LIMPOPO

PROVINCIAL GOVERNMENT

REPUBLIC OF SOUTH AFRICA

PROVINCIAL TREASURY

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Foreword

This quarter quarterly economic bulletin is published at the time when the economy of the country is faced with the challenges of technical recession. Technical recession is defined as two consecutive quarters of declining gross domestic product (GDP) and points to a prolonged slowdown in economic activity, which stuns job creation and damps investment. Following the revisions to growth figures for 2017, this makes it the first recession since the global financial crisis. The contraction was driven largely by the primary sector, with agriculture offsetting the positive growth in the mining sector. While the secondary sector growth was dampened by the contraction in the manufacturing sector.

The slow growth in the provincial and national economy pose a risk for the provincial government as it is trying to meet the needs of its citizenry as a growing economy would enable the government to collect the taxes required to fund better education and healthcare systems, a compassionate welfare programme, effective land reform and restitution programmes, and an effective police service, trained, resourced and equipped to be able to maintain law and order and keep people safe.

Another challenge that was faced during this quarter is the emerging market contagion from Turkey and Argentina that impacted negatively on the value of the South African rand against all major currencies, especially the dollar.

A weaker than expected rand exchange rate will lead to higher overall inflation and this will reduce South Africa's competitiveness and negatively affect trade and decrease the purchasing power of domestic consumers and businesses. A contraction in the economy will threaten employment in the provincial economy.

The platinum mining industry in Limpopo was confronted by a decline in the international platinum price. This puts additional pressure on the marginal mines to continue to operate and to save jobs. It is also important to tackle the challenge of poverty. The measurement of multiple deprivation in Limpopo can assist to address this challenge.

SEMENYA P.A.
Acting DDG: Sustainable Resource Management

1 Introduction

Rapid growth among the major emerging market and developing economies (EMDEs) over the past 20 years has boosted global demand for commodities. The seven largest EMDEs accounted for almost all the increase in global consumption of metals and two-thirds of the increase in energy consumption over this period. As these economies mature and shift towards less-commodity-intensive activities, their demand for most commodities is likely to decelerate. Based on current trends, global metals and foods demand growth could slow by one third over the next decade, while global energy consumption growth may remain broadly steady.

The prospect of persistently lower demand reinforces the need for economic diversification and the strengthening of policy frameworks among commodity exporting EMDEs. This is especially true for commodity exporters like the Limpopo province. Meanwhile, growth across Africa's most-developed economies has been sluggish this year despite early hopes, and the SARB has been hesitant to hike rates in an effort to spur economic activity, stifling the rand and leaving inflation unchecked.

South Africa's economy has hit a snag in 2018, as the country finds itself in a technical recession as it has experienced two consecutive quarters of negative growth. But economists and rating agency are painting a good picture of the country as they predict that the country will come out of this difficult situation as the president is on a drive to attract foreign direct investment and Moody's have placed South Africa as the second country in Africa after Egypt as a preferred investment destination.

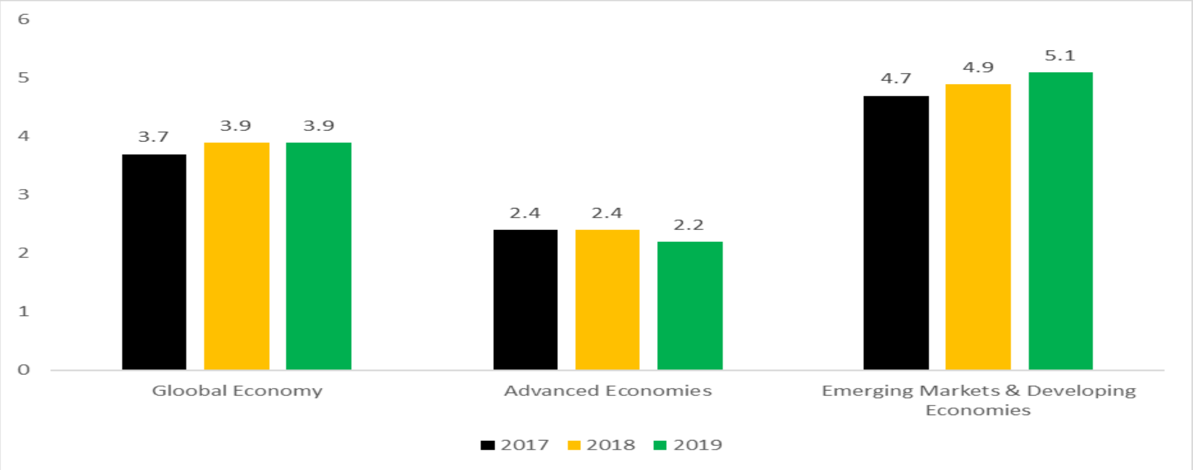
Limpopo's economy has managed to recover from the 2016 negative economic growth as it has hit a favourable 1.8 percent growth in 2017, according to IHS Markit. This is higher than the 1.2 percent that was expected earlier, but is well short of the Limpopo Development Plan target of 3 percent annual growth. This urges well for the provincial economy as it is an indication that the provincial government has managed to uplift and create opportunities for its citizens.

2 World economy

2.1 World Economic Outlook

The global economic growth continues to be driven by the seven largest Emerging Markets and Developing Economies (EMDEs).

Figure 1: World Economic Outlook, July 2018



Source: IMF, World Economic Outlook Update, July 2018

The IMF predicts growth to reach 3.9 percent in 2018 and 2019, in line with the forecast of the April 2018 World Economic Outlook (WEO), but the expansion is becoming less even, and downside risks to the outlook are mounting. The rate of expansion appears to have peaked in some major economies and growth has become less synchronized.

Advanced economy growth is expected to remain above trend at 2.4 percent in 2018, similar to 2017, before easing to 2.2 percent in 2019. The forecast for 2018 is lowered by 0.1 percentage point compared to the April WEO, largely reflecting greater than expected growth moderations in the euro area after several quarters of above-potential growth.

Emerging market and developing economies have experienced powerful crosswinds in recent months: rising oil prices, higher yields in the United States, dollar appreciation, trade tensions, and geopolitical conflict. The outlook for regions and individual economies thus varies depending on how these global forces interact with domestic idiosyncratic factors. Financial conditions remain generally supportive of growth, though there has been differentiation across countries based on economic fundamentals and political uncertainty. With the updraft on oil exporters from higher oil prices largely offset by the combined drag on other economies from the forces described above, the group's overall 2018 and 2019 growth forecasts remain unchanged from the April WEO at 4.9 and 5.1 percent, respectively.

2.2 Turkey's economic troubles

The Turkish economy is 'in the midst of a perfect storm' in recent years, though its economy has been one of the fastest growing economies in the world, but its impressive growth numbers were fuelled by foreign-currency debt. The country's borrowing resulted in deficits in both its fiscal and current accounts, and Turkey doesn't have large enough reserves to rescue the economy when things go wrong. Making the situation worse for Turkey is President Recep Tayyip Erdogan's preference to keep interest rates low even though inflation is more than three times the central bank's target.

The free fall in the Turkish lira has stoked fears of an economic fallout that could spill over into other emerging markets and the banking systems in Europe. Though the Turkish President is blaming the plunge in the currency on "an operation against Turkey" and dismissed suggestions that the country's economy was facing troubles. But the country finds itself "in the midst of a perfect storm" of worsening financial conditions, shaky investor sentiment, inadequate management of the economy and tariff threats from the U.S. The Turkish assets have been under severe pressure, even though Turkey makes up a small percentage of the global economy and financial markets, investors are worried about the issues in Turkey causing damage in other markets around the world, particularly Europe.

In the immediate term, policy decisions out of Washington have sparked Turkey's currency crash: The lira plunged as much as 20 percent against the dollar after President Donald Trump said he approved doubling metals tariffs on Ankara. But the cracks in Turkey's economic foundation were already spreading before the American president made his move.

2.3 Key lessons to be learnt from turkey's troubles

Turkey has in recent years been one of the fastest-growing economies in the world, even outperforming economic giants China and India last year. In the second quarter of 2018, the country reported 7.2 percent growth in its gross domestic product. That expansion, however, was fuelled by foreign-currency debt. At a time when central banks around the world were pumping money to stimulate their economies after the global financial crisis, Turkish banks and companies were racking up debt denominated in U.S. dollars. The borrowing, which fuelled consumption and spending, resulted in Turkey running deficits in both its fiscal and current accounts.

The former happens when government spending exceeds revenue, while the latter essentially means a country buys more goods and services than it sells.

The country's foreign currency debt now stands at more than 50 percent of its GDP, according to estimates by the International Monetary Fund. Turkey is not the only economy with "twin" deficits and high amounts of foreign currency debt. Indonesia, for example, also runs fiscal and current account deficits and its foreign currency borrowing is roughly 30 percent of GDP. But unlike Indonesia, Turkey doesn't have large enough reserves to rescue the economy when things go wrong.

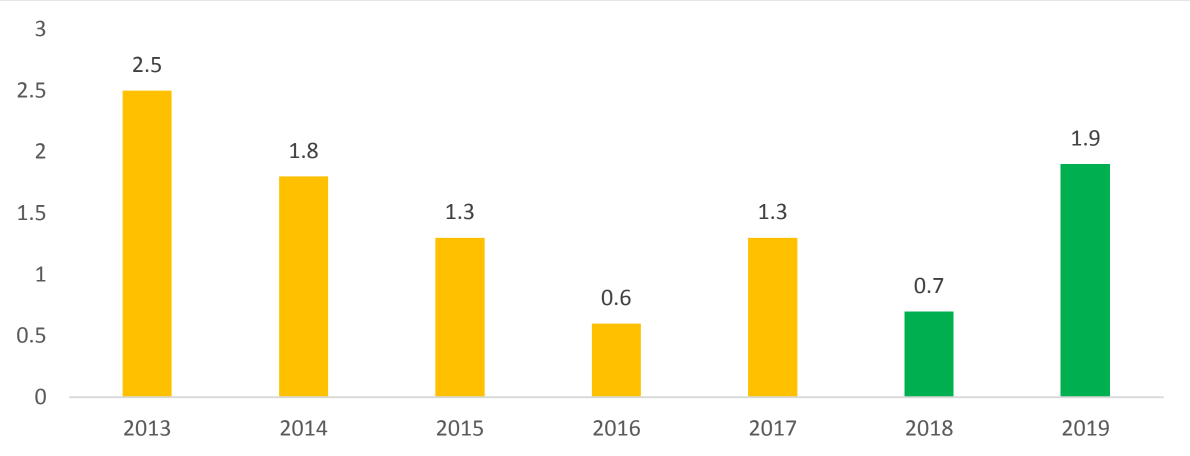
Turkey's reserves are notably low compared to its $181 billion in short-term debt denominated in currencies other than the lira. On top of that, much of the foreign currency in Turkey is held by banks, and those funds could be withdrawn by customers at any given time. That means when the lira falls, Turkey may not be able to buy up its currency to prevent it from spiralling further. If that situation worsens, the country would have to find other ways to finance its debt, including possibly getting bailed out by the International Monetary Fund.

Analysts argue that Turkey wouldn't have gotten into the current predicament if its central bank had been left to do its job as the Turkish economy has been "overheating" with inflation at 16 percent in July, way exceeding the central bank's target of 5 percent. Raising interest rates could have helped to stem such a massive increase in consumer prices: Higher rates tend to attract foreign investors, who would need the lira to buy Turkish assets. That could in turn support the currency, which makes imports cheaper and lessens the burden of paying back foreign debt. But in favour of lower interest rates to continue driving growth, the influence over the country's central bank has undermined investor confidence. The country continues to prioritize growth and lower rates which will extend the current crisis, rather than allowing the economy to rebalance. Without raising interest rates, Turkey has limited options to get out of its economic problems.

3 South Africa Economic Growth

3.1 SA GDP growth

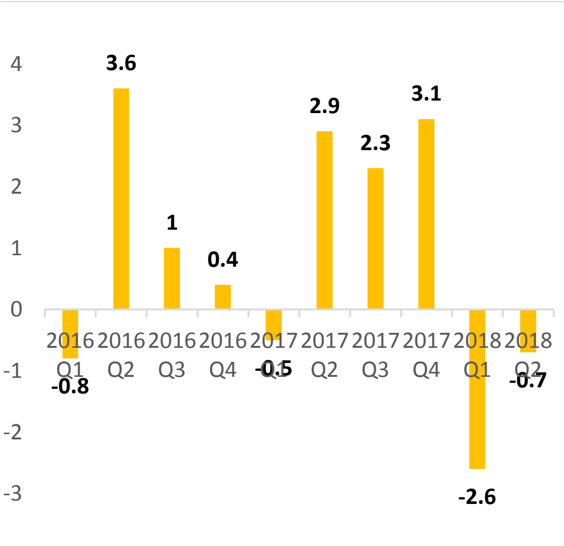
Figure 2: South African economic outlook

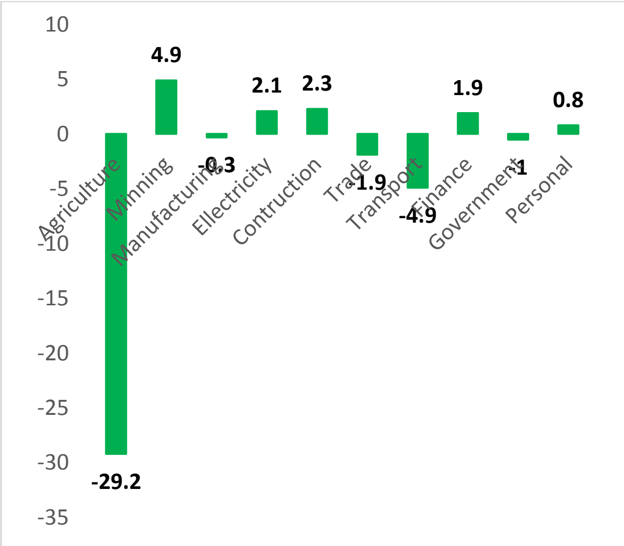


Source: South African Reserve Bank (SARB), 2018

Greater political stability and firm credit ratings bode well for the economy in 2018 as full-year economic prospects look set to largely ride out the weak first two quarters. Real wage gains should support stronger household spending this year, while the government's push to attract investment should bolster capital outlays. Nevertheless, fiscal slippage and a slow reform agenda are likely to constrain growth over the medium term. The South African Reserve Bank reduced its forecast to 0.7 percent in 2018 and 1.9 in 2019.

Figure 3: SA GDP and Sector contribution 2018 (constant 2010 prices)





Source: Statistics South Africa, 2018

Real Gross Domestic Product (measured by production) decreased by 0.7 percent in the second quarter of 2018, following a decrease of 2.6 percent in the first quarter of 2018, putting the country in technical recession. The largest negative contributors to growth in GDP in the second quarter were agriculture, transport and trade. The agriculture, forestry and fishing industry decreased by 29.2 percent, while the transport, storage and communication industry decreased by 4.9 percent and the trade, catering and accommodation industry decreased by 1.9 percent. The main positive contributions came from the mining industry (4.9 percent), Construction (2.3 percent), Electricity (2.1 percent), Finance (1.9 percent) and Personal services (0.8 percent). The agriculture industry contraction was mainly because of a drop in the production of field crops and horticultural products due to the drought in the Western Cape.

3.2 Exchange rate development in South Africa

3.2.1 A key issue in the South African economy is the depreciation of the Rand

Amid the ongoing crisis in Turkey, the selloff in Emerging Markets (EM) continued into August 2018 as contagion from the freefall of the lira spread to other EM currencies. During August 2018, the rand traded at 14.78 per U.S. dollar, shedding 11.8 percent from the same day a month earlier. Moreover, the rand has weakened 19.4 percent against the dollar since the beginning of the year amid the global risk-off.

Although rising U.S. bond yields and weak growth prospects have kept the rand under pressure in recent months, the currency's recent nosedive was primarily driven by contagion over the lira crisis. Given South Africa's fondness for dollar-denominated debt, investors were quick to tie the rand's fortunes to those of Turkey's lira.

Figure 4: South Africa Exchange Rate Chart

Source: SARB, 2018

Despite the fact that some of the international development does not impact on South Africa directly, South Africa bears the brunt because the size and liquidity of the local foreign exchange market.

3.3 Decline in the platinum price

Limpopo is primarily a mining province with the mining industry contributing nearly 30 percent to the local economy. Despite the fact that the platinum mines in the province is supported by the weakening rand the decline in the platinum price is a concern. The long-suffering platinum industry was dealt another blow in August 2018, both locally and internationally, when the metal price hit its lowest level in a decade as investors fled commodities.

South African producers, Impala Platinum and Lonmin Platinum have embarked on major restructuring and job cuts in the face of persistently low platinum prices in recent months. Since August 2018 the price slipped below $800/oz, a level last seen in the 2008 global financial crisis, after US President Donald Trump imposed sanctions against Turkey. This action did not just affect the lira, but emerging-market currencies in general as well as commodity prices and had a baring in the South African.

Figure 5: 2018 Commodity prices

Source: IRESS, August 2018

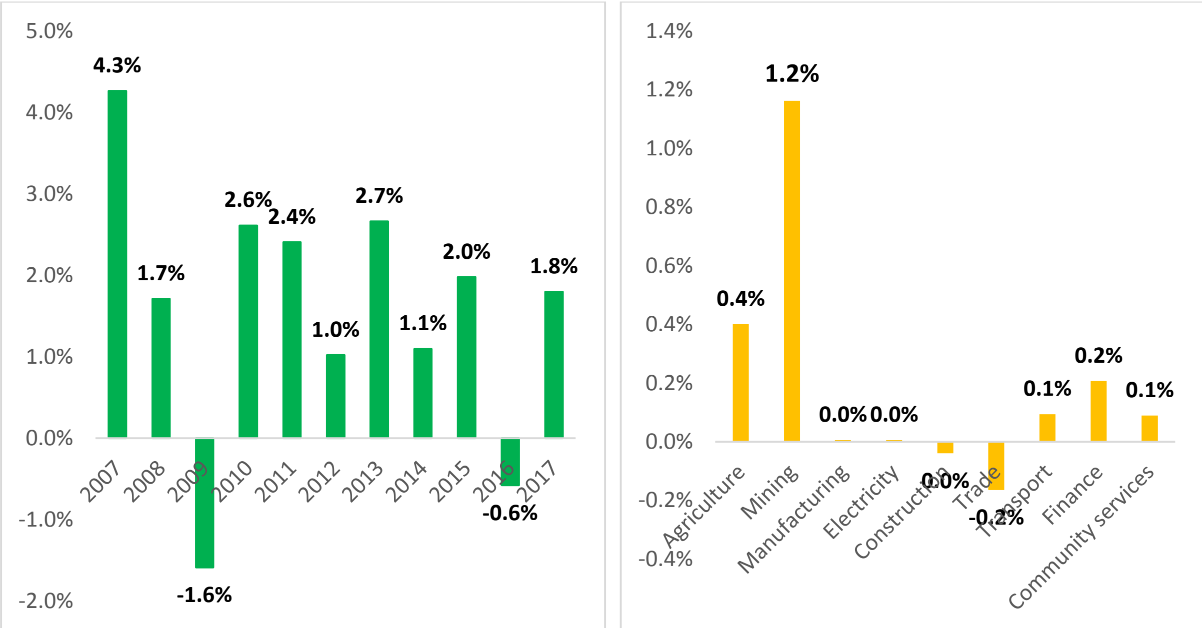
Platinum was trading at $760/oz, which was the lowest in recent years. The lower platinum price will put pressure on SA's already stretched producers, which sell the metal at the dollar price. Mining analysts say the situation is helped by the accompanying rand weakness and the strength in the price of rhodium, a by-product of platinum mining that is in high demand.

Other commodities, like copper and gold, have also been affected by the news of sanctions against Turkey. Both have, however, seen prices dropping for several months. The platinum price has been markedly low in the face of muted demand for the metal. The price dropped below its long-term average of $900/oz in mid-May and ever since early August 2017 has crept closer to the $800/oz edge.

4 Limpopo Economic growth

Limpopo economy grew by to 1.8 percent in 2017 compared to -0.6 percent in 2016. The provincial economy has managed to recover from the 2016 negative economic growth as it has hit a favourable 1.8 percent growth. This positive economic growth urges well for the provincial economy as it is an indication that the provincial government has managed to uplift and create opportunities for its citizens.

Figure 6: Gross Domestic Product (GDP) and Sector Contribution to total economic growth (Constant 2010 prices)



Source: IHS Regional Explorer, 2018

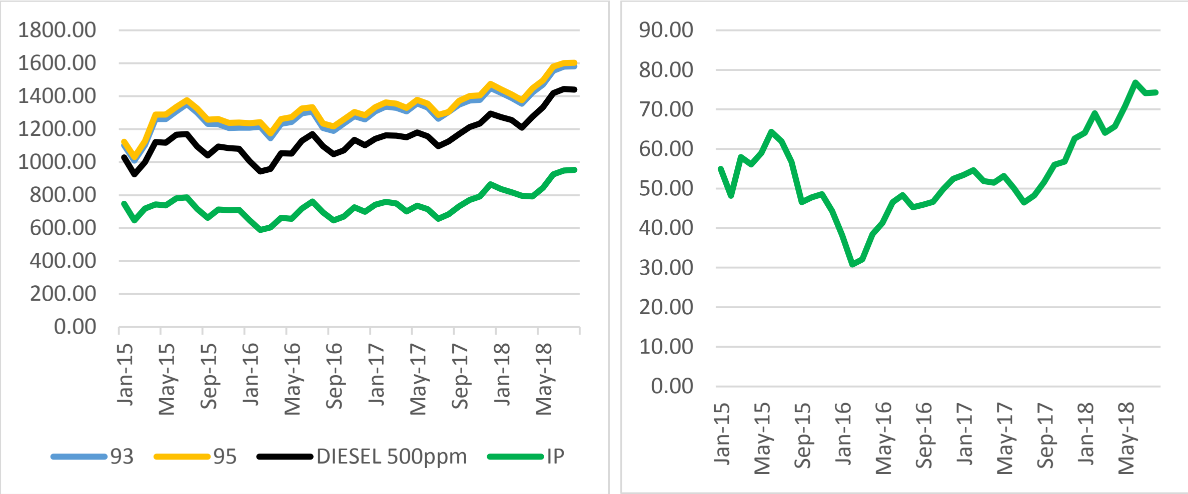
The provincial economic growth is mainly attributed to the primary sectors contribution where mining and agriculture contributed 1.2 and 0.4 percent respectively. The other positive contributors to the provincial economic growth were finance, transport, community services, manufacturing and electricity. Trade and construction contributed negatively with a respective growth of -0.2 and -0.03 percent.

5 Petrol price increase

5.1 The effect of Petrol price increase in SA

The recent significant increases of the fuel price to all-time highs has a decisive impact on the economy in the second quarter.

Figure 7: Petroleum prices v/s Brent crude oil prices



Source: Dept. of energy

The fuel price hike in between March and August 2018 has had an immediate impact on the prices of virtually all goods and services, as the country has seen petrol prices rise from just below R14.00 to above R16.00 during this period. The petrol price has increased by over R6.00 over a period of three years from R10.00 in 2015 to R16.00 in 2018 and it is expected that price will rise to around R17.90 by the end of the year.

The department of energy indicated that the petrol increase is linked to the recent downgrade of South Africa's sovereign credit rating to sub-investment grade by Standard & Poor's Global Ratings and Fitch Ratings has thrown financial markets into turmoil, although the rand has regained some of its initial losses. The increase in the fuel price is almost entirely due to the drop in the rand as crude oil prices had actually come down slightly over the past month.

A petrol price increase will have a ripple effect throughout the economy, because the South African economy is largely powered by diesel, meaning that all goods transported by road would reflect this increase. The value of the rand is expected to decline further in value against the dollar, which is going to impact on "everything" from fuel to food because although South Africa is more or less self-sufficient in grains, all of the inputs such as fertiliser, pesticides and diesel have to be paid for in dollars. Growing unemployment and a slowdown in our already terrible growth rate of 1.2 will soon follow as foreign investors seek greener pastures.

5.2 Consumers feeling the pinch

The fuel price hike is going to bite more to the consumers as the environment is really not complimentary toward household incomes. Average earnings growth in the private sector, including bonuses, used to average about 4.5 percent, but has now declined to 2.6 percent in the past year, this means consumer incomes will not be growing while inflation is likely to remain high.

South African National Taxi Council (Santaco) pronounced that taxi fares for local and long distance operations would increase during august, with a further review due in June 2019. The indication is that the increase for local distance taxis will be between R1.00 and R10.00 while long distance taxi rides would cost between R1.00 and R20.00 more. These increases may be more in some areas especially long distance operations. Santaco regretted the impact of these increases on commuters, especially the poor, but without the fare hikes many taxi operators would struggle to stay in business and continue to offer a much needed service.

6 The multiple deprivation index as a new measure of poverty.

The triple challenge of poverty, inequality and unemployment has been highlighted in various national government policy documents as the key strategic economic targets for South Africa (NDP, 2012).

The Limpopo Growth and Development Strategy (2009) and the Limpopo Development Plan (2014) links to the National Development Plan in setting a target to reduce the level of poverty in Limpopo. The target that has been set in the Limpopo PGDS in 2009 was to reduce the level of poverty by 2014 to halve of that in 2009. No explicit target for poverty was set in the Limpopo Development Plan. The National Development plan wants to reduce the number of people living under R 418 per day from the current 40 percent of the populations to 0 percent.

In the process to develop policy to address the challenges of poverty and inequality it is firstly important to be able to measure the current extent of poverty and inequality in Limpopo.

The objective is to introduce the multiple deprivation index as an additional measure of poverty in Limpopo.

6.1 Theoretical Approaches to measuring poverty

The most commonly used indicator to measure poverty is income poverty. In terms of this measure the level of poverty is measured linked to a specific poverty line that has been calculated. Examples is this approach the dollar and two dollars a day from the World Bank, the calculation of the Minimum Living Level (MLL) and the calculating of the national poverty line for South Africa.

Some other economists use the access to basic services as another indication of poverty in a particular area.

A different approach that is based on the premise that poverty can be defined as the lack of control over the opportunities that will change you live, is the capabilities approach. In terms of the approach no preconceived perceptions enter the measurement of poverty and the development of policy to curb poverty. It also deals with agency. The actual choices that people make and who/what they rely on to help them make their decisions are referred to as agency. Agency relates to people's belief that they are indeed the master of their own destinies or whether they believe that development is outside of their own realm of power/decision making (Mostert and Prinsloo, 2012).

The calculation of a multiple deprivation index is the last approach identified. The approach was developed by Townsend (1987) and focusses on various measures of poverty that is integrated to calculate and index of multiple deprivation.

According to Noble, Dibben and Wright (2010) multiple deprivation can be calculated as a weighted combination of dimensions or 'domains' of deprivation. The domain of deprivation that was utilized in their 2007 study included the following:

- Income and Material Deprivation
- Employment Deprivation

- Education Deprivation
- Living Environment Deprivation

6.2 Measuring poverty in Limpopo using the Multiple deprivation index

Table 1: The level of Multiple deprivation in Limpopo

	Material Deprivation %	**Employment Deprivation %**	**Education Deprivation %**	**Living Environment Deprivation %**
Western Cape	24.8	25.1	16.8	19.1
Eastern Cape	52.0	47.3	28.5	59.6
Northern Cape	39.5	34.1	30.0	32.1
Free State	33.3	38.9	23.4	32.9
KwaZulu-Natal	43.0	42.3	23.4	55.3
North West	41.7	37.9	28.7	55.4
Gauteng	30.8	29.8	12.6	21.5
Mpumalanga	34.9	38.2	24.4	54.5
Limpopo	40.2	46.4	24.3	71.9
South Africa	37.1	36.0	20.9	43.8

Source: Noble et al (2014)

The results indicate that Limpopo is still one of the provinces with highest level of poverty in the country. The biggest challenge is in terms of education deprivation and the living environment deprivation.

Noble et al (2014) highlights the fact that multiple deprivation differs from poverty in the fact that poverty measure that lack of resources that create deprivation. Deprivation' thus refers to people's unmet needs, whereas 'poverty' refers to the lack of resources required to meet those needs

7 Conclusion and recommendations

The current expected GDP growth rates for 2018 to 2019 is too low to make a difference to the unemployment rate for both SA and Limpopo, and this calls for policy deliberation on how to increase the economic growth rate both nationally and provincially. This is also a challenge as the government is projecting a low revenue collection due to the slow economic growth.

Effort should be placed to stimulate the provincial economy to reach at least above three percent growth rates as outlined in the LDP (Limpopo Development Plan) as this is seen to be a desired rate for the provincial government. As to whether the province will achieve the 3 percent growth by 2020, this will be one of the most important test, as this will depend on whether the private sector can create sufficient employment to compensate for the potential decline in public sector jobs as the government is forced to reduce its headcount. Another vital consideration will be the extent of household debt and whether it will depress household consumption.

The global challenges between Turkey and America lead to some tension in emerging markets, with the South African rand depreciating to R14.60. Although this is supporting the mines it is not enough to cover the 3.3 percent decline in metal prices.

South Africans are faced with a rising cost of living, as seen in petrol price increases, the VAT increase and sugar tax. The increased taxes were introduced by government to support it revenue collection. The government need to spend the collected revenues on productive investment that will grow the economy and create employment for the citizens.

Poverty is one of the key challenges that is being faced in South Africa. The multiple deprivation index provides additional information that is not available from the other more standard measures of poverty to inform anti-poverty strategy in Limpopo.