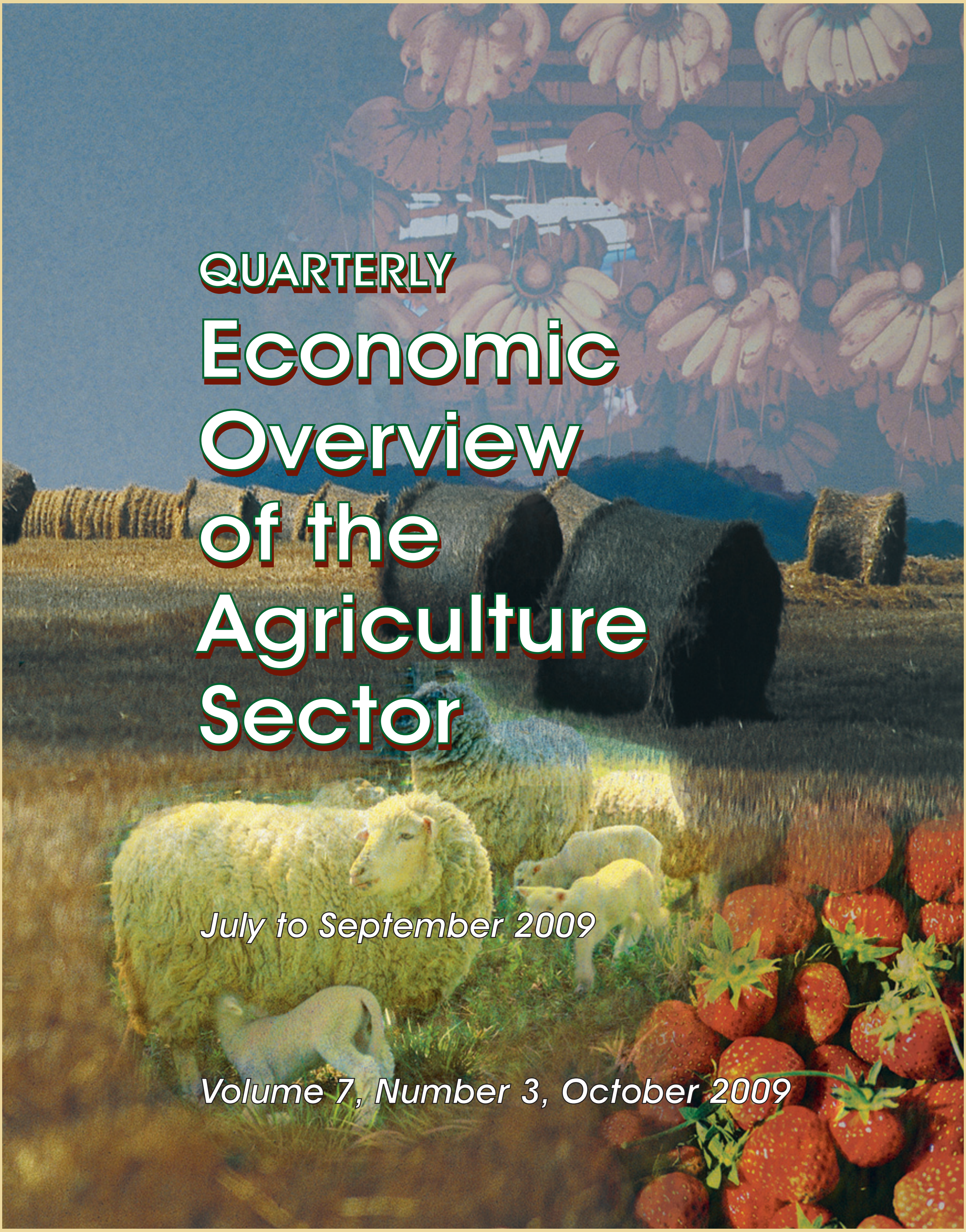

QUARTERLY

Economic Overview of the Agriculture Sector

July to September 2009

Volume 7, Number 3, October 2009

agriculture, forestry & fisheries

Department:
Agriculture, Forestry and Fisheries
REPUBLIC OF SOUTH AFRICA

PREFACE

The core business of the Directorate: Economic Services is to undertake analysis of national-level trends in order to produce agricultural economic information and to render advice for sound decision making on the South African (SA) agriculture sector. To support this important task the Economic Research division/unit concentrates on the economic analysis of the performance of and external impact on the agriculture sector and its industries.

This publication, previously called the Quarterly Agricultural Economic Review and Forecast, developed from a need within the Department of Agriculture, Forestry and Fisheries (DAFF) to be regularly informed on developments and expected economic trends in the agriculture sector. The quarterly report has now been established as a regular feature in the Directorate's work plan. Since the beginning of 2004 the report has also been published for outside consumption to add value to a number of existing regular economic publications on the agriculture sector. It is our vision to maintain it as indispensable reading for every serious student of the SA agriculture sector.

This issue looks at the developments and expected economic trends in the SA agriculture sector given the slowdown in the domestic economy triggered by the global economic slowdown.

Any new comments on the content of this quarterly report series are most welcome.

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October 2009
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1. WORLD ECONOMY

According to the International Monetary Fund, World Economic Outlook Update, July 2009 (IMF WEO, July 2009), the world economy is stabilizing, helped by unprecedented macroeconomic and financial policy support. However, the recession is not over yet and the recovery is likely to be sluggish. Following a disappointing first quarter, during which the global economy contracted almost as fast as during the fourth quarter of 2008, data point to a return to modest growth at the global level. However, the advanced economies as a group are still projected not to show a sustained pickup in activity until the second half of 2010, consistent with the April 2009 WEO forecast. Some indicators are presented in Table 1 below.

Accordingly, global activity is forecast to contract by 1.4% in 2009 and to expand by 2.5% in 2010, which is 0.6% higher than envisaged in the April 2009 WEO. The higher annual average growth rate for 2010 largely reflects carryover from a mark-up in growth during the final half of 2009. The downward drag exerted by the financial shock, the sharp fall of global trade, general increase in uncertainty and collapse of confidence is gradually diminishing. However, supportive forces are still weak. Many housing markets have yet to bottom out. Importantly, financial markets remain impaired and bank balance sheets still need to be cleaned and institutions restructured. Cuts in policy interest rates, continued provision of ample liquidity, credit easing, public guarantees, and bank recapitalization have appreciably lowered concerns about systemic failure. Consistent with these developments, financial stress indexes for advanced and emerging economies have receded since the beginning of 2009. However, the improvements are far from uniform across markets and countries. In particular, bank lending conditions are expected to remain tight and external financing conditions constrained for a considerable time. At the same time, commodity prices have rebounded ahead of the recovery. The recent rally in commodity prices has been strong and broad-based, reflecting improved market sentiment, U.S. dollar depreciation, and commodity-specific factors.

In the oil market, prices have responded strongly to perceptions that market dynamics are shifting from significant oversupply to more balanced conditions. This is in part due to improving demand prospects, and the Organization of Petroleum Exporting Countries (OPEC) members' strict observance of lower production quotas. Oil prices are expected to average $74.50 for 2010, not much above current levels, with high excess capacity expected to buffer growing demand. In this setting, activity and credit growth are likely to remain subdued in many economies. Currently, expansionary macroeconomic policies and an inventory adjustment are supporting global activity but these are temporary forces.

GDP in the advanced economies is expected to contract by 3.8% in 2009 before growing by

0.6% in 2010. Although the projections are 0.6% higher than in the April WEO forecast, growth in 2010 would still fall short of potential until late in the year, implying continuing increases in unemployment. Among the major economies, growth rates have been marked up mainly for the United States and Japan. In the **United States**, indicators point to a diminishing rate of deterioration, including in the labour and housing markets. Industrial production may be close to bottoming out, the inventory cycle turning, while business and consumer confidence has improved. These developments are consistent with stabilization of output during the second half of 2009 and with a gradual recovery emerging in 2010.

Meanwhile in the **Euro Area**, consumer and business survey indicators have been recovering, but data on real activity show few signs of stabilization, and thus activity is expected to strengthen more slowly than elsewhere. Macroeconomic policies are providing support but much of the adjustment in the labour market still lies ahead. Rising unemployment will weigh on consumption and activity, as will the economy's heavy dependence on a still-ailing banking sector. The Euro area trade surplus posted a big increase in July, from -€3.5 billion in July 2008 to +€12.6 billion in July 2009. This indicates that the euro area GDP number received a big contribution from net exports. With indicators of domestic demand also stabilizing, this will almost certainly mean that third quarter Euro area GDP will increase significantly compared to the previous quarter though it will remain down compared to four quarters earlier.

Emerging and developing economies are expected to regain growth momentum during the third half of 2009, with notable regional differences. Low-income countries are facing important challenges of their own because official aid has fallen and these economies are particularly vulnerable to swings in commodity prices. Growth projections in **emerging Asia** have been revised upward to 5.5% in 2009 and 7.0% in 2010 (IMF WEO, July 2009). The upgrade owes to improved prospects in China and India, in part reflecting substantial macroeconomic stimulus, and a faster than expected turnaround in capital flows. However, the recent acceleration in growth is likely to diminish unless there is a recovery in advanced economies.

Inflation pressures have continued to ease with the continued weakness of the global economy. Between December 2008 and August 2009, the seasonally unadjusted U.S. consumer price index increased by 2.7% at an

TABLE 1: The World Economic Outlook-Real GDP growth %

Countries	2008	2009	2010	Countries	2008	2009	2010
World[1]	3.0	-1.1	3.1	China	9.0	8.5	9.0
USA	0.4	-2.7	1.5	India	7.3	5.4	6.4
Japan	-0.7	-5.4	1.7	Latin America	4.6	3.2	7.9
Euroland[2]	0.7	-4.2	0.3	East-central Europe	3.0	-5.0	1.8
ASEAN-5[3]	4.8	0.7	4.0	Sub-Saharan Africa	5.5	1.3	4.1

Source: IMF [1] PPP [2] The 11 Euro countries [3] Indonesia, Thailand, Philippines and Malaysia annualized rate. Yet the yearly change was still -1.5%, due to a drop in the CPI of more than 4% between August 2008 and December 2008. A similar trend can also be seen in the Euro area, where the inflation rate rose from -0.7% in July to -0.2% in August. This trend will likely also be seen in other countries, though less dramatically (or in some cases not at all) as some countries saw their currencies plummet in value late last year, only to rise dramatically in value this year. The Euro area saw its inflation rate rise from -0.7% in July to 0.2% in August. Unemployment rates will reach double digits in some countries, holding back wages and household spending and presenting significant policy challenges. In the emerging economies, stronger disinflationary forces in some regions have prompted modest markdowns to the April projections for inflation, notwithstanding the upward revisions to output growth.

The U.S. trade deficit increased more than expected in July, from an upwardly revised $27.5 billion in June to $32 billion in July. The main causes were higher oil prices and increased imports of car and car parts – the latter being a result of the "cash for clunkers" scheme and the way it particularly benefits buyers of Japanese and Korean cars (G8 Summit, July 2009).

According to IMF's July 2009 Global Financial Stability Report (IMF GFSR, July 2009), while policies still have a long way to go in dealing with the crisis, there will also be a need to increasingly shift from providing short-term support to laying the foundations for a return to strong medium-run growth. This will depend crucially on fostering stronger potential output growth, particularly in advanced economies, and rebalancing global demand. Financial, monetary, fiscal, and structural policies all have a role to play in this regard. The G8 Summit held in July 2009 concluded that $20 billion will be invested by countries which include the G8 and G5, as well as international organisations, including the World Bank, within three years to encourage rural development of poor countries. The money for agricultural development is designed to advance the fight against hunger, according to officials. The food security part of the G8 communiqué points out that, while the prices of food commodities have decreased since their peak of 2008, they remain high in historical terms and volatile. However the G8's solutions rest on liberalizing trade and announcing some extra money. Markets must remain open, protectionism rejected and factors potentially affecting commodity price volatility, including speculation, monitored and analysed further.

Through the $20 billion funding initiative, the G8 group will partner with vulnerable countries and regions to help them develop and implement their own food security strategies, and together substantially increase sustained commitments of financial and technical assistance to invest in those strategies. This is supposed to be done via effective coordination, support for country-owned processes and plans as well as by the use of multilateral institutions whenever appropriate.

2. SUB-SAHARAN ECONOMY

Many countries in Africa have been severely hit by the global economic downturn, but there are emerging signs that the worst is over in many economies, with leading indicators such as economic activity as well as consumer and business confidence registering less sharp falls in the last two months than earlier in the year. Commodity-exporting countries have benefited from China's massive fiscal stimulus and high level of bank lending, which have helped to sustain demand for African exports (thereby boosting a vital source of foreign exchange) and appear to be promoting a more rapid rebound than previously envisaged. Some key indicators are presented in Table 2 below.

TABLE 2: Sub-Saharan Africa – Economic Outlook

	2007	2008	2009	2010
Growth	6.5	5.5	0.6	4.1
Consumer Inflation	6.4	12.6	8.8	6.7
External Debt[1]	168.7	175.3	180.7	190.9
Current Account[1]	-23.1	-19.1	-41.5	-33.2

Source: EIU [1]US$ Billion

Recent data indicate that demand for African minerals is rising again after a sharp fall at the start of the global slowdown. Although China-Africa trade fell to $37.1 billion for the first half of 2009 (compared with $48 billion for the same period last year), China's investment in Africa increased by 81% to $552 million for the first half of the year. Reflecting these changing conditions, forecasts have been upgraded for regional real GDP in 2009 and 2010 over the course of the last three months.

In a June report, a modest growth of 0.4% in 2009 and a rebound of 4.1% in 2010 were expected. Currently, a slightly higher growth of 0.6% in 2009 is expected (Economist Intelligence Unit (EIU), September 2009). This marks the first time that GDP forecasts have not been downgraded since the end of 2008. This partly reflects improved expectations about global growth, which is now expected to contract by 1.4% in 2009 and to grow by 2.7% in 2010, compared with 1.8% and 2.1% respectively at the time of our June report. In spite of the modest upgrade to regional projections, Africa's performance in 2009 will remain extremely disappointing. A downturn in domestic demand and trade will account for much of the contraction, reflecting rising unemployment and falling real earnings. In some economies private consumption will also be hard hit by weakening inflows of worker remittances from the US and the EU. This not only reflects the slowdown in the US and EU economies, but also the fading of reporting gains and tighter immigration control in the US and EU.

Gross fixed investment is also set to fall significantly, reflecting much scarcer credit. Much lower export orders will be offset by a significant fall in import volumes, on the back of weaker domestic demand. This will result in a positive contribution to GDP by the external sector. The expectation of a gradual recovery in regional GDP growth in 2010 is based on the assumption that monetary easing undertaken in 2010 will help boost private consumption, while more supportive credit conditions will help investment to stage a partial recovery. Higher commodity prices are expected to underpin growth in government spending (EIU, September 2009). According to EIU, growth will be lowest in **Southern Africa**, at -1.9% in 2009, recovering to 3.7% in 2010. The global downturn continued to weigh on the South African economy in the first half of 2009, real GDP shrank by a sharp 6.4%. The immediate outlook remains fairly bleak for the region's largest economy, South Africa. The performance of the key financial sector will clearly have a major impact on overall economic activity. The economy is now forecast to contract by 2.2% in 2009, before posting a recovery in 2010 as the global economy begins to recover and the soccer World Cup is held. A sharp deterioration in consumer and business confidence means that there is a high risk that the South African economy may enter a deeper than forecast recession.

Meanwhile in the **Central and West Africa**, sub regional growth is expect to remain low, at 3% in 2009, rising to 4.4% in 2010. The much weaker growth in 2009 will be driven largely by the modest growth in the Nigerian economy. The troubles in the Niger Delta, which have continued to intensify in recent months, are likely to depress oil production throughout the forecast period. In addition, the OPEC quota cut introduced in December 2008 will put pressure on the authorities to reduce production. Given the expected trends in the oil sector, overall economic growth in Nigeria will depend on the performance of the non-oil sector, as has been the case in the past three years. Although growth in the sector should remain positive, largely owing to the continued strong performance of the agricultural sector, it is likely to slow markedly in 2009 as Nigeria suffers from the global financial crisis. Growth is expected to be strongest in **East Africa.** Sub-regional growth is expected to dip from 6.5% in 2008 to 3.8% in 2009 and to rise to 4.9% in 2010. This reflects an expected slowdown in the largest economy in the region, Kenya, where real GDP growth is set to slow further in 2009, to 1.8% (previous forecast was 2%), as a result of the global downturn and weak commodity prices. The economy grew by 3.9% year-on-year in the first quarter of 2009, but came off a low base, while agriculture continued to decline, falling by 0.8% year-on-year. Export growth will also be down, reflecting lower global demand and weak commodity prices continuing to take their toll, although a concurrent downturn in import growth will offset this to some extent. The Kenyan economy is expected to post a small recovery in 2010 (assuming average rainfall), helped by a modest global rebound, which will push up real GDP growth to 2.7%. However, the global turnaround will be no better than patchy in 2010, which will constrain growth in tourism, trade, remittances and foreign investment.

In the **Franc Zone** growth is expected to remain low at 1.6% in 2009 and 3.8% in 2010. In part, this reflects the ongoing economic malaise in the largest economy in the region, Côte d'Ivoire, which in turn reflects the continuing political crisis in the country. Added to this is the fact that growth in Cameroon and Gabon, the other two large economies in the region, is forecast to be relatively low. Oil output is forecast to increase marginally in 2009/10, as declining production at the large, mature oilfields will be offset by the coming-on-stream of smaller, marginal fields. Given the size of these three economies, they account for around 45% of the Franc Zone's GDP and their poor performance more than offsets strong growth in other economies in the region (EIU, September 2009).

External debt: Unlike in much of the developed world, financial systems in Sub-Saharan Africa have not been heavily exposed to toxic assets and off-balance-sheet trades. This reflects generally cautious management practices in the region's financial systems. Consequently, some African governments have been able to focus their policy response to the downturn on fiscal and monetary stimulus. Stimulus packages will be insufficient to avert a severe downturn, but they will help to sustain activity and support a recovery once external and financing conditions improve. An increasing number of African countries have also benefited from large debt write-offs in recent years.

Over the forecast period, new borrowing will remain relatively high, especially from the multilateral lenders led by the World Bank and new bilateral lenders such as China. The growing influence of China as a creditor to the region is creating unease in some quarters, in part because it could entail a diminishing influence over policy and governance for the World Bank and the IMF. Nevertheless, concessional debt contracted from the multilaterals is likely to continue to represent the bulk of borrowing for most countries, especially given the increasing difficulties in accessing financing from the global financial markets in the light of the credit crunch. What has also become clear is that, despite the debt write-offs delivered to date, the need for further high levels of financing for African countries will become pressing in the coming years. Having fallen from $221.2 billion in 2004 to $153 billion in 2006, the region's stock of external debt is forecast to rise to $180.7 billion in 2009 and to $190.9 billion in 2010.

Despite the different policy responses, the rate of inflation has fallen slower than expected outside Southern Africa and the Franc Zone. This reflects the high level of food prices in the consumer price index, over which central banks have only limited control. However, without another good harvest in 2010; with growth picking up relatively quickly and with high levels of government spending, inflation is likely to bottom out in high single digits in many Sub-Saharan African countries, and then climb back into low double digits in 2010. Although food price inflation will be lower in 2009 than in 2008, this will be scant comfort for the majority of the region's countries, which are becoming increasingly reliant on imported food. Agricultural productivity in Sub-Saharan Africa is lower than anywhere else in the world, at $337 per worker (2000 prices), or just 39% of the global average, and below the average for all low-income economies.

The external accounts will deteriorate sharply, with the current-account deficit set to widen from $19.1 billion in 2008 to $41.5 billion in

2009. For this year, the overall deficit would be significantly larger were it not for a fall in the import bill as domestic demand falls and weaker exchange rates further restrict import capacity. The principal driver of the deterioration in the region's external accounts is the eradication of both Angola's and Nigeria's current-account surplus. Although it is expected that both the regional import costs and trade-related costs will fall - in line with reduced domestic activity and financial constraints - both invisibles and transfers inflows are also forecast to fall owing to reduced receipts from tourism and remittances. (EIU, September 2009).

3. SOUTH AFRICAN ECONOMY

As other countries are emerging out of recession, South Africa's recovery is expected to lag behind the rest of the world. South Africa has been very slow to feel the impact of the global economic downturn from its onset, with data showing the first impact of the economic crisis emerging only in the first quarter of 2009. Despite strong GDP figures for many countries, South Africa's economic growth continued to decline in the second quarter of 2009. Similarly employment, Business and Consumer Confidence data painted a bleak picture. Demand has also shrunk as households battle with debt. South Africa's output shrank by an annualised 3% in the second quarter of 2009 – this is the third quarterly contraction in a row. The manufacturing sector remained stagnant, contracting by 10,9%, which saw the government initiating joint talks with development finance institutions and commercial banks to extend credit to domestic companies that have been hit the hardest by global recession. GDP growth trends are presented in Figure 1 below.

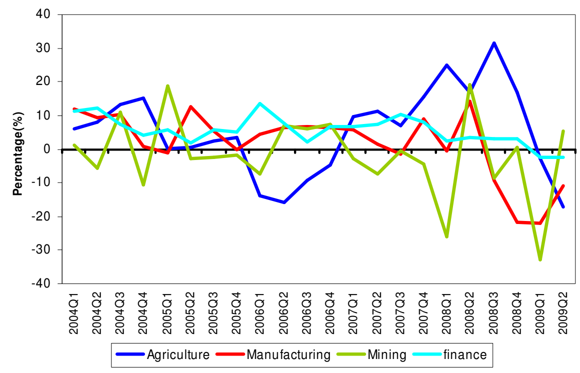

Fig. 1: GDP growth of selected sectors

Source: StatsSA

According to the Reserve Bank, credit extended to companies has fallen 0.4% in the year to June. Meanwhile, the agricultural and financial services sectors shrank by 17.1% and 2.4%, respectively. SA tractor sales fell by 32.4% year-on-year in July and again, by 6% in September due to tight bank regulations in obtaining finances for farmers, declining crop prices and a firmer Rand. However, the R2.6 billion pledge in conditional grants by the government to provinces, for agriculture infrastructure investment, is expected to boost the overall infrastructure sales and increase growth in the agricultural sector. Despite a contraction in most of the sectors of the economy, the mining sector grew by 5.5% in the second quarter on account of the rising global commodity prices after collapsing by 32.8% in the previous quarter. Increase in civil summonses issued in the first half of 2009 is a reflection of a continued difficulty in the economic environment, where households and businesses continue to struggle. Data released by StatsSA in August showed the total number of civil summonses issued for debt in June rose 11.5% year-on-year after rising 1.8% in the previous month. In the agricultural sector for instance, more than 283 emerging farmers owed a total of R232 million to the Land Bank, which resulted in the Minister of Agriculture, Forestry and Fisheries promising to assist the farmers to find solutions to get them out of debt.

Household expenditure, the most important component of domestic demand, which account for about two-thirds of GDP, fell sharply in the second quarter as consumer confidence remained weak after another contraction in household disposable income. Household disposable income declined by 5.7% in the second quarter, from 4.1% in the first quarter. As a result of a knock in household wealth, the first quarter data showed that household saving to income ratio stood at zero, an improvement from a record low of -0.7%. Household expenditure dropped by a seasonally adjusted 5.8% in the second quarter, which relates to stubbornly high levels of inflation. Despite the decline in debt servicing costs to 9.5% of disposable income along with falling interest rates, consumers are now opting for cash purchases rather than building up additional debt. (SARB, September 2009). Interest rates dropped from 15.5% in December 2008 to 10.5% in August. The 0.5% cut in interest rates in August is believed to be the last one, before the newly appointed Reserve Bank Governor, Gill Marcus, resumes her appointment from the first of November 2009. Figure 2 below presents household expenditure and disposable income trends.

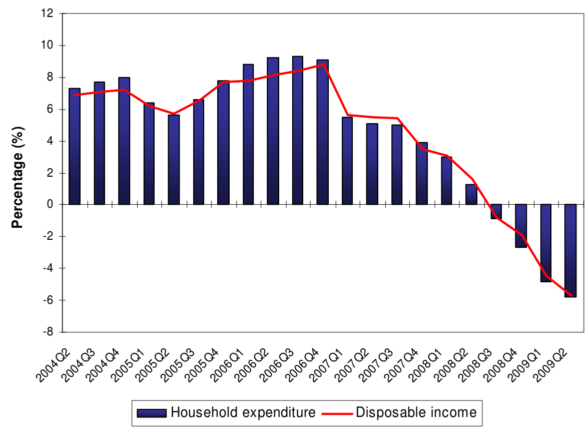

Fig. 2: Household expenditure vs disposable income

Source: SARB

Meanwhile, inflation trends have been more upbeat, although the movement was slower than expected. The CPI inflation moderated to 6.7% year-on-year in July, down from 6.9% in June. Higher insurance and financial services costs as well as administered price increases where the main culprits of the monthly rise. Food prices fell by 0.6% - this is the second monthly fall in a row. However, the development of El Nino weather conditions later this year poses a threat to food inflation, with a range of agricultural commodity prices expected to edge up.

Over 500 000 jobs were lost in the first half of 2009, out of a total workforce of 17 million; a further 300 000 are expected to lose their jobs by the end of the year. According to the Economist.com, one in every 4 people in the formal economy is now unemployed. The manufacturing, wholesale as well as retail trade and financial intermediation were the biggest contributors to job declines. At the end of the second quarter 2009, employment in agriculture had declined by 28 000 quarter-on-quarter (80 000 year-on-year). The employment situation was aggravated by a wave of protests by trade unions across the country which took place between July and August, pressing businesses and government for double-digit wage increases. The South African Chamber of Business has warned that the protests could dampen further business and investor confidence and would undermine growth prospects and job opportunities which are already under pressure. In order to counteract the effects of the economic slowdown on employment, President Jacob Zuma has set aside a R2.4 billion job fund to assist in the training of workers affected by the recession.

According to UNCTAD World investment report (UN, 2009), Foreign Direct Investment (FDI) into South Africa plunged by 80% in the first quarter due to disinvestment by transnational corporations as a result of the economic downturn. Similarly, the decline in FDI is the latest common phenomenon in the rest of Africa and the world. However, the report indicates that global cross-border investment in agriculture are increasing, which is significant for developing countries. This increase is being driven by overall concerns about food security and increased commercial farming. Surprisingly, South Africa recorded a third successive trade surplus in July. This has boosted the current account deficit which improved dramatically from 7% of GDP in the first quarter to 3.2% of GDP in the second quarter. Exports increased by 3.1% month-on-month while imports rose by 10.5% month-on-month.

4. INTERACTION BETWEEN SA, AFRICA AND THE WORLD

The global economic crisis has severely affected international economic relations and development between South Africa and other African countries. As a result, mounting renewed calls have been made for more emphasis to be placed on South-South co-operation, in developing a fairer system of international trade and financial management in Africa. A South-South perspective propagates expanding trade with economies in the South as a growth engine. However much has been debated on the sustainability of the co-operation, arguing that Brazil, China and India will have a competitive advantage over other African countries given their ability to produce low-cost, labour intensive goods than Africa.

The EU Economic Partnership Agreement (EPA), has in particular, been a cause for serious concern for South Africa and other SACU members. All SACU members have already signed the interim EPA except for South Africa and Namibia, of which, debate over the future of SACU has been at the centre stage lately. SACU has been using the Common External Tariff which applied to imported goods coming outside SACU, therefore, it is feared that the EPA membership will result in the emergence of two tariff regimes within the Customs Union. Equally, trade between South Africa and Africa has been substantially affected by the crisis, with value of exports to Africa declining substantially by 12.3% year-on-year in September, and by 14% quarter-on-quarter, while imports from Africa declined by 48% year-on-year in September and by 13.6% quarter-on-quarter. Despite the decline in export and import values to Africa, Mozambique remained the main export destination for South Africa, followed by Zimbabwe and Zambia. Meanwhile Nigeria remained the main import destination for South Africa, followed by Angola and Mozambique.

The South African Rand appreciated by over 15% in the quarter under review (see Figure 3 below), from levels above R10 in the first quarter to levels just below R8 in the second quarter - which explains much of the drop in value of exports to Africa. Other reasons have been linked to the tightening of international credit markets which made it difficult for countries to access trade finance as well as poor flow of worker remittances from other countries owing to job cuts world-wide.

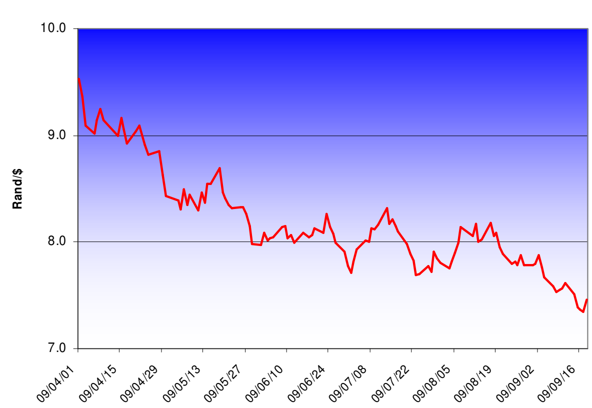

Fig.3: Rand vs Dollar, Second Quarter 2009

Source: SARB

Asia has overtaken Europe as South Africa's largest export destination. The value of exports to China alone (+41.3%), were close to exports to SADC countries combined, while exports to the US and the UK declined by approximately 50% and 40% respectively, year-on-year in September, respectively. South Africa's imports from China, US and UK have declined significantly by approximately 17%, 19.6% and 40.7%, respectively as compared to the second quarter of 2008. A drop in trade between SA and the North is attributable to a stagnant demand and increased protectionist measures taken by other developed countries.

5. MACROECONOMIC VARIABLES AND THEIR IMPACT ON AGRICULTURE

5.1 Inflation

Overall inflation is gradually coming down with the August data showing inflation has moderated to 6.4 % year-on-year, down from 6.7% in July. Again, food prices, which have been the main driver behind persistent rise in inflation, are gradually declining, with recent data showing a drop from a 7.6% year-on-year rise in July to a 6.0% rise in August. However, costs of production inputs, which have been rapidly rising since late 2006, have offset the immediate benefits of declining food prices by consumers. Input costs increased by between 20% and 30% since 2006. Fertiliser prices rose to historical highs of 70.6% in 2008/09, driven by increased demand of fertilisers by China, India and Brazil. Costs of seeds increased by 21.6%, while that of feeds increased by 20.1% during 2008/2009. However, prices of major grains remained persistently low in September as compared to last year. If prices received by farmers continue to fall, while input costs remain at current high levels, many more farmers will find it difficult to cover production cots.

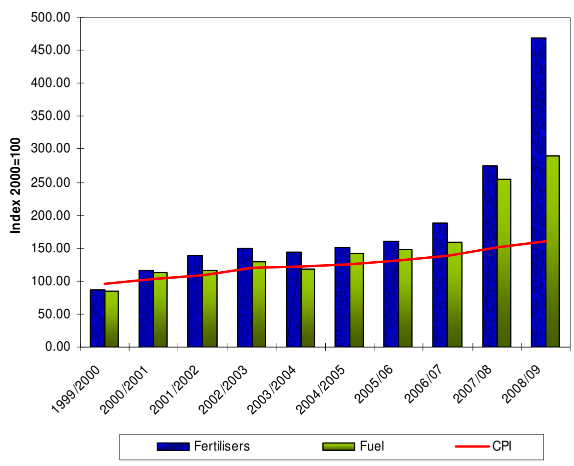

Fig. 4: Input prices of selected products

Source: DAFF

Prices paid and received by farmers have generally outpaced general inflation measures in the South African economy. Prices paid by farmers for all items rose by approximately 25% in 2008/09 (See Figure 4 above). This was far greater than the producer price index (PPI), which declined by 0.7% during the same period. The PPI remained in the deflationary territory in July 2009, falling 3.8% year-on-year, from 4.1% in June. Prices received by farmers have been decreasing in recent months due to, inter alia, lower demand amid the global economic downturn. Figure 5 below shows the prices received by farmers for a selected few products at the end of September 2009 compared to the same period in 2008.

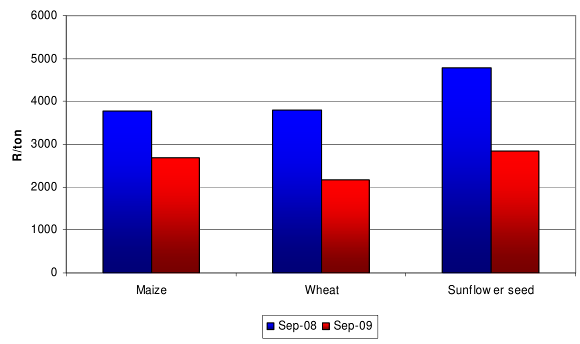

Fig. 5: Prices received by farmers on selected grains

Source: Safex

5.2 Growth

Following a sharp contraction of 6.4% in the SA economy during the first quarter of 2009, the SA economy showed some signs of recovery contracting by 3.0% in the second quarter. However, this was the economy's third consecutive GDP contraction. Table 3 below presents GDP projections for 2009 and 2010.

TABLE 3: Annual real GDP growth rates

2008		2009	2010
3.1	BER	-2.0	2.7
	Standard Bank	-1.5	3.0
	ABSA	-2.1	2.0
	Average	-1.9	2.6

Sources: BER, Standard Bank, ABSA

The agriculture, forestry and fishing industry contributed -0.5 percentage points to GDP in the second quarter 2009 – following a 17.1% contraction in its value added during the second quarter. This was mainly attributed to declining contribution by the animal products to the value added by agriculture.

The estimated volume of agricultural production in 2008/09 was only 0.7% higher than in 2007/08 (See Figure 6 below). Field crop production declined by 31.7% in 2008/09 compared to 2007/08, due to a decline in maize production and a sharp decline in oats production. International prices for maize were lower due to good harvesting recorded globally.

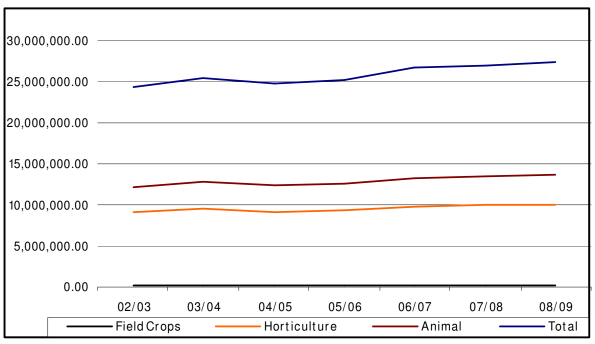

Fig. 6: Agricultural production

Source: DAFF

The global economy has started showing some signs of recovery, with China's domestic market rampant, and export-dependent economies like South Korea, Taiwan and Singapore also doing surprisingly well. France and Germany also surprised many with positive results, while even Japan has posted modest growth. If the economic recoveries are prolonged, it might bode well for agriculture.

Some of the factors that may affect the contribution of agriculture to GDP:

The total estimate for area planted for **maize** in 2008/09 is 15.3% lower than the 2007/08 production season. Maize production estimate for the 2008/09 production period is 7.6% lower than the 2007/08 final production total, due to inter-alia lower international prices for maize and increased US production outlook. According to the crop estimate committee's seventh forecast in 2009, the area planted for **sunflower seed** increased by 12.7% compared to 2007/08 production period. The international price for oil and fats increased by 8.3% in August compared to June 2009 FAO (2009). Sunflower seed increased due to the tightness of global supplies. The area planted to **soybeans** for the 2008/09 period is 43.7% higher than in 2007/08 as farmers moved away from lower maize prices to attractive prices in oil and fats products. Production is 80.6% higher in 2008/09 compared to 2007/08 due to higher international prices for oilseeds. Soybeans prices increased due to tight old crop supplies and record crop shortfalls in South America, which led to a sharp drop in global inventories and increasing demand from China and India.

The area estimated for **wheat** plantation for the 2009 is 12.1% lower than the area planted to wheat in 2008 and production is expected to be 5.6% lower than in 2008. International wheat prices are lower globally due to, inter-alia, better than expected crop harvest results in the US and EU. The area planted and production forecast for **malting barley** is 9.5% and 14.9% higher for 2009 compared to 2008 respectively. Dry conditions are expected in the Southern Cape which is likely to affect yields. Prices are expected to remain fixed due to contracts between farmers and producers. **Animal production** is increasing slightly, after declining in the second quarter of 2009. International meat prices returned to the January 2009 price levels. Meat prices remained stable between June and August 2009. (FAO,2009). International prices for **dairy products** seem to be rebounding due to the declining supply as most dairy producers were probably washed-out by the global melt-down. According to Ernst Janovsky (2009) of ABSA agricultural division, input costs have increased and as a result farmers will have to increase production to counter the cost curve. **Production** of agricultural products like oil-seeds is expected to increase in the following year. According to FAO (2009), the current oilseeds market tightness and price firmness could also spread into the next season, considering that, irrespective of a likely revival in global oilseed production, 2009/10 supplies of oils and meals will be conditioned by low carry-in stocks. Wool production is also expected to rebound as demand improves in China. International sugar prices have increased by 21.8% in August compared to July 2009, continuing their upward trend, which might boost production.

5.3 Exchange rates

The currency was weaker in the second quarter of 2009 as risk aversion dominated in markets. However, the Rand strength accelerated by 15% in the second quarter, but was weaker than the same period last year, trading between R7/$ and R8/$ during the period May – June 2008 compared to R8/$ - R9/$ in 2009. However, Investors' appetite for risk drove the Rand higher in the third quarter of 2009 – further boosted by the reduced current account deficit (BER, 2009). The Rand is projected to end the year at R8.46 against the US dollar in 2009, strengthening to R8.19 at end of 2010 (See Table 4 below).

TABLE 4: End of year R/$ exchange rates

2008		2009	2010
8.26	BER	8.30	8.79
	Standard Bank	8.63	8.25
	Absa	8.51	7.66
	Average	8.46	8.19

Source: BER, Standard Bank and ABSA

Agricultural exports increased by 37.7% in the second quarter of 2009 compared to the corresponding period last year - benefiting from the weaker Rand among other factors. Sagis maize exports figures show that maize exports for May to June 2009 were 539 000 tons compared to 337 000 tons for the corresponding periods last year. Figure 7 below presents the exports and imports trends over the past few months.

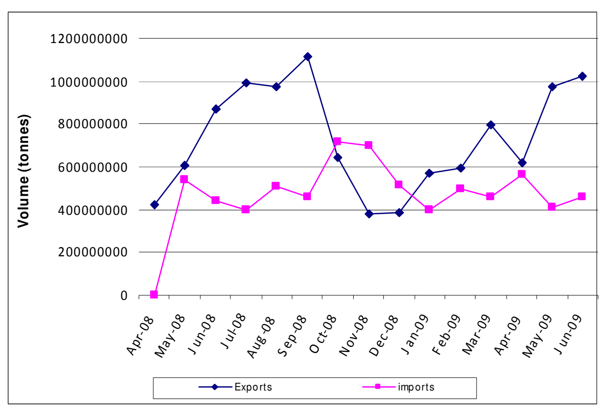

Fig. 7: Volume of Agricultural Exports vs. Imports

Source: DAFF

Agricultural imports declined sharply from October 2008 as the Rand depreciated against major currencies and global demand subsided due to the global economic crisis. Imports were 1.9% lower in quarter 2 of 2009 compared to the same period last year. The Rand volatility is expected to remain high and periods of currency strength within a broader weaker trend are also expected (BER, 2009). Against this background, the Rand is expected to weaken in the long run. A weaker currency bodes well for agricultural exports, but that will depend on the speed to which the global recovery turn to spending in economies.

5.4 Interest rates

Real household consumption expenditure weakened further in the second quarter of 2009 alongside declining real disposable income and high levels of household debt (SARB,2009). The Monetary Policy Committee (MPC) of the Reserve Bank left the repo rate unchanged at 7% during their meeting in October 2009. Consequently, commercial banks also left their prime lending rate unchanged at 10.5%. The Governor of the Reserve Bank has previously alerted markets to the fact that SA's interest rate cutting cycle is nearing an end. Table 5 below presents the projected average prime lending rates for 2009 and 2010.

TABLE 5: Average yearly Prime interest rates

2008		2009	2010
15.1	BER	11.00	11.00
	Standard Bank	10.50	12.50
	Absa	8.0	7.6
	Average	9.83	10.36

Sources: BER, Standard Bank, ABSA

Farmers are under pressure to pay off their debts as farm income decline, due to rising input costs, lower prices and decelerated demand. Net farm income is expected to decline further in quarter 3 after declining by 11% in quarter 2 of 2009 compared to quarter 2 of 2008. The total farming debt as at the end of June 2009 is estimated at R47 862 million (R44 940 million)—an increase of 6.5%. Gross investment in respect of fixed improvements for the year ended 30 June 2009 increased by 6.5% to R3.9 billion. In the case of machinery, implements and vehicles, investment increased by 24.8% and amounted to R7.8 billion. The livestock inventory decreased by R47.3 million compared to the previous year due to, inter-alia, increased feed costs and the projected decline in beef consumption due to the economic slowdown lag effect. Income from restaurants also declined in the second quarter of 2009 underlining the decline in household's disposable income. Consumption of products like beef, pork, mutton, fruits and citrus fruits is projected to decline in the 2009 season due to the declined disposable income. Although recent interest rate cuts have brought some level of relief, consumers are still using the lower interest rates to pay their debts. Most economists project that it will take longer, before the lower interest rates trickle to spending in the economy. On the positive, investment banks are fairly optimistic about the global economic outlook and are bearish on the dollar's prospects and vice versa (BER, 2009). A further interest rate cut would help highly indebted consumers and also stimulate demand.

6. CONCLUSION

Though most economies are still in recession, leading indicators suggest that the global economy is stabilising. GDP growth is still projected to remain sluggish for most countries, implying further increases in unemployment - which in turn imply further declines in household spending. Most African countries were severely hit by the global economic downturn, but there are emerging signs that the worst is over in many economies. Economic activity as well as consumer and business confidence have registered less sharp falls in the last two months than earlier in the year. South Africa has been relatively slow to feel the impact of the global economic downturn from its onset, and the SA economy's recovery is expected to lag behind the rest of the world. SA's economic growth continued to decline in the second quarter of 2009; with employment, business and consumer confidence data confirming a bleak picture. Despite lower interest rates, consumer spending has also shrunk as households battle with debt – which also has negative implications for demand for agricultural products. SA's CPI inflation has been coming down since the beginning of 2009 and this has dual implications for farmers; on the positive side it implies lower input costs, but on the negative side, it implies lower food prices which might reduce farm income. The Rand exchange rate was weaker in the second quarter of 2009 which saw agriculture exports increase by 37.7% in that period – but the rand regained its strength in the third quarter of 2009. The value added by the agriculture, forestry and fishing industry to GDP contracted by 17.1% in the second quarter of 2009 as the contribution by animal products to value added by agriculture declined – this may be attributed to a shift by consumers from "luxury" food items such as meat and meat products to cheaper substitutes. Though SA's economy is expected to lag behind other countries on terms of recovery, most analysts are optimistic that the worst is over.

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