

Economic Commentary

Weekly Monitor

Review of 20 to 24 September and preview 27 September to 1 October 2010

- **The rand rose to its strongest level since the beginning of 2008**
- **The current account deficit narrowed more than expected during the second quarter**
- **Growth in gross domestic expenditure eased during the second quarter**
- **Gold rises to a new record high**
- **US housing starts pick up, while new home sales remain near record lows**

Comment

The **rand** appreciated strongly against the US dollar and the British pound last week, supported by higher precious metal prices and the release of a smaller than expected current account deficit data for the second quarter of this year. After the release of the current account numbers on Wednesday, the local unit broke through the psychologically important R7 against the US dollar, its strongest trading level since January 2008, before pulling back to close at R7,06 on Thursday, up from R7,14 at the end of the previous week. The unit also gained significant ground against the British pound, closing at R11,05 on Thursday from R11,16 at the end of the previous week. However, it weakened to R9,40 from R9,32 against the euro during the period.

Bonds were firm in line with the rand, with the yields on the benchmark **R157 2015** and on the **3-, 5- and 10-year BESA actuaries** falling to 7,17%, 6,83%, 7,30% and 7,80% respectively on Thursday from 7,35%, 7,00%, 7,47% and 7,99% at the end of the previous week.

Money market rates eased further, with the **3-, 9- and 12-month JIBAR** ending at 5,94%, 6,13%, 6,28% and 6,39% respectively on Thursday, down from 5,96%, 6,14%, 6,29% and 6,41% at the end of the previous week.

Local equities continued to be supported by firmer global markets. The **FTSE-JSE all share index** closed at 28 714,8 on Thursday, gaining 1,1% from 28 413,6 at the previous week's close, with **industrials** and **financials** both up by 1,6% to end at 29 013,4 and 21 169,8 respectively, while **basic materials** increased by a marginal 0,1% to end at 26 653,8.

The **South African Reserve Bank's (SARB) Quarterly Bulletin (QB)** showed that the **current account deficit** narrowed to 2,5% of gdp in the second quarter of this year, its lowest level since the first quarter of 2004, from 4,6% in the first quarter, helped by a swing back into surplus on the trade account, higher travel receipts and lower dividend payments. The **trade account** recorded a surplus of R13,2 billion following a R12,9 billion deficit in the first quarter as exports rose faster than imports, with export values benefiting from the strong rise in international commodity prices, particularly in precious metal prices, while import values were contained by the firmer rand and low global inflation. **Merchandise exports** rose by seasonally adjusted and annualised 6,4% q-o-q, while **imports** increased at a slower pace, up by only 2,9%, with import volumes increasing by 3,1%, mainly on the back of the purchase of four military aircraft. The **terms of trade** (the ratio of export to import prices) improved by 5,1% after rising by 0,6% in the first quarter.

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The deficit in the **net service, income and current transfer account** narrowed significantly during the second quarter, boosted mainly by travel receipts related to the hosting of the 2010 FIFA World Cup and lower dividend payments. The deficit eased to R80,1 billion from R103,2 billion in the previous quarter, equivalent to 3,0% of gdp, its lowest level since the third quarter of 2005. The Reserve Bank estimated that total spending by foreigners amounted to R15 billion in the second quarter, with about R3,5 billion of that attributable to spectators attending the 2010 FIFA World Cup.

The **financial account** remained in surplus due to strong portfolio inflows as foreign investors continued to inject funds into emerging economies, particularly commodity exporters. Inflows (including unrecorded transactions) amounted to R21,8 billion from R48,6 billion in the previous quarter. The financial account surplus fell to 3,3% of gdp from 7,8% in the first quarter.

Net portfolio inflows remained strong at R25,5 billion during the quarter, with foreign investors pumping a net R28,4 billion into local markets during the quarter, although this was down from the R44,1 billion recorded in the first quarter. Net foreign portfolio inflows amounted to R179,6 billion in the first half of 2010, made up of R98,9 billion and R80,7 billion of net equity and bond purchases, respectively. Domestic investors sent only R2,9 billion to offshore markets in the second quarter, down from R5,5 billion in the first quarter.

Net direct investment outflows amounted to R2,5 billion, following net inflows of R4,6 billion in the first quarter. Inward investment by foreigners was R1,7 billion from R3,7 billion in the previous quarter, while South African residents invested R4,2 billion in other countries.

Net other investment inflows amounted to R8,6 billion in the second quarter from a R13,4 billion outflows in the previous quarter as foreign investors pulled R1,5 billion from the local economy, mainly in the form of deposits in local banks, while domestic investors repatriated R10,1 billion from other economies.

Growth in **gross domestic expenditure** eased to a seasonally adjusted and annualised 2,3% q-o-q during the second quarter following 12,1% q-o-q rise in the first quarter, mainly reflecting slower growth in household expenditure and a slower rate of change in inventory depletion.

Household consumption expenditure growth slowed to 4,8% over the quarter, but remained impressive following a 5,7% rebound in the first quarter. Spending on durable goods accelerated by a seasonally adjusted and annualised 37,8% q-o-q, and on semi-durable goods also performed well, growing by 10,6% off a high base. Spending on non-durable goods also rose strongly (up by 10,9% q-o-q), helped by the FIFA World Cup, which enhanced spending on goods such as fuel and power as well as medical services and pharmaceutical products. In contrast, spending on services contracted by 7,7% and this was attributed to weak spending by South Africans on travel and accommodation during the World Cup relative to increased spending by foreigners.

Government spending remained buoyant, boosted by the purchase of four military aircraft.

Fixed capital formation increased marginally by a seasonally adjusted and annualised 0,8% q-o-q following a 0,2% q-o-q increase in the first quarter, helped by some rise in private sector (up by 0,4% following sharp declines throughout 2009 and early part of this year) and public corporation spending (up by 6,5% q-o-q, although the growth rate moderated from 7,4% q-o-q in the first quarter), which offset decline in investment by government (down by 7,2% q-o-q following an 8% drop in the first quarter).

The rate of decline in **real inventory investment** eased further to R7,2 billion during the second quarter from R8,7 billion in the first quarter, mainly due to a slower rundown of inventories in the manufacturing, trade and transport sectors in line with improved economic conditions.

Weak credit conditions helped the **household debt to disposable income ratio** to edge down to 78,2% during the second quarter from 78,7% during the previous quarter, while the debt service cost to disposable income edged down to 8,0% from 8,2%. Household disposable income grew by 4,8% during the second quarter following a 5,1% increase in the previous quarter.

According to Statistics South Africa, growth in **retail sales** picked up further to 7,9% y-o-y in July, its fastest annual increase since July 2007, after growing at a revised 7,6% y-o-y in June. Retail sales probably benefited further from World Cup spending as well as improved consumer confidence. Sales at general dealers, which make up around 40% of retail sales, rose by 9,2% y-o-y, after recording growth of 8,3% y-o-y in the previous month. Clothing and footwear retailers recorded double-digit sales growth for a second consecutive month, while sales of

pharmaceuticals and personal care products jumped sharply on an annual basis, increasing by 13,9%. In contrast, sales of hardware and paint continued to fall over the year, declining by 3,3%.

Statistics South Africa's **Quarterly Employment Statistics (QES)** showed that the number of people employed in the formal non-agricultural business sector increased by 41 000 or 0,5% between the first and second quarter of this year, mainly boosted by the host of the FIFA World Cup. On an annual basis, the rate of decline in the number of employed people eased to 1,4%, the lowest since the last quarter of 2008, from 2,9% in the first quarter. Gross earnings increased by 1,8% over the quarter to R296 526 million over the quarter, and increased by 14,6% on an annual basis.

Domestic preview for the week: 27 September to 1 October 2010

Table 1 : Domestic releases

	Release	Period	Consensus forecast	Nedbank forecast	Previous
Monday					
Tuesday					
Wednesday	Consumer inflation	August	3.6% y-o-y 0.3% m-o-m	3.5% y-o-y 0.1% m-o-m	3.7% y-o-y 0.6% m-o-m
Thursday	Money supply	August	4.5% y-o-y	4.5% y-o-y	3.7% y-o-y
	Private Sector Credit Extension	August	2.7% y-o-y	2.7% y-o-y	2.0% y-o-y
	Producer inflation	August	7.7% y-o-y 0.4% m-o-m	7.3% y-o-y 0.4% m-o-m	7.7% y-o-y 1.3% m-o-m
	Trade balance	August	R-1,0 billion	R-1,0 billion	R2,0 billion
Friday	Kagiso PMI	September	51.2	-	50.3

Source: Nedbank Group Economic Unit and Bloomberg

Key economic releases scheduled for this week include **inflation** and **credit** numbers for August. We expect that **consumer inflation** will ease further to 3,5% y-o-y in August from 3,7% y-o-y in June, helped by the strength of the rand and weak domestic demand. Credit growth is likely to improved to 2,7% on an annual basis, coming off last year's low base. However, demand for credit is likely to have remained relatively weak over the month given tight lending conditions and cautious households.

International

Better-than-expected US economic data helped US equities end the week higher. The **Dow Jones**, the **NASDAQ** and the **S&P500** rose by 2,4%, 2,8% and 2,1% respectively, to close at 10 860,3, 2 381,2 and 1 148,7. The **UK FTSE 100**, the **German DAX** and the **French CAC** also ended the week higher, closing at 5 598,5, 6 298,3 and 3 782,5, up by 1,6%, 1,4% and 1,6% respectively. The **NIKKEI 225** fell by 1,6%, to close at 9 471,7.

The **US dollar** weakened further against major currencies last week on concerns that the US Federal Reserve may embark on another round of quantitative easing. The US unit fell to \$1,3489 and \$1,5825 against the euro and the British pound from \$1,3034 and \$1,5619. The Japanese yen strengthened against the dollar, closing at ¥84,26 from ¥85,8.

The price of **gold** rose to a new record high of \$1 300,05 per ounce last week on the back of a weak dollar and concerns that the Federal Reserve might undertake further quantitative easing. The price of gold rose by 1,7% to close at \$1 296,9 per ounce, while the price of **platinum** ended at \$1 645,3 per ounce, up by 1,8%. **Brent crude oil** closed at \$78,87 per barrel, up by 1,3%.

US housing starts rose more than expected in August, increasing to their highest level in four months, rising by 10,5% m-o-m, to a seasonally adjusted annualized 598 000. New building permits, a leading indicator of conditions in the housing market, rose by 1,8% to 569 000. **New home sales** stalled in August, remaining near record lows. Over the year, sales were down by 29%. Low interest rates have failed to boost the property market, which remains hampered by high unemployment and oversupply. **Initial jobless claims** rose by 12 000 for the week ending 18 September to 465 000. The market had expected a slight increase to 455 000. The four-week moving average, a less volatile measure of conditions in the labour market, fell by 3 250 to 463 250. The **Conference Board's leading indicator index** rose more than expected in August, increasing by 0,3% m-o-m, following a 0,1% m-o-m gain in July. **New orders of durable goods** fell by 1,3% m-o-m to \$191,2 billion, the third monthly decline in four months. New orders of transportation equipment, recorded the largest decline, falling by 10,3% m-o-m to \$46,6 billion.

The **Eurozone's manufacturing PMI** fell to a six-month low of 55,1 in September, down from 56,7 in August, due to a further slowdown in new orders. This suggests that conditions in the manufacturing sector will continue to slow in the remaining months of the year. The **German Ifo business confidence index** rose to its highest level since 2007, increasing to 106,8 from 106,7 in August. However, an index measuring business' expectations for the next six months slipped to 103,9 from 105,2.

International preview for the week: 27 September to 1 October 2010

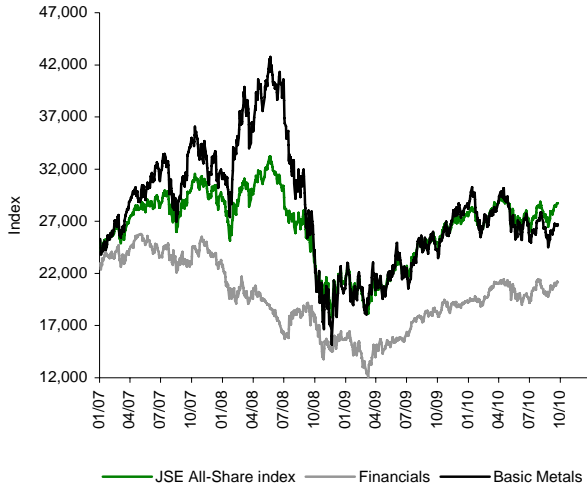
Table 2 : International releases

Country	Release	Month	Forecast	Previous
United States				
Monday				
Tuesday	Consumer confidence	September	52,5	53,5
Wednesday				
Thursday	Initial jobless claims	Week ending 24 September	460 000	465 000
	Gdp - revised	2010 Q2	1,6% q-o-q	1,6% q-o-q
	Chicago PMI	September	56	56,7
Friday	Consumer spending	August	0,3% m-o-m	0,4% m-o-m
	University of Michigan consumer confidence	September	67	66,6
Eurozone				
Monday				
Tuesday				
Wednesday				
Thursday	Consumer inflation	August	1,8% y-o-y	1,6% y-o-y
Friday	Unemployment	August	10%	10%
United Kingdom				
Monday				
Tuesday				
Wednesday				
Thursday				
Friday	Manufacturing PMI	September	53,8	54,3
Japan				
Monday				
Tuesday	Tankan survey	2010 Q3	6	1
Wednesday	PMI - manufacturing	September		50,1
Thursday	Consumer price index	September	-1% y-o-y	-1,1% y-o-y
	Unemployment	September	5,2%	5,2%
Friday				

Source: Reuters

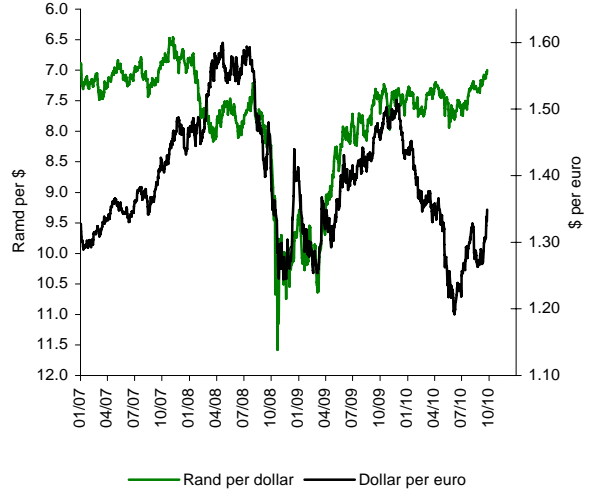
Overview of the week: 20 to 24 September 2010

Chart 1 : JSE All share Index



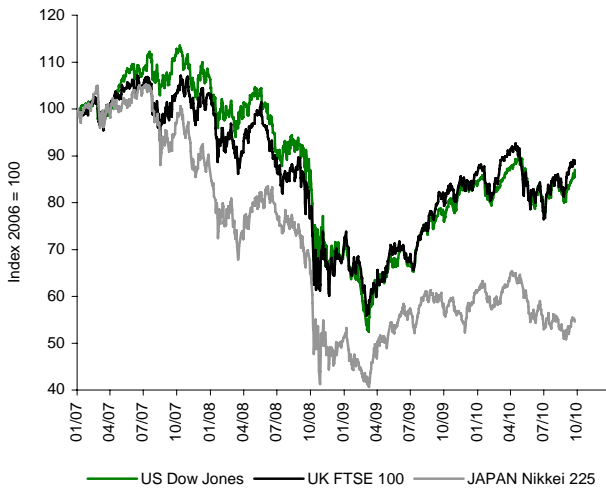
Source: Reuters

Chart 2 : Currency markets



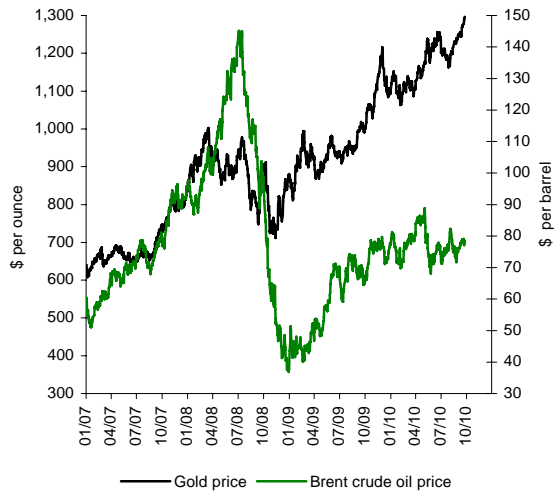
Source: Reuters

Chart 4 : International equity markets



Source: Reuters

Chart 3 : Commodity prices



Source: Reuters

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