

# Nedbank

## Economic commentary

18 August 2009

### Gross Domestic Product Estimates

Real gdp output contracted further in the second quarter, but at least the rate of decline moderated somewhat

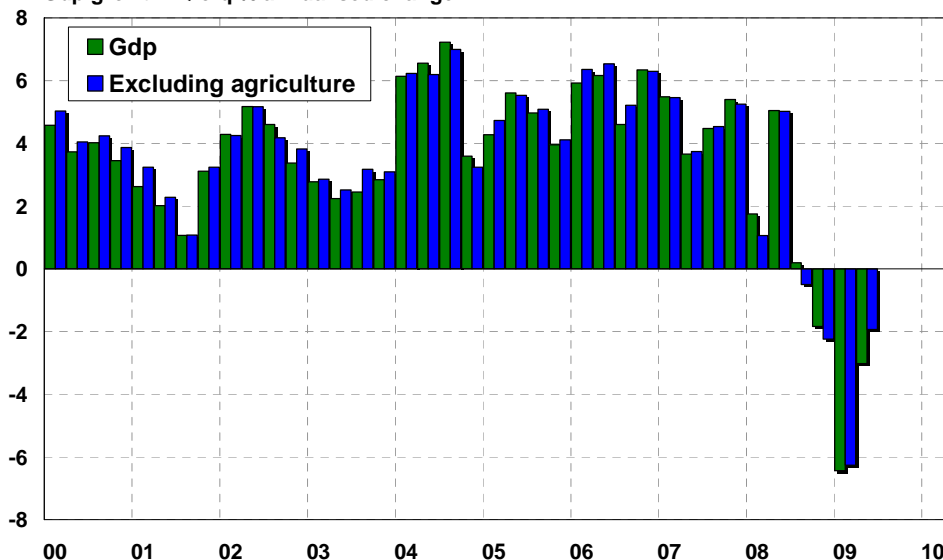
Latest (Q2 2009)

Summary of key growth rates:

|                       | 2006 | 2007 | Q1'08 | Q2'08 | Q3'08 | Q4'08 | 2008 | Q1'09 | Q2'09 |
|-----------------------|------|------|-------|-------|-------|-------|------|-------|-------|
| <b>Q-o-q % (saar)</b> |      |      |       |       |       |       |      |       |       |
| Total value added     | 5.2  | 5.1  | 1.6   | 5.3   | 0.3   | -1.7  | 3.2  | -6.2  | -2.4  |
| Gdp @ market prices   | 5.3  | 5.1  | 1.7   | 5.0   | 0.2   | -1.8  | 3.1  | -6.4  | -3.0  |
| Gdp excl agriculture  | 5.6  | 5.2  | 1.1   | 5.0   | -0.5  | -2.2  | 2.8  | -6.3  | -1.9  |
| <b>Y-o-y %</b>        |      |      |       |       |       |       |      |       |       |
| Total value added     | 5.2  | 5.1  | 4.0   | 4.6   | 3.1   | 1.1   | 3.2  | -1.1  | -2.5  |
| Gdp @ market prices   | 5.3  | 5.1  | 3.9   | 4.5   | 3.0   | 1.0   | 3.1  | -1.2  | -2.8  |
| Gdp excl agriculture  | 5.6  | 5.2  | 3.6   | 4.0   | 2.7   | 0.8   | 2.8  | -0.9  | -2.6  |

### Quarterly growth in gdp

Gdp growth: Q-o-q % annualised change



### Comment

The second quarter gdp figures again show a sombre picture of the economy. Although confidence has picked up and equity prices have moved higher over the past few months, the economy remains in recession. Real gdp shrank by another 3% in the second quarter, recording its third consecutive quarterly contraction. Apart from mining, activity levels in most major sectors either declined sharply or grew at a much slower pace.

Real value added by the mining sector grew by 5,5% over the quarter off an exceptionally low base in the first quarter. The sector benefited from a revival in Chinese demand for some commodities, which translated in higher production of mainly platinum, manganese, chrome, nickel, iron ore and diamonds.

In sharp contrast, real value added by the manufacturing sector dropped by a further 10,9% over the quarter, with all ten major industries recording lower output. However, the

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worst affected industries remained those focused on the export markets, including basic metals, chemicals, petroleum refineries and transport equipment. The broader agricultural sector also posted poor results, due to weak output in the animal farming industry.

A similar trend prevailed in most other sectors. Weaker electricity demand contained electricity generation in the second quarter, dragging real value added by the 'electricity, gas and water' sector down by 1,4% over the quarter. Conditions in the broader retail sector deteriorated even further as rising unemployment undermined confidence and depressed household demand, while the number of foreign tourists and business travelers dropped sharply as recessionary conditions globally continued to bite. As a result, real value added by the 'wholesale and retail trade, hotels and restaurants' industries contracted by a sharp 4,5% over the quarter. The weak global and domestic trade conditions also continued to undermine transport activity, pulling real value added by the usually resilient 'transport and communication' sector down by another 1% in the second quarter. Tough conditions also prevailed in the 'finance, real estate and business services' industries, where banks and insurance firms continued to feel the effects of weak household and corporate demand, while rising unemployment, low confidence and expectations of further declines in house prices still undermined real estate activity.

The only sectors that recorded positive growth over the past quarter were construction (boosted mainly by the public sector's ongoing infrastructure expansion programme), general government and personal services (both supported mainly by the state's coffers and continued spending on some basic services). However, activity levels in all three these sectors appear to be losing momentum as real value added grew at a slower pace in the second quarter.

### Gdp breakdown by sector Q-o-q % change (Seasonally adjusted annualised rates)

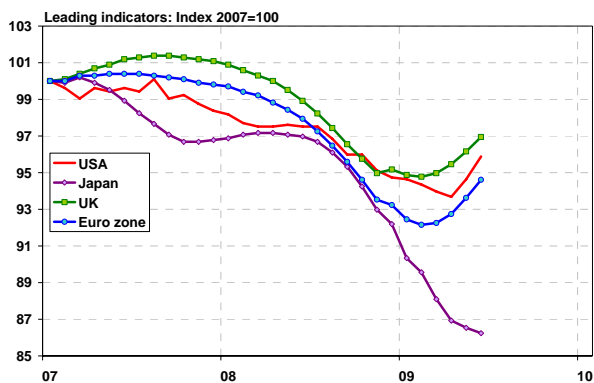
| Industries         | Gdp growth (q-o-q % change saar) |       |       |       |       |      |       |       | Size             |
|--------------------|----------------------------------|-------|-------|-------|-------|------|-------|-------|------------------|
|                    | 2007                             | Q1'08 | Q2'08 | Q3'08 | Q4'08 | 2008 | Q1'09 | Q2'09 | % total in Q2'09 |
| Agriculture        | 2.9                              | 25.0  | 16.7  | 31.6  | 16.7  | 18.8 | -2.9  | -17.1 | 2.9              |
| Mining             | 0.0                              | -25.8 | 19.2  | -8.8  | 0.4   | -6.5 | -32.8 | 5.5   | 4.6              |
| Manufacturing      | 4.5                              | -0.6  | 14.3  | -9.4  | -21.8 | 1.2  | -22.1 | -10.9 | 14.4             |
| Power & Water      | 3.0                              | -5.8  | -2.1  | 3.0   | -2.7  | -1.2 | -7.9  | -1.4  | 2.0              |
| Construction       | 17.1                             | 13.9  | 9.1   | 15.0  | 10.8  | 13.9 | 14.7  | 12.2  | 4.1              |
| Trade              | 5.2                              | 4.1   | -4.0  | -6.9  | -0.2  | 0.5  | -2.5  | -4.5  | 13.8             |
| Transport & comm   | 5.6                              | 3.4   | 4.3   | 4.5   | 1.8   | 4.0  | -1.8  | -1.1  | 10.3             |
| Finance            | 6.8                              | 2.6   | 3.3   | 3.2   | 3.0   | 5.0  | -2.3  | -2.4  | 20.5             |
| General government | 3.7                              | 4.6   | 2.5   | 5.2   | 4.5   | 3.9  | 2.7   | 2.4   | 13.1             |
| Personal services  | 4.0                              | 4.8   | 4.1   | 6.3   | 2.8   | 4.1  | 3.1   | 2.3   | 5.6              |
| Value Added        | 5.1                              | 1.6   | 5.3   | 0.3   | -1.7  | 3.2  | -6.2  | -2.4  | 91.3             |
| GDP                | 5.1                              | 1.7   | 5.0   | 0.2   | -1.8  | 3.1  | -6.4  | -3.0  |                  |

### Outlook

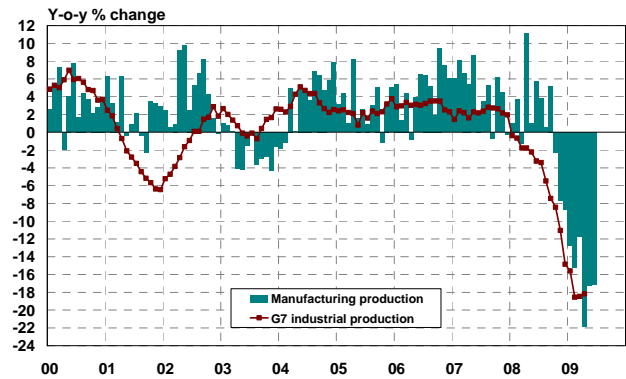
Economic conditions will remain weak for the rest of this year, but some levelling out is expected in the third quarter followed by a slightly better performance in the final quarter. Much still depends on the state of the global economy. Global activity improved slightly in the second quarter. China's economy picked up pace, boosted mainly by a massive fiscal stimulus package and aggressive credit growth. The rates of decline in US and UK gdp slowed down to around 1%, while Germany, France and Japan even managed to produce positive, albeit modest, growth rates. Overall, the global economy appears to be gradually levelling out, helped mainly by highly stimulatory fiscal and monetary policies as well as aggressive stockpiling of bulk commodities by China. However, we still expect only a slow and weak recovery off a very low base over the next 6 to 12 months as the short-term effects of the various fiscal stimulus packages start to fade and the anticipated build up in global inventories proves disappointing. The global economy will instead be hampered by altered credit markets, a massive debt overhang and higher unemployment, resulting in subdued and sluggish growth in the second half of 2009 and for much of 2010.

Volatile and weak performance is therefore still expected from the main exporters in the mining and manufacturing sectors. Mining should fare better than manufacturing, supported by stronger Chinese demand and some degree of restocking in some industrialized countries. Higher unemployment, falling income and fragile confidence will continue to undermine household demand, keeping spending in check and containing credit demand. As a result, the retail trade, hotels, restaurants, finance, insurance and real estate industries will all be subdued, but some consolidation is likely in the third quarter before a modest recovery starts in the fourth quarter. Lower interest rates and heavily discounted pricing may revive demand for durable goods in the months ahead, but a broad recovery is only likely once job losses and household finances improve. In contrast, construction and general government activity is likely to remain positive, but the rate of growth is expected to slow further in the months ahead. This is partly as some projects related to the hosting of the FIFA World Cup nears completion and the flow of new projects from the private sector dries up, but also as pressure on government finances starts to mount in face of falling tax revenue. Overall, gdp is still expected to contract by about 2% in 2009 as whole, before growing by around 1,7% in 2010.

**Figure 1: The leading indicators of major economies point to a turn in the cycle**



**Figure 2: South Africa continues to track global activity**



### Implications

Today's weak gdp figures validate the Reserve Bank's decision to cut interest rates further in August. Even though some economic indicators suggest that the worst of slide is probably behind us and that the local economy may even emerge gradually from 'official recession' later this year, the recovery, both globally and locally, is expected to be slow and sluggish, while excess capacity and weak demand will reinforce the downward trend in inflation in the months ahead. As a result, we still expect another 50 basis point cut in interest rates in October, bringing prime down to 10% by year end.

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