the iron ore segment were mainly due to strong external demand, particularly from China. However, overall mining output in 2012 was still substantially lower than the production levels achieved in 2005. Tense labour relations, renewed threats of labour strikes and excessive wage demands highlight the importance of resolving these issues in a collaborative manner so as to avoid more production disruptions and job shedding in this troubled sector.

The manufacturing sector, in turn, was severely affected by the continuing recession in the Eurozone, a fragile recovery world-wide, as well as by weaker domestic demand. Although manufacturing activity managed to recover from the recent economic downturn, output remained fairly subdued and quite volatile from quarter to quarter. A number of key sub-sectors reported large contractions in output volumes over the first quarter of 2013, whilst consumer-oriented sub-sectors such as motor vehicles, parts and accessories, food products, clothing and footwear, along with the electrical machinery industry, were among the few sub-sectors that reported positive rates of growth.

Employment creation is still being constrained by a sluggish pace of economic growth. The economy managed to create 44 000 new jobs in the quarter to March 2013, the majority within the agricultural and public sectors. However, the overall employment level, which stood at just over 13.6 million by March, is still some 400 000 less than that recorded prior to the onset of the crisis in 2008/09.

Consumer price inflation edged steadily higher in recent months, measuring 5.9% by April 2013. Significant inflationary pressures emanated from administered prices (including fuel and electricity), whilst food prices also increased at a fast pace, although moderating to some extent. Despite inflation being expected to breach the 6% target ceiling over the next couple of months, the Monetary Policy Committee (MPC) decided to keep the repo rate unchanged at 5% at its May 2013 meeting. The MPC expressed concerns over the state of the economy as growth prospects deteriorate, whilst inflation risks are on the upside. The sharp depreciation of the rand in recent times could pose strong upward inflationary pressures in coming months, thereby limiting the scope for an interest rate cut in the foreseeable future.

IMPLICATIONS FOR BUSINESS

- Trading conditions in external markets vary significantly across regions, demanding close scrutiny of market developments by export-oriented South African businesses in order to penetrate areas of significant growth such as parts of the African, South American and Asian continents. Those relying strongly on traditional markets in the Eurozone may be facing continued challenges over a protracted period of time, although the performance may vary depending on the type of product being exported. Market conditions in the USA, in turn, appear to be improving.

- Manufacturing operations are likely to face a difficult year, although certain sectors may experience reasonably good performances. Market development opportunities are emerging domestically through state procurement, localisation initiatives and changing trends within South Africa's consumer base. Externally, the focus on Africa's markets should be prioritised where possible, as exemplified by the successes recorded in certain export sectors over the course of last year. The continent's importance as a potential export market for domestic manufacturers must not be underestimated, with many of the perceived challenges likely to be overcome in reality.

- Although a glimmer of hope emerged from the strong rebound in mining activity, albeit from a low base, prospects for this sector remain challenging in light of subdued global demand and rising input costs, including labour and utility costs, productivity issues and labour unrest. These factors will not only have a direct impact on mining output, but, considering the strong backward, forward and lateral linkages of the mining sector with various sectors of economic activity, the ultimate impact could be quite substantial.

- The moderation in consumer spending and a fairly pessimistic outlook for household expenditure can have far-reaching implications for those sectors relying on the domestic consumer market, especially over the short-term. Local demand conditions are still generally unsatisfactory, whilst competition from abroad remains fierce. A welcome development has been the stabilisation signs emerging in the clothing and footwear industries, possibly reflecting a measure of success of state support mechanisms.

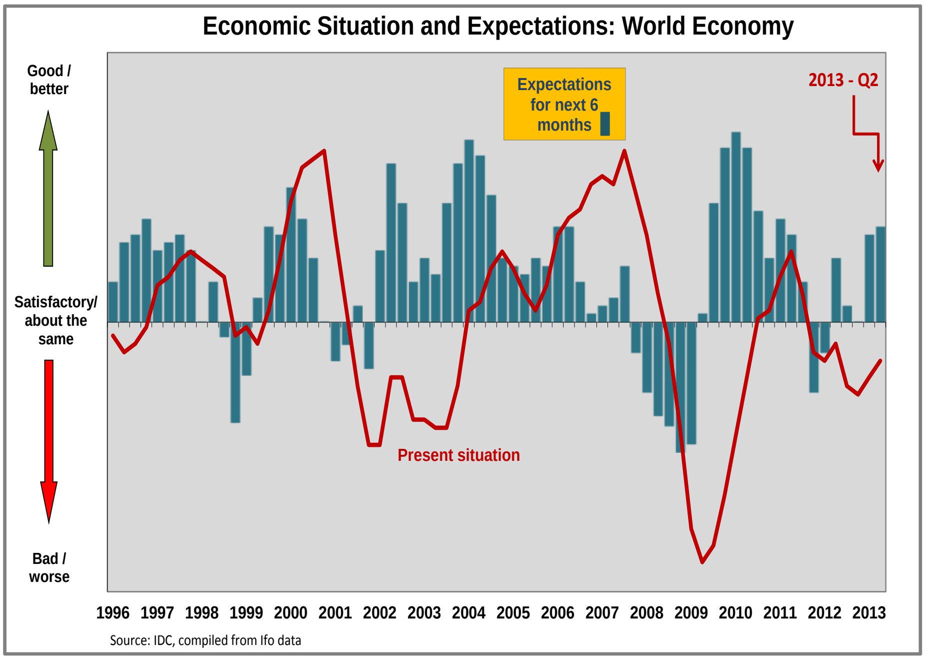
- Despite high consumer price inflation at present and expectations of a further rise in the next few months, possibly breaching the inflation target ceiling of 6% by mid-2013, interest rates are anticipated to stay at current levels for some time.

- Although the price competitiveness of South African export products in global markets may have improved through a sharply weaker currency, the benefits will not be fully realised in light of weak demand conditions in parts of the world. However, South African producers who have been struggling to retain local market share against import competition are being given some relief. Nevertheless, this improved price competitiveness will be gradually eroded over time through inflationary effects.

- The rand's sharp depreciation has adverse cost implications for businesses relying on imported products for their operations (e.g. raw materials and intermediate products), as well as from an investment perspective since imported capital goods (e.g. machinery and equipment) and other necessary items that have become more expensive.

GLOBAL ECONOMIC CONDITIONS

Although current economic conditions globally still reflect a tepid recovery, signs of stabilisation may be eminent and prospects appear to be improving slightly. The Ifo World Economic Survey for the second quarter of 2013 supports this view, in light of a less negative assessment by respondents of the economic situation at present, although conditions are certainly not yet satisfactory. Furthermore, the outlook for the next six months is not only more optimistic, but has improved modestly relative to the previous quarter (refer to the accompanying graph).

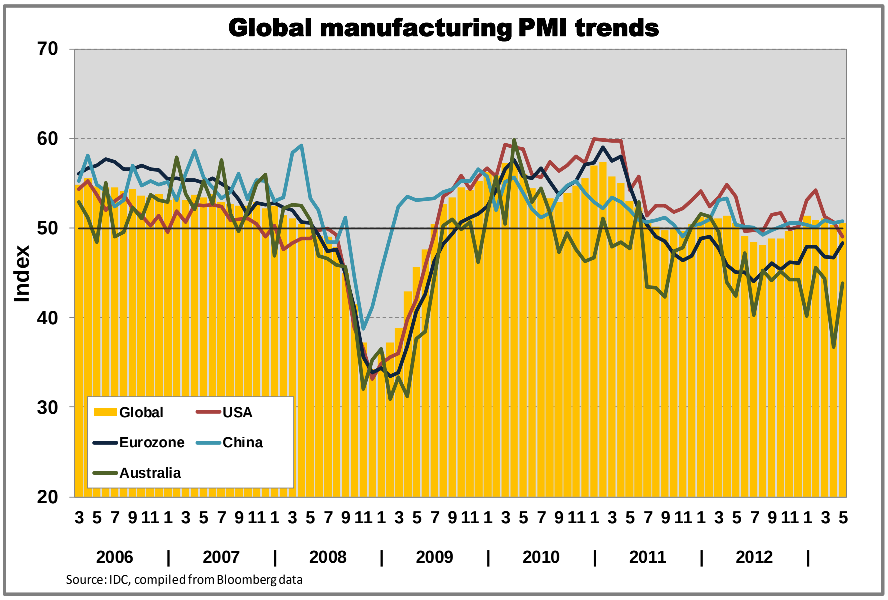


Examining the survey results at the regional level, the assessment of economic conditions in Asia continues to improve as the economic climate indicator reached its highest level since the end of 2010 and is substantially higher than its long-term average. Within Asia, the best performing economies include Indonesia, Malaysia, the Philippines and Thailand. Although current economic conditions have been rated as satisfactory in China, the six-month outlook has deteriorated to some extent. Economic conditions in Japan appear to be improving, judging from the strong uptick in the forward-looking indicator over the past two quarters. In the USA, high public deficits and unemployment are weighing on the assessment of the economic situation presently. In contrast, prevailing economic conditions in Western Europe remain highly unsatisfactory, with rising unemployment in countries such as France and Ireland being a key concern.

Despite a continuous, yet modest expansion in the global economy since the final quarter of 2009, the growth momentum appears to have moderated more recently. According to the All-Industry Output Index compiled by JPMorgan and Markit, a deceleration in world output for both the manufacturing and services sectors has been recorded, with the April 2013 figure indicating the weakest rate of expansion since October 2012. According to the Purchasing Managers Index (PMI) data for individual countries, this slowdown in growth is widespread across many parts of the globe. Furthermore, world trade flows have also been under strain as reflected by a rather modest increase in global export volumes in the first quarter of 2013, following a substantial slowdown in overall world trade during 2012.

Economic activity in the Eurozone remains subdued mainly as households, banks and governments continue to deleverage, whilst financial imbalances remain prevalent. This regional bloc is experiencing the longest recession since its inception, at six consecutive quarters of contraction, although the extent is not as severe as in 2008/09. Core economies such as Germany and France are also being impacted upon, with the latter once again in recession and the German economy only just managing to avoid a contraction in output during the opening quarter of 2013. Although industrial production for the euro area recorded modest growth in the first quarter of 2013 on a quarter-on-quarter basis, this was from a very low base. Moreover, when compared to a year earlier, industrial output actually contracted by 2.5%.

The dire state of manufacturing activity in the euro area is illustrated by PMI data, which reveals declining output levels for the past 21 months and a further deterioration of trading conditions, including somewhat disappointing new order volumes, according to the April 2013 readings. Lower manufacturing output has been reported for all surveyed countries, confirming the generalized weakness across the Eurozone. The unemployment rate in the 17-nation bloc increased to 12.1% in March 2013, from 11% a year earlier. This is the highest rate on record, with some 19.2 million people finding themselves without a job. Economic activity is unlikely to improve notably in coming months as confidence levels from within the euro area and in export markets remain restrained.



In the USA, industrial production has continued to post gains, albeit at a more moderate pace. Growth in manufacturing output decelerated in real terms over the first four months of 2013 (year-on-year), although output declined on a monthly basis both in March and April. Moreover, the official PMI data for May dipped to 49 points, indicating a further slowdown in manufacturing output in the world's largest economy. The short-term manufacturing outlook indeed appears to be deteriorating as new order volumes dropped quite sharply from 52.3 points to 48.8 points. Although US GDP posted relatively stronger growth of 2.4% (on a quarter-on-quarter and annualised basis) in the first quarter of 2013, indications are that this stronger momentum could be compromised to some degree by the budget cuts effective from 1 March 2013 and the eventual phasing out of the quantitative stimulus known as QE3. However, positive signs on the economic front include a rising trend in consumer confidence, continued job creation and subsequent lowering of the unemployment rate (at 7.5% in April 2013, the US unemployment rate is at its lowest since December 2008), the recovery in the housing market, as well as the performance of equity markets.

Industrial output in Brazil has been disappointingly subdued in recent months, particularly in light of the fact that this large emerging economy is gearing itself to host the FIFA World Cup in 2014. Weaker than expected outcomes have largely been ascribed to sluggish economic activity in general, which in turn has been exacerbated by industrial inefficiencies on the back of infrastructure bottlenecks, low investment levels and high/rising labour costs. The production of capital and consumer goods has also been recording comparably low growth rates in recent months on the back of weaker demand.

The Brazilian economy is projected by the IMF to expand by 3% in 2013 (0.9% in 2012) as a low interest environment (note that this forecast preceded the recent hike in Brazilian interest rates) and renewed efforts to increase private sector fixed investment are likely to boost economic growth. A further acceleration to 4% is project by the IMF for next year. In order to provide more impetus to economic growth and development, the Brazilian government is incentivising the export sector's expansion. Although external trade represents a relatively small share of GDP (exports and imports each account for about 12% of GDP), Brazil has a substantial fuel import bill. The trade balance recorded a sizeable deficit over the period January to April 2013, compared to a huge surplus over the same period a year earlier. Weak demand for commodities globally, coupled with domestic factors such as underinvestment in the industrial sector and poor infrastructure, have been blamed for this worsening trend as Brazilian companies find it increasingly difficult to remain competitive. Going forward, the preparations for the global soccer tournament are expected to boost economic activity, particularly through the upgrading of transportation and logistics infrastructure.

Russia's GDP growth measured only 1.6% in the first quarter of 2013 - the fifth consecutive quarter of decelerating year-on-year growth. In recent months, economic activity has been driven largely by demand for consumer goods, while fixed investment remained fairly modest. Being the second largest producer and exporter of oil and gas (after Saudi Arabia), Russia is likely to benefit from higher export earnings once broad-based demand normalises. However, competitive forces are emerging in the gas industry. For instance, in Europe (Russia's key market for gas) not only are demand levels currently weak, but there is also a trend towards more flexible gas pricing systems, which could adversely affect Russia's export earnings. The unconventional gas boom in North America and China, who are exploring alternative gas supplies, are further unfavourable developments for Russia's export-oriented gas industry.

Industrial production in India posted gains in the opening months of this year, supported largely by a recovery in consumer demand. However, an underlying slowdown in the growth momentum of the manufacturing sector may be observed. In addition, the production of capital goods, which is a key indicator of investment activity, remained low. Persistent power cuts, delays in the roll-out of salient industrial and much-needed infrastructure projects, as well as the Indian government's policy reversals have been highlighted as some of the key factors underlying weaker economic activity and dampening investor confidence. The IMF expects the Indian economy to grow by 5.7% in 2013, but this will be largely dependent on both local and external demand conditions, as well as on improvements in government policy. Similarly to other emerging markets, India has infrastructure challenges that are limiting its growth potential. However, plans are underway to address stumbling blocks in the form of policy constraints and endemic red tape that continue to restrain infrastructure funding in this country.

The growth of the Chinese economy slowed to 7.7% in the first quarter of 2013, from 7.9% in the previous quarter. The expansion of value added by the industrial sector has moderated and, although still very brisk, so has the rate of expansion in retail sales. The manufacturing PMI in China has been reflecting a less than satisfactory operating environment amongst manufacturers in recent months, a situation that is likely to persist should demand conditions in key external markets, namely, America, Asia and Europe, remain subdued in the near term. The IMF has revised its growth forecast for China downwardly to 7.75% for 2013 (previously 8%) and has expressed concern over the excessive levels of "social lending" to Chinese households in order to stimulate internal demand.

ECONOMIC DEVELOPMENTS IN AFRICA

Despite the often-cited impressive rates of economic growth posted by Africa at large over the past decade, as well as the relatively positive outlook, the continent continues to face serious challenges. Key amongst these are the high levels of unemployment, underemployment and poverty. Faster economic growth and increasing foreign investor interest have not necessarily translated into meaningfully positive developmental outcomes for the populations of several African countries, raising concerns over the inclusiveness and sustainability of such growth. Furthermore, most African economies still remain highly dependent on primary commodities, with their economic performance often tied to commodity price movements and thus exposing their vulnerability to external shocks.

Some of the challenges faced by the continent were discussed at the 2013 World Economic Forum on Africa held recently in Cape Town, while its achievements over the past few years, including the attainment of middle-income status by almost half of Africa's countries, were noted. The key messages centred on the "need for African leadership to strengthen the continent's competitiveness, foster inclusive growth and [also] to build resilience in a volatile global environment". This will require an acceleration of economic diversification, further investments in strategic infrastructure, as well as unlocking Africa's talent.

According to the World Economic Forum (WEF), for countries to be competitive they need to possess a number of factors, including a 'solid infrastructure, a healthy and educated labour force, efficient markets and a propensity for technological adoption and innovation'. Its *Africa Competitiveness Report 2013*[1] indicates that Africa is the least competitive region in the world, as depicted in the following table, although some countries such as South Africa and Mauritius are either on par or more competitive than certain peers in emerging markets such as India and Russia, based on some of the pillars that constitute the overall global competitiveness index.

However, many African countries feature towards the bottom of the rankings, with increased competitiveness constrained by a continuous deficit in infrastructure, inadequate performances on the educational front, poor macroeconomic policies, poor governance and a lack of sound public and private institutions, as well as small market sizes (in certain cases). These factors are considered critical as a foundation for higher value-added sources of and more diversified growth - hence the need for continuous improvement to place Africa on a sustained, rapid and more inclusive growth trajectory that creates employment opportunities.

Nevertheless, African countries such as Nigeria and Ethiopia, among others, have registered improvements with respect to some of the individual pillars of the overall competitiveness index, albeit modestly, over the 2008/09 to 2012/13 period. South Africa's overall score, on the other hand, has remained relatively stable at around 4.4, placing it ahead of India and Russia, while the scores of China and Brazil have improved from 4.7 to 4.8 and from 4.1 to 4.4, respectively, over the above-mentioned period.

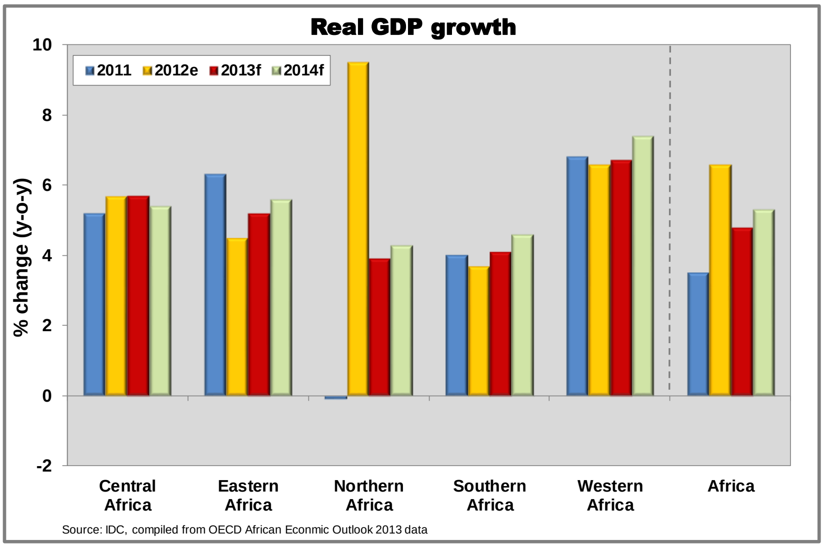
[1] A joint publication of the World Economic Forum, World Bank and the African Development Bank, which is published by the World Economic Forum.

The Global Competitiveness Index 2012/2013 - Africa and comparator regions					
	Overall ranking (out of 144 countries)	**Overall score (1 - 7 best)**	**Basic requirements[2]**	**Efficiency enhancer[2]**	**Innovation & sophistication factors[2]**
Sub-Saharan Africa		**3.57**	**3.72**	**3.44**	**3.19**
South Africa	52	4.37	4.28	4.53	3.94
Ghana	103	3.79	3.85	3.77	3.27
Kenya	106	3.75	3.62	3.97	3.68
Nigeria	115	3.67	3.52	3.96	3.53
Ethiopia	121	3.56	3.74	3.33	2.96
North Africa		**3.82**	**4.20**	**3.47**	**2.98**
BRICs (excl. SA)		**4.44**	**4.70**	**4.48**	**3.78**
China	29	4.83	5.25	4.64	4.05
Brazil	48	4.40	4.49	4.52	3.97
India	59	4.32	4.26	4.48	3.94
Russia	67	4.20	4.79	4.26	3.16
Latin America & Caribbean		**3.97**	**4.31**	**3.86**	**3.39**
South-East Asia		**4.46**	**4.82**	**4.24**	**3.83**

Source: World Economic Forum, *Africa Competitiveness Report 2013.*

Notwithstanding some of these challenges, prospects for the African continent remain favourable, with the *2013 African Economic Outlook* report recently released by the African Development Bank and OECD forecasting growth of 4.8% and 5.3% for 2013 and 2014, respectively. These projections are subject to various risks and uncertainties, particularly at the regional and/or country levels, including economic conditions globally and socio-political developments domestically.

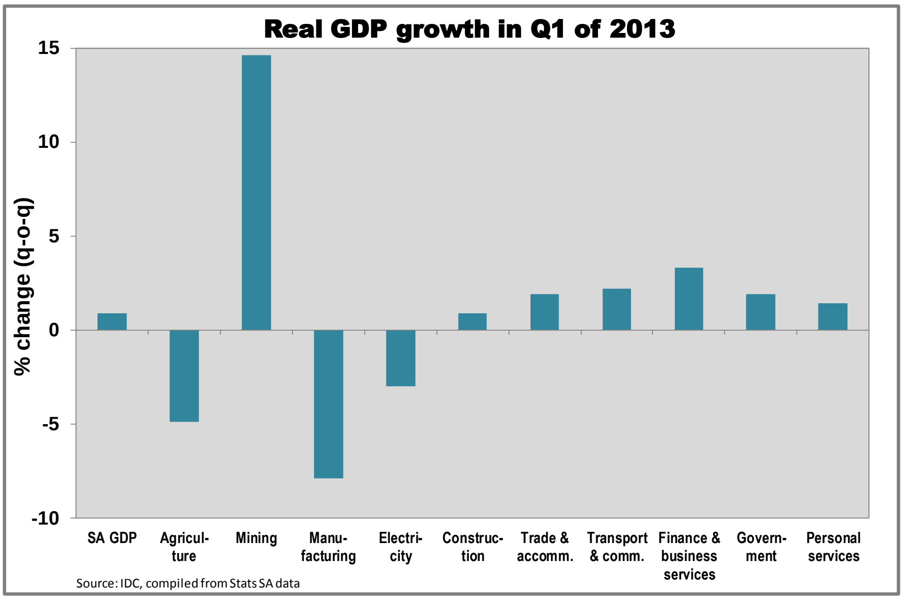
On average, all of Africa's principal regions are expected to grow by more than 4% over 2013-14, with Western Africa posting the fastest growth. However, the outcomes will differ significantly across the continent, with Libya (average of 11.6%) and Sierra Leone (9.6%) expected to record the fastest growth over the forecast period, whilst the lowest growth projections pertain to Swaziland (1.3%) and Equatorial Guinea (1.4%).



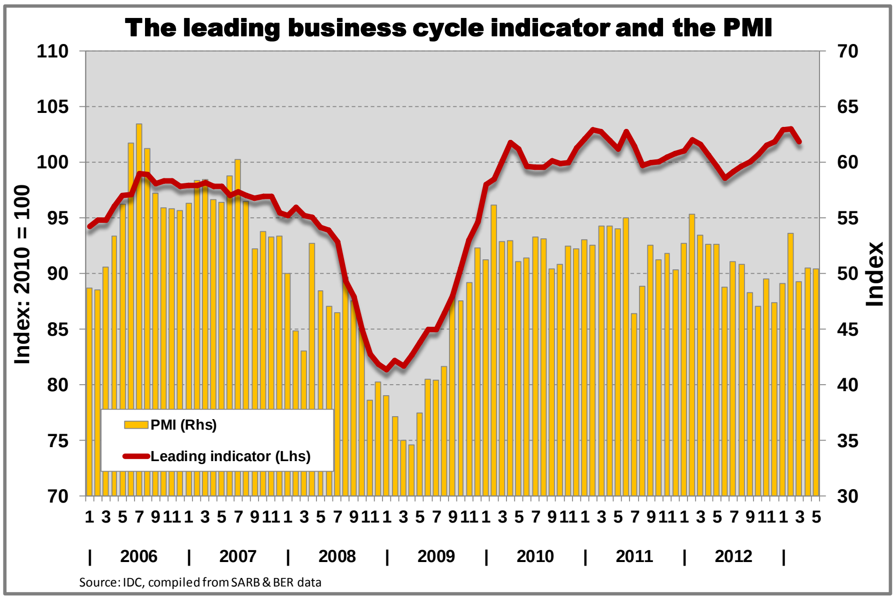
[2] **Basic requirements**: Institutions, infrastructure, macroeconomic environment, health and primary education. **Efficiency enhancer**: Higher education and training; goods market efficiency; labour market efficiency; financial market development; technological readiness; market size. **Innovation and sophistication:** Business sophistication; innovation.

ECONOMIC DEVELOPMENTS IN SOUTH AFRICA

An unsatisfactory global economic growth performance, uncertainty about the sustainability of the recovery and domestic factors are still weighing on the South African economy. After recording a relatively subdued 2.5% rate of economic expansion in 2012, the pace decelerated steeply in the first quarter of 2013 as real GDP expanded by a mere 0.9% (quarter-on-quarter and annualised rate). The sharp contraction of 7.9% in real manufacturing value-add reduced overall GDP growth by 1.2 percentage points, whilst the agricultural and electricity sectors each subtracted 0.1 of a percentage point. The mining sector staged a strong rebound, albeit from a very low base, whilst a number of service-related sectors, including finance and business services; trade, catering and accommodation; transport, storage and communications; as well as the construction sector, managed to achieve a slightly higher growth momentum. Nonetheless, these positive contributions were not sufficient to meaningfully counter the sharp declines.



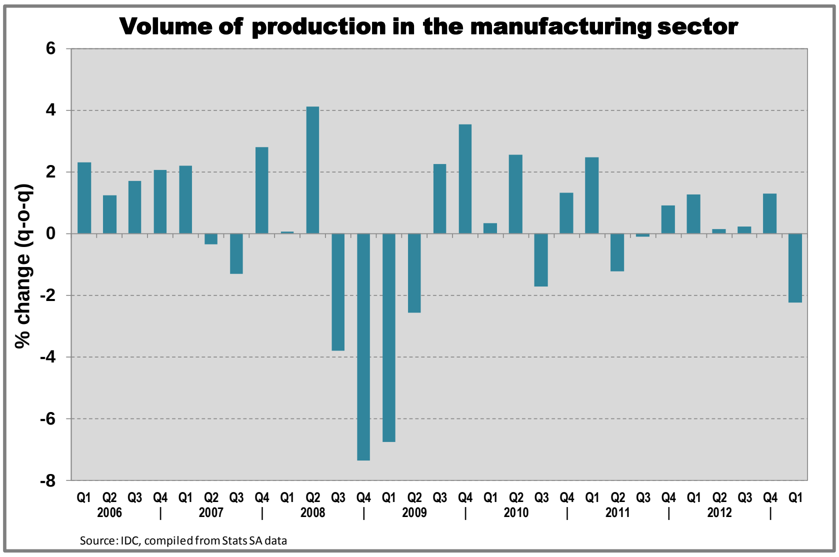
Economic activity is being hamstrung by weak sentiment across a number of sectors, with the business confidence index for the economy at large having dropped by 4 points to 48 in the second quarter of 2013. Four out of the five broad sectors surveyed by RMB/BER reported a drop in business confidence. In the manufacturing sector, confidence levels fell sharply since demand conditions remained unsatisfactory locally and abroad, resulting in spare production capacity. Manufacturers are still pessimistic, expecting a fairly difficult year ahead. Investment in machinery and equipment by manufacturers is also expected to be rather weak. The manufacturing PMI is currently hovering around the 50 point mark, confirming sluggish growth for this sector over the short term.



Consumer confidence, in turn, fell to a 9-year low in the first quarter of 2013, signalling a somewhat weak contribution of household spending to economic growth in general. Furthermore, consumer confidence levels at present are far lower than in the 2008/09 economic recession. Although the upward trend in the leading business cycle indicator in recent months to a 2-year high by February 2013 was encouraging (refer to the previous graph), the halt observed in March was disappointing. Nonetheless, this index still points towards sustained but fairly weak growth for the year as a whole.

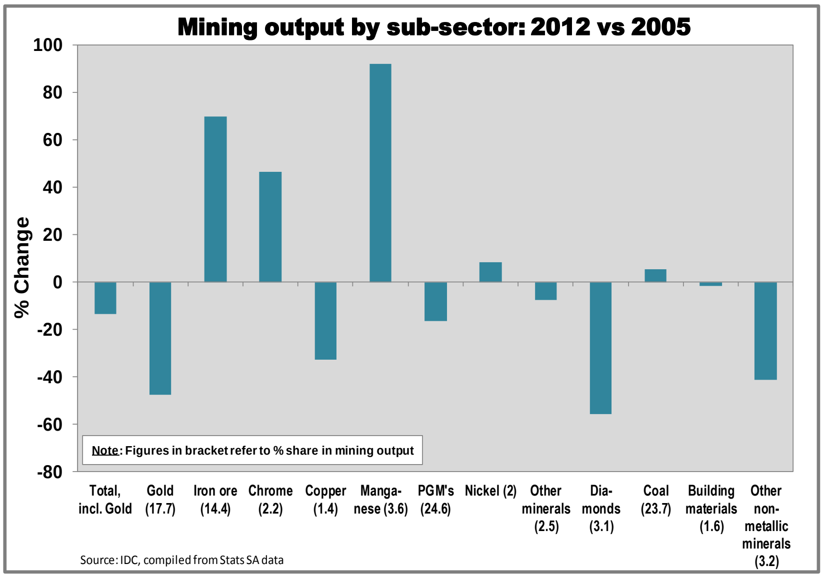
Considering that the Eurozone is amidst its longest recession on record and that the global economic recovery remains generally fragile, it is not too surprising that the domestic manufacturing sector recorded a sharp drop in output volumes during the opening three months of 2013. In addition to weak demand both domestically and abroad, other factors weighing on the sector include rising input costs, a squeeze on profit margins, increased competition from foreign producers in traditional export markets as well as locally, and skills constraints.

Manufacturing output contracted by 2.2% when compared to the final quarter of 2012 (or at a substantially higher -8.7% when calculated as a seasonally adjusted and annualised rate). A worrying trend is that most of the main sub-sectors within manufacturing reported lower output volumes, with sharp contractions having been evident in sub-sectors such as wood, paper and printing, as well as in chemicals, rubber and plastics. Contractions were also recorded in television, radio and professional equipment; basic iron and steel; machinery and equipment; fabricated metals; and furniture, among others.



On the positive side, the motor vehicle industry recorded relatively strong growth of 7.7% over the above-mentioned period, although the segment producing parts and accessories for motor vehicles performed fairly poorly (1.6% growth). Electrical machinery production expanded by 2.3%, possibly benefitting from the on-going capital expenditure programme of state-owned companies. The clothing, footwear and leather products sub-sector reported modest growth over the first quarter of 2013 - a welcoming development, considering the state-led efforts to stabilise its performance.

The mining sector has in recent years been plagued by a number of factors, including unfavourable trends in international demand, infrastructure and logistics related constraints, rising operating costs, production stoppages due to safety concerns and technical aspects, serious problems on the labour front and policy uncertainty. By 2012, output volumes for a number of mining sub-sectors were still below the peak levels achieved in 2005, as illustrated in the following graph. For the mining sector at large, output in 2012 was still 13.4% lower than the levels achieved in 2005.

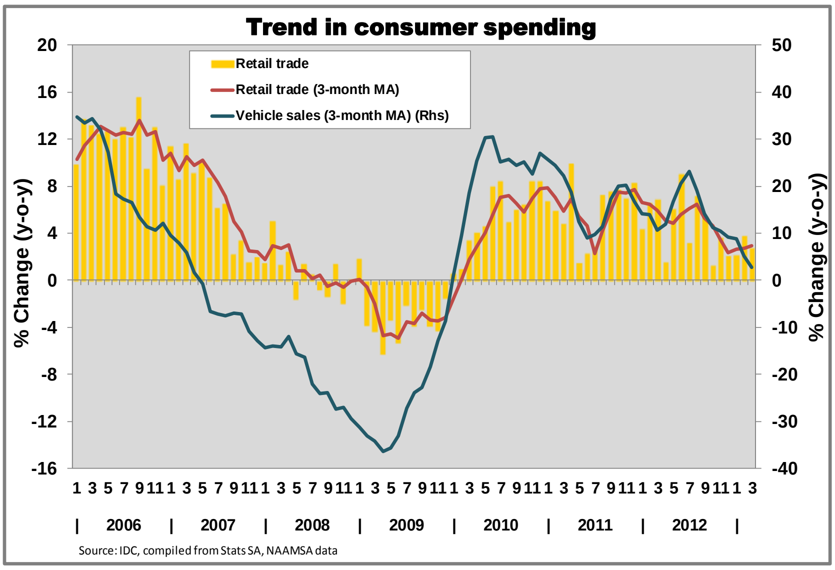


Gold production continued on its long-term declining trend, with output levels by 2012 being almost 48% lower than seven years earlier. The output of the platinum group metals (PGMs) segment was particularly affected in 2012 due to prolonged labour-related production stoppages, falling short of the 2005 levels by approximately 16%. In sharp contrast, strong demand for iron ore in recent years saw production volumes in 2012 exceeding those of 2005 by almost 70%, whilst the equivalent with respect to manganese amounted to 92%.

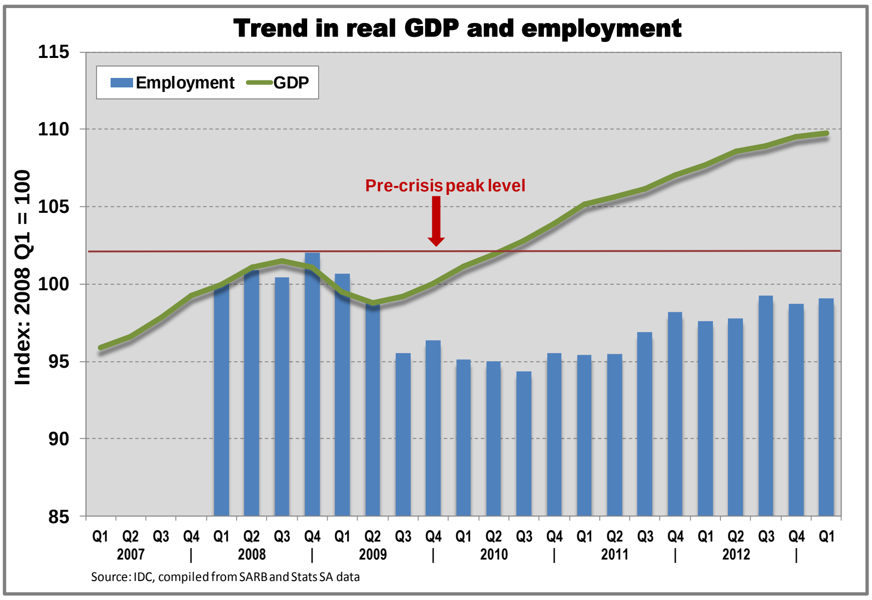
A strong rebound in the mining sector's performance was recorded in the first quarter of 2013, albeit from a very low base. Output volumes expanded by 6.1% on a quarter-on-quarter, non-annualised basis, underpinned by robust growth in gold production, which measured 31.4%, compared to the preceding three-month period. Higher output volumes were also recorded in the following mining sub-sectors: copper (+34.8% increase in output); manganese (+19.8%); chrome (+14.6%); iron ore (+11.2%); as well as PGMs (+2.8%), among others.

Nonetheless, short-term prospects for the mining sector remain quite challenging in light of weaker global demand and the recent sharp drop in commodity prices (e.g. gold and platinum prices), although partly cushioned by the currency depreciation, whilst threats of renewed strike action and excessive wage demands could have detrimental consequences. Investor confidence is being negatively affected in the process and the possibility of further mine closures and concomitant job losses must not be ruled out, which could once again lead to violence and instability in the sector.

Consumer spending continued to moderate in the first quarter of 2013, underpinned by high household indebtedness, lower growth in disposable incomes and an uncertain labour market. Household spending on durable items such as furniture, appliances and equipment was severely affected, with sharp declines reported both in February and March. Similarly, growth in new vehicle sales has also been softening.



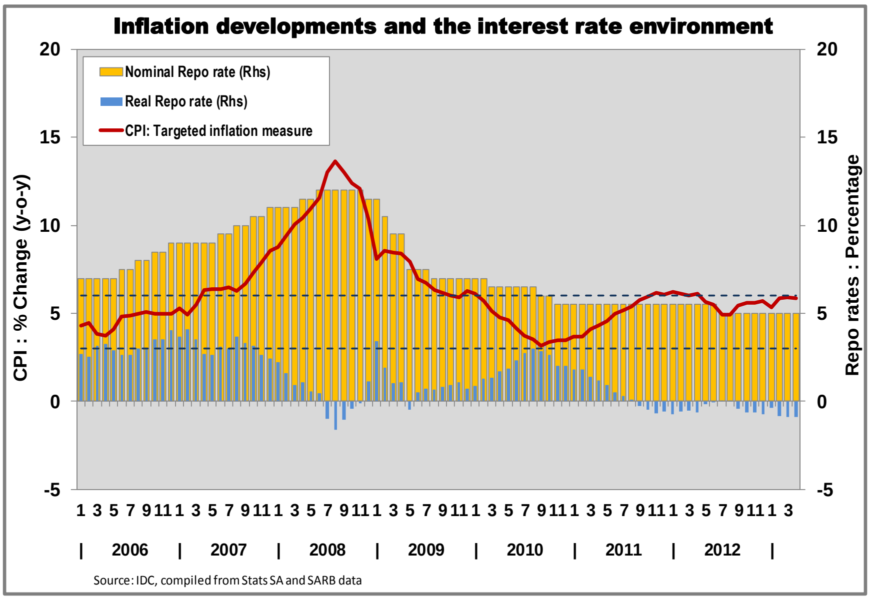
Subdued economic growth rates have stifled job creation, with only moderate increases in overall employment levels, largely driven by the public sector, having been reported since the recession.



Source: IDC, compiled from SARB and Stats SA data

Whereas real GDP already exceeds the pre-crisis peak by about 8%, employment levels are still some 3% below the highs recorded prior to the 2008/09 recession. However, a gradual uptick in employment numbers has been observed since mid-2010, with an additional 44 000 new jobs created in the first quarter of 2013. Nevertheless, there is still a substantial shortfall of around 400 000 jobs relative to the employment levels attained before the economic downturn. The unemployment rate increased marginally to 25.2%, from 24.9% in the fourth quarter of 2012, and 4.6 million South Africans are presently unable to find a job.

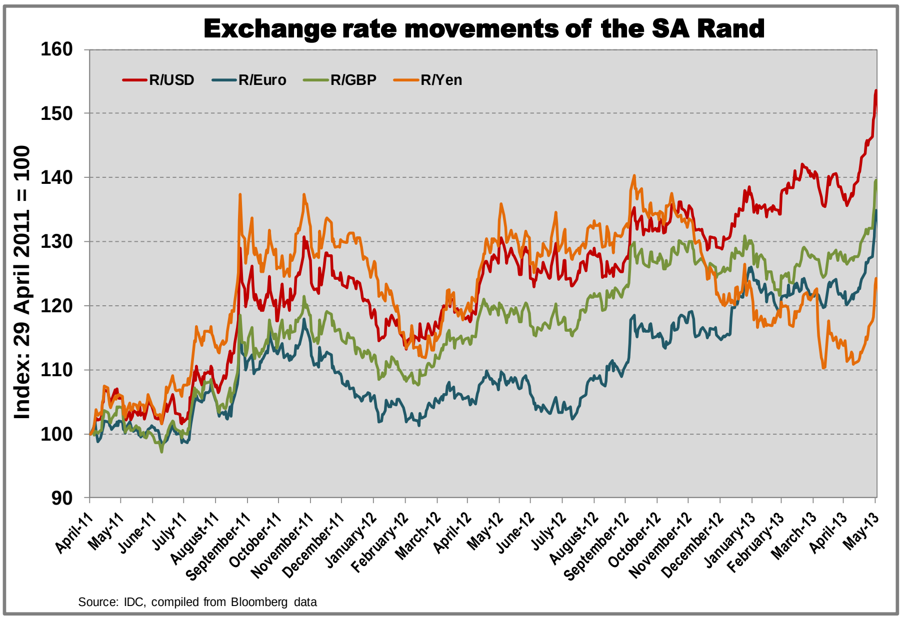
On the inflation front, consumer prices approached the 6% mark of the target band, with rising fuel, energy and high food prices behind this upward trend. The substantial depreciation of the rand has also pushed inflation higher through increased prices of imported goods. Despite the rising inflation trend, the Monetary Policy Committee (MPC) decided at its meeting of 23 May 2013 to leave the repo rate unchanged at 5%. Factors considered by the MPC included: subdued growth; insufficient job creation; the absence of demand-pull inflationary pressures; as well as the fact that core inflation (i.e. consumer price inflation excluding food, non-alcoholic beverages, petrol and energy) remains within the 3% to 6% target range. However, core inflation also edged higher over the past twelve months, reaching 5.2% in April 2013 compared to 4.5% a year earlier. The MPC expects a brief breach of the target band in the third quarter of 2013, when consumer price inflation is projected to average 6.1%. A downward trend should ensue, towards an average of 4.9% by the final quarter of 2015.



Source: IDC, compiled from Stats SA and SARB data

The MPC is expected to maintain the repo rate unchanged for quite some time, considering the inflationary pressures presently experienced and the likelihood of a weak currency providing further upward pressure on prices. In real terms, the repo rate has been in negative territory since September 2011, with the exception of two months in mid-2012.

Trading around R10.25 per US dollar on 11 June 2013, the rand had depreciated by 56% relative to its fairly strong closing level of R6.57 per dollar on 29 April 2011. It is clear from the accompanying graph that the dollar's relative strength has played a particularly important role in augmenting the rand's weakness against this currency. Nevertheless, the rand has weakened substantially against major currencies due to factors such as: the sizeable twin deficits on the government balance and the current account of the balance of payments; labour unrest and excessive wage demands; the strong reliance of South Africa's very open economy on external market developments, particularly the recession-stricken Eurozone and a slowing Chinese economy; a recent growth performance well below market expectations and a rather uncertain short-term outlook; excessively high unemployment and, among others, serious challenges encountered in stimulating job creation.



Under normal circumstances such currency weakness would be largely welcomed due to the increased price competitiveness of South African products in global markets. However, the poor state of traditional export markets and fiercely intense competition amongst global producers scrambling for a diminished marketplace, are likely to prevent the potential export gains from being fully realised.

A substantially weaker rand exchange rate will bring along adverse cost implications through more expensive imports, thereby raising the costs of doing business for companies relying heavily on imported machinery and equipment, intermediate products and/or raw materials. Although a depreciating currency may provide some protection against import competition in the domestic market, this automatic shield is likely to be eroded over time due to higher inflation.