



**Quarterly Economic
Bulletin
2018/19
Q 4**

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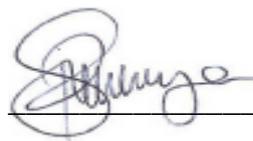
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Foreword

This Quarterly Economic Bulletin is presented at a time when the South African economy appears to be slowly recovering from the short-lived technical recession in the first two quarters of 2018. Given that the country has been underperforming, economic growth enhancers should be supported in both the fiscal and monetary policy instrument adjustment. Although economic growth is not the ultimate solution to development but necessary conditions to usher in broad-based development.

The National budget speech highlighted the tight fiscal conditions with the lower than expected revenue earned in the previous financial year plus the additional funding needed to support Eskom. Moreover, troubles at Eskom, the state-owned power utility, have sparked rolling blackouts and its crippled finances could potentially destabilize the economy. The state of Eskom is disruptive to the country's future and is posing a threat to the recovery that the country might have begun to realize.

This year's elections are expected to dictate the pace of the recovery over the short-term as President Cyril Ramaphosa's economic reforms will depend on the outcome of the election. Higher real wages and new business-friendly policy prescriptions are expected to lift economic sentiment and encourage household spending and fixed investment, respectively. Key downside risks remain, however, and a credit-rating downgrade by Moody's would trigger large-scale capital outflows and undermine any short-term recovery. Medium-term growth prospects are being held back by concerns over a possible fiscal cliff and the inadequate pace of structural reforms. Though the economic outlook for the country remain positive and growth is expected to be 1.6 and 1.9 percent in 2019 and 2020 respectively. The changes in the provincial demographics will require the provincial government to make changes in terms of policies that are inclined towards youth development.



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28/03/2019

Date

1. Introduction

The IMF projects that the World economic growth will average around 3.5 percent from 2018 leading to 2021. The global growth will be fuelled by the growth in the Emerging Markets and Developing Economies which is projected to be above 4.5 percent in the same period. Growth rates in the advanced economies have been marked down for many economies due to soft private consumption, weak industrial production following the introduction of revised auto emission standards, and subdued foreign demand. The latest set of Gross Domestic Product (GDP) figures released by Statistics SA provides an overview of economic performance in 2018 and the economy of the South Africa continued with its slow but stable growth path. The slow national economic growth is spilling over to the provincial economic performance.

Significant demographic shifts are expected to take place in the World over the next few decades. In particular, the world population is projected to grow at a much slower pace and to become older. The South African and Limpopo provincial population has already experienced a structural transformation over the past two decades which is characterised by a growing cohort of young people. This is the age group that has unique demands for public goods that may differ for the infant and old aged. A rise in the number of people in the age cohort, prompts government to assess policies and programmes that will harness the productive capacities of the youth like for instance increased access to education.

Due to inefficiencies at ESKOM in terms of providing electricity the province has experienced load shedding. It is important to assess the impact of the load shedding on the performance of the provincial economy. Research has indicated that load shedding could lead to job losses at a time when there is widespread concern about present levels of unemployment. Load shedding also impacts negatively on economic growth as it leads to lower production and consequently a lower Gross Domestic Product. ESKOM is also requesting for significant increases in the price of electricity that will lead to an increase in the food prices and inflation. Security of power supply remains an essential factor for sustained business and consumer confidence.

2. Economic Outlook

2.1. World Economic Outlook

The World is manoeuvring through the difficult storms of trade and political uncertainty as seen with the ongoing spats between United States of America (USA) and China. These tensions have multiplier effects, particularly in developing economies which heavily rely on these economic giants as their export market. South Africa suffered because of the import duties levied by the USA, especially on steel exports, however the country managed to remain resilient as it exited the technical recession boosted by manufacturing and Financial Services sector.

Global economic growth rate averaged 3.6 percent since 2014, maintaining positive yet moderate trends amidst trade and geopolitical tensions. These tensions, combined with concerns about softening global growth prospects, have weighed on investor sentiment. World economic growth in 2018 is projected to be 3.7 percent. Global growth is projected by the IMF to decline to 3.6 percent in 2019 before picking up slightly to 3.7 percent in 2020. The World Bank is even more bearish than the IMF, only expecting 2.9 percent world economic growth during 2019. This growth pattern reflects a persistent decline in the growth rate of advanced economies together with a temporary decline in the growth rate for emerging market and developing economies in 2019. The current trade tensions between America and China had a bigger negative impact on China than America and fears exist that China can run into a current account deficit during 2019.

Table 1: World Gross domestic product (GDP), constant prices Percent change

Country Group Name	2014	2015	2016	2017	2018	2019	2020	2021
World	3.58	3.45	3.27	3.74	3.73	3.65	3.66	3.64
Advanced economies	2.07	2.31	1.71	2.34	2.36	2.13	1.72	1.68
Euro area	1.42	2.05	1.89	2.39	2.03	1.88	1.65	1.55
Emerging market and developing economies	4.72	4.30	4.39	4.72	4.68	4.68	4.93	4.88
Emerging and developing Asia	6.81	6.80	6.46	6.54	6.52	6.31	6.42	6.31
Emerging and developing Europe	3.91	4.73	3.27	5.98	3.77	1.98	2.83	2.55
Sub-Saharan Africa	5.14	3.27	1.40	2.75	3.07	3.76	3.91	3.95
South Africa	1.85	1.28	0.57	1.32	0.76	1.40	1.74	1.80

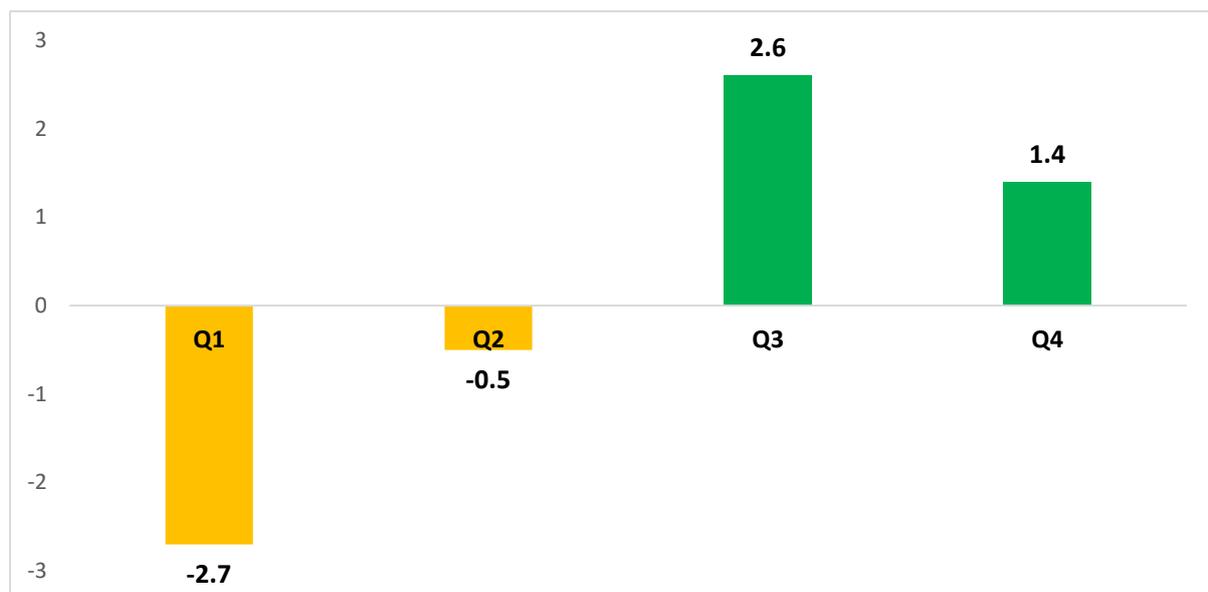
Source: IMF World Economic Outlook Database, October 2018

In Sub-Saharan Africa, growth is expected to slightly pick up in the medium term from 3.0 in 2018 percent to 3.9 in 2021. Softening oil prices have caused downward revisions for some oil producing African economies, such as Angola and Nigeria, where oil is the most traded commodity and major revenue generator. African growth potential is subdued by lack of interregional trade, geopolitical tensions and less developed financial markets. It should be noted that the South African economy is expected to grow at only 1.4 percent in 2019 compared to the 3.0 percent in the sub-region.

2.2. The South African Economic Outlook

The South African economy grew by 1.4 percent in the fourth quarter of 2018, contributing to an overall growth rate of 0.8 percent for the entire year of 2018.

Figure 1: SA 2018 Quarterly GDP growth

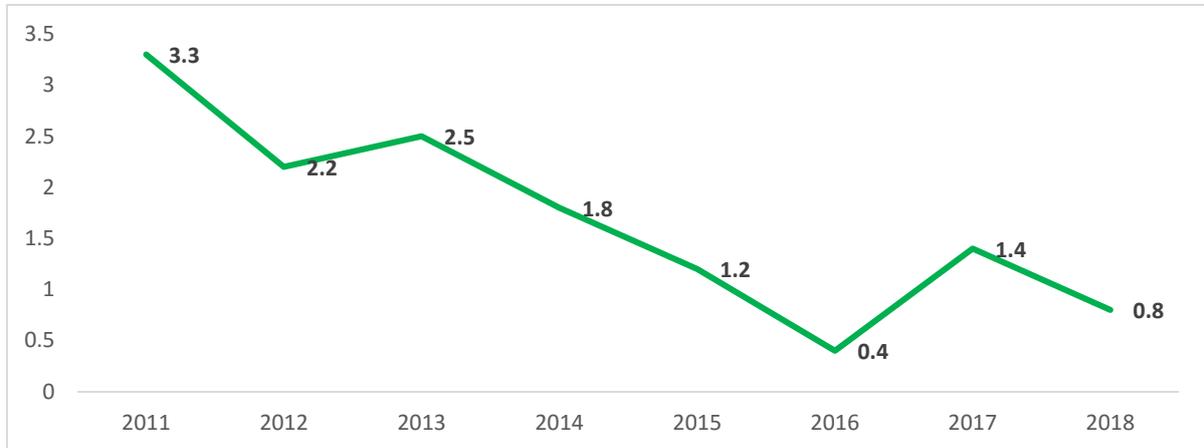


Source: StatsSA GDP, 2019

South Africa found itself in economic recession in 2018, its second since the early 1990s. The 2018 recession was due to the negative growth of the first two quarters of the year, with the economy shrinking by 2.7 percent in the first quarter and contracting further by 0.5 percent in the second. Despite the recession, positive growth in the third (2.6 percent) and the fourth (1.4 percent) quarters was just enough to push overall growth for the year into positive territory, with the real annual growth rate reaching 0.8

percent, which is lower than the 1.4 percent in 2017 but higher than the 0.4 percent growth in 2016.

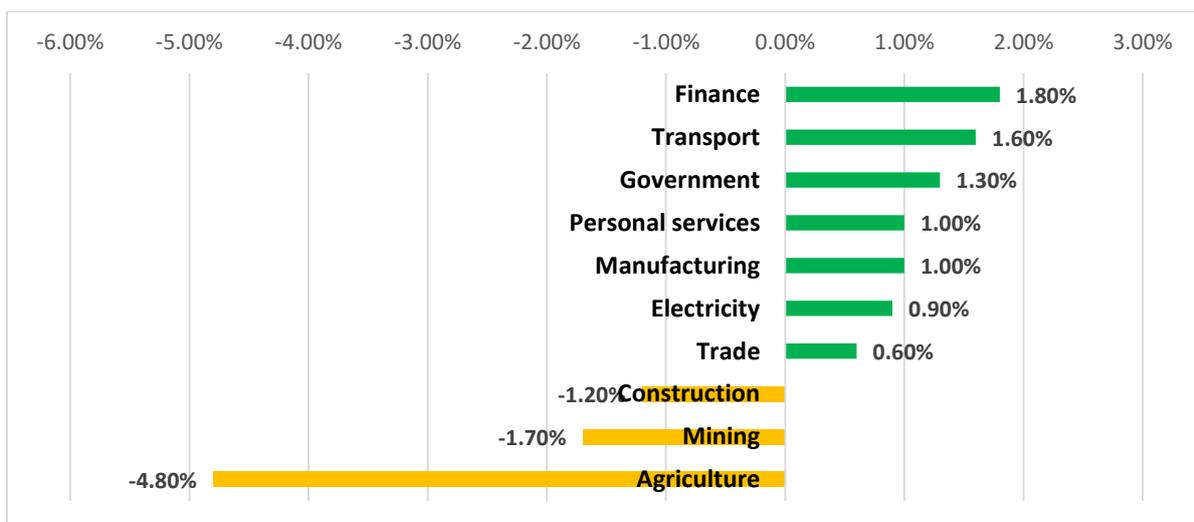
Figure 2: SA GDP Growth



Source: StatsSA GDP, 2019

The finance, real estate and business services industries were strong supporters of overall growth in 2018, increasing by 1.8 percent during the year. The second largest contributor to positive growth was government, which expanded by 1.3 percent. These two industries contributed 0.4 and 0.2 percentage points respectively to the overall growth of 0.8 percent for the year.

Figure 3: SA quarter 4 2018 Sector contribution



Source: StatsSA GDP, 2019

Agriculture, mining and construction all stumbled, however. Agriculture in particular had a difficult year, registering a contraction of 4.8 percent. A slowdown in the production of field crops and horticultural products stunted growth in the first two quarters.

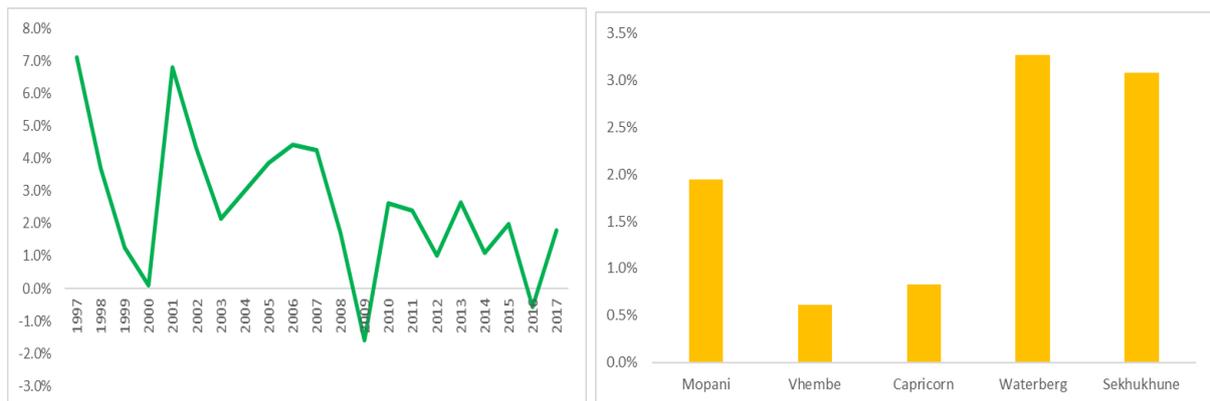
Mining activity fell by 1.7 percent. Gold, copper and iron ore were the biggest drags on production in 2018, according to Statistics SA. Gold production fell by 14.5 percent in 2018, the biggest annual slump since 2008. Copper production tumbled by 28.5 percent in the same year, the biggest fall on record since 1981.

The construction industry had its worst year in two decades in 2018, as production slumped by 1.2 percent, the industry's biggest annual fall since 1999. The industry has struggled to keep its head above water, experiencing its second consecutive year of economic decline in 2018. The mining and construction industries are in recession, as both industries recorded negative growth in the third and fourth quarters of 2018. The slump in the construction industry is partly caused by slow government expenditure on infrastructure projects.

2.3. Limpopo Economic Growth

The provincial economy has been underperforming or experiencing a negative growth trajectory since 1997. In 2017, the province recorded growth of 1.8 percent, an improvement from -0.6 percent in 2016. The 2017 growth was supported by Waterberg and Sekhukhune districts recording growth of 3.3 percent and 3.1 percent respectively. The subdued provincial growth can be associated with unfavourable commodity prices, increasing operating expenses for mines, El Nino climate phenomenon that farmers are still recovering from.

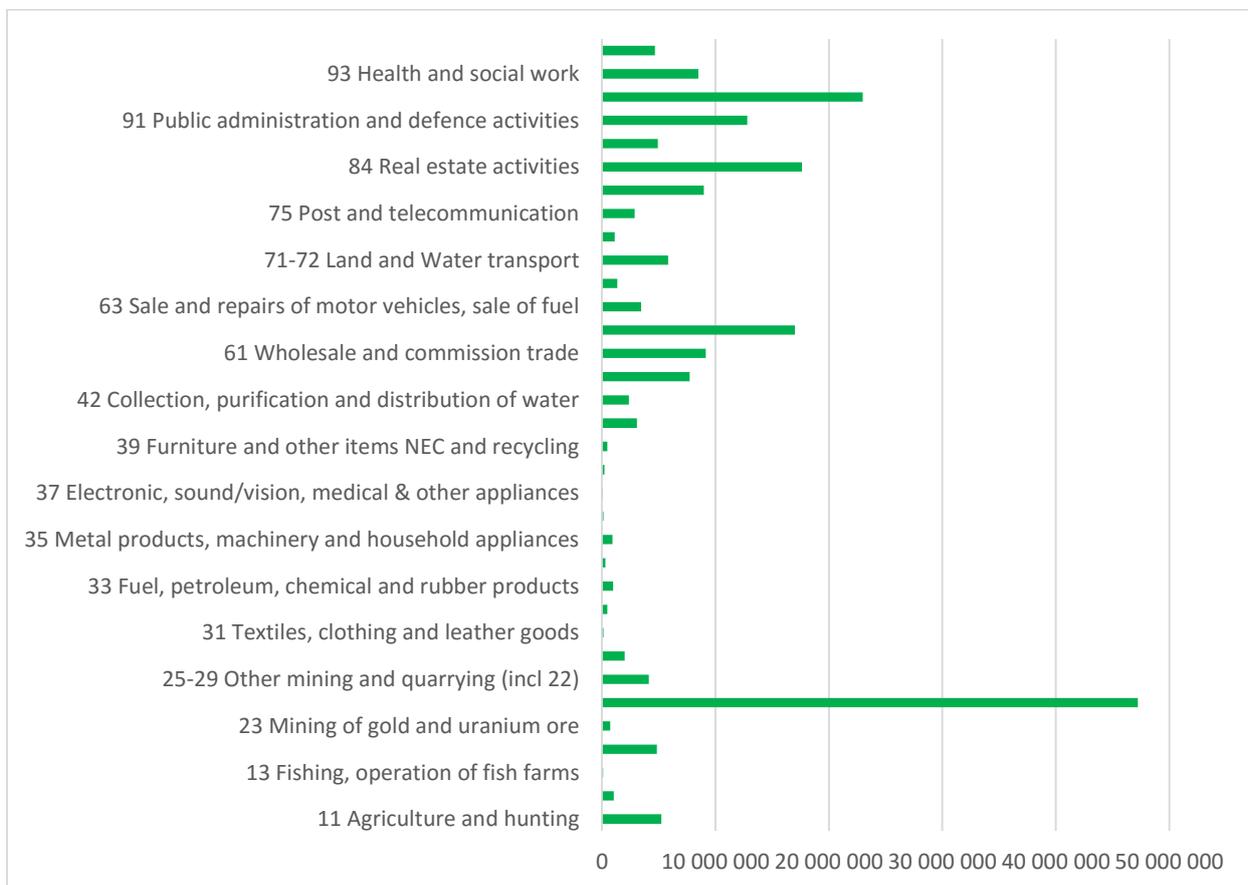
Figure 4: GDP Constant 2010 prices percentage change



Source: IHS Markit Regional Explorer 2019

The provincial overview of the detailed sectors shows that there are two sectors dominating the provincial economy being the primary (Mining to be particular) and tertiary sector (Retail trade and repairs of goods, Real estate activities, Public administration and Education.

Figure 5: Detailed Economic Sectors (34 sectors) Constant 2010 prices (R 1000)



Source: IHS Markit Regional Explorer 2019

3. Responsiveness of provincial fiscal policy to demographic dynamics

Significant demographic shifts are expected to take place in the world over the next few decades. In particular, the world population is projected to grow at a much slower pace and to become older (United Nations 2015). It is important to analyse the impact of these demographic changes on government expenditure and the significant fiscal challenges it poses. The proportion of the provincial government budget is determined by the Provincial Equitable Share (PES) formula. Of the 43 percent national division of revenue allotted to provinces, Limpopo province's share is only 11 percent.

The section will analyse literature to assess the relationship between demographic changes and fiscal policy. The section will therefore critically reflect on the existing literature and data trend analysis to develop policy suggestions that will ensure fiscal sustainability in the country and the province in particular.

3.1. Demographic trends in Limpopo

In reference to the table below, the Limpopo population, which is predominantly composed of African population, has increased from 4.7 million in 1996 to 5.8 million in 2018. The increase was mainly driven by 20 - 44 years' age cohort and 50 to 69 years' age cohort. Mopani, Capricorn, Vhembe, and Sekhukhune relatively have the same share of the total population recording 1.1 million, 1.3 million, 1.3 million and 1.1 million respectively. Waterberg district has the least population of 746 thousand people.

Generally, it might follow that the fiscal expenditure in the province will be shared almost equally among the districts, however, it must be born in mind that the levels of development in these districts are not the same. In many instances economic concentration occurs in a centre and other regions become peripheries who supplies raw material and labour to the centre. Arguably, Capricorn district is the centre of the province and the district is likely to attract people and other resources such as capital and government spending.

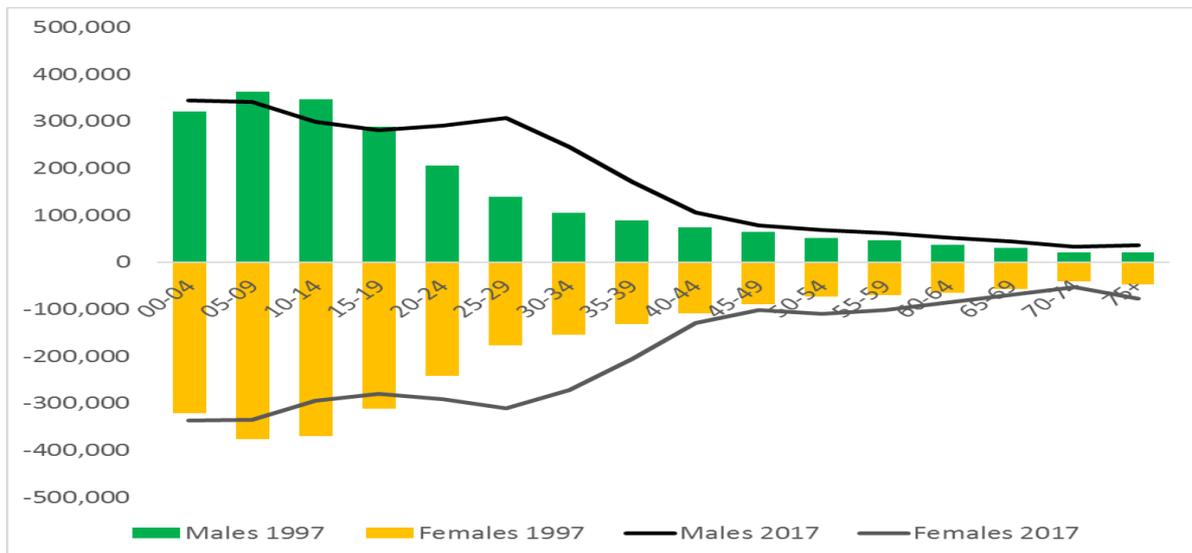
Table 2: Population numbers and growth rates (over 5 year periods)

Population					
	1996	2002	2007	2012	2017
Limpopo	4,791,481	5,093,690	5,300,527	5,500,524	5,813,302
Mopani	1,007,055	1,085,055	1,109,671	1,108,532	1,145,704
Vhembe	1,147,865	1,221,285	1,272,200	1,315,786	1,386,821
Capricorn	1,128,327	1,181,299	1,226,337	1,280,424	1,353,381
Waterberg	552,216	622,831	662,395	694,966	746,772
Sekhukhune	956,019	983,220	1,029,924	1,100,816	1,180,624

Source: IHS Markit- Regional Explorer 2019

The composition of the population is increasingly becoming youthful as shown in Figure 6. According to IHS Markit data the youth population has increased by 652 972 since 1997 to 2017. Female youth has grown faster than male youth, which leaves a gender gap as years' progress.

Figure 6: Limpopo population by gender and by age between 1997 to 2017

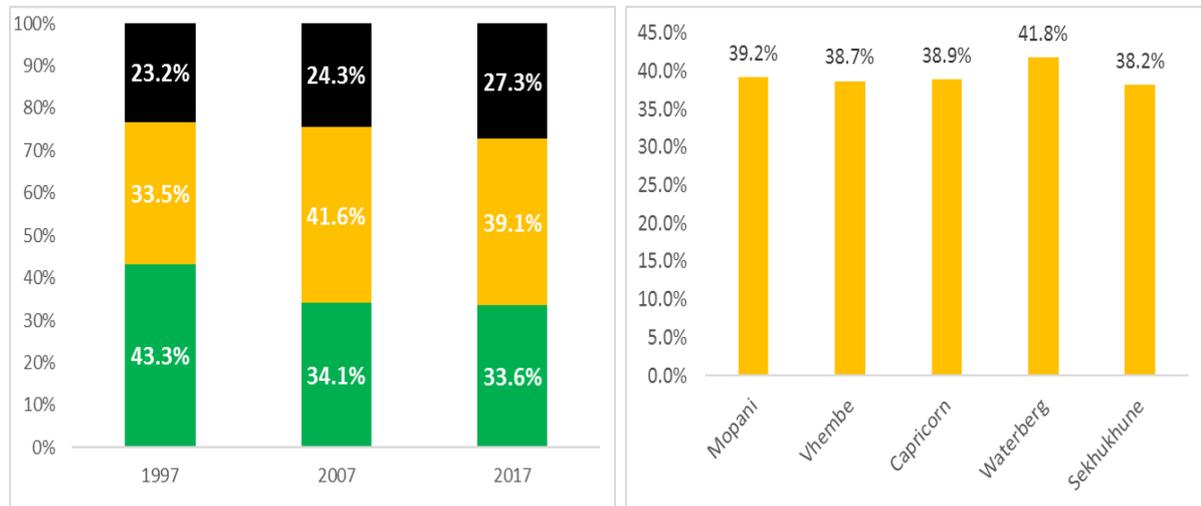


Source: IHS Markit- Regional Explorer 2019

The gradual rise in the percentage of youth population in the province from 33.5 percent in 1997 to 39.1 percent in 2017, is attributed to successes in improving individual and population health as part of past development strategies and high fertility rates. The district with the largest youth population as a proportion of the

population is Waterberg recording 41.8 percent composition of youth, followed by other district with sub 40 percent composition.

Figure 7: Limpopo population by age cohort and average youth population by district between 1997 to 2017



Source: IHS Markit- Regional Explorer 2019

3.2. Dependency trends in Limpopo

The results in Figure 8 indicate a general decrease of total dependency ratio¹ at national and provincial level. Despite the decrease on both national and provincial level the Limpopo dependency ratio is relatively higher than the national average. In 1997, the ratio was 91.8 percent, this implied that every 100 persons of economically active population (15 - 64), were expected to cater for 91.8 people. The ratio improved significantly to 63.9 percent in 2017, but is still relatively high compared to other provinces. The Dependency ratio is relatively equally spread across the districts of the province.

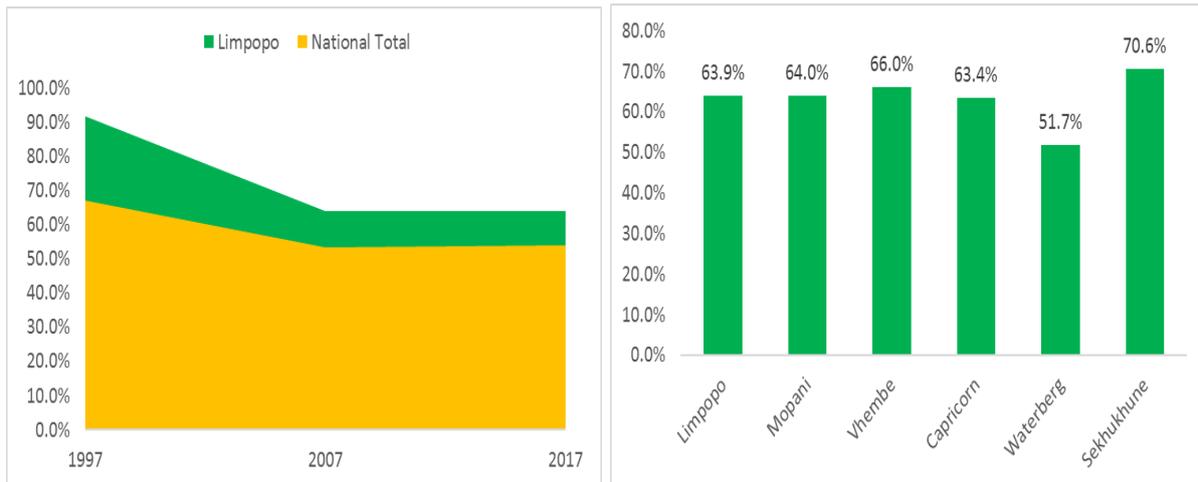
A long term decline in the dependency ratio could lead to the realisation of demographic dividend². This decreased support ratio also means that, all things being

¹ The dependency ratio is an indicator of potential dependency burden of children and the elderly on those who are of economically productive ages in a population.

² Two potential dividends which contribute to long-term economic growth and development. The first demographic dividend is triggered by falling fertility rates after a decline in mortality rates, particularly among children. The second can be realised through capital deepening.

equal, income per effective consumer rises in the sense that they have a relatively smaller burden to carry than before. This in turn implies higher standards of living and an improved scope for human capital investment. The outcomes are a less government dependent population and increased tax base. Government is able to redirect resources to other priorities that are pro-growth.

Figure 8: Total dependency ratios and by district



Source: Own calculation data sourced from IHS Markit- Regional Explorer 2019

The implications of these demographic patterns for the province are worth considering because they pose some challenges for policymakers and resource allocation. The magnitude of the effects will depend on policy responses.

3.3. Population composition and the impact on the health sector

Changes in the age structure of the population are among the most intuitive and commonly mentioned drivers of health cost growth in public commentary. This stems from the observation that per capita healthcare costs are higher among certain age cohorts. Average per capita costs are relatively high for groups such as infants and women of child bearing age. Particularly notable is the escalation of average spending among the elderly. Expenditure increases rapidly following middle age, reaching many multiples of younger age costs (Goldrick-Kelly, 2016).

The average per capita health spending by age group increased with age since 2007. With the traditional projection method of health expenses, population ageing, with its increase in the relative weight of older age groups, has an upward effect on health spending. The projection of public health spending applies the foreseen demographic structure to per capita spending by age and sex as observed in the recent past (Mester, 2017).

The relatively young population in Limpopo implies lower health expenditure than regions with an ageing population.

3.4. Findings and Final analysis

The province is transiting into a youth dominated population structure. In this case the province is experiencing a relatively declining mortality rates for the young population. The dependency ratio of rural provinces such a Limpopo will likely to remain high relative to other provinces for the reason that older persons are left in the rural areas or villages because they are economically inactive through unemployment or retirement from the cities. This increases their dependency on the working age population and the government. More often than not, the middle aged population leave their children with the elderly in the villages. Basically total dependency (Child dependency and aged dependency ratios) will be high in rural provinces. This is further worsened when unemployment is high. This places the whole burden on government to provide public services without expecting to recover the costs. The costs that will be incurred depends on the nature of the changes in the demographic profile in the province.

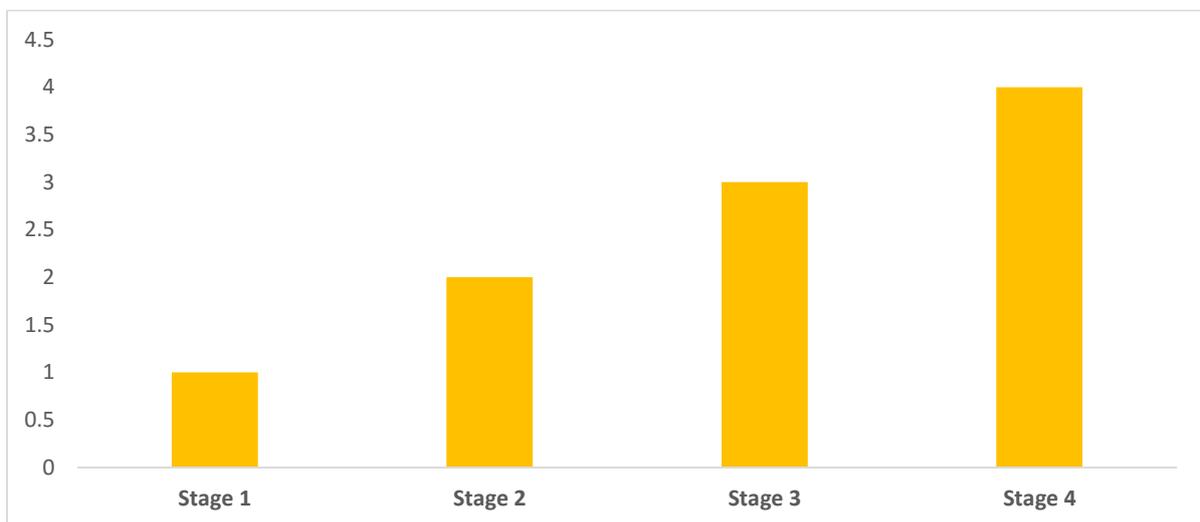
4. The impact of load shedding on the South African economy

The load shedding is taking place at a time that the national economy is growing at only 0.8 percent. If the economy was growing at its long term average of 3 - 3.5 percent, the incidence of load shedding would have been much higher and more frequent.

4.1. The impact of load shedding on the South African economy

Load shedding is very costly and have a devastating effect, not only to Eskom, because they cannot sell as much electricity as they want to, but also for the country as it affects different facets of the economy. Many of the companies using electricity, like the steel industry and others, would have to reduce operating hours because of load shedding and all these things have a negative effect on the economy. Load shedding in South Africa comes at a time when the country wants to boost investor confidence, uncertainty is then set into business decision-making. Prolonged load shedding will not only negatively impact on investor sentiment, but will damage vulnerable small businesses and the economy. The price of unserved energy, which is energy that never arrives due to load shedding costs the country R1 billion per stage, per day during stage one of load shedding. Stage two costs an amount of R2 billion loss over a 24-hour period and Stage three costs R3 billion and stage four could cost the economy R4 billion per day. The load shedding could cost the country as much as R5 billion rand a day.

Figure 9: Cost of load shedding to the economy per day (R' billion)



Source: Department of Energy 2019

Load shedding could also lead to job losses and lower economic growth at a time when there is widespread concern about present levels of unemployment and low levels of economic growth. Security of power supply remains an essential factor for sustained business and consumer confidence.

The President announced in the State of the Nation address that, due to the current challenges, Eskom must be split into three sections taking responsibility for generation, transmission and distribution to try and improve the efficiency of Eskom. Fears have been expressed that this may lead to more job losses. Another challenge is to allocate the current debt burden at Eskom to the three sections.

4.2. The impact of load shedding on the cost of electricity

Due to the severe impact of load shedding on businesses many of them have started to install backup generators. The average cost of a 50 KVA generator is R200 000 and it uses 13 litres of diesel per hour. The concern is however that the cost to buy diesel to run these generators is much more expensive than buying electricity directly from Eskom. This higher cost of electricity leads to a decline in the profitability of businesses. The business must also fund the capital cost to acquire a generator. Some of the smaller SMME's cannot absorb these costs and face the full negative impact of load shedding. It has also been calculated that the loss in profit in the major shopping centres like Sandton City can be as high as R200 000 per hour of load shedding.

4.3. Load shedding and renewable energy sources

If turnaround strategy at Eskom is not implemented successfully, businesses will start to make their own arrangements which might apply going off grid using solar energy. This will undermine Eskom's future customer base resulting in lower revenue from electricity sales and bigger challenges for Eskom to service its outstanding debt. Without a reliable electricity supply, South Africa becomes more uncompetitive leading to even slower economic growth. With the current slow growth in South Africa, the country has to nurture the local manufacturing sector and local SMMEs for the country to make any economic progress. This is hampered by the load shedding that is currently experienced.

5. Conclusion and recommendations

The World is going through the difficult storms of economic uncertainty as is evident by the ongoing trade war between United States of America and China. These storms have multiplier effects, particularly in developing economies which rely heavily on these economic giants as their export market mostly for their minerals. South Africa suffered because of the import duties levied by the USA, however the country managed to remain resilient as it exited the technical recession boosted by manufacturing and Financial Services sector. The economic conditions of the country and the province continue to remain sluggish and resulted in calls for the province to start discussions on how to add value by the processing of primary goods, like minerals and agricultural products, to be able improve the money earned from exports.

The recent changes in the population numbers and the demographic structure in the country and province prompts government to implement policies and programmes that will harness the productive capacities of the young age cohort. The main challenge facing the province is translating the young population into capable and productive human resource to foster provincial economic development. This will require the province to provide education facilities up to tertiary level and creating sufficient jobs to get them employed. The abundance of young well educated and healthy workers could see the province and the country in general attain higher levels of economic growth and a higher development trajectory. Some of the other policy recommendations includes to expand early childhood education facilities to ensure all children attend such schools to improve their aptitude for learning and to provide high quality teaching materials and trained teachers to improve quality of education and progression from primary to secondary school and to tertiary institutions.

In terms of health a recommendation is to expand interventions to reduce child mortality in order to facilitate fertility decline, with particular emphasis on child nutrition, which is critical for development of cognitive capacity and productivity later in life. Interventions to address diseases that undermine the productivity of workers including HIV/AIDS, tuberculosis, and accidents/injuries should also be enhanced. The key pillars of the health system including training, recruitment, and retention of health

workers; supply chain management; healthcare financing; and use of evidence in decision-making should be strengthened.

The current electricity challenges in the country are happening at an undesirable time, where the country is in dire economic condition. Load shedding has a high potential to lead to low firm productivity which is highly likely to result in massive job losses. This occurs at a time when there is widespread concern about present levels of unemployment and low levels of economic growth. Security of electricity supply remains to be an essential factor to ensure sustained business and consumer confidence, and also influencing the investor confidence in South Africa.