LIMPOPO

PROVINCIAL GOVERNMENT

REPUBLIC OF SOUTH AFRICA

PROVINCIAL TREASURY

Quarterly Economic Bulletin 2017/18 Q 3

The heartland of southern Africa - development is about people

Foreword

The Limpopo provincial Quarterly Economic Bulletin is presented at a time where the South African economy has sustained positive economic growth in two consecutive quarters. This trajectory was above market expectations. Much of the growth was supported by the primary sector of the economy with disappointing performance in the tertiary sector. The Limpopo provincial economy is expected to perform relatively well in 2017 given that 28 percent of the local economy is attributed to the mining sector, which has improved in its productivity in the second and third quarter of this year.

Much economic growth is desirable so that the multiplier effects could deal with the socio-economic challenges in the province. The rising unemployment and poverty levels could be mitigated by an inclusive and buoyant economy. However, macroeconomic vigour requires appropriate policy balance; fiscal and monetary policy readjustments. Although fiscal consolidation is necessary to salvage the country from adverse credit rating outcomes, albeit it should not restrict resources directed to investment expenditure; which is the stimulant of economic growth.

The Gini Coefficient along with the Palma ratio still indicates the wide income inequality in the province. Joblessness and poverty are the major obstacles in closing the income gap. Tourism and the Agricultural sector have proven to be key sectors that could play a major role in narrowing the income gap in the country; as the two sectors have a high elasticity of absorbing low and unskilled workers.

The Limpopo Development Plan (LDP) conspicuously outlines economic drivers in the province. The province should merge development plans around the LDP imperatives and maximise on leveraging from each department's resource implementation.

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LIMPOPO PROVINCIAL TREASURY

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1 Introduction

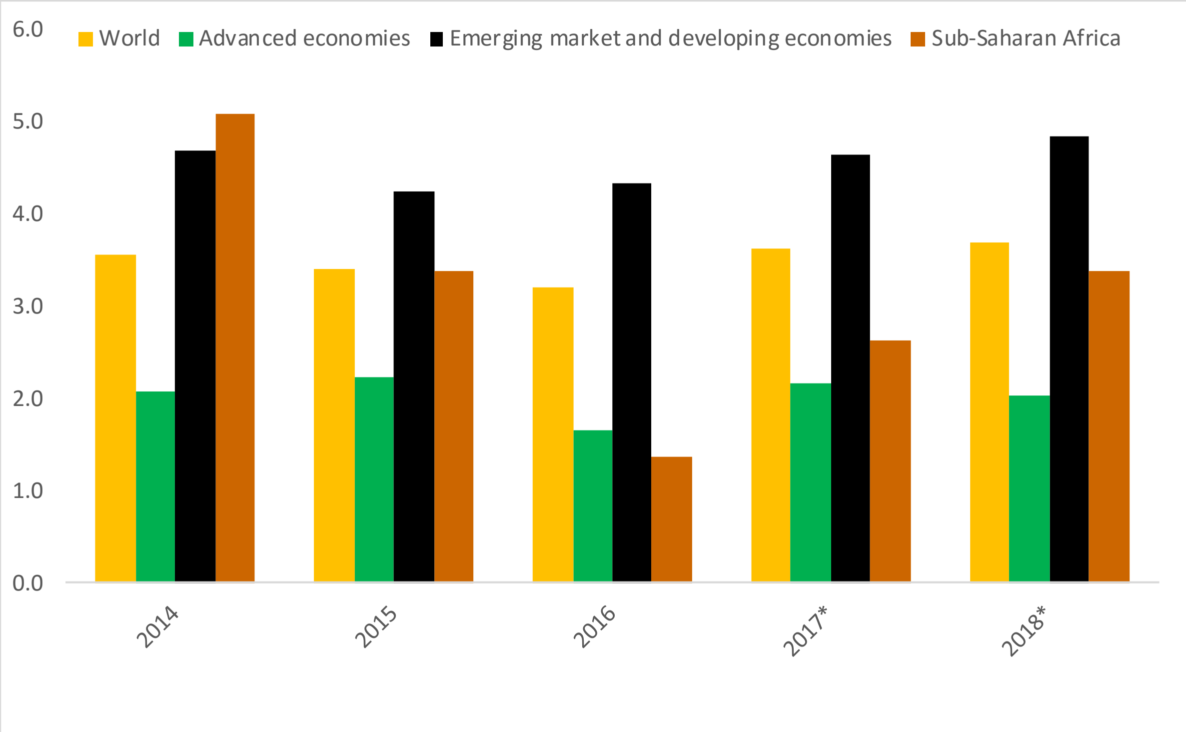
World economy remains moderate, influenced by subdued aggregate demand on commodities while economies such as China are undergoing economic rebalancing. Despite the passive economic prospects, South Africa recorded positive economic growth over two consecutive quarters mainly driven by the agricultural and mining sectors of the economy. However, the growth is amplified by the fact that the agricultural sector's growth is attributed to its low base that was as a result of the 2016 Al Nino phenomenon.

It is evident that the low economic growth is affecting the fiscal sustainability of the country. Government spending is growing year on year, however, economic growth and revenue collection is not growing concomitantly, raising the risk of widening government debt to GDP ratio. Fiscal consolidation and stringent fiscal discipline may save the country from adverse sovereign credit ratings and aid in boosting investment and consumer confidence in the medium to long run.

2 Global Overview

According to figure 1, World economy grew at 5.6 percent in 2007 prior the global financial crisis. The growth trajectory was interrupted and many economies have not fully recovered from the 2009 financial crisis leading to world economy growing at 3.2 percent in 2016. Economic activity in advanced, developing and Sub Saharan Africa is forecast to accelerate in 2017, to 2.2 percent and 4.9 percent and 2.6 percent respectively. While the world economy is projected to grow at 3.6 percent in 2017 and 3.7 percent in 2018.

Figure 1 World GDP Growth



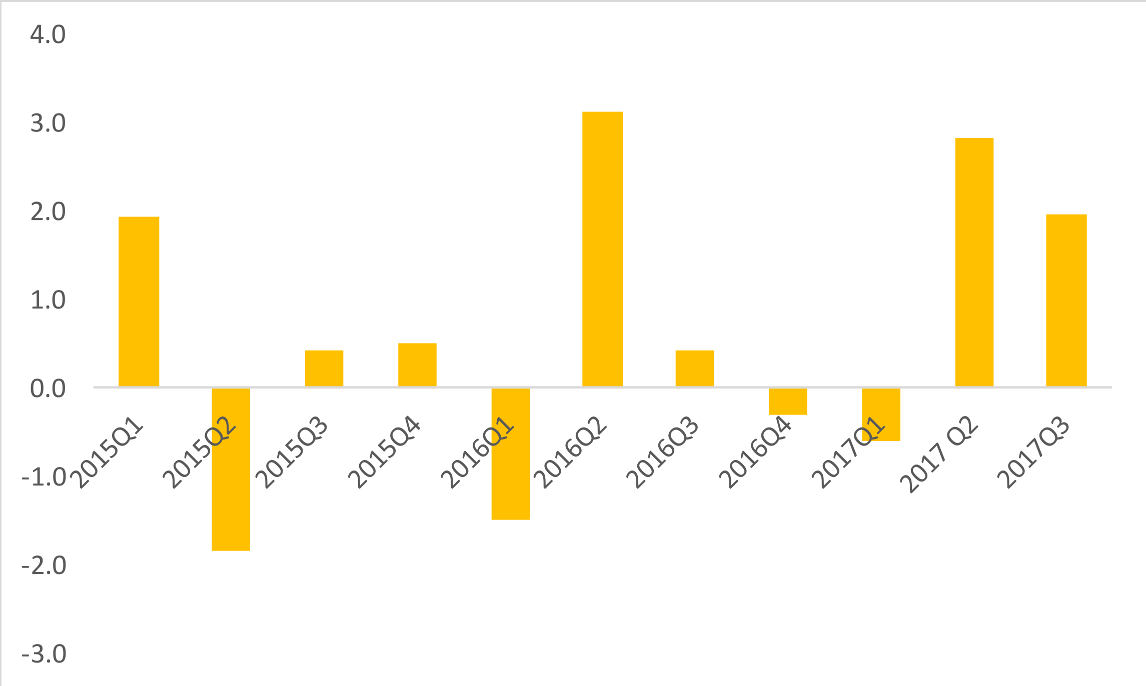
IMF, Oct 2017

3 National Overview

3.1. South African Economic outlook

The South Africa's Gross Domestic Product (GDP) grew by 2.0 percent in the third quarter of 2017, performed poorly compared to the previous 2.8 percent. According to StatsSA agriculture, mining and manufacturing were the main drivers of the expansion, while there was a contraction in general government services resulting from low employment numbers in the public sector.

Figure 2 SA GDP Constant 2010 prices, seasonally adjusted



StatsSA Q3 2017

The agricultural sector has boosted its performance as expanded by 44.2 percent in the third quarter comparing to the second quarter where it recorded an increase of 38.7 percent. These growth number is of a low base because of the drought in South Africa. The mining and manufacturing also were major contributors to economic growth in the third quarter, a good production from gold and platinum sector increased by 6.6 percent, meanwhile 4.3 percent rise was recorded from manufacturing which increased by both petroleum and metal products. The financial and business sectors also grew by 1.2 percent, helped by an increased activity in financial mediation, insurance and auxiliary services and also recorded positive growth in personal services (0.9 percent) and transport and communication (0.5 percent).

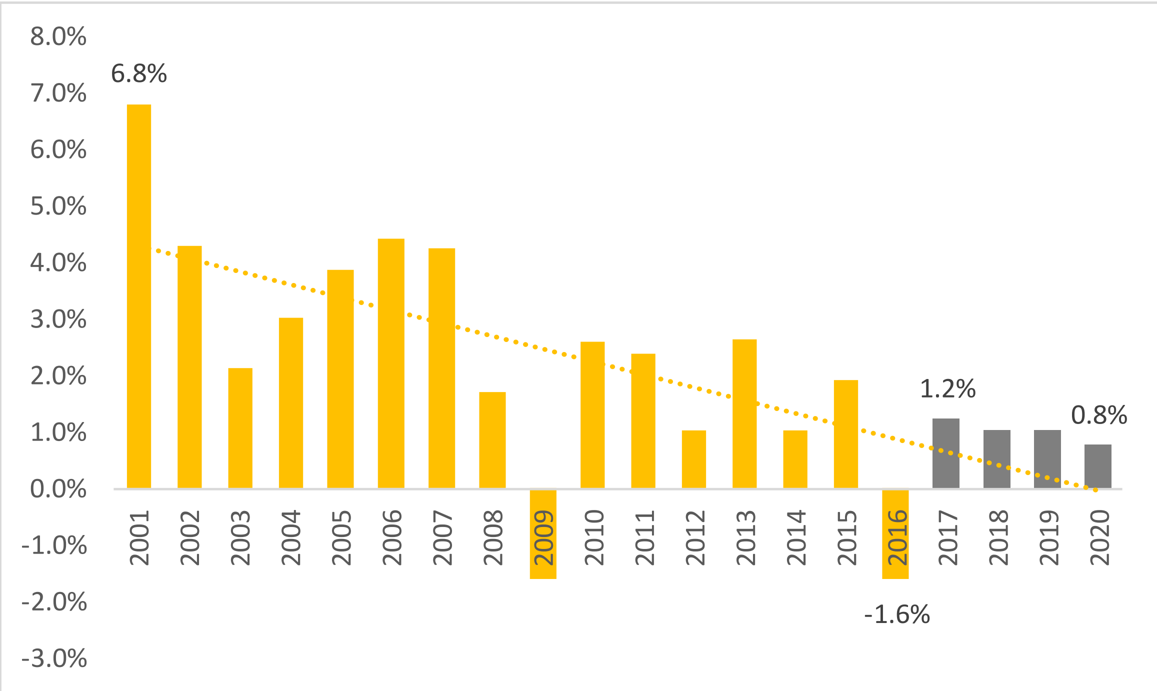
It is a concern that the tertiary sector, supposedly the growth engine of the South African economy, performed so poorly.

4 Provincial Overview

4.1. Limpopo Economic Outlook

The GDP growth rate as measured by the Gross Domestic Product (GDP) at market prices for 2016 in Limpopo was recorded at -1.6 percent, following a 1.9 percent growth in 2015. The negative growth was caused by the relentless drought, deteriorating commodity prices and volatile rand exchange rate. The mining sector also had a dismal growth performance declining by -5.9 percent. The average growth in the mining sector between 1996 and 2016 was only 1.5 percent per annum (Global Insight, 2016) The Limpopo economic growth is forecast to grow at 1.2 percent in 2017 by the Limpopo Provincial Treasury, which is higher than the projected national growth rate of 0.7 percent. The forecast depends primarily on the performance of the mining sector during 2017. However, the projected growth rates of the province are significantly lower than the anticipated 3 percent in the Limpopo Development Plan (LDP).

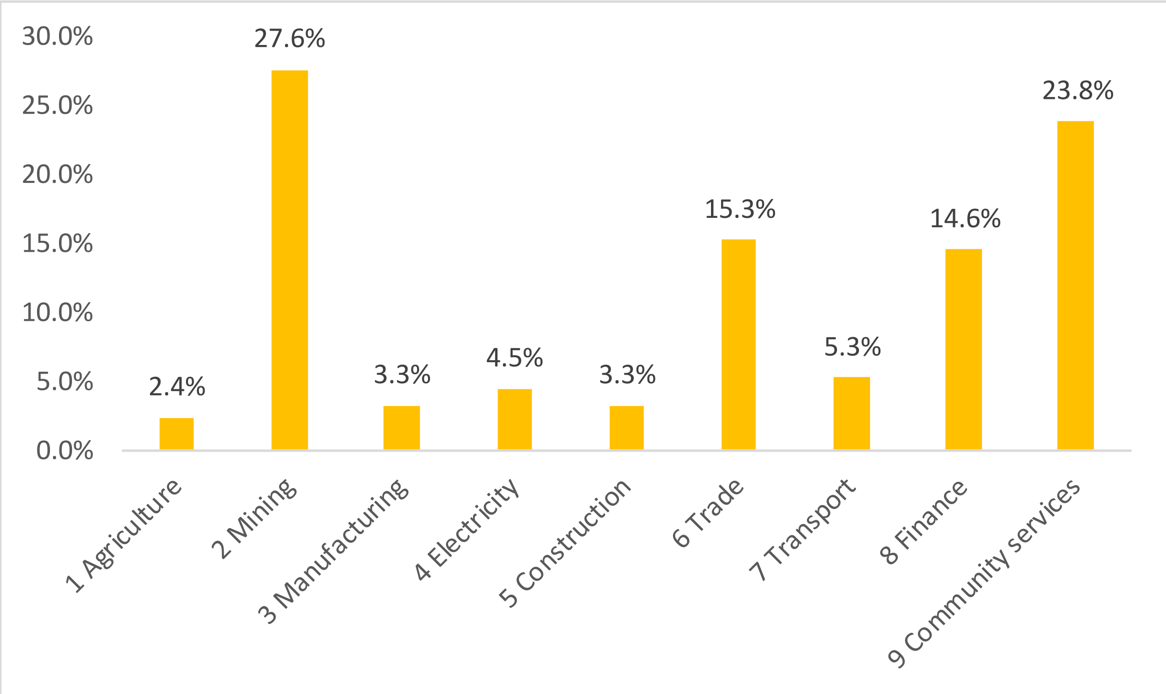
Figure 3 GDP Average annual growth (Constant 2010 Prices)



Regional Explorer 2016 (Forecast by Limpopo Treasury)

The provincial economy is predominantly driven by two main sectors being Mining and Community services contributing 27.6 percent and 23.8 percent respectively. They are followed by Trade and Finance contributing 15.3 percent and 14.6 percent respectively. On the other hand, the Agriculture, Manufacturing and Construction sector have the lowest contribution towards provincial GDP at 2.4 percent, 3.3 percent and 3.3 percent respectively.

Figure 4 Limpopo Sector's share of regional total GVA (percent) 2016



Regional Explorer 2016

Limpopo is strategically located to be the trade and logistical hub of Africa; at least in the Sub Saharan Africa in the long term. This is acknowledged in the LDP which promotes the importance of growing the secondary sector of the provincial economy. Africa is one of the fastest growing regions and thereby a possible stimulant to South Africa's and provincial exports.

It is also important that the provincial government promote the services sector, were possible. The provincial government plays an important role in promoting the Tourism sector. An overview of this sector will now be provided.

5 Tourism Overview

5.1. Global Tourism

Globally, tourism remained resilient over the last seven (7) years with an average 4 percent growth rate. The industry has proven to be the most resilient economic sector worldwide and remains one of the sectors known to address some of the world´s most pressing challenges, including economic growth, inclusive development and environmental preservation. In 2016 1.2 billion tourist travellers were recorded, a 4.6 million increase since 2015. This resulted in Tourism contributing to 30 percent of the services exports on global level. Asia and the Pacific regions demonstrated renewed strength receiving 9 percent more international arrivals in 2016, the highest growth recorded across the worlds' regions. In the Americas, international arrivals increased by 4 percent, led by Central America and South America

5.2. National Tourism

Within the South African context tourism forms part of the sectors that could potentially be the new "gold" in the economy. South Africa received 10 million international tourists in 2016 (12.8 percent increase) and recorded 39.4 million domestic day trips, a decrease from 44.4 million trips recorded in 2015. Although a decrease in the total domestic trips were recorded, the domestic indicators e.g. the direct spend, length of stay, bed nights sold, geographical spread and seasonality showed a steady increase since 2015. The National Tourism Sector Strategy's mission is to increase the number of tourists through implementing the 5 in 5 strategy over the next 5 years (5 million tourists in 5 years). The objective is also to increase the current direct contribution of tourism to the economy from R118 billion to R302 billion by 2026 through collaborative planning, and the implementation of agreed priority actions. This is a 3.0 percent contribution to the total national GDP. The current total contribution of tourism to the national GDP is recorded at 375.5 billion and the number of direct jobs created (mostly by international visitors) is 702 824 jobs. The jobs supported by the sector is estimated at 1.5 million jobs.

5.3. Limpopo Tourism

Limpopo received 1.5 million International tourist arrivals in 2016 which represent a 15.4 percent share in national arrivals. The main international source markets that visited Limpopo is within the SADC region Zimbabwe, Botswana and Mozambique and in the other regions the USA, Germany, UK and Netherlands. The United States was in particular identified as a future market in reaching the 5 in 5 targets. This is mainly due to the potential of Limpopo as hunting and safari destination.

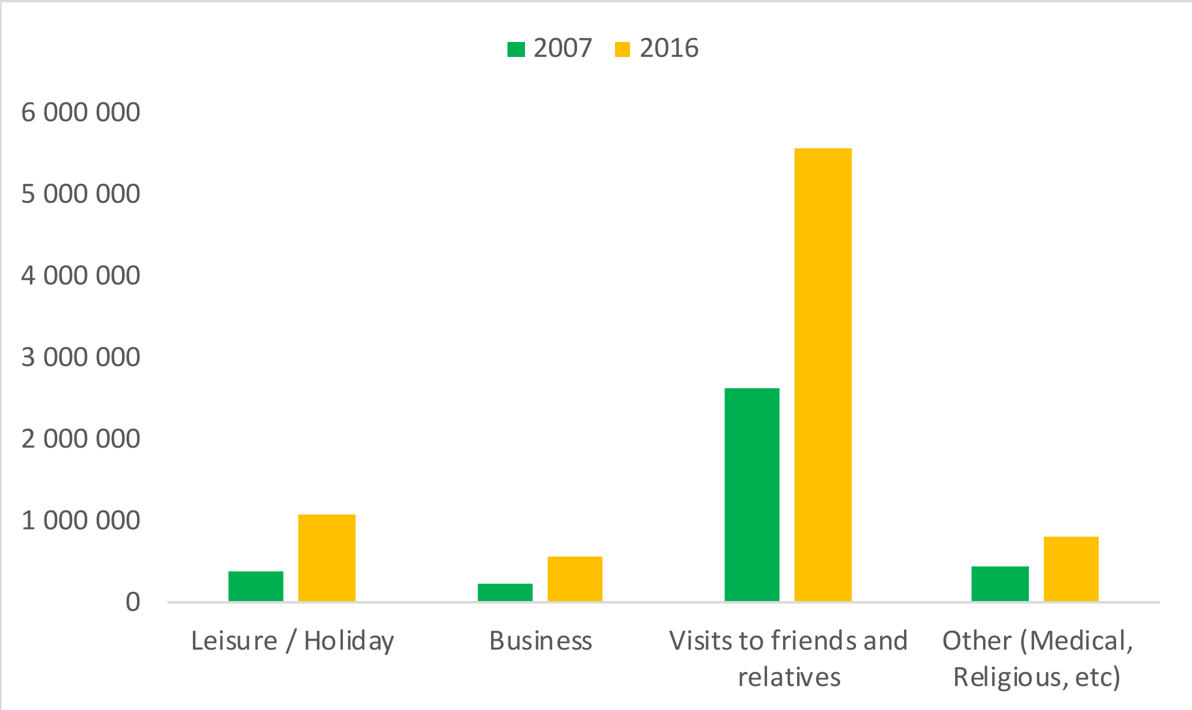
While the domestic market showed a decrease in numbers on national level, Limpopo remains to be the leading province. The province resiliently increased its market share on the domestic front and recorded 8.3 million travellers in 2016. While Gauteng and Western Cape joined Limpopo as the most popular destinations for day traveller's, overnight traveller's mostly preferred visiting Limpopo (approximately 4.7 million while an average of 3.6 million were recorded as leisure tourists). Most tourists undertook overnight trips mainly to visit friends and relatives and preferred using a car or taxi. They mostly used unpaid accommodation and stayed with friends and relatives. Of all the overnight trips undertaken, more than 80 percent lasted an average of one week at their destination. Day trips were largely undertaken for shopping, followed by visiting friends and relatives. Tourists that undertook overnight trips were mostly for leisure, attending funerals and visiting friends and relatives.

Figure 5 Limpopo Growth in Tourism (using bednights) by origin

Regional Explorer 2016

The purpose of most trips are to visit family and friends. Followed by holiday and other purposes such as medical or religious purposes. The tourism sector contribution is steadily increasing in the province, however the sector can do better by attracting both international and domestic tourists

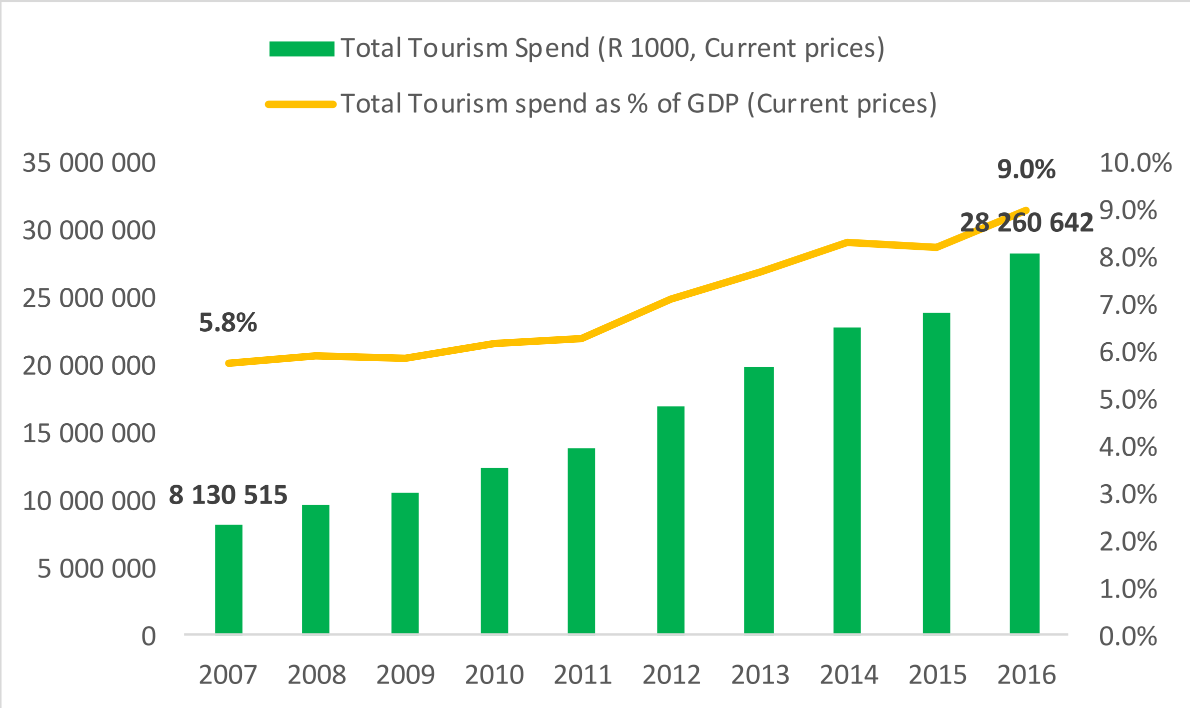
Figure 6 Limpopo number of Trips by Purpose of trip



Regional Explorer 2016

In 2016, tourism contributed R28.0 billion to the provincial GDP translating to 9.0 percent, which grew from 5.8 percent contribution to the provincial GDP in 2007.

Figure 7 Total Tourism Spend (R 1000, Current prices)



Regional Explorer 2016

On the policy platform the Department of Economic Development, Environment and Tourism is in the process to re-evaluate the Limpopo Tourism Growth Strategy to assess the relevancy of the six tourism clusters within the identified markets and to realign its focus and interventions to reach its new targets as set in the 5 in 5 national marketing strategy.

To achieve these targets, the following critical factors should be addressed:

1. **An improved road network**. The provincial heritage icons and cultural settings are mainly found in the rural parts of Limpopo. To unlock these areas and routes as tourist destinations the current road network requires serious attention. The department commenced with a Rural Tourism/Township Tourism initiative that will focus on Homestays and route development. This depends on good road access.

2. **Affordable airlift**. To open routes between destinations within Limpopo, with neighbouring provinces and SADC countries air access should be a priority.

3. **Access to affordable and quality standard accommodation for the growing domestic market to increase the length of stay**. The commercialization of state owned properties to enhance tourism especially in the nature reserves should be prioritized.

4. **Safety and security**. The safety of tourists traveling to Limpopo should serve as an important agenda point on the relevant forums. A large number of international tourists visiting Limpopo are self- drive tourists and are increasingly exploring the rural and cultural offerings of the province. It is a growing market that Limpopo can benefit from. Effective safety measures and awareness programs should be put in place.

5. **Technological revolution**. Limpopo is not keeping track with the current technological revolution. Our marketing platforms need constant updates and our wildlife destinations requires internet access. This remains a serious challenge and has a tremendous impact on the growth of tourism.

6 Fiscal Framework

6.1. National Fiscal framework

Over the past four years, government has followed a path of measured fiscal consolidation, aiming to stabilise the debt-to-GDP ratio by reducing spending and introducing tax increases. This strategy met with some success, reflected in a narrowing primary deficit. But debt has continued to rise as a share of GDP as economic growth rates have declined. During the 2017/18 financial year, a sharp deterioration in revenue collection and further downward revisions to economic growth projections have significantly eroded government's fiscal position.

Government is highly aware of the dangers of unchecked debt accumulation. Debt-service costs are the fastest-growing category of expenditure, crowding out social and economic spending. By 2020/21, nearly 15 percent of main budget revenue will be spent servicing debt. The National Treasury estimates that stabilising gross debt below 60 percent of GDP over the coming decade will require spending cuts or tax hikes amounting to 0.8 percent of GDP. In 2018/19, 0.8 percent of GDP would amount to R40 billion.

As a result of revenue shortfalls, the consolidated budget deficit for 2017/18 is expected to be 4.3 percent of GDP, compared with a 2017 Budget estimate of 3.1 percent. The main budget deficit, which determines government's net borrowing requirement, will be 4.7 percent of GDP this year. In contrast to projections set out in the last budget, the revised projection is for the deficit to remain at this elevated level over the medium term. On this estimate, gross national debt is projected to continue rising, reaching over 60 percent of GDP by 2022.

Table 1 Fiscal framework aggregates

	2016/17	**2017/18**	**2018/19**	**2019/20**	**2020/2021**
R billion/Percentage of GDP	**Outcome**	**Revised**	**Medium-term estimates**		
Revenue	1 298.20	1 363.30	1 477.50	1 594.20	1 707.30
(Percent)	29.50	29.50	29.50	29.50	29.50
Expenditure	1 445.70	1 566.60	1 670.60	1 802.30	1 935.10
(Percent)	32.80	33.50	33.60	33.90	33.90
Budget balance	-147.5	-203	-193.1	-208.1	-225.8
(Percent)	-3.30	-4.30	-3.90	-3.90	-3.90
Total gross loan debt	2 232.90	2 530.50	2 829.60	3 094.20	3 415.60
(Percent)	50.70	54.20	57.00	58.20	59.70

Source: National Treasury 2017

In this context, government faces difficult choices. To offset revenue shortfalls and reduce borrowing, the contingency reserve has been pared down to R16 billion over the next three years. This leaves government little room to manoeuvre if risks to the expenditure ceiling materialise. Beyond this, it is likely that some programmes will need to be eliminated, or their funding reduced. South Africa's stated policy aspirations and its social needs far exceed available public resources. Moreover, there is little space for tax increases in the current environment. Any new policy proposals, or expansion of existing programmes, should address only the most effective and necessary interventions.

Government remains committed to operating within the expenditure ceiling over the medium term. In the current year, however, the recapitalisation of SAA and the South African Post Office put the ceiling at risk of a R3.9 billion breach.

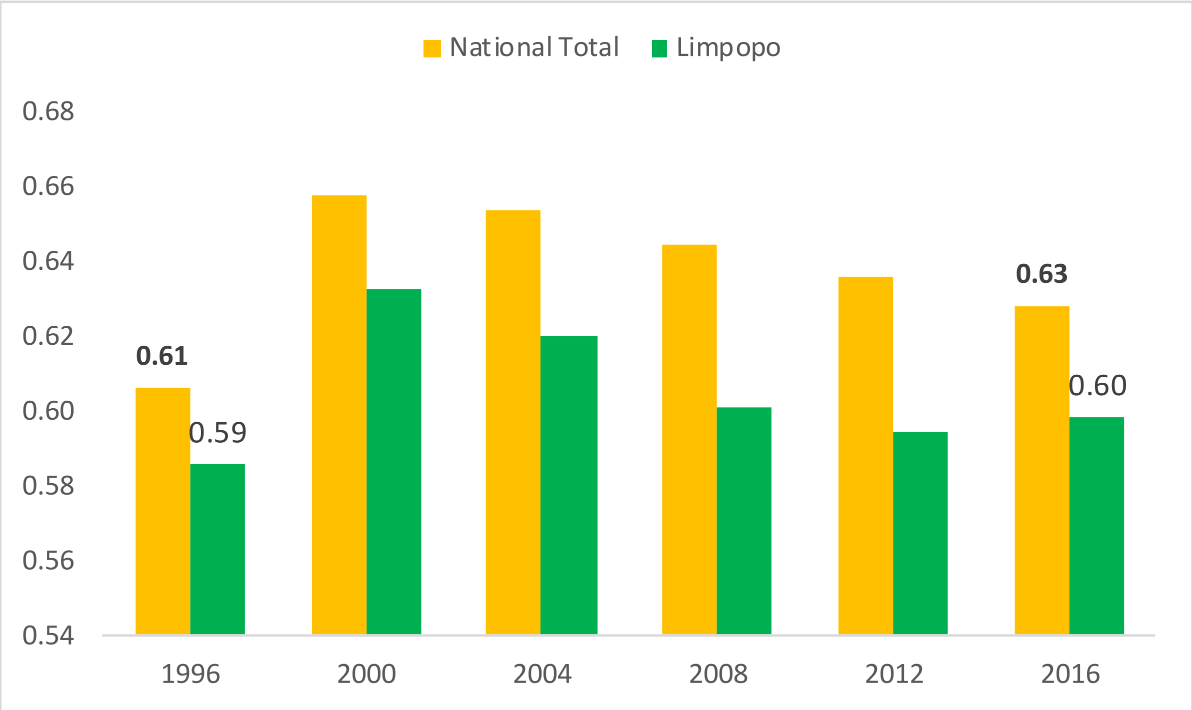
According to National Treasury, there are several risks to the fiscus over the period ahead:

1. The economy and revenue could underperform compared to the projections as indicated in the budget documentation of National Treasury. The GDP growth outlook may be improving, but the relationship between growth and revenue collection could deteriorate further. Fears exist that the public is becoming less inclined to comply with paying taxes.
2. Strains and imbalances within the public finances may become more pronounced. The public-sector wage bill has increasingly crowded out other spending and limited government's ability to increase public employment.
3. Debt-service costs are set to absorb a rising share of revenue.
4. Several years of fiscal restraint have left funding gaps in both infrastructure and social services, reflected in the build-up of unpaid accounts and financial imbalances.
5. Continued financial deterioration of major state-owned companies is a clear and substantial danger to the public finances.

7 Income Inequality

Since 2000 National and Provincial Gini Coefficients have been trending downwards but marginally. This is an indication that the income inequality in South Africa and Limpopo is improving marginally. The South African and provincial Gini Coefficient is above 0.60 indicating presence of income inequality. If the Gini Coefficient is equal to zero it means that incomes are distributed in a perfectly equal manner, indicating a proportional distribution of income between high and low income earners in the population. From the below diagram, there is presence of income inequality in both the country and in the province. The income distribution in Limpopo is more equal than on national level.

Figure 8 Limpopo Gini Coefficient



Regional Explorer 2016

Gini coefficient has dominated the inequality indicator landscape. However, lately many critical voices have risen, saying that Gini coefficient cannot offer any answers on the question of which group is benefitting more or less when the income inequality improves. However, this is the question that seems to concern the most people. It is not primarily about all changes of income distribution; it is about the relative changes that is being experienced by the low income earners versus the high income earners. It is about changes to the situation of the poor and the rich.

The Gini coefficient on the other hand weights changes to the income distribution just the same, whether they happen at the top, at the bottom or in the middle of the income scale. Thus, compared to a common understanding of inequality the index is over-sensitive to changes in the middle of the distribution while being insensitive to changes at the top and bottom of the distribution. However, it is still the most used indicator when it comes to the task of measuring income inequality. The popularity of the Gini index might be explained by the ease of understanding (what the coefficient indicates and how it is computed), making explanation, communication and dissemination relatively easy.

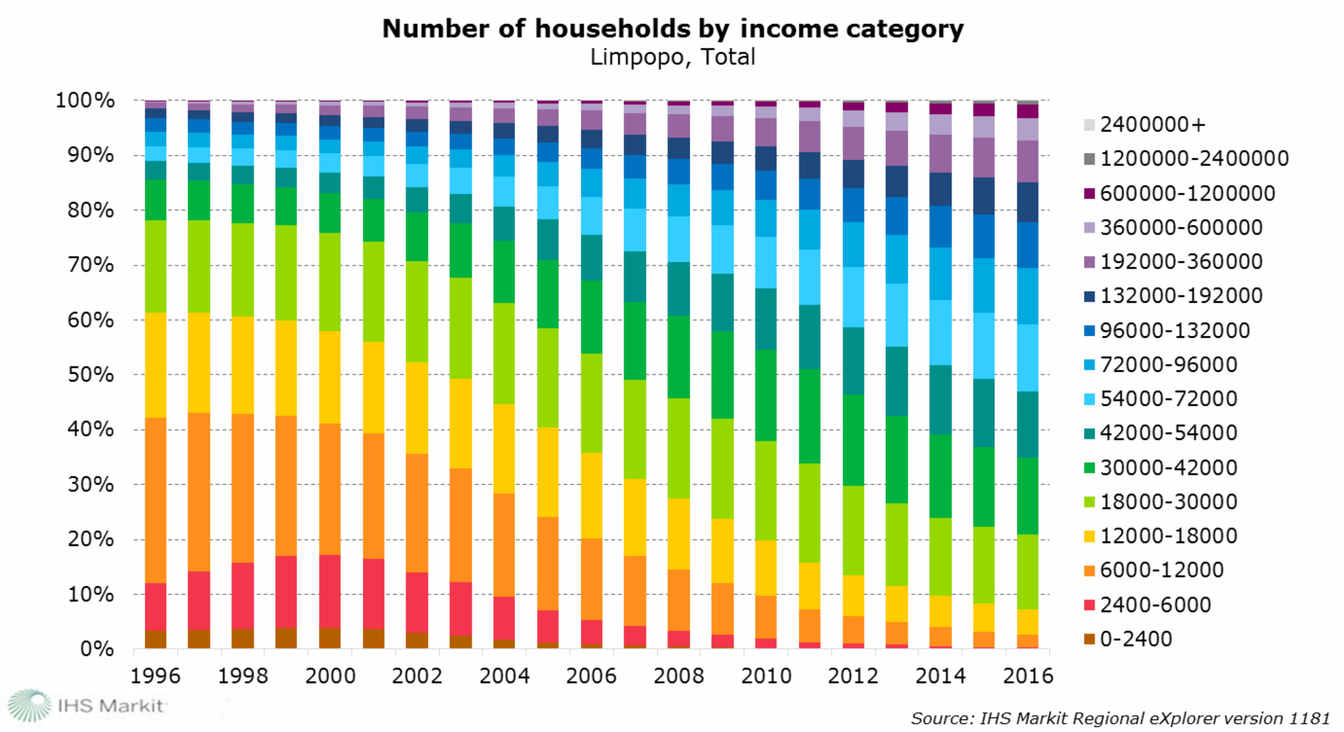
However, the Palma ratio is increasingly being used in order to tackle the knowledge gap about the top and the bottom of the income scale. This ratio is defined as the ratio of the richest 10 percent of the populations Gross National Income share divided by the poorest 40 percent's share. This means, in a society with a Palma ratio of 4, the top 10 percent is grabbing four times the income of the bottom 40 percent. Contrarily to Gini coefficient, the Palma ratio therefore measures only changes to the distribution of income if it either affects the lowest earners or the highest earners and therefore relates better to the common understanding of inequality.

The Palma ratio for the Limpopo province has been calculated for 2006 and 2016 respectively. In 2006 the top 10 percent of the income earners in Limpopo earned 5.89 times more than the bottom 40 percent. This ratio improved slightly to 5.4 in 2016.

The bottom 40.0 percent of income earners increased their share of income from 8.6 percent in 2006 to 9.0 percent in 2017. This is a relatively small increase taking into account that the national budget in South Africa is focused on addressing this income inequality by providing more services to the poor. South Africa also has a progressive tax system that seeks to address the same issue. Although the poor experienced an increase in terms of access to basic services the impact on the income distribution was insignificant.

As expected theoretically the middle 50 percent of income earners managed to at least slightly improve their share of total income. This is despite the significant improvement in income levels in Limpopo as indicated in fig 9. The middle 50 percent share increased from 40 percent in 2006 to 42.25 percent in 2017.

Figure 9 Income levels in Limpopo



The conclusion is that government policy should continue to focus on addressing the plight of the bottom 40 percent. The most important contributor to a better income distribution will be higher job creation.

8 Conclusion

Economic growth may not be a panacea of the development challenges the country and the province is facing, yet it is a necessary condition to create jobs, government revenue and general development. The provincial administration should champion the attainment of the LDP plans with strong private sector participation to grow the provincial economy.

It is important that all tiers of government and public entities should employ fiscal discipline to avert exposing the country to growing debt and thereby increasing the chances of credit downgrade.

Government should support accelerated economic growth and labour absorbing development projects to deal with joblessness thereby addressing the income inequality in the province.