DEPARTMENT: AGRICULTURE
REPUBLIC OF SOUTH AFRICA

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PREFACE

The core business of this directorate is to do analysis on national level in order to produce agricultural economic information and advice for sound decision-making on the South African (SA) agricultural sector. In an effort to support this important task a new division (Economic Research) has been established in the directorate to concentrate on economic analysis relating to the performance of and external impact on the agricultural sector and its industries.

This publication developed from a need within the Department of Agriculture (DoA) to be regularly informed on recent developments and expected economic trends relating to the agricultural sector. To provide in the last mentioned need a quarterly report has been compiled for internal consumption over the last two years. Since the beginning of 2004 the report is also published for outside consumption as it can add value to a number of existing regular economic publications on the agricultural sector. The launch of this new series is therefore a historical landmark in the short history of the new Economic Research Division. It is our vision to establish it as indispensable reading for every serious student of the SA agricultural sector.

The format and content is still in the experimental phase. At this stage most of the content is based on sources outside the DoA. In time we hope to incorporate more departmental generated material. We would, therefore, appreciate comments on the content of this quarterly report series.

Mr B J van Wyk
Senior Manager: Economic Analysis
October 2004
Pretoria

1 WORLD ECONOMY

During the second half of last year, the world economy grew at an annualised rate of 6%. According to the IMF, this rapid rate of expansion continued during the first quarter of the year. However, there are signs of some slowing during the second quarter, as the higher crude oil prices impacted on US consumer spending and China's high fixed investment rate slowed sharply in response to administrative and monetary tightening measures implemented by the Chinese authorities. The slowdown in the US is expected to be temporary and that in China should be contained as the economy experiences a soft landing. Furthermore, real economic growth continued to accelerate in the rest of the world. In Japan especially, economic prospects are the most promising in a decade with business confidence measures on decade-highs and domestic-demand growth taking over from the initial export-led growth. European economic prospects are improving with accelerating labour market reforms. Real Gross Domestic Product (GDP) growth for a few important industrial and developing countries are summarized in Table 1.

2 SUB-SAHARAN ECONOMY

Although Sub-Saharan Africa's real GDP growth rate dipped in 2003 to 3.3%, from 3.8% in 2002, the growth is expected to rebound, to 4.5% in 2004 and 4.6 in 2005. This is according to the Economist Intelligence Unit (EIU). The increase in the overall growth rate for Sub-Saharan Africa will be driven by a steady rise in growth in three of the four subregions into which the subcontinent is broken down for analytical purpose, the three being Southern African Development Community (SADC), the Franc Zone and East Africa. In contrast, growth in the final region, Central and West Africa is set to fall back quite quickly, from being easily the fastest-growing subregion in 2003 to the slowest-growing by some margin in 2004-5. The economic growth is forecast to pick up fastest in the Franc Zone, up from 3.1% in 2003 to 7.2% in 2004, before moderating to 4.8% in 2005. The acceleration in 2004 is driven largely by the continuing good economic performance of the agricultural sector, both in terms of food crops and a buoyant cotton harvest, in many of the Sahelien countries, notably Burkina Faso, Mali, Niger and Senegal. In addition, a very sharp pick-up in growth is expected in the two new oil producers in the subregion, Equatorial Guinea and Chad. Although these two countries are only small, their rates of growth will be rapid enough to have an impact on the overall growth rate.

TABLE 1: The World Economic Outlook-Real GDP growth

Industrial countries	2003	2004	2005	Developing countries	2003	2004	2005
Major seven	2.2	3.7	3.2	Emerging Asia[2]	3.7	5.8	4.4
USA	3.1	4.4	3.8	China	9.1	8.6	7.6
Japan	2.5	4.8	2.7	India	8.2	6.5	6.5
Euroland[1]	0.5	2.1	2.6	Latin America	1.5	5.2	3.7
UK	2.2	3.6	3.0	Emerging Europe[3]	5.4	6.1	5.1

[1] The 11 Euro countries

[2] Taiwan, Hong Kong SAR, Singapore, South Korea, Malaysia, Indonesia, Thailand and Philippines

[3] Bulgaria, Czech Republic, Hungary, Poland, Slovak Republic, Russia, Turkey

Source: *Economic prospects, Third quarter 2004*

3 SOUTH AFRICAN ECONOMY

The South African economy continued its long-term trend of positive economic growth with 3.9% growth rate in the last quarter. This growth rate is not enough for rapid poverty eradication. A range of economic indicators firmly suggest that the buoyancy in real domestic expenditure is continuing with fixed capital formation showing a steady increase. Household expenditure is increasing although at a cautionary rate. The government consumption expenditure has stabilised and seemingly under control. The current macroeconomic environment of low interest rates, a strong currency, negligible inflation pressure and above-inflation wage growth is proving a boon to the domestic market and is expected to persist for the foreseeable future, albeit that some slowdown in the current heady pace is possible towards year end. The real domestic expenditure is forecasted to accelerate to growth of 4.5% on average during this year and to decelerate only moderately to about 4.3 the following year.

4 MACROECONOMIC VARIABLES AND THEIR IMPACT ON AGRICULTURE

4.1 Inflation

Recent trends: South African inflation climbed at a slower pace than expected in July and August, thanks to lower food prices. According to the latest data released by Statistics South Africa, the CPIX (the annual percentage change in the consumer price index excluding interest rates on mortgage bonds) rose 4.2% year on year in July and 3.7% year on year in August. Furthermore, producer price index (PPI) for all commodities for South African consumption only rose by 1.1% year on year in August from 0.7% year on year in July. The figures mentioned above virtually confirm that CPIX would remain within the 3% to 6% target range for the next 12 to 18 months.

TABLE 2: Annual CPIX inflation rates

	2003	2004	2005
BER	6.8	5.0	5.4
BMI	4.0	5.5	5.2
CONSENSUS	5.0	5.5	5.1

Bureau for Economic Research (BER); Business Monitor International (BMI); Consensus between ABN Amro, ABSA bank, Deutsche Bank, Goldman Sachs, IMF, ING, JP Morgan, Lehman Brothers,

CPIX has stuck within the target mainly due to the strong currency that actually kept the prices of imported products subdued.

Forecast: The CPIX inflation is expected to remain within the target as indicated in table 2 above. The consensus between various financial institutions is that inflation will average 5.5 % for the year 2004 and decelerate to 5.1% for the early part of 2005. However, some analysts warned that rampant global oil prices could negatively affect the country's inflation trend.

Impact on agriculture: The soaring global oil prices could exact some increased cost pressure on the sector but the low and stable interest rates can provide a shield from any knock-on effect. A fairly strong rand could also assist in containing the inflationary effect of an oil shock, allowing the Reserve Bank to keep interest rates steady.

4.2 Growth

Recent trends: The economy expanded by about 2.5% year on year in real terms in the last quarter and the strength of the rand suggests that the growth continue to be driven by domestic demand. Importantly, the manufacturing sector finally emerged from four consecutive quarters of contraction, with growth of 1.2% year on year, a performance that suggests that it is able to

TABLE 3: Annual real GDP growth rates

	2003	2004	2005
BER	1.9	2.7	3.6
BMI	1.9	2.7	3.5
Consensus		2.8	3.2

Bureau for Economic Research (BER); Business Monitor International (BMI); Consensus between ABN Amro, ABSA bank, Deutsche Bank, Goldman Sachs, IMF, ING, JP Morgan, Lehman Brothers, Merrill Lynch, Nedcor Bank, Standard Bank, West LB Asset Management

cope with a stronger currency. According to the South African Reserve Bank's Quarterly Bulletin (June 2004), real household expenditure increased by an annualised rate of 5% and real private fixed capital formation by close to 10%. The government and parastatals are also said to have made a strong contribution. Both consumer and retail confidence have reached historical highs with retail sales volumes expanding at a rate around 5% year on year and new vehicles sales reported by NAAMSA are said to be on historical highs. The BER building confidence index also reached a 22-year high. The current macro-economic environment is proving a boon to the domestic market

Forecast: The low interest rates, a strong currency, negligible inflation pressures as well as the above-inflation wage growth has created an environment many analysts expect will persist for the foreseeable future. The BER is forecasting real domestic expenditure to accelerate to growth of 4.5% on average during 2004 and to decelerate only moderately to 4.3% next year. Previously the BER forecasted the GDP for 2004 at 3.3% and has since revised it to 2.7%, mainly due to the weak net exports (i.e. exports minus imports) which could subtract substantially from growth. The Business Monitor International (BMI) has reviewed their forecast from 2.2% to 2.7% for this year and from 3.7% to 3.5% for next year. Consensus by various financial institutions has somewhat improved marginally despite expectations that the rand will end the year firmer than originally anticipated. The consensus' latest forecast has improved from 2.6% to 2.8% for 2004 and to 3.2% for 2005 from the previous forecast of 3.1% - see table 3.

Impact on agriculture: The South Africa's growth prospects as well as the fact that agricultural industry was mentioned as one of the main contributors to the increase in economic activity for the last quarter, has a positive impact on the sector.

4.3 Exchange rates

Recent trends: The rand has been the best performing emerging market currency both last and this year, appreciating against the US dollar by about 28 percent in 2003 and 14 percent in 2004. It actually breached the R6/$ level at the beginning of this quarter. The rand's strength is mainly driven by external factors such as US dollar weakness, large interest rate differentials with foreign currencies and positive outlook for commodities. According to the BER, the interesting aspect of the rand's continued appreciation during the 2004 is the fact that the dollar has not really weakened as it fluctuated between 1.25 and 1.20 against the euro. Recently the rand appreciated by more against the Japanese yen and euro than against the US dollar. The rand actually tended to strengthen against all of these currencies in 2004. This rand resilience has been able to contain inflation below the 6% upper limit of the target range inspite of high international oil prices and as a result, interest rates have remained at their lowest levels in nominal terms in decades.

Forecast: The external factors mentioned above are expected to only reverse well into next year, in which case the rand may come under increasing selling pressure to revert back to a "fairer" value. As indicated in table 4, the BER forecast R6.90/$ for 2004

TABLE 4: Annual average R/$ exchange rates

	2003	2004	2005
BER	6.74	6.90	8.30
BMI	6.64	7.00	7.80
Consensus	7.20	7.00	7.60

Bureau for Economic Research (BER); Business Monitor International (BMI); Consensus between ABN Amro, ABSA bank, Deutsche Bank, Goldman Sachs, IMF, ING, JP Morgan, Lehman Brothers, Merrill Lynch, Nedcor Bank, Standard Bank, West LB Asset Management

and R8.30/$ for 2005. BMI is forecasting

R7.00/$ and R7.80/$ for 2004 and 2005 respectively. The consensus by financial institutions forecasted R7.00/$ and R7.60/$ for 2004 and 2005 respectively. However, the rand's strength could still persist if the capital inflows are in South Africa's favour given the rand demand for financing the widening current account deficit.

Impact on agriculture: The impact of the strong rand has mixed fortunes for the sector. On the positive side, the rand's strength has provided the opportunity to replace old equipment. According to the industry leaders, the price cuts on farming equipment by local distributors have contributed directly to the revival of the agro-business. For example, the prices in all four categories of agricultural equipment i.e. tractors, combine harvesters, haymakers and implements, have fallen by some 6.4% year on year by June with combine harvesters 8% lower than a year ago. On the negative side it has rendered the sector less competitive.

4.4 Interest rates

Recent trends: Earlier in this quarter, the South African Reserve Bank cut the repo interest rate by an unexpected 50 basis point (half a percentage) to 7.50%. The rate cut was widely seen as an attempt to weaken the currency and stimulate growth and job creation. Some economists were sceptical of the effects of the move as they cautioned that there would not be a material difference to either export performance and therefore unemployment or the inflation outlook. The strong rand seems to have served as an implicit monetary tightening tool over the course of the past few quarters and has kept inflation firmly in check and resulting in the lower interest rate. The historical lower levels of the interest rate have contributed to the continued buoyancy in domestic consumer spending.

Forecast: Global interest rates led by United States of America and to a lesser extend the United Kingdom, are on their way up and naturally this would have had an impact on the South African economy. At the beginning of the year many observers were predicting a rate hike in the third or fourth quarter, with expectation being that the rand would be around R7.50 to the dollar. Given the strength of the rand and the controlled inflation environment, increased interest rate seems implausible. According to economists at Global Trader, a rate hike in the first quarter of next year is likely. In general, the consensus view is that interest rates will remain constant for some time, but may move up towards the end of 2004 or in early 2005, mainly due to the continuing global oil price hike.

Impact on agriculture: The current level of the interest rates continues to benefit agriculture. Agricultural producers are taking advantage of the prevailing environment (low interest rates) to increase their debt (through more current and capital expenditure on credit), hence the rise in total agricultural debt. The envisaged currency strength can impact negatively on the agricultural export sector.

5 OTHER FACTORS IMPACTING ON AND RELATED TO AGRICULTURE

5.1 Climatic conditions

Most of the country except over the Northern Cape, Free State and North West provinces observed normal to above normal rainfall conditions during July 2004. The conditions gradually dried up over the most of the country except Mpumalanga, parts of KwaZulu-Natal and the eastern part of the Western Cape where the above – normal rainfall conditions continued during August 2004. It was dry over the country during September. Levels of dams dropped below 40% of normal storage capacity with exception of the Western Cape where they are at around 50% due to recent good rains. The country in general experienced poor grazing conditions which resulted in most farmers feeding their livestock. Winter crops over the Western Cape were in good condition except for the north-western part where drought conditions persisted. Both the SARCOF- 8 and SAWS forecasts indicate likelihood of near normal rainfall conditions with a bias to below normal accompanied by above normal temperatures. Rainfall prospects are expected to deteriorate in early 2005 according to the latest seasonal forecast but this will depend on the developments over the oceans and as such monthly updates of the forecasts would be crucial. Despite some good winter rains over most of the country, dry and hot conditions are prevailing at the moment.

5.2 Crop production and estimates

Table 5 summarises the final estimated plantings and production of the most important summer crops for the 2003/04 season. The expected commercial maize crop is 8,706 million tons – 5,346 million tons white maize and 3,360 million tons yellow maize. The area planted to commercial maize is 2,646 million ha, of which 1,728 million ha (65%) is for white maize and 0,918 million ha (35%) is for yellow maize. The majority of South Africa's maize is produced in the Free State, Mpumalanga and the North West provinces and represents respectively 31,7 %, 23,7 % and 28,3 % of pro-

TABLE 5: Estimated plantings and production of summer crops for the 2003/04 season

Crop	Estimated plantings for the 2003/04 season	Change from the 2002/03 season		Estimated production for the 2003/04 season	Change from the 2002/03 season	
	Ha	Ha	%	Tons	Tons	%
Total maize	2 645 600	(539 350)	(16,93)	8 706 250	**(685 200)**	**(7,30)**
White maize	1 727 600	(504 850)	(22,61)	5 346 150	**(1 019 400)**	**(16,0)**
Yellow maize	918 000	(34 500)	(3,62)	3 360 100	**334 200**	**11,04**
Sorghum	118 750	23 253	24,35	336 370	**116 856**	**53,23**
Groundnuts	62 300	12 500	25,10	98 265	**38 260**	**63,76**
Sunflower seed	526 125	(80 325)	(13,25)	663 400	**20 790**	**3,23**
Soya-beans	122 260	22 130	22,10	217 885	**81 365**	**59,59**
Dry beans	56 200	5 190	10,17	78 570	**18 275**	**30,31**

Source: Directorate Agricultural Statistics duction. Table 6 summarizes the estimated plantings of the most important winter crops for the 2004/05 season. The preliminary area estimate for wheat is 851 200 ha, which is 13,8% higher than the 748 000 ha planted for the previous season. An estimated 375 000 ha or 44,1% are in Free State, 356 000 ha or 41,8% in Western Cape and 51 000 ha or 6% in the Northern Cape.

TABLE 6: Estimated plantings and production of winter crops for the 2004/05 season

Crop	Estimated plantings for the 2004/05 season	Change from the 2003/04 season		Estimated production for the 2004/05 season	Change from the 2003/04 season	
	Ha	Ha	%	Tons	Tons	%
Wheat	851 200	103 200	13,80	1 976 475	436 475	28,34
Barley	82 650	(1 570)	(1,86)	204 790	(35 210)	(14,67)
Canola	45 500	1 300	2,94	45 500	4 730	11,60
Sweet lupines	7 100	(3 000)	(29,70)	5 000	960	23,76

Source: Directorate Agricultural Statistics

5.3 Food pricing report

The report of the Food Pricing Monitoring Committee has been recently released after a year-long investigation into food prices. The prices are said to have rocketed in 2002 on the back of a weakening rand. At the time there were allegations made against the businesses in the value chain that they were making excessive profits. The report found that the food inflation escalated by 20% whilst the currency depreciated and only decline by 3.8% when the rand strengthened. Various income groups were found to have been affected differently by food inflation. Poor households experienced food inflation as high as 23% year on year whilst the richer households experienced lower increases at 19% year on year. The South African government through its parliament has decided to strengthen the capacity of the agricultural department to collect information and strengthen partnerships in dealing with food relief programmes. It also called on the department to continue analysing the performance of strategic food value chains to improve their performance, efficiency, competitiveness and the management of food supply risk. The continued monitoring will ascertain whether or not lower food prices and the benefits of a strengthening currency are being passed on to the consumer.

5.4 Ban on poultry exports

South Africa's global position as the largest exporter of ostrich meat is threatened due to ban on poultry and related products. DoA placed a ban on the export of ratites (flightless birds) after an outbreak of avian influenza virus was discovered at two ostrich farms in the Eastern Cape. The European Union, Namibia, Switzerland and Hong Kong announced bans on South African poultry, including ostrich products. About 95% of South Africa's ostrich meat is exported and the industry contributes R1.2 billion to the country's annual export earnings with employment standing around 20 000 people. About 6 000 birds have been targeted in the culling operation and the farmers will be compensated as the Animal Disease Act provides for such compensation.

5.5 Agricultural census - key findings

The preliminary results of **Census of Commercial Agriculture 2002** were released on the 15th September 2004. According to the results, the number of paid employees in formal agriculture decreased by 13.9% (152 450 paid employees) from 1 093 265 to 940 815 over the nine years since 1993. Of the nine provinces, the Western Cape employed the largest number of paid employees (22.5% or 211 808), followed by Free State (13.1% or 123 429), Mpumalanga (12.8% or 120 065) and KwaZulu-Natal (12.4% or 117 207). The formal agricultural sector generated a gross farming income of approximately R53 billion. Over R21 billion (40.1%) of this was generated from commercial farming in animals and animal products. In 1993, the share of gross farming income generated by formal agriculture from animals and animal products was 49.8%. Field crops and horticultural products contributed most of the balance of income in the sector, with contributions of 31.1% and 26.8% respectively. This means that the percentage contribution of field crops and horticultural products has increased at the expense of the animals and animal products since 1993. Total expenditure by the formal agricultural sector amounted to R42 billion. The ratio of farming debt to the market value of farming assets rose from 22.9% in 1993 to 31.3% in 2002. Farming debt amounted to R31 billion with Western Cape being responsible for 23.7% of farming debt , followed by Free State (16.9%) and Northern Cape (11.2%), while Gauteng had the lowest proportion of debt (3.4%). The detailed census report will be published in December this year.

5.6 Gross domestic product (GDP) benchmarking.

GDP is calculated via three methods, i.e. production, income and expenditure approach as recommended in the System of National Accounts 1993 (SNA93). SARB uses the expenditure approach while Stats SA follows the income and production approach. **The Department of Agriculture (DoA)** plays a pivotal role in the estimation of GDP, as it provides the information used for calculating the value added of the agricultural industry as well as some of the expenditure information on food. All these methods require periodic rebasing and benchmarking. Rebasing is the process in which the reference year of the constant price estimates is updated, e.g. reference year is changed from 1990=100 to 1995=100. This exercise (benchmarking) entails the incorporation of new areas of economic activity that were previously un- or under covered as well as the incorporation of new detailed information. DoA, Stats SA as well as the SARB have previously (1998) worked together in similar exercise. In June 1999, the first national accounts results based on the SNA93 were published and they revealed that the level of the revised GDP at current prices was significantly higher (between 11 and 14 percent) than previous estimates for the period 1993 to 1998. Similar outcome is anticipated in the November 2004 GDP benchmarking exercise. International practice requires national accounts estimates to be revised at least every five years. As noted above the last revision was done in 1999 by benchmarking and rebasing to 1995. Stats SA has therefore planned to revise the national accounts estimates from 1998 to 2003 and to change the base year from 1995=100 to 2000=100. This process started in the third quarter of 2003, with the cooperation of SARB and DoA. The plan is to publish the revised national accounts estimates in November 2004.

5.7 AgriBEE for South Africa unveiled.

This quarter saw the unveiling of the AgriBEE framework by the agriculture and land affairs minister. The ministry proposes that the agricultural sector should avail some of the farming land to black individuals and communities by 2014. This would be constituted by ownership and lease-holding. The ministry further proposes that some of the farmland be made available for use by farm workers in order to address issues of poverty alleviation as well as creating opportunities for small, medium and micro enterprises in this sector. The framework distinguish between land and enterprise and also proposes that the industry enter into joint ventures and partnership arrangements to ensure that export market opportunities are created for black-owned enterprises. The framework also aims at the elimination of illiteracy by 2010. Management level representation of black people within the industry, i.e. executive, middle and junior levels, is also dealt with in the framework. The framework with proposals is now in the public arena for further debates with the stakeholders. The ministry has formed a steering committee that will be considering further proposals and charting the way forward. The closing date for these further proposals is the 20th December 2004.

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