Annual Economic Report 1979

A review of economic and financial conditions in the Republic of South Africa presented as background to the Chairman's Address to Stockholders at the Fifty-Ninth Ordinary General Meeting to be held on 21 August 1978.

South African Reserve Bank

Hierdie Verslag is ook in Afrikaans beskikbaar.

Contents

Summary and general observations

Economic conditions in South Africa improved in several respects during the year under review.* Real gross **domestic** product increased moderately, after a small negative rate of economic growth had been recorded in 1977/78. This increase was accompanied by a substantial improvement in the country's terms of trade and a decline in real net factor payments to the rest of the world, which resulted in a significantly higher rate of increase in the real gross **national** product. Most sectors of the economy contributed to the growth in real economic activity, but the wholesale and retail trade, construction and gold mining can be singled out as sectors of which the real value added either declined or remained at the level reached in the preceding year. The higher level of real economic activity was reflected in an increase in non-agricultural employment. Employment in the private sector, which had declined in the preceding two years, increased moderately. In addition, public sector employment continued to rise, although at a lower rate than in recent years.

The improvement in the terms of trade, partly reflecting a sharp rise in the price of gold, was a major reason for a substantial surplus on the current account of the balance of payments. Small increases in the volume of exports and the volume of the net gold output also contributed to the current account surplus. On the other hand, apart from higher net invisible payments to the rest of the world, the volume of imports showed a small rise. This rise would have been larger if the supply of petroleum products during the first half of 1979 had not been partially disrupted. The current account surplus was sufficiently large to finance a substantial net outflow of capital and to raise the country's gross gold and other foreign reserves.

The increase in **net** reserves, which was even more pronounced than the rise in **gross** reserves, contributed to an increase in the supply of money and near-money and assisted in expanding the liquidity of the banking system and maintaining liquidity levels in the private non-banking sector. In addition, the general availability of funds was increased by a marked rise in gross domestic saving. In these circumstances, interest rates declined and a climate more conducive to further economic expansion was created.

Improved economic conditions in 1978/79 were also reflected in a considerable increase in government revenue, despite reductions in certain indirect and direct taxes. Part of the increase was accounted for by the proceeds of the general sales tax, but even if these proceeds are excluded, revenue collections still showed an appreciable rise. This was due largely to higher taxable company profits, particularly in the mining industry.

Notwithstanding the higher level of economic activity, the cyclical upswing, which had commenced at the end of 1977, gained little momentum during the subsequent eighteen months. A comparison with preceding business cycles since 1960 shows that economic recovery, in terms of changes in real gross domestic product and expenditure, was much weaker during the first eighteen months of the current upswing than during any of the earlier recovery phases. This was partly explained by the fact that the recovery was not fully diffused throughout the economy, as was indicated by the lack of growth in the real product of certain sectors. Reflecting these conditions, the rate of increase in employment was too low to match the rate of growth in the economically active population.

Several other symptoms of the inertness of the economy were evident in the year under review. One of these was the low ratio of the volume of imports to the real gross domestic product. Others included the low rate of expansion in total domestic credit extended by the monetary banking sector and, more generally, a comparatively moderate rate of growth in the supply of money and near-money. Net bank credit to the government sector declined and only a low rate of increase was recorded in bank credit to the private sector. The latter reflected the small rise in the type of lending which is associated with ordinary business demand for bank credit. Another symptom was the marked increase in financial activity in the secondary section of the capital market, apparently because of funds being available in excess of financing requirements.

A major reason for the tardiness of the economic recovery appears to have been sluggish real aggregate domestic demand which could not sustain a higher rate of growth. Public sector demand was limited by policy considerations, whereas the weakness of private sector demand was to some extent related to the effect on personal income of the persistently high rate of inflation. The rate of increase in consumer prices not only was high at the beginning of the current economic recovery phase, but started to rise even further relatively early during the upswing. In addition to the effect of sluggish domestic demand, the volume of exports made only a small contribution to growth in the year under review, whereas it increased sharply in the preceding three years.

As regards changes in the components of real aggregate demand in 1978/79, a higher level of real private consumption expenditure was discouraged by a further decline in the average real remuneration per worker. Real **disposable** personal income increased moderately, however, because of tax concessions granted in the 1978/79 Budget and a fortuitous rise in real agricultural income that was the result of shifts in the harvesting period of summer crops, but this increase found its way into higher personal saving. It would appear that consumer confidence was affected adversely by the acceleration in the rate of inflation during the first half of 1979 as well

* The year under review refers to the twelve-month period which ended on 30 June 1979 and is denoted as 1978/79. It represents the latest twelve-month period for which statistics are available.

as by expectations of a still higher rate of increase in consumer prices. Real government consumption expenditure and real fixed capital outlays of public authorities continued to be limited by the government's policy of curbing the increase in public authority spending. The private sector's real fixed investment was constrained by the effect of inflation on investment returns (net of depreciation allowances), the existence of surplus production capacity, and an aggregate demand that was inadequate to effect a significant reduction of excess production capacity. A substantial swing in real inventory investment which resulted in a small, and probably involuntary, build-up of stocks, provided evidence of a demand that was weaker than anticipated.

Official policy recognised the need for further stimulation of the economy by means of encouraging demand. To achieve this aim, monetary policy during the year under review was directed towards the creation of more scope for bank credit extension to the private sector and the orderly downward adjustment of interest rates in accordance with changes in market conditions. In the formulation of fiscal policy, as presented in the 1978/79 and 1979/80 Budgets, emphasis was placed at first on encouraging economic growth and later on adding momentum to the current economic upswing. Policy measures, however, were not aimed at stimulating growth by means of increased government expenditure, but rather at encouraging expansion in the private sector. In accordance with this approach, several tax concessions were granted to individuals and companies in the latest Budget. These concessions should begin to have their expansionary effect from the second half of 1979. In addition to monetary and fiscal policy measures, a more flexible exchange rate system was introduced with a view to affording the authorities more scope for the application of monetary and fiscal policies and, more particularly, to easing a possible balance of payments constraint on more rapid economic growth.

National accounts

Moderate rate of economic growth

A moderate rate of economic growth was recorded in 1978/79. Real gross domestic product increased by 3 per cent, compared with a small decline of ¼ per cent in 1977/78 and an increase of only 1¾ per cent in 1976/77. As is shown in the accompanying table, economic growth during the year under review originated largely in the secondary sector and, to a lesser extent, in the primary sector of the economy. The real value added by the tertiary sector showed only a small increase.

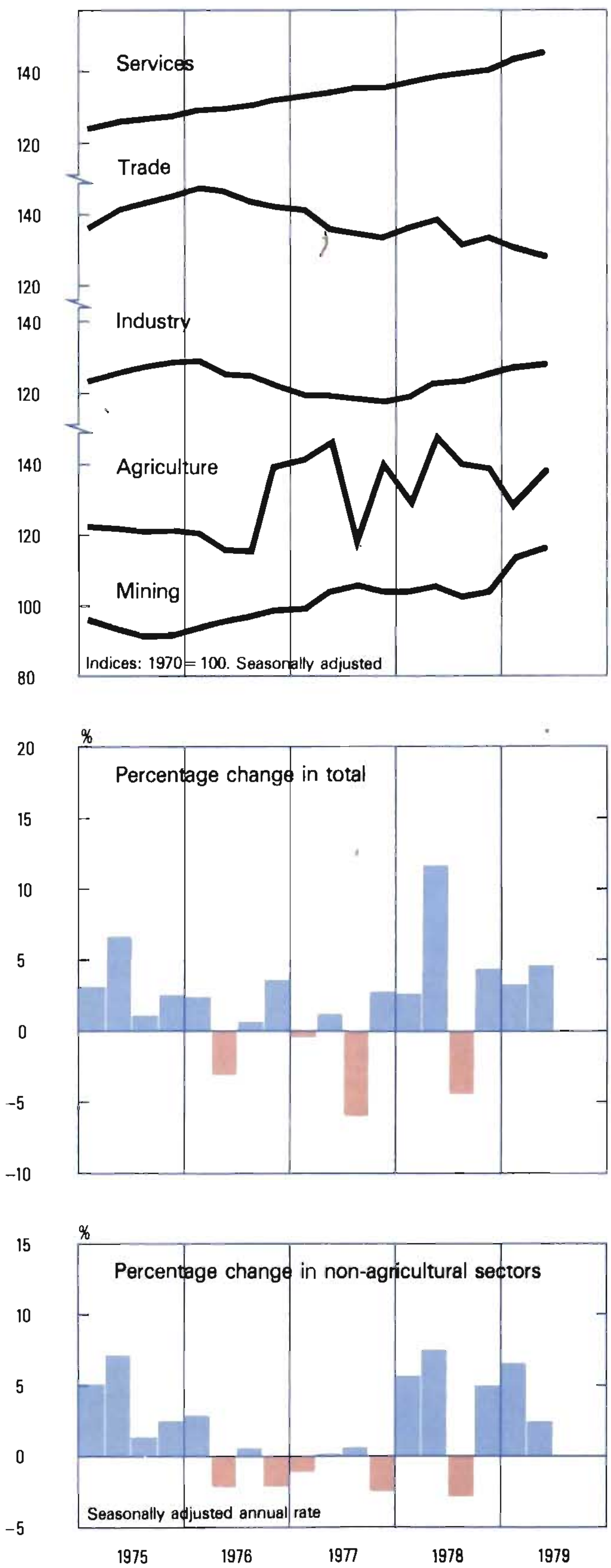
A higher level of activity in the secondary sector was reflected in an increase of 5½ per cent in the real product of manufacturing, which had already started to increase in the first quarter of 1978. In addition, the real product of construction increased slightly, after it had declined substantially in 1977/78. Lastly, the rate of increase in the real value added by electricity, gas and water in 1978/79 even exceeded the comparatively high rate which had been recorded in 1977/78.

The moderate rise in the real value added by the primary sector was accounted for by increases in agricultural and non-gold mining production. As in the preceding year, the volume of gold production remained more or less unchanged in 1978/79. The increase in the real product of agriculture was due to shifts in the harvesting period of summer crops rather than to an actual increase in production. Although it is expected that summer crops will be lower in the 1979 season, a large part of the crop was harvested during the second quarter and included in the 1978/79 production figure. In addition, production in the third quarter of 1978 included a substantial part of the crop in the 1978 season. The rate of

Percentage change in real gross domestic and national product

	Year ended 30 June 1977	1978	1979
Primary sector	16	-1½	3
Agriculture	25	-7	3
Gold mining	-½	—	—
Non-gold mining	12	9	5
Secondary sector	-4½	-2	5
Manufacturing	-5	-2	5½
Electricity, gas and water	2	5½	6½
Construction	-9	-7	½
Tertiary sector	1½	1	2
Wholesale, retail and motor trade	-3	-4	-3½
Services	3½	3	4
Transport and communication	4½	4½	6
General government	5	4	3
Financial and other	2	1½	3
Total gross domestic product	1¾	-¼	3
Non-agricultural sectors	—	½	3
Non-primary sectors	-½	—	3
Total gross national product	1½	-¼	5½

Gross domestic product at constant 1970 prices



increase in the real product of non-gold mining decelerated for the second consecutive year, but non-gold mining production nevertheless rose at an average annual rate of 8½ per cent from 1975/76 to 1978/79.

Although the real value added by the tertiary sector increased only slightly in 1978/79, this was a reflection of sluggish conditions in the retail and wholesale trade. The real value added by the trade sector as a whole declined for the third consecutive year, largely because of weak consumer demand. This decline, however, was more than compensated for by an increase in the real value added by the services sector.

Notwithstanding a moderate rate of economic growth in 1978/79 as a whole, seasonally adjusted quarterly estimates of the real gross domestic product did not show any acceleration in growth in the course of the year. This was due partly to wide fluctuations in the real value added by agriculture, which in some quarters tended to accentuate and in others to offset changes in the real product of the non-agricultural sectors of the economy. Even the real value added by the non-agricultural sectors showed fairly large quarterly swings, especially during the second half of 1978 when it was affected by the newly imposed general sales tax. In the first quarter of 1979 the real value added by the non-agricultural sectors increased at a comparatively high rate, but this growth was not maintained in the second quarter.

South Africa's terms of trade improved considerably during 1978/79 because of a higher rate of increase in export prices (including gold) than in import prices (including petroleum products). In addition, real net factor payments declined during the review period. The net result was that the real gross **national** product increased at a higher rate than the real gross **domestic** product, namely by 5½ per cent, after it had decreased by ¼ per cent in 1977/78 and had risen by only 1½ per cent in 1976/77.

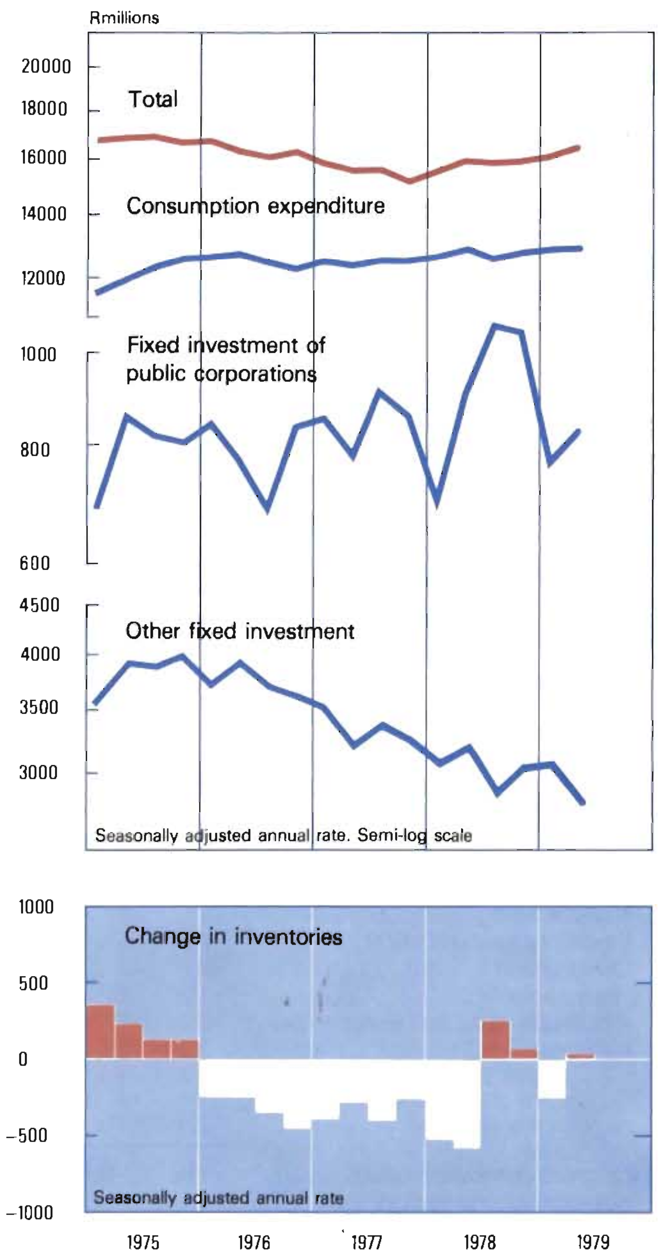
The rate of increase in the gross domestic product at current prices accelerated from 11½ per cent in 1977/78 to 18 per cent in 1978/79. All components, i.e., remuneration of employees, gross operating surplus, and indirect taxes net of subsidies, increased at higher rates than in 1977/78. The acceleration of the rate of increase in the remuneration of employees from 9½ per cent in 1977/78 to 12½ per cent in 1978/79 originated in mining, manufacturing, and general government services. Almost all sectors contributed to the rise in the rate of increase in the gross operating surplus from 13½ per cent in 1977/78 to 22½ per cent in 1978/79, with the largest contributions coming from mining, manufacturing, and agriculture.

The difference in the growth rates in the gross domestic product at current and at constant prices in 1978/79 implied an increase of about 14½ per cent in the derived gross domestic product deflator, compared with a rate of 12 per cent in 1977/78. This acceleration reflected a higher rate of increase in the prices of gold and other export commodities, as well as in domestic retail and wholesale prices.

Moderate increase in real aggregate domestic demand

Real gross domestic expenditure increased moderately during the year under review, after annual declines had occurred during the period 1975/76 to 1977/78. This change was due largely to a turnabout in real inventory investment, namely from a substantial decrease in 1977/78 to a moderate increase in 1978/79, and, to a lesser extent, also to a smaller decline in real fixed investment in 1978/79 than in the preceding year. In contrast, real private

Gross domestic expenditure at constant 1970 prices



Percentage change in real gross domestic expenditure

	Year ended 30 June 1977	1978	1979
Private consumption expenditure	-1½	2	1
Government consumption expenditure	-½	2½	1
Gross domestic fixed investment	-7½	-6	-5
Change in inventories (R millions*)	-300	-380	25
Gross domestic expenditure	-3	-3	3

*At constant 1970 prices.

and government consumption expenditure increased at lower rates than during the preceding year. Notwithstanding a substantial acceleration in the rate of increase in gross domestic expenditure at current prices during 1978/79, its absolute level was markedly lower than that of the gross national product at current prices. This difference was reflected in a substantial surplus on the current account of the balance of payments.

Slight increase in real private consumption expenditure

Real private consumption expenditure rose only marginally in 1978/79. Its failure to rise more rapidly was an important reason for the slow growth of economic activity in the year under review. The increase in expenditure on durable goods in 1977/78, which had been the result largely of purchases in the second quarter of 1978 ahead of the introduction of the general sales tax, was not maintained in 1978/79. Outlays on semi-durable goods declined for the third consecutive year and expenditure on the more essential non-durable goods showed its usual moderate rate of increase. A more normal rate of increase was recorded in outlays on services, in contrast with sharp fluctuations in the preceding two years.

Seasonally adjusted quarterly estimates show that real private consumption expenditure declined in the third quarter of 1978 and, although it increased subsequently, the rate of increase became progressively lower. The annual rate of increase of 7 per cent in the fourth quarter of 1978 was followed by annual rates of 4 per cent and 1½ per cent in the first and second quarters of 1979, respectively.

Percentage change in real private consumption expenditure

	Year ended 30 June 1977	1978	1979
Durable goods	-21	6	-4
Furniture and household appliances	-13	4	-6
Motor cars, etc.	-23	14	1
Other durable goods	-32	-1	-9
Semi-durable goods	-2	-1	-4
Non-durable goods	2	3	3½
Services	5	1	4
Total private consumption expenditure	-1½	2	1

Small increase in real government consumption expenditure

After real government consumption expenditure had increased at an average annual rate of about 7 per cent during the period 1970/71 to 1975/76, the rate of increase declined to an average of only 1 per cent during the past three years. This change reflected the government's policy of curbing the increase in public authority expenditure. The actual rate of increase in real government consumption expenditure amounted to 1 per cent in 1978/79, compared with 2½ per cent in the preceding year. The further decline in the rate of increase was caused by a lower rate of increase in the remuneration of employees and the fact that outlays on goods and other services, including defence expenditure, rose only marginally.

Further decline in real gross domestic investment

Real gross domestic fixed investment continued to decline in 1978/79. As is shown in the accompanying table, this was caused by a decrease in the fixed capital expenditure of the private sector and public authorities, which was only partly offset by a rise in the public corporations' fixed investment.

In the private sector only the real fixed capital expenditure of gold mining increased in the year under review, largely because of higher outlays on uranium plant. Particularly large declines were recorded in manufacturing, reflecting the continued high level of unused production capacity, and in the transport sector, largely because fewer ships were purchased for the containerisation programme and for exporting iron ore. Private residential construction decreased for the fourth consecutive year and reached a level that was 46 per cent lower than in 1974/75.

A sharp increase in capital outlays by Sasol on its second oil-from-coal plant and by Escom on its nuclear and other power stations caused total real fixed capital expenditure by public corporations to rise at a high rate in 1978/79. Real fixed capital outlays by public authorities, on the other hand, continued to decrease, but the rate of decline was markedly lower than in the preceding year.

Notwithstanding the further decline in total real **gross** domestic fixed investment in 1978/79, real **net** investment remained positive, enlarging the real fixed capital stock further by 3½ per cent during this period. The stock of real fixed capital assets of the private sector, however, increased by only 1 per cent, largely because of a decline of 2 per cent in the real fixed capital stock of private manufacturing. As a result of the sustained rise in the investment outlays of public corporations, the share of the public sector, i.e. public corporations and public authorities, in the

Percentage change in real gross domestic fixed investment and real fixed capital stock

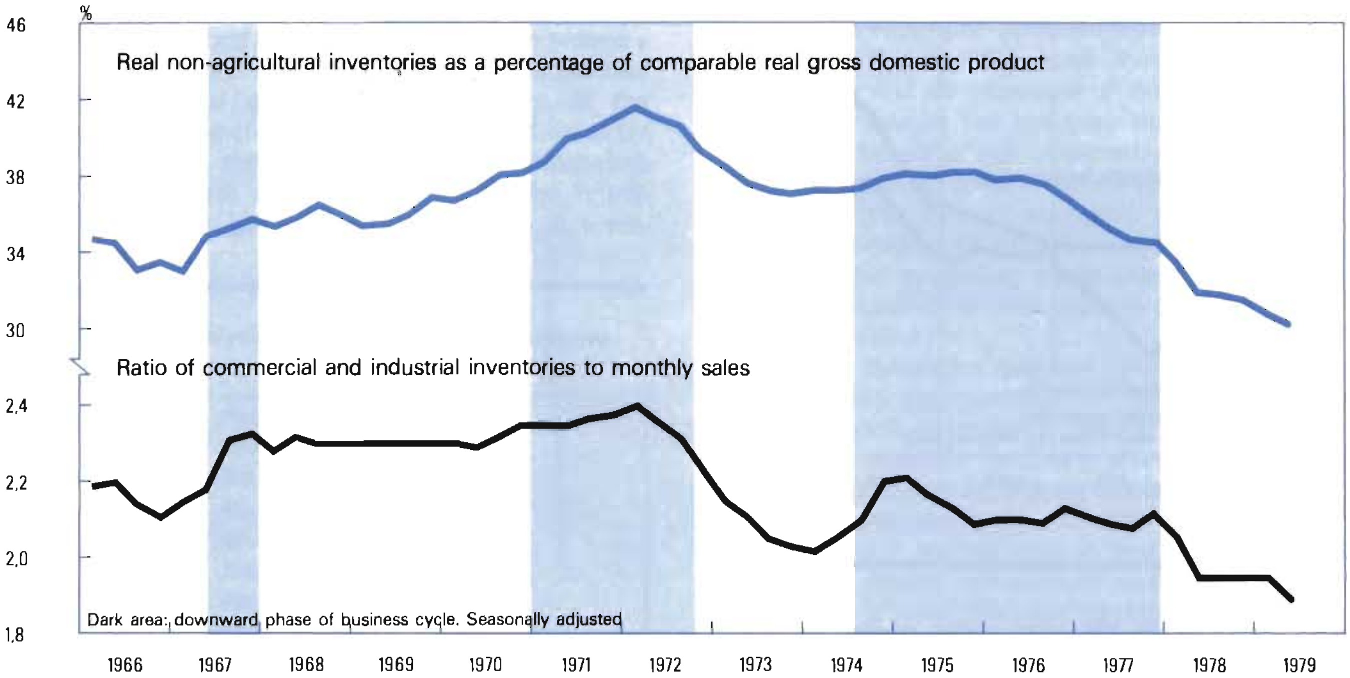
	Year ended 30 June 1977	1978	1979
Real gross domestic fixed investment			
Private sector	-10	-1	-11
Agriculture	-10	—	-12
Gold mining	-10	-3	16
Non-gold mining	7	-7	-6
Manufacturing	-14	-6	-16
Transport	-25	190	-22
Private residential construction	-12	-21	-10
Public corporations	—	4	12
Manufacturing	2	45	21
Electricity, gas and water	32	11	12
Other (mining, transport, etc.)	-35	-53	-16
Public authorities	-8	-19	-6½
S.A. Railways Administration	3	-42	-10
Other business enterprises	-13	-6	-5
General government	-13	-8	-5
Total gross domestic fixed investment	**-7½**	**-6**	**-5**
Real fixed capital stock			
Private sector	3	2	1
Mining	6	4	4
Manufacturing	1	—	-2
Public corporations	13	11	11½
Manufacturing	8	13	15
Electricity, gas and water	16	15	14
Public authorities	6	4	4
S.A. Railways Administration	8	4	3
General government	6	5	4
Total real fixed capital stock	**5½**	**4**	**3½**

total stock of real fixed capital assets of the country amounted to 57 per cent at the end of June 1979, compared with 51 per cent at the beginning of the nineteen-seventies. The percentage share of the private sector declined accordingly.

Turnabout in real inventory investment

Total inventories at constant 1970 prices increased by R25 million during 1978/79, compared with fairly large decreases of R380 million and R300 million in 1977/78 and 1976/77, respectively. This considerable swing in inventory Investment from 1977/78 to 1978/79 contributed significantly to the increase in real aggregate domestic expenditure during the period under review. At constant 1970 prices, rises in industrial inventories, diamond stocks and agricultural stocks-in-trade were partly neutralised by declines in inventories of the wholesale and retail trade. Seasonally adjusted quarterly estimates show that a depletion of real inventories occurred in the first quarter of 1979, but that small additions to inventories were made in the remaining three quarters

Inventory ratios



of the year under review. The ratio of real non-agricultural inventories to the comparable real gross domestic product nevertheless declined further from 31,9 per cent in the second quarter of 1978 to 30,3 per cent in the second quarter of 1979, compared with the most recent peak of 38,1 per cent in the third quarter of 1975. Apart from being consistent with its long-term trend, the behaviour of this ratio also reflected its relationship with the business cycle in so far as the real gross domestic product usually increases more rapidly than real inventory investment during the initial stages of an economic upswing.

Substantial further increase in gross domestic saving

After gross domestic saving had increased at an average annual rate of approximately 15 per cent during the period 1974/75 to 1977/78, it rose markedly further by 36 per cent in the year under review. For the second consecutive year gross domestic saving exceeded the amount required to finance total investment. The record excess of R2 395 million in 1978/79 resulted in a reduction of the country's net indebtedness to the rest of the world. The further marked increase in saving in 1978/79 increased the ratio of gross domestic saving to gross domestic product to 30 per cent, compared with 26 per cent in 1977/78 and an average rate of 25½ per cent during the period 1971/72 to 1976/77.

As is indicated in the accompanying table, all components of gross domestic saving contributed to the increase of R3 498 million in this aggregate in 1978/79. The further large increase in corporate saving originated mainly in the mining and financial sectors, reflecting a sharp rise in net corporate profits, which was only partly offset by higher dividend and income tax payments. The current surplus of general government increased markedly, largely as a result of a higher rate of increase in current income than in current expenditure. The introduction of the general sales tax, higher income tax receipts from the corporate sector and increased revenue from gold mining leases (as a result of a sharp rise in the price of gold), were the main factors responsible for the increase in current income during the year under review. The further rise in the provision for depreciation reflected, in addition to normal growth, the higher replacement cost of existing assets.

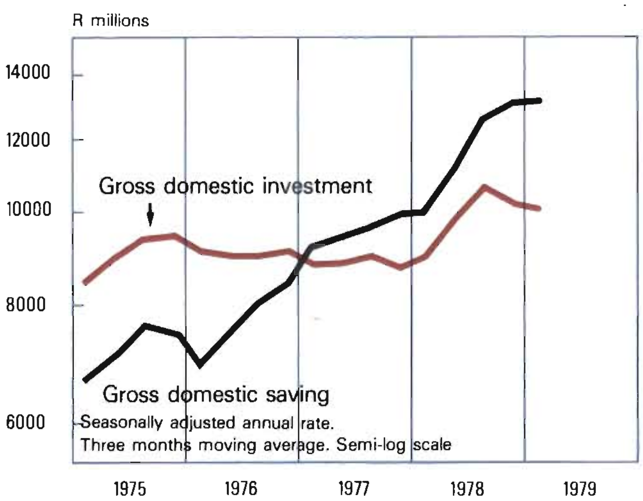
Personal saving, which had declined in 1977/78,

Changes in gross domestic saving
R millions

	Year ended 30 June		
	1977	1978	1979
Personal saving	23	-847	987
Corporate saving[1]	916	776	942
Current surplus of general government	-321	435	602
Provision for depreciation[2]	740	651	967
Total gross domestic saving	1 358	1 015	3 498

1) After inventory valuation adjustment and provision for depreciation at replacement cost.
2) At replacement values.

Financing of gross domestic investment



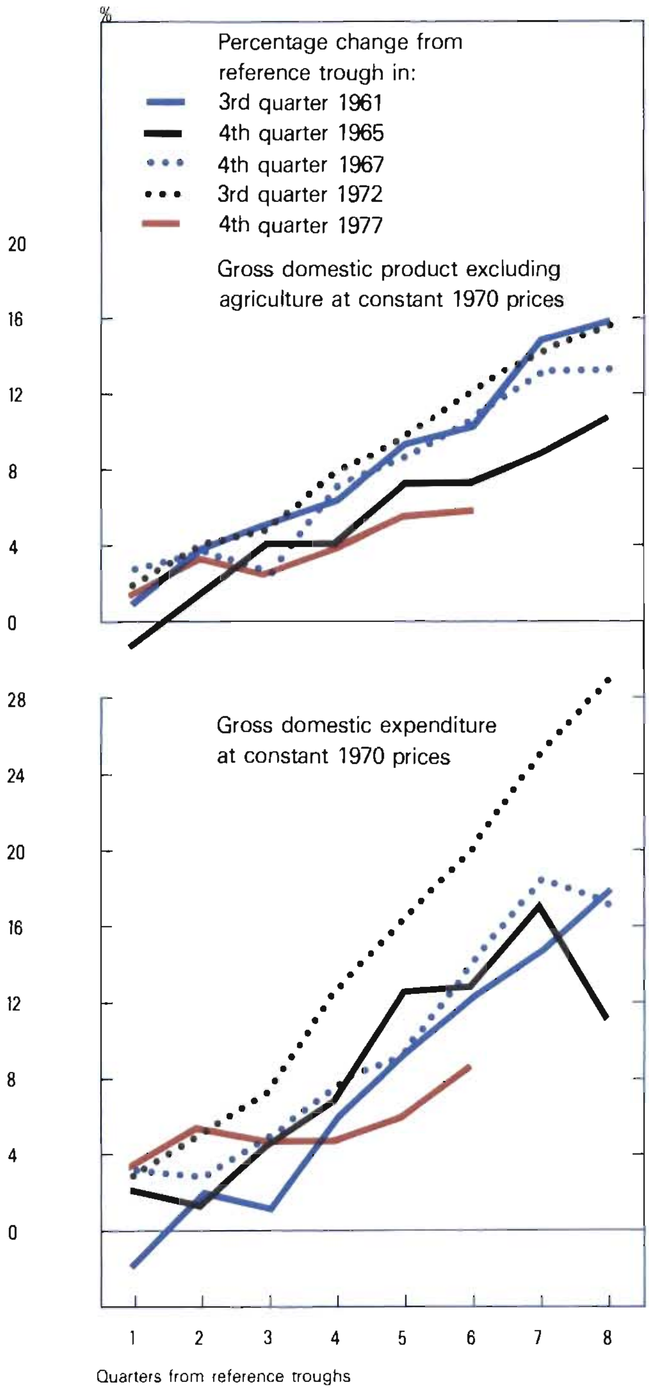
rose markedly in the year under review to a level which was slightly higher than in 1976/77. The main reasons for the increase in 1978/79 were the rise in net agricultural income (against a decrease in 1977/78) as a result of shifts in the harvesting period of summer crops, the smaller use made of consumer credit to finance private consumption expenditure, and the increase of 3½ per cent in real disposable personal income (compared with an average annual decrease of 2½ per cent from 1975/76 to 1977/78). The increase in personal saving in 1978/79 brought the ratio of personal saving to disposable personal income to 8½ per cent, compared with only 6 per cent in the preceding year. The ratio in 1978/79, however, was still substantially lower than the average of 11 per cent recorded during the period 1971/72 to 1976/77.

Business cycle developments, labour situation and prices

Slow recovery of economic activity

The cyclical recovery of economic activity, which had commenced at the end of 1977, gained little momentum during the first eighteen months of the recovery phase. As a broad measure of changes in economic activity, the real gross domestic product of the non-agricultural sectors of the economy increased by 4 per cent from the end of the cyclical downswing, namely the fourth quarter of 1977, to the fourth quarter of 1978, and thereafter increased at a seasonally adjusted annual rate of 7 per cent in the first quarter and 2½ per cent in the second quarter of 1979. The absence of any significant acceleration in the rate of economic expansion reflected a recovery that was not fully diffused throughout the economy, as is indicated by the contribution of the various sectors of the economy to the real gross domestic product. The slow recovery was apparently due to weak aggregate domestic demand which was insufficient to sustain a higher rate of economic growth. In addition, the volume of exports, which had increased sharply in the preceding three years, made only a small contribution to real economic growth in the year under review.

Business cycle analysis – recovery phase comparisons



Although successive business cycles are unique in many respects, an impression of the strength of the present economic recovery can be gained from a comparison with the recovery phases of preceding cycles. As is shown by the accompanying graph, the increase in the real gross domestic product of the non-agricultural sectors and in real gross domestic expenditure during the current recovery phase was significantly smaller than during the recovery phases of all preceding cycles since 1960. This deviation was especially pronounced in the case of real gross domestic expenditure, thus confirming the present comparative weakness of aggregate demand.

Despite the dampening effect of measures aimed at conserving oil and of a higher rate of inflation, the prospects are that a moderate rate of economic growth will be maintained. The full expansionary effect of Budget measures aimed at stimulating consumer demand, will only be felt from the third quarter of 1979.

Increase in private sector employment

The growth in economic activity during 1978 and the first half of 1979 was reflected in an increase in non-agricultural employment and in a slight decline in unemployment. The rate of increase in non-agricultural employment, which had been declining for four consecutive years and amounted to only 0,2 per cent in 1977/78, came to 1,7 per cent in the first three quarters of the year under review in comparison with the corresponding period in 1977/78. This higher rate of increase was still well below the estimated annual rate of growth in the economically

Percentage change in non-agricultural employment

	Year ended 30 June 1975	1976	1977	1978	1979[1]
Public sector	5,3	4,5	3,1	2,7	0,8
Private sector	2,0	1,8	-0,1	-0,9	2,1
Total	2,8	2,5	0,8	0,2	1,7

1) Figures up to 31 March 1979 compared with figures for the corresponding period of the preceding year.

active population and was accounted for by private sector employment, which was 2,1 per cent higher in the first three quarters of 1978/79 than in the corresponding period in 1977/78. In 1976/77 and in 1977/78 private sector employment actually declined. With the exception of construction, higher levels of employment were recorded in all sections of the private sector. In the public sector central government employment declined in the first nine months of 1978/79, whereas employment by other bodies and institutions increased at a lower rate. Total public sector employment, therefore, rose by only 0,8 per cent during this period, compared with significantly higher rates in the immediately preceding years.

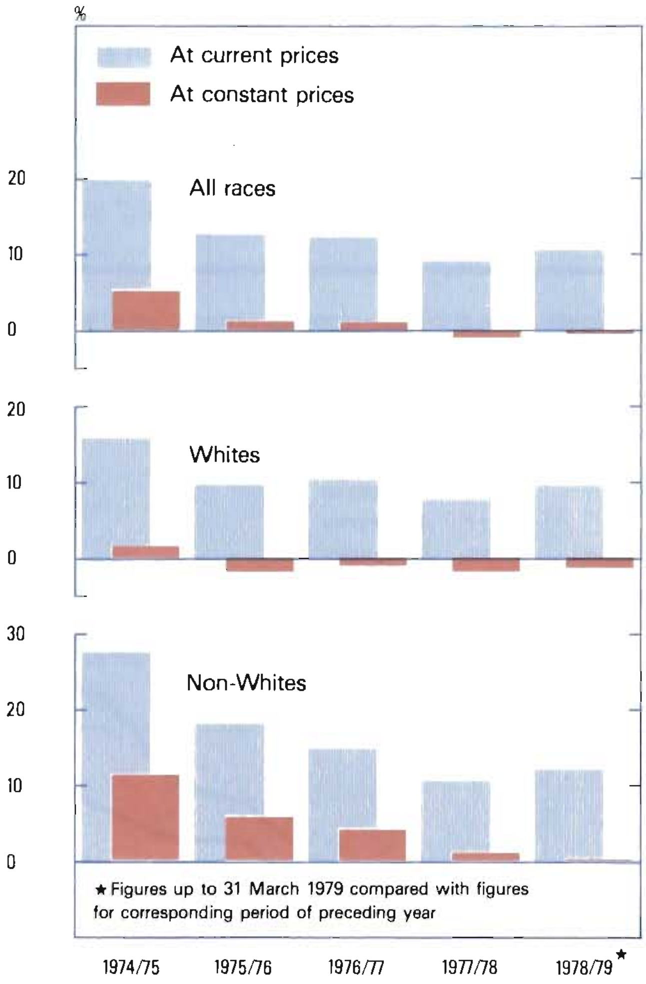
Seasonally adjusted non-agricultural employment increased by 0,4 per cent in the third and by 1,4 per cent in the fourth quarter of 1978, but remained unchanged in the first quarter of 1979. These changes reflected the course of employment in the private sector, and the slow-down in the first quarter of 1979 was due to a decline in employment in non-gold mining and in the banking and insurance sector. A significant change occurred, however, in employment in the construction sector. After a persistent decline from the first quarter of 1976 to the third quarter of 1978, seasonally adjusted employment in this sector increased by 0,2 per cent in the fourth quarter of 1978 and by 0,5 per cent in the first quarter of 1979. Employment in gold mining, seasonally adjusted, increased at an accelerating rate, namely by 0,8 per cent in the third quarter of 1978, 1,3 per cent in the fourth quarter, and 3,1 per cent in the first quarter of 1979.

Production per worker in the non-agricultural sectors increased by 1,5 per cent in the first three quarters of 1978/79, compared with 0,5 per cent in 1977/78. A significant improvement in productivity was apparent in manufacturing, as is indicated by the increase of 4,0 per cent in the production per man-hour in the first eight months of 1978/79. In 1977/78 and in 1976/77 production per man-hour in manufacturing declined by 0,4 per cent and 2,6 per cent, respectively.

Mirroring the rise in employment, a slight decline in unemployment occurred in 1978/79. The seasonally adjusted number of registered unemployed Whites, Coloureds and Asians decreased from its most recent peak of 31 750 in July 1978 to 27 270 in April 1979, before increasing slightly to 27 950 in June 1979. The latter figure represented 1,4 per cent of the estimated corresponding labour force. The ratio of the number of unemployed Blacks to the economically active Black population declined from 9,8 per cent in July 1978 to 9,4 per cent in February 1979.

The rate of increase in the average remuneration per worker in the non-agricultural sectors of the economy, which had declined during the preceding three years, amounted to 10,5 per cent in the first three quarters of 1978/79, as against 9,1 per cent in

Percentage change in salaries and wages per worker in the non-agricultural sectors



1977/78. If the effect of increasing prices is taken into account, however, the average real remuneration per worker declined by 0,8 per cent in 1977/78 and further by 0,6 per cent in the first three quarters of 1978/79. As is shown by the accompanying graph, the average real remuneration of White workers declined for the fourth consecutive year, whereas that of Non-White workers showed only a slight increase in the first three quarters of 1978/79.

The improved productivity of labour and slow growth in labour remuneration contributed significantly to a lower rate of increase in labour costs, and therefore in prices, in manufacturing. In the first eight months of 1978/79 labour costs per unit of production in manufacturing increased by 8,8 per cent, compared with 8,7 per cent in 1977/78 and 20,1 per cent in 1976/77.

Higher rate of increase in prices

The declining trend in the rate of increase in consumer prices since 1975/76 was arrested in 1978/79 as a result of the imposition of the general sales tax.

Consumer prices rose by 11,9 per cent in 1978/79, as against 9,9 per cent in 1977/78. If the estimated effect of the general sales tax is excluded, the rate of increase in the year under review amounted to 8,8 per cent, reflecting lower rates of increase in the prices of most goods other than food and petroleum products. In addition to the more rapid rise in the prices of food and petroleum products, higher rates of increase were also recorded in service items such as flat rent and servants' wages. Taking into account differences in incomes and expenditure patterns, consumer prices in 1978/79 increased by 12,2 per cent for households with an income of less than R2 000 in the base year 1975, by 11,7 per cent for households with an income ranging from R2 000 to R5 999 in 1975, and by 11,6 per cent for households with an income of R6 000 or more in the base year. The higher rate of increase recorded for the lower income group reflected the relatively larger weight and higher price rises of food, including the effect of the general sales tax.

As shown in the accompanying table, the rate of increase in consumer prices fluctuated markedly in the course of the year under review. After an initial upward surge in the third quarter of 1978 when the general sales tax came into effect, the rate of increase declined substantially in the fourth quarter, but thereafter accelerated significantly in the first half of 1979. Compared with the corresponding month in the preceding year, consumer prices rose by 12,8 per cent in both April and May, and by 13,6 per cent in June 1979. Because of an early cut-off date for the inclusion of new prices in the monthly consumer price index, the increase in the price of petroleum products in June will only be reflected in the price index figure for July. Between July 1978, the month in which the general sales tax came into effect, and June 1979 consumer prices increased at a seasonally adjusted annual rate of 10,2 per cent.

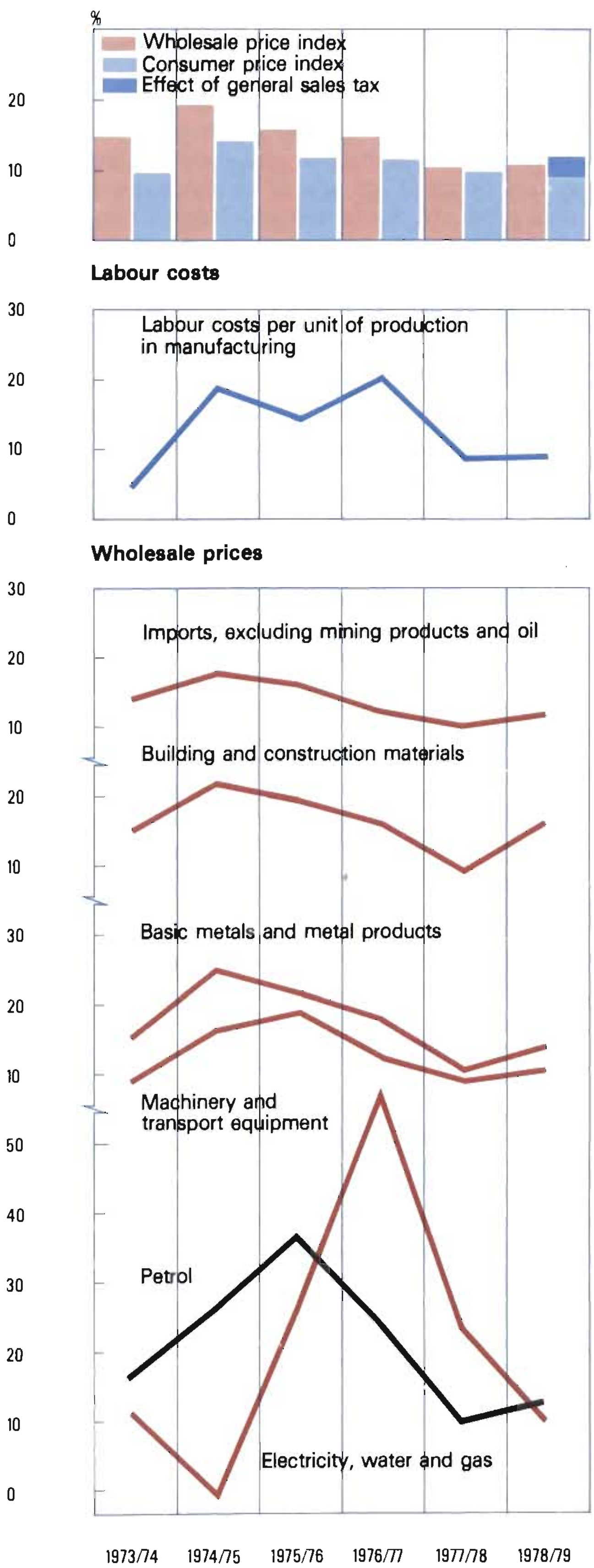
The rate of increase in wholesale prices rose slightly from 10,4 per cent in 1977/78 to 10,7 per

Prices

Annual percentage change in quarterly averages of seasonally adjusted monthly indices

	2nd qtr. 1978 to 3rd qtr. 1978	3rd qtr. 1978 to 4th qtr. 1978	4th qtr. 1978 to 1st qtr. 1979	1st qtr. 1979 to 2nd qtr. 1979	1977/ 1978 to 1978/ 1979
Consumer prices	21,5	9,0	10,7	11,6	11,9
Goods	26,1	9,1	11,5	12,2	13,0
Services	12,2	8,8	8,1	10,0	9,4
Wholesale prices	8,2	12,9	12,9	15,6	10,7
S.A. produced goods	8,5	13,1	12,7	13,9	10,7
Imported goods	7,8	12,1	13,4	20,6	10,7

Percentage change in prices and labour costs



cent in 1978/79, largely because of an acceleration in the rate of increase in imported goods, including petroleum products, from 9,9 per cent in 1977/78 to 10,7 per cent in 1978/79. Wholesale prices of domestically produced goods increased at the same rate as in 1977/78, namely by 10,7 per cent. Lower rates of increase occurred in the wholesale prices of food manufactures, beverages, tobacco, textiles and clothing, as well as in electricity, gas and water tariffs, whereas prices of agricultural products, basic metals, metal products, machinery and transport equipment showed higher rates of increase

The accompanying table shows that the rate of increase in wholesale prices accelerated sharply in the course of the year under review. More recently, wholesale prices rose by 11,4 per cent in April, 12,3 per cent in May, and 13,4 per cent in June 1979, compared with the corresponding month in 1978.

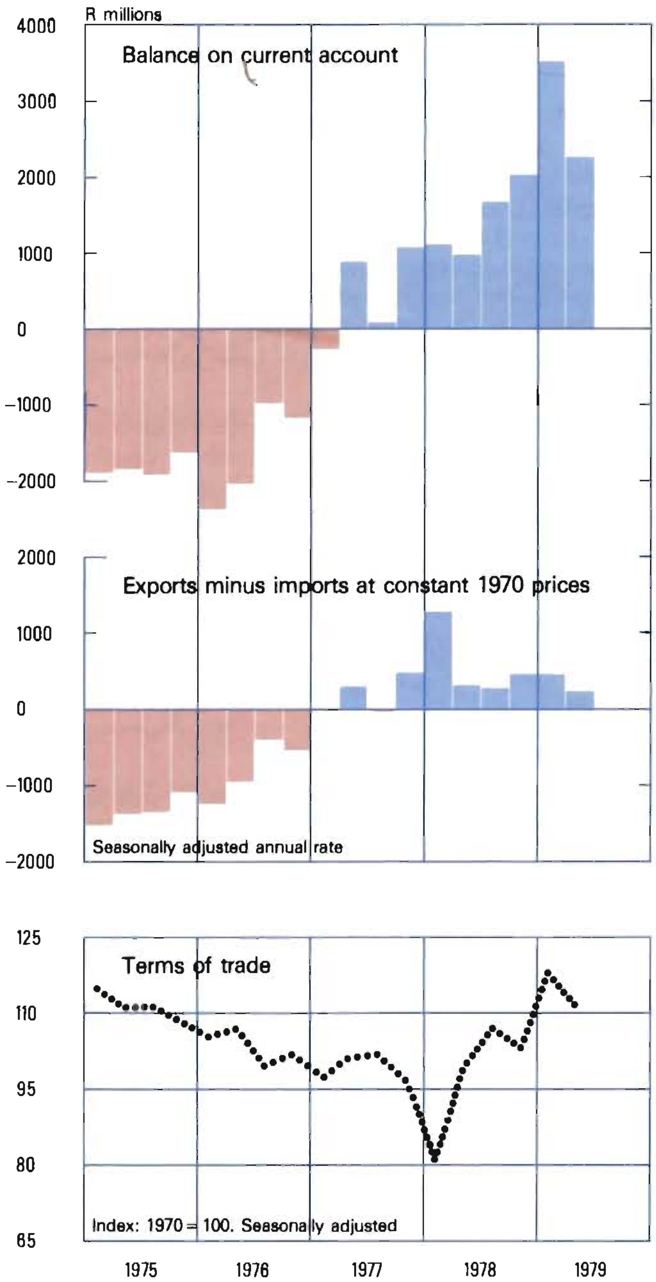
Balance of payments

Substantial current account surplus

After the current account of the balance of payments had shown a surplus of R888 million in 1977/78, a substantially higher surplus of R2 395 million was recorded in 1978/79. A dramatic improvement in the current account balance occurred during the past four years. At a seasonally adjusted annual rate, the balance changed from a deficit of R2 375 million in the first quarter of 1976 to a record surplus of R3 517 million in the first quarter of 1979, before changing to a smaller surplus of R2 257 million in the second quarter. As a ratio of the gross domestic product, the surplus on the current account amounted to 5,0 per cent in the second quarter of 1979, compared with 5,5 per cent in 1978/79 as a whole and 2,4 per cent in 1977/78.

The initial improvement of the current account during 1976 and 1977 was due to an improvement in volume terms, the effect of which was partly neutralised, however, by a marked deterioration in the terms of trade. From the beginning of 1978 a further improvement in terms of real transactions coincided with a considerably better terms of trade, resulting in a substantial current account surplus. The surplus recorded in 1978/79 was the net result of an increase in the net gold output and in merchandise exports, and an only partly offsetting increase in merchandise imports and in net invisible payments to the rest of the world.

Balance of payments current account



Further large increase in the net gold output

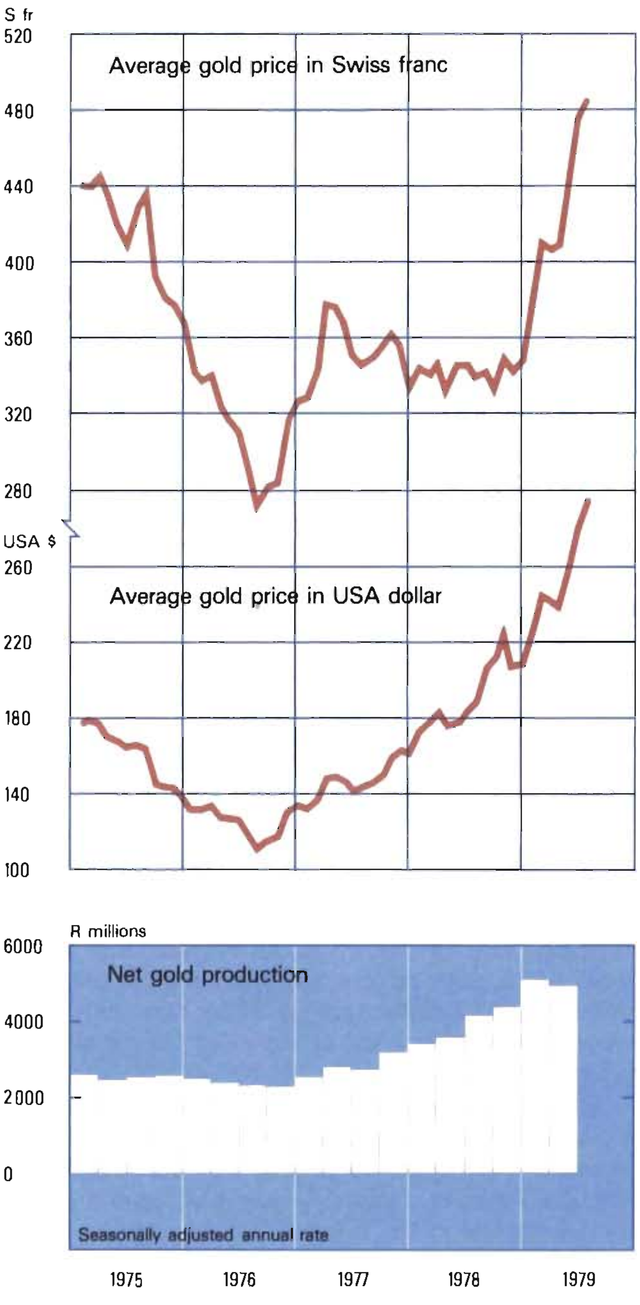
The value of the net gold output, which had increased by 31 per cent in 1977/78, rose further by no less than 43 per cent to R4 613 million in 1978/79. As in the preceding year, the increase in 1978/79 was largely the result of a strong rise in the price of gold. In volume terms, the net gold output showed only a slight increase which was achieved despite a lower grade of ore being milled.

The average fixing price of gold on the London market rose from \$165,81 per fine ounce in 1977/78 to \$228,29 per fine ounce in 1978/79, or by 38 per cent. During the early part of the year under review, the increase in the price of gold continued to be inversely related to a weakening of the effective exchange rate of the US dollar. From June to October 1978, for example, the London price of gold in terms of the US dollar rose by 24 per cent, whereas in terms of the Swiss franc it increased only slightly by 0,7 per cent.

Measures announced by the United States on 1 November 1978 to strengthen the dollar, including an increase in the quantity of gold that would be sold at the US Treasury's monthly auctions, caused a temporary decline in the price of gold during November.. In early December, however, the price started to increase again, notwithstanding a slight appreciation of the effective exchange rate of the US dollar. This indicated that changes in the effective exchange rate of the dollar no longer constituted a significant factor determining the price of gold. Movements in the price of gold became more directly related to increases in the price of oil and to expectations, based on the disruption of world oil supplies by political developments in Iran, of further upward adjustments in oil prices. As a result, the price of gold increased not only in dollar terms, but also in terms of all major currencies.

Apart from minor fluctuations, the gold price rose to \$254,00 per fine ounce on 8 February 1979, before declining to \$231,75 per fine ounce on 17 April. The price rose substantially to a record of \$307,00 per fine ounce on 26 July as a result of the

Gold price and net gold production



announcement on 18 April that the US Treasury would halve the quantity of gold sold at its monthly auctions, the subsequent reduction of the quantity of gold that the International Monetary Fund would sell at its regular auctions, the anticipated effect of further oil price increases on world inflation and balances of payments, and a sharp depreciation of the effective exchange rate of the US dollar. From the end of November 1978 to 31 July 1979, the London gold price rose by 53 per cent in terms of the US dollar and by 48 per cent in terms of the Swiss franc.

Continued good export performance

The value of merchandise exports increased from R6 800 million in 1977/78 to R8 015 million in 1978/79, or by about 18 per cent. This further rise brought the average annual rate of increase in the past four years to 25 per cent. The increase in 1978/79 was almost entirely due to higher export prices, whereas increases in volume had largely been responsible for the considerable rise in the preceding three years. Export commodity prices which, in accordance with international commodity price movements, did exceptionally well in the year under review were those of platinum, uranium, diamonds, wool, karakul pelts and copper.

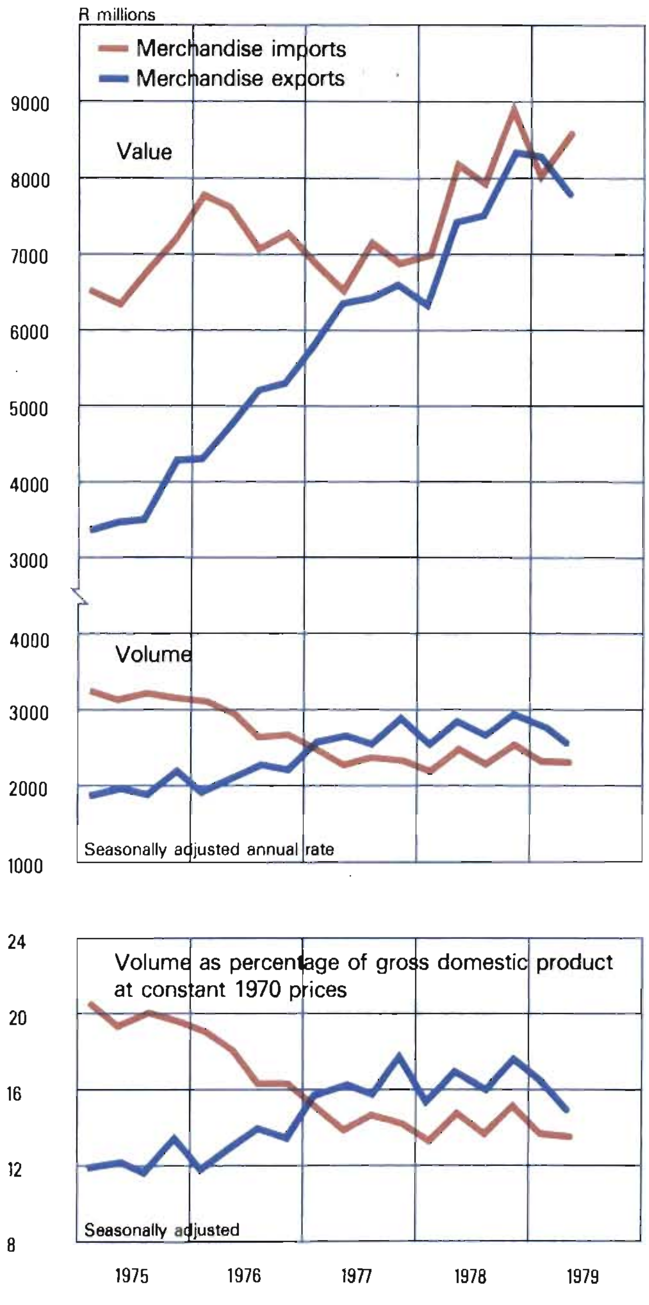
The volume of exports rose only slightly by 1 per cent in 1978/79, after an average annual rate of increase of 13 per cent had been recorded in the preceding three years. As a ratio of real gross domestic product, the volume of exports rose from 12 per cent in 1974/75 to 16 per cent in 1978/79, which was well above the post-war average annual figure of 13 per cent. This outstanding export performance was the result of the economic recovery in the major industrial countries, the completion of two new harbours and connecting railway lines, and the slow growth of domestic demand which, in conjunction with the higher degree of international competitiveness that was brought about by the 1975 devaluation of the rand, induced domestic producers to exploit foreign markets.

During the first half of 1979 the volume of merchandise exports declined appreciably, causing the value of exports, at a seasonally adjusted annual rate, to decrease slightly from R8 334 million in the fourth quarter of 1978 to R7 768 million in the second quarter of 1979. The lower export volume was to a large extent attributable to lower diamond sales. The value of exports of commodities, such as platinum, uranium and ferro-chrome, continued to rise strongly.

Increase in merchandise imports

Merchandise imports increased from R7 335 million in 1977/78 to R8 357 million in 1978/79, a rise of 14 per cent. Although the volume of imports rose slightly, higher import prices were largely responsible for the increase in the value of imports. After the rate of increase in import prices had decelerated in 1977 in conformity with lower world inflation rates, it started accelerating again from the beginning of 1978. Consequently, the value of merchandise imports, at a seasonally adjusted annual rate, increased from R6 901 million in the fourth quarter of 1977 to R8 920 million in the fourth quarter of 1978. Subsequently, import prices rose substantially further because of increases in the price of petroleum products, but a simultaneous sharp decline in the import volume resulted in the value of imports decreasing to a seasonally adjusted annual rate figure of R8 014 million in the first quarter of 1979, before rising to R8 586 million in the second quarter.

Merchandise exports and imports



The increase in the volume of imports in 1978/79 amounted to 1 per cent, compared with an average annual decrease of 12 per cent in the preceding three years. As a ratio of real gross domestic product, the volume of merchandise imports declined from 23 per cent in the third quarter of 1974 to 13½ per cent in the first quarter of 1978, before increasing to 15 per cent in the fourth quarter of that year. Reflecting the disruption of oil supplies, the ratio declined again to 13½ per cent in the second quarter of 1979. The relatively low volume of imports in recent years could be associated generally with the low rate of economic growth and, to a lesser extent, with progress made towards import replacement.

The increase in the value of merchandise imports in 1978/79 could be observed in a wide range of commodities. In particular, sharp rises were recorded in imports of machinery and electrical equipment, transport equipment, textiles, chemical products and defence equipment. The only major categories of imports to decline were mineral products, including petroleum products, and prepared foodstuffs.

Continued increase in net invisible payments to foreigners

A sharply increasing trend could be observed in net invisible payments to the rest of the world from 1974/75 to 1977/78. In 1978/79, however, these payments increased by only 5 per cent to R1 876 million. This further rise was attributable to a sharp increase in service payments that was only partly offset by considerably higher service and net transfer receipts. The increase in service payments, in turn, resulted from higher freight and insurance payments, related to the increase in the value of merchandise imports, and to higher dividend payments, in particular, by mining companies. Ships' stores and dividend receipts on foreign investments were mainly responsible for an appreciable rise in service receipts.

Substantial net outflow of capital

A net outflow of capital amounting to R2 238 million was recorded in 1978/79, compared with R970 million in 1977/78. The net capital outflow consisted entirely of short-term capital, including unrecorded transactions (i.e. errors and omissions relating to the current as well as the capital account), whereas a small net inflow of long-term capital occurred. The latter small inflow, together with the large current account surplus, resulted in the basic balance being in surplus to the extent of R2 440 million, as against R798 million in 1977/78.

The outflow of short-term capital amounted to R2 283 million, or more than double the amount recorded in 1977/78. As shown in the accompanying table, an appreciable part of this outflow consisted of repayments on loans obtained previously to supplement foreign exchange holdings. The largest proportion, however, comprised a net outflow of capital from the private sector, including unrecorded transactions. This outflow increased from R395 million in the first half of 1978 to R776 million in the second half and to R1 324 million in the first half of 1979.

Features of the long-term capital movements in 1978/79 were, firstly, a net repayment on foreign loans by the central government and banking sector. Secondly, there was a net inflow of capital to public corporations and local authorities. This consisted mostly of funds raised for the purpose of financing

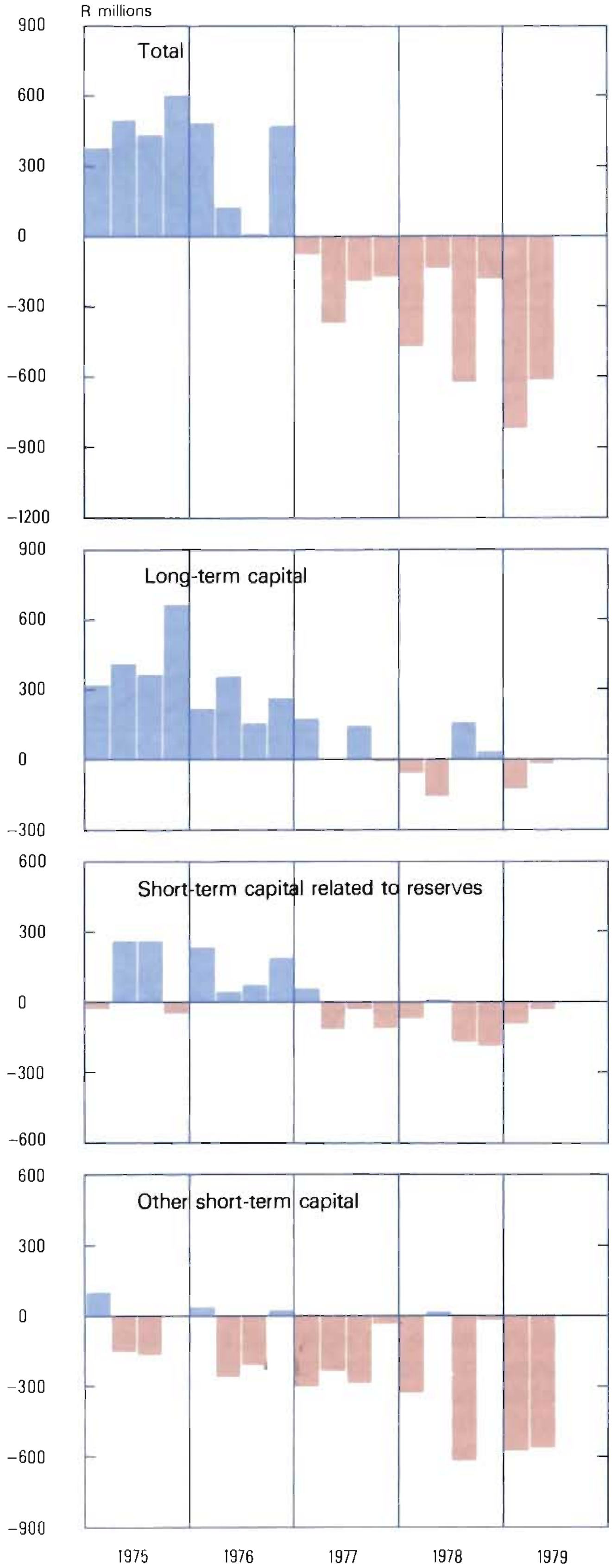
Net capital movements
R millions

	Year ended 30 June 1977	1978	1979
Long-term capital			
Central government and banking sector	173	-397	-266
Public corporations and local authorities	247	202	170
Net purchases of securities quoted on the Johannesburg Stock Exchange	-57	-11	-79
Other private sector	223	116	220
Total long-term	586	-90	45
Short-term capital			
Liabilities related to reserves	193	-226	-500
Other, including unrecorded transactions[1]	-735	-654	-1 783
Total short-term	-542	-880	-2 283
Total net capital movements	**44**	**-970**	**-2 238**

1) I.e. errors and omissions relating to the current as well as capital account.

specific projects, such as the nuclear power station and the oil-from-coal plant, and offsetting repayments on existing loans in accordance with the public corporations' policy of financing a larger part of their capital expenditure from their own resources. Thirdly, foreigners' sales of securities listed on the Johannesburg Stock Exchange exceeded their purchases. They were net sellers of securities during the first half of 1979, after they had been net purchasers during the second half of 1978. This change reflected transactions that were aimed at creating financial rand, after the purposes for which financial rand may be used had been extended at the end of January 1979. . The increased demand for financial rand led to a decline in the financial rand discount from 42 per cent at the end of January to 25 per cent at the end of June, but subsequently the discount increased again to 27½ per cent at the end of July. Net sales by foreigners of securities on the Johannesburg Stock Exchange were also related to expectations of a relaxation of exchange control in the United Kingdom as it applies to the dollar premium. The effective dollar premium fell from 49 per cent at the end of February 1979 to 23 per cent at the end of March and then to 8½ per cent on 26 July. Finally, there was a fairly large net inflow of capital to the private sector, including a contra item for the outflow of capital which represented stock exchange sales of listed securities for the purpose of creating financial rand. This inflow could be associated with the financing of the containerisation programme, mining ventures and motor vehicle manufacturing.

Net capital movements



Increase in gross as well as net foreign reserves

The gross gold and other foreign reserves increased by R878 million during 1978/79 to a level of R2 807 million at the end of June 1979. The larger part of this increase was due to the revaluation of the gold reserves at market-related prices and other valuation adjustments. If the effect of these adjustments is excluded, the gross reserves increased by R157 million, compared with a decline of R82 million in 1977/78. Because of a reduction of R500 million in liabilities related to reserves, the net gold and other foreign reserves increased by R657 million during the year under review, compared with R144 million during 1977/78. The increase in the net reserves during the first eleven months of 1978/79 amounted to R873 million, but this was followed by a decline of R216 million during June 1979. During July the net gold and other foreign reserves of the Reserve Bank decreased further by about R110 million.

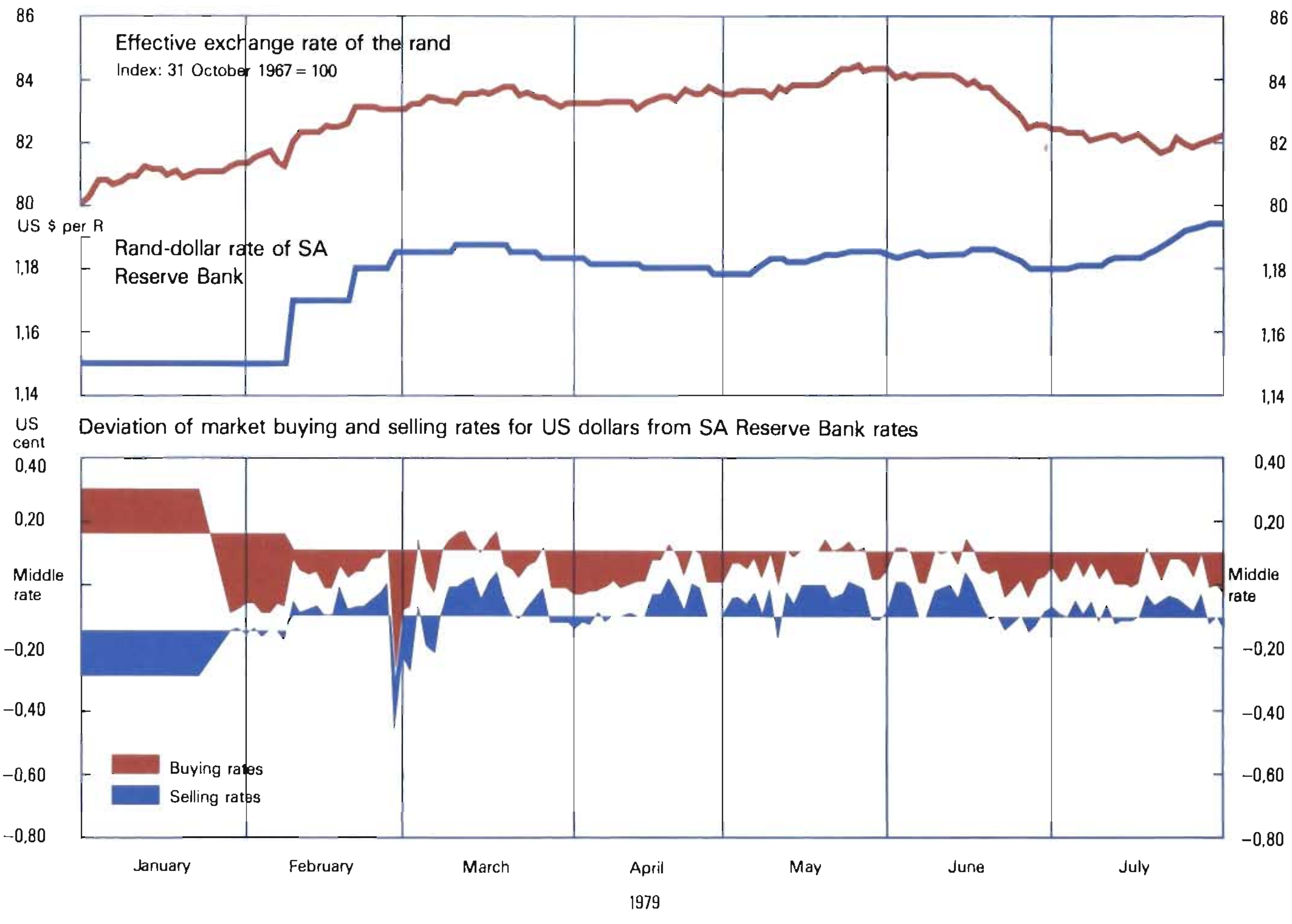
The composition of the reserves changed considerably during 1978/79. As a result of the sharp rise in the price of gold and the procedure followed in valuing the gold reserves at a market-related price, these reserves increased substantially from R1 413 million at the end of June 1978 to R2 070 million at the end of June 1979. The volume of gold holdings, however, declined from 9,79 million fine ounces to 9,67 million fine ounces over the same period. The foreign exchange component of the reserves increased by R221 million during 1978/79 to R737 million at the end of June 1979.

Changes in exchange rate policy and practices

On 24 January 1979 a new exchange rate policy was adopted, following upon recommendations by the Commission of Inquiry into the Monetary System and Monetary Policy in South Africa. The Commission recommended that the eventual aim should be to establish a unitary exchange rate system under which an independent and flexible rand will find its own level against other currencies in competitive spot and forward foreign exchange markets. Movements of the exchange rate of the rand are to be managed through Reserve Bank intervention by means of purchases and sales of foreign exchange.

During an initial transitional period after 24

Exchange rates



January the Reserve Bank continued to quote fixed predetermined buying and selling rates for US dollars. This practice was discontinued on 27 February and since then the Reserve Bank's rates have been changed as and when adjustments have been deemed necessary by the Bank. From July 1978 to the beginning of February 1979, the period in 1978/79 during which the rand-dollar exchange rate remained unchanged, the effective exchange rate of the rand depreciated by 5 per cent. During February the rand appreciated by 3,0 per cent against the US dollar. Thereafter, until the middle of July, the rand-dollar exchange rate remained approximately unchanged, except for minor fluctuations, but subsequently until early August the rand appreciated again by 0,6 per cent against the dollar. The effective exchange rate of the rand appreciated by 3,9 per cent from early February to the third week in May, but then depreciated by 2,1 per cent until early August.

Several other measures were taken to give effect to the new exchange rate policy. Firstly, with effect from 29 January, the commission of 1 per cent per annum on forward cover was abolished and the Reserve Bank's forward margin on US dollars was set at a dollar discount (or rand premium) of 2 per cent per annum. The discount was increased to 2½ per cent on 5 April. This new procedure caused an immediate narrowing of the margin between the effective cost of trade financing in US dollars and in rand to less than 1 per cent. Subsequently, this margin widened to more than 2 per cent at the end of June. On 8 March the Reserve Bank started to base its forward rates on the ruling spot rate, instead of on the closing spot rate of the preceding day. Secondly, the Reserve Bank extended forward cover facilities to foreign loans negotiated by the private sector with exchange control approval, but only in respect of the rand-dollar exchange risk and only for a period of one year at a time. The Bank continued to provide forward cover on public sector loans, but the rate on forward cover against liabilities denominated in stronger currencies was set at a higher level than that in respect of the US dollar. Thirdly, on 5 March a new arrangement came into effect in terms of which the proceeds of Krugerrand sales were channelled directly to authorised dealers in the foreign exchange market instead of to the Reserve Bank. Fourthly, during April an internationally linked information system, the Reuters Monitor, was installed in the foreign exchange market to facilitate the distribution of up-to-date information on exchange dealings in the market. Finally, limits were set early in April for the foreign exchange holdings and risk exposure of authorised dealers. Procedures to ensure adherance to these limits were instituted by the Reserve Bank on 9 April.

As a first step in the direction of a market-related unitary exchange rate for the rand, the "securities rand" was transformed into a "financial rand" by widening the range of purposes for which financial rand may be used. Instead of being allowed to use the former securities rand for purchases of listed securities and special non-resident government bonds only, non-resident holders of the new financial rand were permitted to make investments also in unlisted securities, real estate and capital assets, subject to approval by the Reserve Bank. The latter types of investment, however, had to represent the acquisition of a proprietor's interest as distinct from providing loan funds. On 21 June 1979 the Minister announced that future outward capital transfers by residents as well as transfers of funds by migrants had to be effected through the financial rand instead of the commercial rand system.

Monetary and banking situation

Virtually no change in growth rate of money and near-money supply

The supply of money and near-money increased by R736 million, or 7 per cent, during 1978/79. This rate of increase was fractionally lower than in 1977/78, the year during which a lower turning point of the business cycle was reached. The narrowly defined money supply rose rapidly by 14 per cent during 1978/79, as against a slight increase of 2 per cent during the preceding year. In marked contrast with the first eighteen months of the preceding cyclical upswing in 1973/74, during which the supply of money and near-money had risen by 35 per cent, the increase in the supply of money and near-money during the first eighteen months of the current upswing amounted to a comparatively modest 12 per cent.

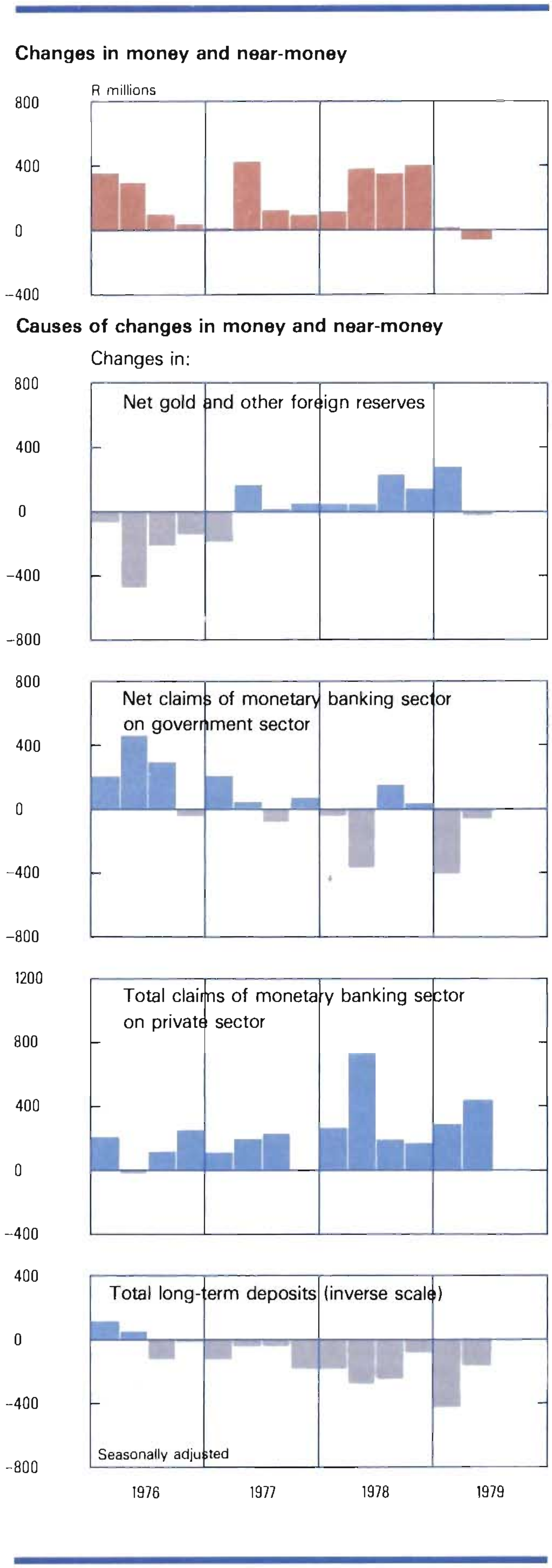
The average level of the quantity of money and near-money in 1978/79 was 11 per cent higher than in 1977/78. This increase fell short of the rate of growth in the gross domestic product at current prices. As a result, the ratio of money and near-money to the gross domestic product, both seasonally adjusted, declined further from its most recent peak of 29,6 per cent in the first quarter of 1976 to 24,8 per cent in the second quarter of 1979, its lowest level during the nineteen-seventies.

Marked fluctuations in the rates of growth in the monetary aggregates occurred in the course of the period under review. The seasonally adjusted money and near-money supply, for example, increased at an annual rate of 15 per cent during the second half of 1978, but declined at a rate of nearly 1 per cent during the first half of 1979. The narrowly defined money supply, seasonally adjusted, declined at an annual rate of 6 per cent during the third quarter of 1978, but increased at an exceptionally high annual rate of 34 per cent during the subsequent six months, and thereafter decreased again at an annual rate of approximately 1 per cent during the second quarter of 1979.

Causes of changes in money and near-money supply

The causes of changes in the supply of money and near-money showed the kind of pattern that is typically found during the more advanced stages of cyclical downswings and the early stages of cyclical upswings in the South African economy. This generally reflects rising net gold and other foreign reserves of the monetary banking sector accompanied by declines in this sector's net claims on the government sector, and accelerated increases in long-term deposits of the private sector with monetary banks. Monetary banks' claims on the private sector rose moderately during 1978/79.

The net gold and other foreign reserves of the monetary banking sector, which in 1977/78 had made the first positive contribution to the increase in the money and near-money supply since 1972/73, rose substantially during 1978/79. In contrast with



Causes of changes in money and near-money
R millions

	Not seasonally adjusted						Seasonally adjusted			
	Year 1977/ 1978	1978 Third Qtr.	1978 Fourth Qtr.	1979 First Qtr.	1979 Second Qtr.	Year 1978/ 1979	1978 Third Qtr.	1978 Fourth Qtr.	1979 First Qtr.	1979 Second Qtr.
Net gold and other foreign reserves	171	225	167	291	-28	655	235	144	295	-28
Claims on government sector:										
Gross claims	587	-25	-165	-425	106	-509	...	...	...	...
Government deposits (increase -, decrease +)	-1 044	-92	220	-226	289	191	...	...	...	...
Net claims	-457	-117	55	-651	395	-318	149	26	-413	-63
Claims on private sector	1 222	294	122	220	443	1 079	188	174	274	443
Long-term deposits (increase -, decrease +)	-717	-226	-90	-339	-304	-959	-257	-93	-429	-169
Net other assets	502	111	215	226	-273	279	...	...	...	...
Total causes of changes	721	287	469	-253	233	736	356	400	25	-66

1977/78, this rise reflected not only a substantial further reduction in the banking sector's short-term foreign liabilities, amounting to R437 million, but also an increase of R218 million in monetary banks' gross reserve holdings, excluding the effect of the monthly revaluation of the Reserve Bank's gold stock.

Net claims of the monetary banking sector on the government sector decreased further during 1978/79, following a decline during the preceding year. On the basis of seasonally adjusted figures, this decrease was concentrated in the first half of 1979, most of it representing a decline in monetary banks' gross claims on the government sector. Credit extended by monetary banks to the private sector rose by a smaller amount during 1978/79 than during 1977/78. Total domestic credit extended by the monetary banking sector increased by R761 million, or 6 per cent, compared with a rise of R765 million in the preceding year.

Long-term deposits of the private sector with monetary banks continued to exert an important contractionary influence on the supply of money and near-money during 1978/79. The rise of 30 per cent in these deposits during 1978/79 was even larger than during 1977/78, and for the two years the total increase amounted to as much as 68 per cent. To an important extent, this accelerated increase in long-term deposits could be regarded as a cyclical phenomenon. An analysis of changes in monetary banks' deposit liabilities during the past twenty years shows that, on average, long-term deposits accounted for 18 per cent of the increase in such liabilities during the second half of cyclical upswings and the first half of cyclical downswings, but for 36 per cent during the second half of downswings and the first half of upswings. Cyclical shifts between the money, near-money and long-term deposit components of changes in the banks' total deposit liabilities may be related, among other things, to changes in interest rates and interest rate expectations (including changes in deposit interest rate control) as well as to changes in personal saving, varying needs for transactions and precautionary balances, the lack or availability of attractive alternative financial or non-financial investment outlets, and changing levels of activity in financial markets. Roughly mirroring the cyclical fluctuations in the share of long-term deposits in total deposit liability changes, near-money deposits accounted for 54 per cent, on average, of the increases in total private sector deposits during the second half of cyclical upswings and the first half of cyclical downswings and for 31 per cent of such increases during the second half of downswings and the first half of upswings since 1959.

Reduced rate of increase in bank credit to private sector

The increase of 10 per cent in the monetary banking sector's claims on the private sector during 1978/79 was somewhat lower than the rise of 13 per cent during the preceding year. After an exceptionally rapid increase at an annual rate of 34 per cent during the second quarter of 1978, associated with an upsurge in consumer expenditure prior to the introduction of the general sales tax in early July, the seasonally adjusted claims on the private sector rose at annual rates of 7 per cent, 11 per cent and 17 per cent during the second half of 1978 and the first two quarters of 1979, respectively. Business demand for credit remained slack throughout the year under review.

As regards changes in the main components of the monetary banks' credit to the private sector, investments in private sector securities increased by R219 million, or 14 per cent, or at a somewhat higher rate than total claims on the private sector. Cash credit advances by the Land Bank rose by R150 million, or 13 per cent, against R107 million in 1977/78. The discounts, loans and advances of commercial banks, merchant banks and monetary hire-purchase and general banks rose relatively slowly by R532 million, or 7 per cent.

A breakdown of the discounts, loans and advances of the institutions concerned shows that discounts of trade bills and bankers' acceptances declined sharply further during the second half of 1978, recovered during the first half of 1979, but on balance decreased slightly during 1978/79 as a whole. Hire-purchase credit and leasing finance, in contrast, continued to advance rapidly by R326 million, or 33 per cent, and R193 million, or 20 per cent, respectively, after increases of 41 per cent and 24 per cent, respectively, had been recorded in 1977/78. "Other" advances, which generally may be regarded as indicative of ordinary business demand for bank credit, increased by only R37 million, or less than 1 per cent, during 1978/79, a decrease during the second half of 1978 being slightly more than offset by a rise during the first half of 1979. Heavy emphasis during the year under review on the extension of hire-purchase credit and leasing finance raised the relative importance of these forms of credit from 26 per cent of total discounts, loans and advances at the end of June 1978 to 31 per cent at the end of June 1979, as against a ratio of only 15 per cent at the end of June 1974. About 60 per cent of the total increase in discounts, loans and advances during the past five years consisted of hire-purchase credit and leasing finance.

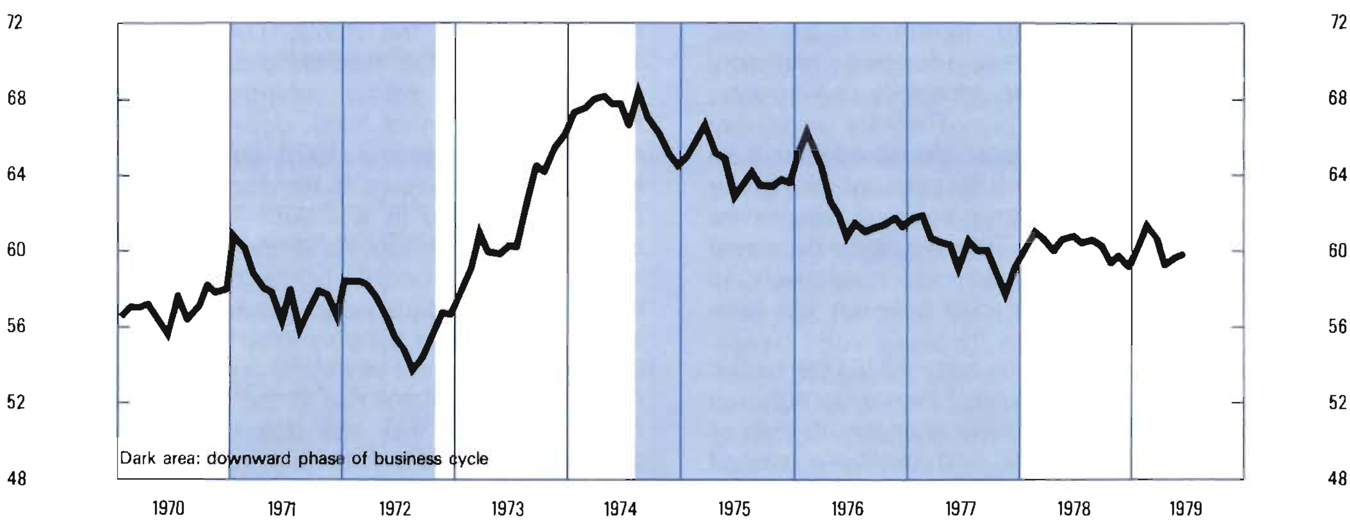
As shown in the accompanying graph, the ratio of commercial, merchant and monetary hire-purchase and general banks' claims on the private sector to their total assets up to the end of June 1979 had largely failed to show its customary cyclical upswing. In the past, upward and downward movements of this ratio had accompanied similar movements of the general business cycle with a fair degree of consistency. Similarly, the ratio of the monetary banking sector's claims on the private sector to the gross domestic product at current prices up to the second quarter of 1979 had failed to respond to the economic recovery and continued on a downward trend after an upper turning point had been reached in the first quarter of 1976.

The authorised ceilings on the discounts, loans and advances of all registered banking institutions were increased by R707 million during the year. Of this amount, approximately R360 million was accounted for by an additional 5 per cent increase which became effective from the end of March 1979. The amount of authorised ceilings actually utilised rose by R710 million, resulting in a decrease of R3 million in unused facilities. The authorised ceilings on investments in private sector securities were raised by R83 million, ceilings utilised rose by R44 million, and unused facilities increased by R39 million.

Further improvement in bank liquidity

The average excess liquidity ratio of all banking institutions increased from 2,2 per cent in 1977/78 to 2,7 per cent in 1978/79. An improvement in liquidity was experienced by all classes of banking institutions. The commercial banks' average excess liquidity ratio rose from 2,9 per cent in 1977/78 to 3,4 per cent in 1978/79 and that of other monetary banks from 0,7 to 1,8 per cent. The average liquidity ratio of non-monetary banks, excluding two banks that are in the process of repaying deposits, increased

Commercial banks, merchant banks, monetary hire-purchase and general banks: ratio of claims on the private sector to total assets



from 0,5 to 2,1 per cent. Margins of excess liquidity were enlarged notwithstanding a continued downward trend in yields and interest rates during the larger part of the year, the improbability of a further increase in liquid asset requirements, and the general absence of any prospective large or sudden increase in the demand for credit.

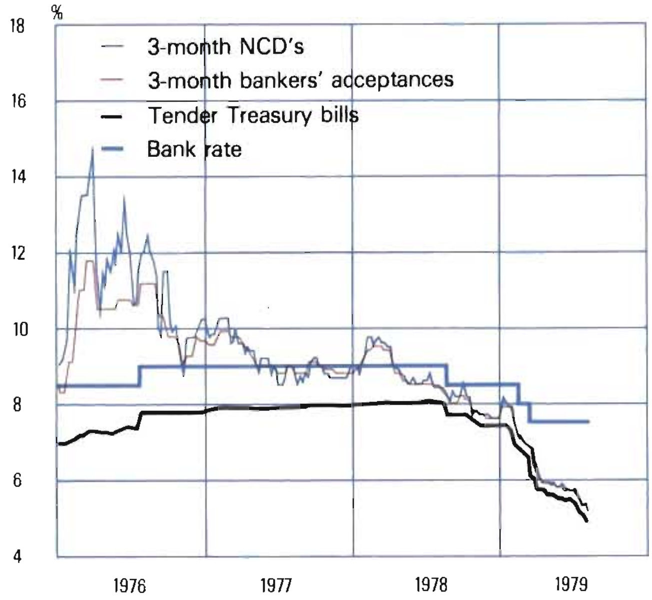
Statistically, the increase in the banks' excess liquidity arose from two sources. Firstly, the banks' actual holdings of liquid assets rose fairly rapidly by R594 million, or 13 per cent, from the end of June 1978 to the end of June 1979, compared with an increase of only 4 per cent in 1977/78. Most of this accelerated increase was due to the sharply rising contribution of the foreign sector to the banks' liquidity base, which was only partly offset by diminishing contributions from the government and private sectors. Secondly, the increase in the banks' required liquid asset holdings, amounting to R367 million, or 9 per cent, not only was smaller than the increase in their actual liquid assets but, in relative terms, also fell short of the increase of 15 per cent in their liabilities to the public. This less than proportional rise in the banks' required liquid assets, in turn, partly reflected a continuing shift in the composition of their liabilities towards long-term liabilities and liabilities under acceptances, both of which are subject to comparatively low liquid asset requirements. In addition, the liquid asset requirements were lowered twice during 1978/79, notably with regard to the increases in the banks' short-term and medium-term liabilities since the end of September 1975. The effect of these reductions on the banks' statutory minimum holdings of liquid assets was approximately R250 million at the end of June 1979.

Money market conditions and interest rates

In several respects, developments in the money market during 1978/79 represented a continuation of trends that had been in evidence since early 1976. Interest rates in the market, for example, while occasionally responding to month-end or more prolonged seasonal tightness, declined markedly further throughout the year, especially in February, March and early April 1979. The rate on 90-day negotiable certificates of deposit decreased from 8,80 per cent on 7 July 1978 to 5,50 per cent on 13 July 1979. The rate on three-month bankers' acceptances and the tender rate on Treasury bills decreased from 8,50 per cent and 8,00 per cent, respectively, to 5,50 per cent and 5,18 per cent between the same dates.

As had been the case since early 1978, the banks' free balances with the National Finance Corporation tended to be depleted regularly over month-ends or for more extended periods, and generally reached significant levels only after the second or third week in months during which the availability of call money increased relatively rapidly. As a counterpart of this phenomenon, the discount houses still had to absorb

Money market interest rates

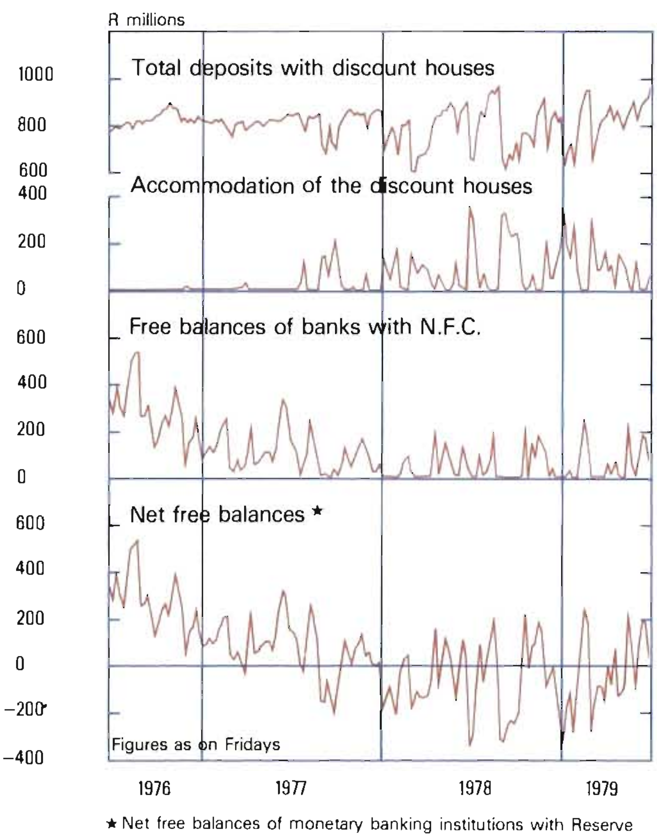


a substantial proportion of the usual month-end and other fluctuations in the availability of call money in the market and continued to experience an enhanced degree of volatility in their call loans. Accordingly, they had to make use of Reserve Bank accommodation frequently, and occasionally for large amounts.

Relatively tight conditions in the money market occurred especially in late June and early July 1978, over the August month-end, in September and during the first week of October 1978, during the first week and at the end of January 1979, and over the month-end of February 1979. Total call loans to the discount houses during these tight periods occasionally declined to between R500 million and R600 million. Mirroring these declines, accommodation extended to the discount houses, including call loans made by the Public Debt Commissioners, from time to time reached peaks of about R400 million. Rapidly easing conditions in the money market, on the other hand, occurred during part of August 1978, October 1978 and February 1979. Peaks in total call loans to the discount houses during these periods and in late June 1979 amounted to almost R1 000 million. As in the past, a large part of the more pronounced tightening effects on the market was attributable to substantial flows of tax and other funds to the government sector. Conversely, the easing of the market in February 1979 apart from reflecting a large rise in the Reserve Bank's net foreign reserves, was also due to a large drop in government deposits with the Reserve Bank and the National Finance Corporation during most of that month.

The continuing decline in short-term interest rates and a further narrowing of the margins between the rates on liquid and non-liquid assets were in accordance with the gradual recovery of the excess liquidity of banking institutions referred to earlier. During part of the year, expectations of further declines in yields and interest rates generally, provided an incentive for investors to shift towards longer-dated securities and for banks to lengthen the average maturity of their liquid asset portfolios. The commercial banks, for example, further reduced their average month-end holdings of call money with the discount houses and the National Finance Corporation from R694 million, or 21 per cent of their total liquid assets, in 1977/78 to R560 million or 15 per cent of total liquid assets in 1978/79, while continuing to build up their holdings of short-term and long-term government securities. From approximately February 1979, however, both the banks and the discount houses commenced to build up the level of their holdings of Treasury bills. A counterpart of this phenomenon, which was also apparent in an average amount of applications in the weekly tender for Treasury bills of more than R140 million from late January 1979 to the middle of July for the amount of R50 million or R60 million of bills on offer, was a further diminution of the Reserve Bank's and the National Finance Corporation's rôle as "residual holders" of Treasury bills. The commercial banks' holdings of Treasury bills of R289 million at

Selected indicators of money market conditions



★ Net free balances of monetary banking institutions with Reserve Bank and N.F.C.

the end of April 1979 were, in fact, considerably higher than at any earlier month-end.

Also indicative of a change in market sentiment and in longer-term interest rate expectations among market participants, was the fact that the trend in the monetary banks' net free balances with the Reserve Bank and the National Finance Corporation changed in the course of the year. As shown in the accompanying graph, the trend in these balances continued downwards throughout 1977/78 but levelled off during the second half of 1978 and moved upwards during the first half of 1979, essentially reflecting higher average levels of call loans to the discount houses and a commensurately reduced average level of Reserve Bank accommodation of the discount houses during this period.

In the course of the year under review, the Reserve Bank effected sales of securities in the open market of somewhat over R500 million and purchased securities to an amount of approximately R160 million. Most of the Bank's security sales were made during periods of increasing money market ease in August and October 1978 and April 1979. Roughly two-thirds of these sales consisted of sales of short-dated government stock, an overwhelming proportion of which was taken up by the discount houses and the banks. Purchases of securities by the Bank were effected during the period of money-market tightness from late August to early October 1978 and again in March, May and June 1979. However, whereas the Bank bought short-dated securities during the earlier period, its purchases in the changing investment climate during the first half of 1979 exclusively consisted of medium-term and long-term stock with unexpired maturities of three to ten years and more than ten years, respectively.

Monetary policy measures

Apart from the Reserve Bank's open-market operations, certain monetary policy measures were taken during 1978/79 within the framework of the authorities' intention to stimulate the economy. A lowering of Bank rate from 9 to 8½ per cent was announced on 22 August 1978, partly in acknowledgement of the generally lower level and declining trend of domestic interest rates and despite the need for a close monitoring of changes in the relative levels of interest rates domestically and abroad in order to prevent large-scale switching of trade financing and other outflows of capital. This reduction in Bank rate was followed by a lowering of the commercial banks' prime overdraft rate from 12½ to 12 per cent from 24 August and to 11½ per cent from 15 September 1978. It was also followed by a lowering by a full percentage point of a majority of deposit and related interest rates quoted by the banks, the building societies, the Treasury on its non-marketable issues, and the Post Office, causing the rates offered by the banks and the building societies to decline below the deposit interest rate control ceilings.

Further reductions in Bank rate, from 8½ to 8 per cent on 6 February 1979 and to 7½ per cent on 17 March 1979, were followed by decreases in the commercial banks' prime rate by one-half per cent to 11 per cent in February and by a full per cent to 10 per cent in March. Deposit interest rates, with the exception of the rate on ordinary savings accounts, generally were adjusted downwards by one-half per cent on both occasions.

A reduction in the liquid asset requirements for banking institutions, previously referred to, was announced in August 1978 to become effective from approximately 21 September 1978. Earlier differentiation of the requirements between commercial banks and "other" banks was replaced by a distinction between "large" banks (i.e., banks whose total assets exceed R800 million) and other banks. In order to allow the smaller banks to compete more effectively for medium-term deposits, the supplementary liquid asset requirement against medium-term liabilities to the public, as it applied to these institutions, was reduced from 29 per cent to 27 per cent; in addition, the requirement in respect of **increases** in such liabilities since the end of September 1975 was abolished for the smaller banks while being reduced from 10 per cent to 8 per cent for the "large" banks. A second, more important, reduction of the banks' liquidity requirements was announced on 12 March 1979 to become effective from approximately 21 March. In terms of this measure, the requirements pertaining to the increases in "large" banks' short-term and medium-term liabilities to the public since September 1975 were halved from 20 and 8 per cent to 10 and 4 per cent, respectively; the related requirement in respect of the increases in smaller banks' short-term liabilities was abolished entirely.

A general increase in the ceilings applying to banking institutions' discounts, loans and advances to the private sector and their investments in private sector securities, over and above the regular monthly increases in these ceilings by ½ per cent of the relevant "base" figures as at the end of December 1975, was announced on 12 March 1979 to become effective from 31 March. Amounting to 5 per cent of the "base" figures, this increase had the effect of raising the banks' maximum permissible lending to the private sector and their maximum holdings of private sector securities to 128 per cent and 126 per cent, respectively, of the levels thereof as at the end of 1975. The aggregate amount of credit to the private sector which a banking institution may not exceed without becoming subject to the ceiling requirements, which had been raised from R10 million to R15 million in May 1978, simultaneously was raised further to R20 million.

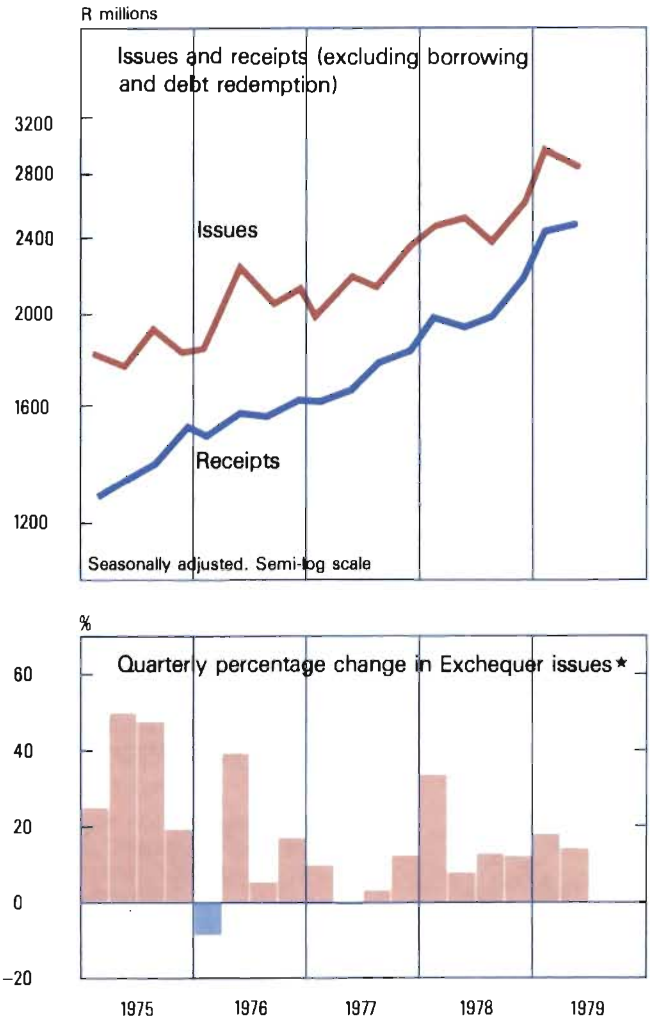
Government finance

Stable growth in Exchequer issues

Issues from the Exchequer Account during 1978/79 continued to reflect official policy of maintaining discipline in government expenditure. Exchequer issues to the various government departments during 1978/79 amounted to R10 774 million, or 14 per cent more than during the preceding year. A roughly similar rate of increase was recorded in 1977/78 and is expected to be maintained also during the 1979/80 fiscal year. The 1979/80 Budget provided for an increase of 12 per cent in government expenditure, but the usual additional appropriations towards the end of the fiscal year could raise this percentage to approximately the same level as in the year under review.

Not only was the rate of increase in Exchequer issues approximately equal to that in 1977/78, but the seasonal pattern of issues during 1978/79 was fairly consistent with that during the preceding year. In the past, shifts in the seasonal pattern frequently caused the rate of change in Exchequer issues in different quarters to vary considerably from year to year, as is shown in the accompanying graph.

Exchequer Account

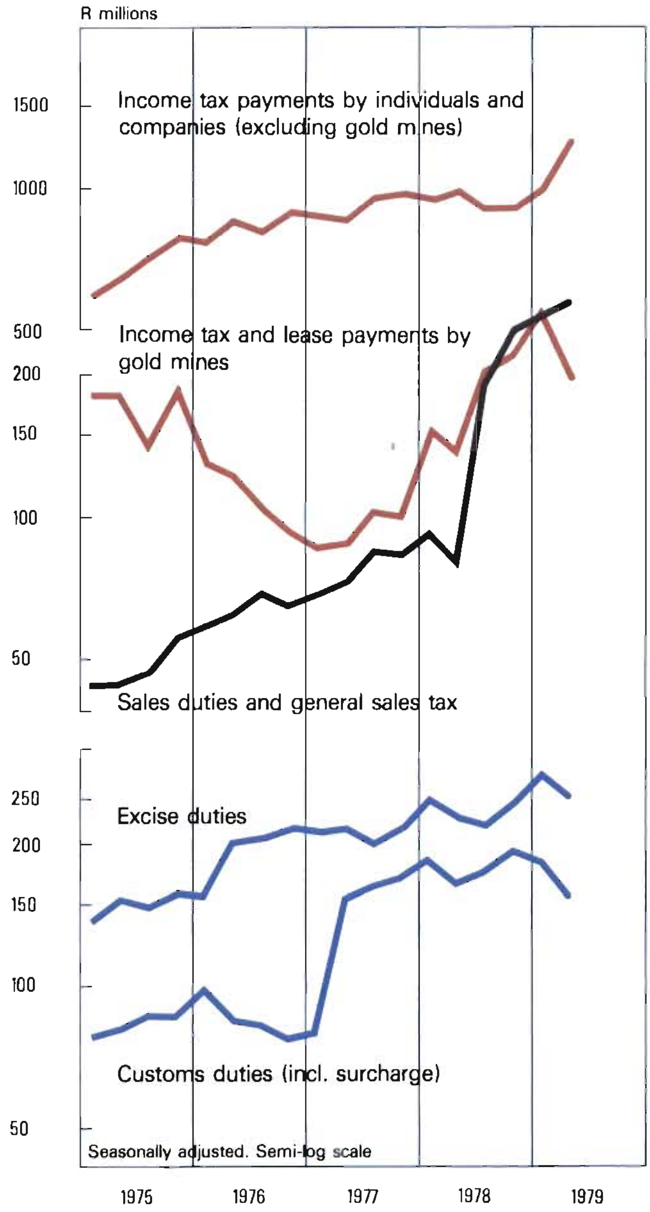


★Compared with the same period in the preceding year

Change in composition of government revenue

Receipts on the Exchequer Account during 1978/79 amounted to R8 920 million, or 19 per cent more than in the preceding year. Although the rate of increase was only slightly higher than in 1977/78, the composition of receipts was notably different. This was caused, firstly, by a change in the tax structure and, secondly, by a substantial increase in receipts from gold mining companies. The change in the tax structure resulted from the

Revenue collections — State Revenue Fund



imposition in July 1978 of a 4 per cent general sales tax levied at the retail level, the abolition of the sales duty levied at the manufacturing or import level, a lowering of the surcharge on imports, and reductions in the rates of income tax applicable to companies and individuals. The increase in income tax and mining lease payments by gold mining companies was due to higher profitability on account of a substantial rise in the price of gold.

The composition of revenue collections for the credit of the State Revenue Fund, which are used as an approximation of Exchequer receipts, reflected an increase in the relative importance of indirect taxes and a change in the relative importance of the various components of income tax receipts in 1978/79. Indirect tax collections, referred to in the accompanying table, amounted to 29 per cent of total revenue, as against 25 per cent in 1977/78. This change was in accordance with government policy to broaden the tax base by relying to a larger extent on indirect taxes as a source of revenue. It also represented a continuation of a trend that has been in evidence since 1974/75, when only 20 per cent of total revenue consisted of indirect taxes. If the portion of indirect taxes on petroleum products, which is channelled to the State Oil Fund and the National Road Fund and is not included in revenue available to the Treasury, is added to indirect tax collections, the ratio of indirect taxes to total tax receipts reached a level of 42 per cent in 1978/79, compared with 37 per cent in 1977/78.

Indirect tax collections in the form of customs and excise duties, the surcharge on imports, sales duties and proceeds of the general sales tax, rose by 40 per cent to an amount of R2 695 million in 1978/79, compared with an increase of 26 per cent in the preceding year. This high rate of increase was largely accounted for by general sales tax collections of R928 million which was substantially more than the loss of revenue resulting from the abolition of the sales duty. Collections of customs duties, which had declined in 1976/77 and had risen only slightly in 1977/78, increased appreciably in 1978/79 because of an increase in imports. The surcharge on imports, however, declined during the period under review as a result of the lowering of the rate from 15 to 12½ per cent in March 1978 and to 7½ per cent in March 1979.

The most important change in inland revenue collections in 1978/79 was the sharp increase in income tax and mining lease payments by gold mining companies referred to earlier. Receipts from gold mining companies almost doubled from R480 million in 1977/78 to R901 million in the year under review, causing the relative contribution of gold mining companies to total revenue collections to rise from 6 to 10 per cent during this period. The abolition of the surcharge on income tax payable by individuals and the lowering of the surcharge on income tax payable by companies in the 1978/79 Budget contributed to a relatively low rate of increase of 3 per cent in receipts of income tax from sources other than gold mining companies. It may be expected that this rate of increase will be affected even more when the tax concessions announced in the latest Budget become fully effective in the second half of 1979. The small increase in this part of income tax receipts resulted in a decline in its relative importance as a source of revenue from 51 per cent in 1977/78 to 43 per cent in 1978/79.

Revenue collections — State Revenue Fund

R millions

	Year ended 30 June			
	1976	1977	1978	1979
Customs, excise, sales duties and general sales tax[1]				
Customs duties	356	313	316	388
Surcharge	—	86	373	330
Excise duties	666	850	895	1 003
Sales duties	237	278	343	46
General sales tax	—	—	—	928
Total	1 259	1 527	1 927	2 695
Inland revenue				
Income tax (excluding payments by gold mines)	3 080	3 397	3 839	3 970
Payments by gold mines[2]	596	378	480	901
Other	1 060	1 186	1 329	1 643
Total	4 736	4 961	5 648	6 514
Total revenue collections[1]	**5 995**	**6 488**	**7 575**	**9 209**

1) Including amounts payable to neighbouring countries in terms of Customs Union agreements.
2) Comprising income tax and mining lease payments.

Exchequer Account deficit more than covered by domestic non-bank borrowing

The deficit on the Exchequer Account, excluding borrowing and debt redemption, amounted to R1 854 million in 1978/79, or R231 million less than in the preceding year. Although government borrowing from domestic non-banking sources was about R96 million lower than the corresponding figure in 1977/78, it exceeded the Exchequer deficit by a substantial margin and enabled the Treasury to reduce its net indebtedness to the monetary banking and foreign sectors.

Although borrowing from the private non-banking sector amounted to R1 127 million, or R511 million less than in 1977/78, it was sufficient to finance 61 per cent of the Exchequer Account deficit. The net investment of R349 million in marketable government securities by this sector was substantially smaller than the figure of R1 006 million during 1977/78. Net investments in non-marketable National Defence Bonds and Defence Bonus Bonds, however, increased from R96 million in 1977/78 to R370 million in 1978/79. Borrowing by means of tax-free Treasury bonds and compulsory loan levies amounted to R121 million and R280 million, respectively, or R67 million and R97 million, respectively, less than in the preceding year. The decline in the amount of loan levies was due to the early repayment of levies before their actual dates of maturity, largely with a view to stimulating private consumption expenditure and improving company liquidity.

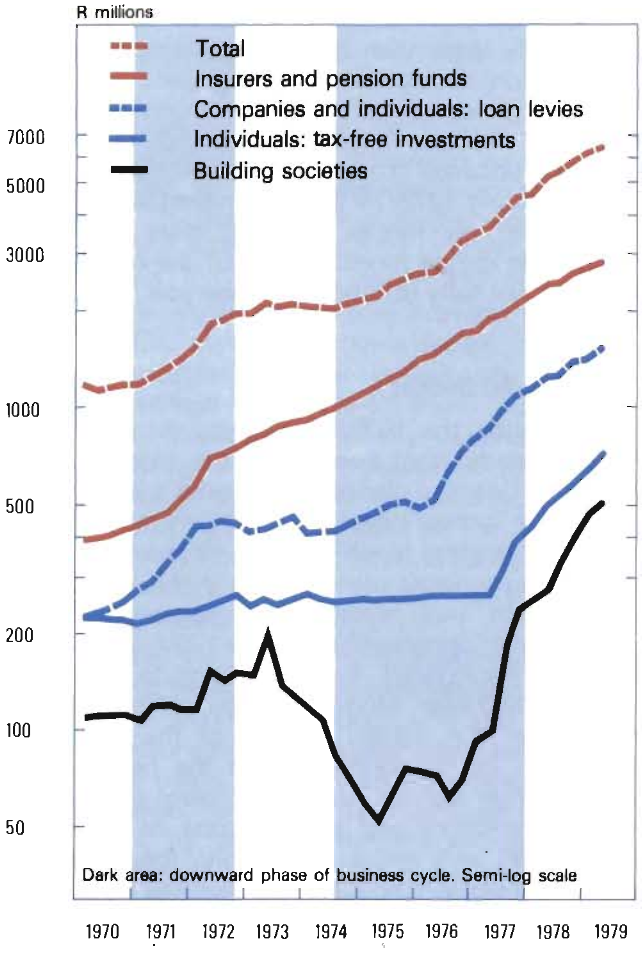
The largest contribution to Exchequer financing by investors in the private non-banking sector during 1978/79 was made by insurers and private pension funds. The relative importance of contributions by individuals and building societies, however, continued to increase during the year. Individuals invested mostly in tax-free securities, which provided an attractive investment outlet as a result of the inflationary rise in incomes during recent years and the higher tax rates that apply to the higher income levels. Building societies experienced a substantial net inflow of funds which could not be employed fully for the granting of mortgage loans, and had to divert part of these funds to prescribed investments, including government securities.

Exchequer Account financing
R millions

	Year ended 30 June 1977	1978	1979
Deficit (excluding borrowing and repayment of debt	1 851	2 085	1 854
Financed by:			
Domestic non-banking sources	1 163	2 319	2 223
Public Debt Commissioners[1]	295	681	1 096
Paymaster-General	-120	—	—
Private sector	988	1 638	1 127
Monetary banking sector	323	-44	-112
Foreign sector	365	-190	-257
Total financing	1 851	2 085	1 854

1) Including the Department of Posts and Telecommunications.

Investment in government securities by private non-banking sector



The other component of domestic non-bank borrowing, consisting of the net investment in government securities by the Public Debt Commissioners, rose substantially from R681 million in 1977/78 to R1 096 million in 1978/79. Funds placed with the Commissioners increased by R1 219 million during the year under review and were contributed mostly by the South African Railways Administration, public pension funds and public corporations. A part of these new funds was invested in other public sector securities. At the same time the Commissioners withdrew their investment with the National Finance Corporation, which had amounted to R270 million at the end of June 1978, and extended call loans to the discount houses amounting to R60 million at the end of June 1979.

Funds borrowed from the domestic non-bank sector in excess of the Exchequer Account deficit were used, for the second consecutive year, to reduce the Treasury's net indebtedness to the monetary banking and foreign sectors. The reduction of R112 million in net bank credit in 1978/79 was appreciably larger than the corresponding amount of R44 million during the preceding year. The Treasury's net indebtedness to the foreign sector declined by R257 million, largely because of repayments on loans obtained from the International Monetary Fund. During 1978/79 the government succeeded in negotiating new foreign loans at more favourable terms than during recent years, but the credit facilities were not fully utilised during the year.

The 1979/80 Budget

In presenting the 1979/80 Budget, the Minister of Finance stated that because of the success of the policy of financial discipline, the time had arrived to move into a new phase of the government's broad economic strategy in which more emphasis would be placed on economic growth. A higher rate of economic growth was necessary to generate adequate employment opportunities and a rising standard of living. Accelerated economic growth could be justified on such grounds as the continued large surplus on the current account of the balance of payments, the substantial rise in the net gold and other foreign reserves, adequate control over government expenditure and over the rate of increase in bank credit and the money supply, the absence of any undue pressure on resources resulting from excess demand, and the further improvement in South Africa's credit rating abroad. The Minister stressed, however, that such a policy of more vigorous growth should be combined with financial discipline. Budget measures were not aimed at stimulating growth by means of increased government expenditure, but rather at encouraging expansion in the private sector. To achieve this aim, tax concessions were granted to individuals and to companies. At the same time, as had been the case in the preceding year, the Budget contained elements of structural tax change, particularly with regard to the longer-term objective of distributing the tax burden more equally between direct and indirect taxes.

The tax concessions announced in the Budget included the lowering of the marginal rates of taxation on individuals, increases of income abatements, a decrease in the rate of diminution of these abatements, the abolition of the additional income tax surcharge of 2½ per cent applicable to gold and diamond mining companies, and the lowering of the surcharge on imports from 12½ per cent to 7½ per cent. In addition, the rate of the loan levy payable by companies was reduced from 15 to 10 per cent. The loss of revenue resulting from these tax concessions was estimated at R612 million, consisting of declines of R455 million and R157 million in direct and indirect taxes, respectively. The decline in loan levy receipts, including the effect of the lower rates of personal income tax, was estimated at R150 million.

Because of the tax concessions granted, receipts on the State Revenue Fund during the 1979/80 fiscal year were estimated to rise by only 4 per cent to R8 383 million. This anticipated rate of increase was considerably lower than that of 16 per cent in the preceding fiscal year. Taking into account proposed increases in expenditure on pension and other social benefits and on bread subsidies and aid to farmers, as well as a first payment for the purpose of extending the country's second oil-from-coal plant, total expenditure in the 1979/80 fiscal year was estimated at R11 190 million, representing an increase of 12 per cent in comparison with the preceding fiscal year.

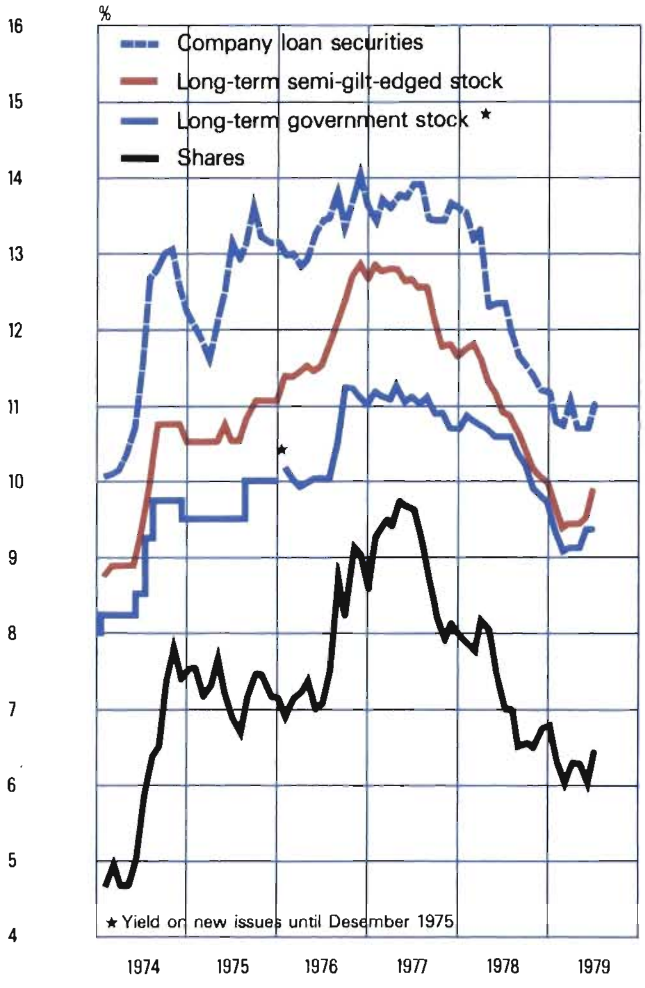
Expenditure was estimated to exceed revenue (excluding redemptions of government debt) by R2 807 million. Adding loan repayments of R1 112 million, the total financing requirement amounted to R3 919 million. The amount to be met from domestic borrowing was estimated at R3 462 million, of which R1 350 million represented an anticipated net investment in government securities by the Public Debt Commissioners. Foreign borrowing was estimated to amount to R200 million. The remaining R257 million was to be financed by the utilisation of available cash balances.

Capital market

Lower yields and larger trading in market for fixed-interest securities

Easy conditions continued to prevail in the market for fixed-interest securities during the larger part of the year under review. Only in the second quarter of 1979 did yields in this market tend to rise, while support for new issues weakened. The apparent tightening of the market towards the end of 1978/79 appeared to have been caused more by uncertainties regarding yield movements in the near future, an actual and expected higher rate of inflation, the pending large share issue by the new holding company of the South African Coal, Oil and Gas Corporation Ltd, and portfolio adjustments of institutional investors, than by the availability of loanable funds or the demand for new capital.

Secondary market security yields



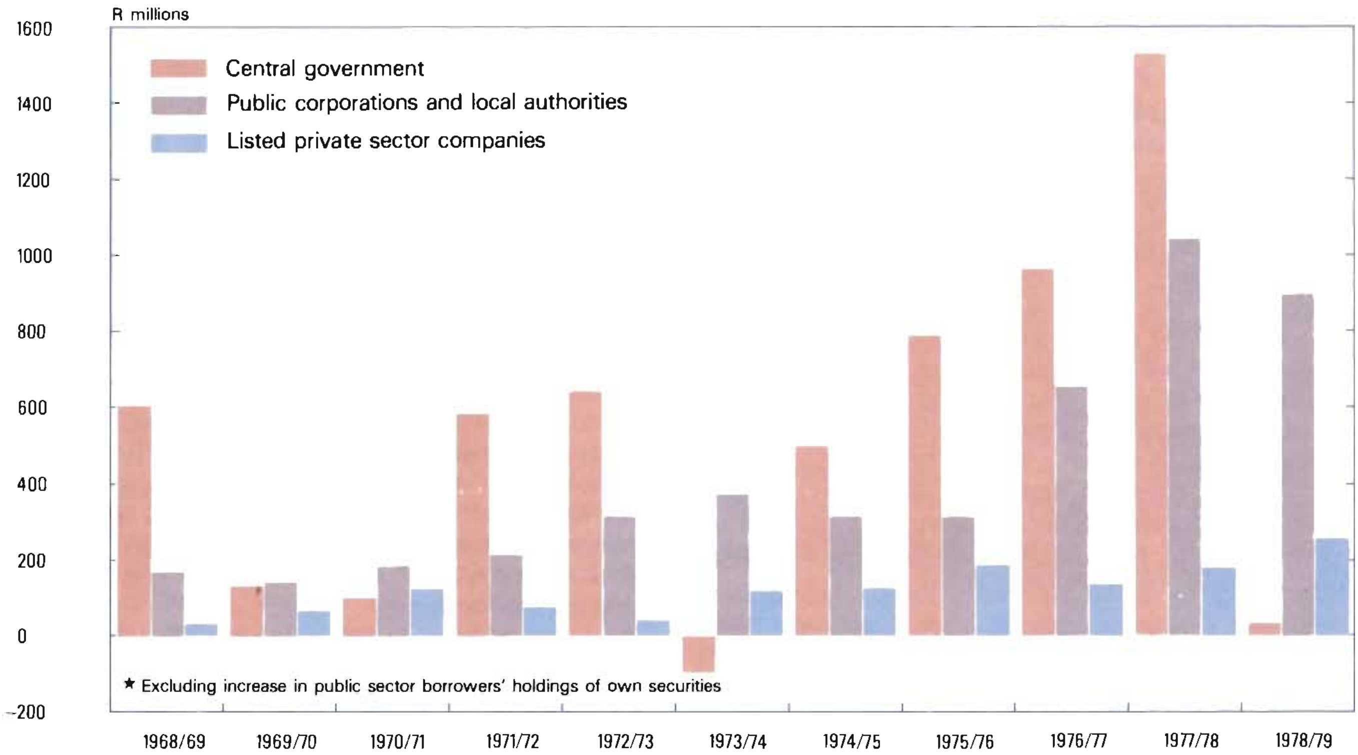
Portfolio adjustments by institutional investors were reflected in a dramatic increase in the trading of gilt-edged and semi-gilt-edged stock on the stock exchange. The nominal value of this stock traded rose from R89 million in 1976/77 to R259 million in 1977/78 and to as much as R1 417 million in 1978/79. It would appear that attempts to realise capital profits, stemming from a decline in interest rates, on substantial earlier investments in fixed-interest gilt-edged and semi-gilt-edged stock were beginning to force market prices down and to cause yields to rise in the second quarter of 1979. The rapid increase in the turnover of public sector stock was facilitated by an amendment to the Stock Exchanges Control Act in June 1978 in terms of which stockbrokers were permitted to trade in such stock for their own accounts.

The increased activity in the secondary market for gilt-edged and semi-gilt-edged stock was also reflected in substantial secondary market purchases and sales of public sector stock by such important institutional investors as banks, building societies, insurers and private pension funds. Gross purchases of public sector stock by these institutions increased from R2 275 million in the year that ended on 31 March 1978 to R4 660 million in the year to March 1979. Gross sales of stock by the institutions concerned increased by 147 per cent from R1 733 million to R4 272 million during the same period.

The changing market situation was reflected in movements of secondary market yields on fixed-interest securities. The yield on long-term government stock declined from 10,57 per cent in June 1978 to 9,11 per cent in March 1979, before rising to 9,35 per cent in May and remaining at this level during June. Long-term yields on the highest grade semi-gilt-edged stock decreased from 10,87 per cent to 9,43 per cent and increased to 9,89 per cent during the corresponding periods. Yields on long-term loan securities of companies declined from 12,34 per cent in June 1978 to 10,67 per cent in April 1979 and thereafter rose only slightly to 11,01 per cent in June.

The amount of new funds raised in the fixed-interest security market during 1978/79 was considerably less than in the preceding year. Net new issues of public sector stock, excluding the increase in the borrowers' holdings of their own stock, amounted to R910 million, as against R2 560 million in 1977/78. Issues by the central government, which had dominated the market in 1977/78, were insignificant during the year under review when issues by public corporations predominated. Private sector companies listed on the stock exchange raised an amount of R257 million, or R77 million more than in

Net issues of domestic marketable fixed-interest securities *



1977/78, in the fixed-interest security market. Two large issues accounted for the increase in the amount of new funds raised by companies during the period under review.

Continuation of upward trend in turnover and prices in share market

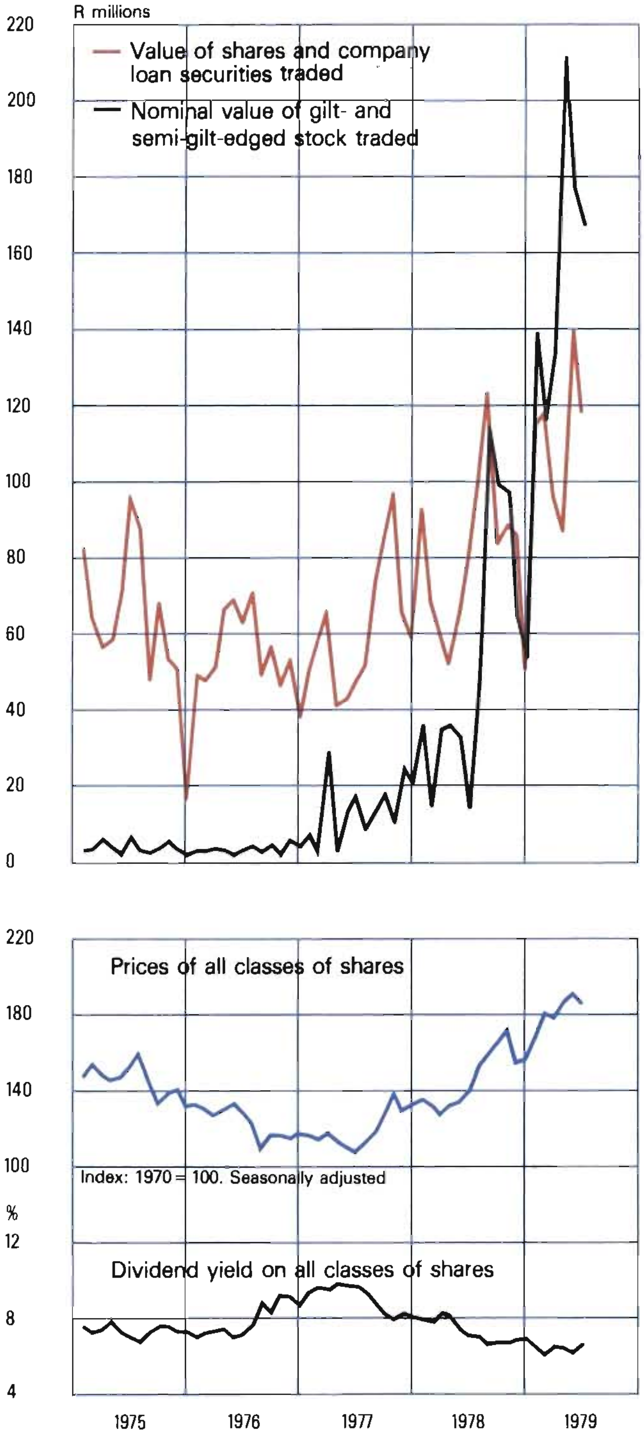
The strong upward trend in turnover and prices in the share market since the second half of 1977 continued during 1978/79, except for temporary interruptions towards the end of 1978 and again in March and in June 1979. The number and value of shares traded on the Johannesburg Stock Exchange increased by 27 per cent and 42 per cent, respectively. During this period the comprehensive share price index, covering all classes of shares, advanced by 32 per cent, compared with an increase of 30 per cent during 1977/78.

As indicated in the accompanying table, all classes of shares recorded appreciable price gains during the year under review. An increase of 41 per cent in mining share prices was followed by a rise of 29 per cent in financial share prices, whereas industrial and commercial share prices increased at a rate of 23 per cent. Of the individual classes of shares, coal mining share prices showed the largest increase, reflecting the effect of the rise in the price of oil and in the cost of energy generally. Gold mining share prices increased considerably as a result of the sharp rise in the price of gold, despite the dampening effect of sales of foreign-owned shares on the Johannesburg Stock Exchange for the purpose of creating financial rand. Gross sales by foreigners of securities listed on the Johannesburg Stock Exchange, for example, increased from R374 million in 1977/78 to R501

Percentage change in share prices

Year ended 30 June	Mining shares: Gold	Mining shares: Coal	Mining shares: Other metals & minerals	Financial shares: Mining	Financial shares: Industrial and general	Financial shares: Real estate	Financial shares: Banking and insurance	Industrial shares	Commercial shares	All classes of shares
1977	-26,6	26,2	1,1	-18,4	-12,5	-33,3	-14,5	-15,4	-18,7	-17,3
1978	43,3	13,6	35,1	31,0	22,0	6,8	47,5	20,5	20,7	30,0
1979	40,6	54,2	29,1	50,0	33,3	19,1	15,5	24,5	16,2	32,2

Stock exchange



million in 1978/79. Net sales of such securities by foreigners amounted to R11 million and R79 million in 1977/78 and 1978/79, respectively. Share prices were probably also affected by the strong rise in the turnover of listed gilt-edged and semi-gilt-edged stock, which overtook the value of shares traded during the year under review.

Financial rand is created when foreign-owned South African securities and other assets are sold by the foreign owners to South African residents. The proceeds of such sales are not freely transferable out of the country and may be held in the country as financial rand balances, or used to make authorised investments in South African assets, or sold to other foreigners. The utilisation of financial rand for the acquisition of assets other than listed securities is also subject to the requirement that the investment should represent a proprietor's interest. Financial rand balances or financial rand investments are sold to other foreigners at a discount, the so-called financial rand discount, which at present amounts to about 30 per cent. An often-used procedure in the creation of financial rand is for foreigners to buy South African shares listed on a foreign stock exchange, mostly the London Stock Exchange, and to sell these shares on the Johannesburg Stock Exchange to South African residents. The prices of South African shares on the London Stock Exchange, after providing for the United Kingdom investment currency premium, stand at a discount, which is at present equal to the financial rand discount, to prices on the Johannesburg Stock Exchange. Share transactions related to the creation of financial rand have recently tended to depress some share prices on the Johannesburg Stock Exchange.

Like other yields, the dividend yield on all classes of shares declined during 1978/79, namely from 7,0 per cent in June 1978 to 6,4 per cent in June 1979. The inverse yield gap between ordinary shares and long-term government stock narrowed from 3,6 to 2,9 per cent during the review period.

Because of the low level of real investment activity and the high level of corporate saving during 1978/79, new share capital raised by companies listed on the stock exchange amounted to only R25 million. This compares with an already low figure of R181 million in 1977/78.

In spite of a net outflow of funds, amounting to R20 million, the market value of the unit trusts' net assets increased by R70 million during 1978/79 to reach a level of R419 million at the end of June 1979. This increase reflected the rise in share prices during the review period. The average selling price of units increased by 28 per cent and the average yield on units declined from 6,5 per cent in June 1978 to 5,5 per cent in June 1979.

Substantial further increase in longer-term funds invested with deposit-receiving and related savings institutions

Longer-term funds invested with deposit-receiving and other savings institutions increased sharply by R3 000 million during 1978/79, after a substantial rise of R2 110 million had been recorded in 1977/78. This further increase was probably due, among other things, to an increase in domestic saving, changes in the relative levels of interest rates and in interest rate expectations, the lack of alternative financial and real investment outlets, and the shift among the various deposit liabilities of banking institutions referred to earlier.

In contrast with the preceding two years, the inflow of new funds to building societies exceeded the increase in savings and long-term deposits of banking institutions. The considerably larger inflow of funds to the societies included increased investment by companies, which reflected the high level of corporate saving and liquidity of the corporate sector. The lowering of interest rates and a discontinuation of issues of certain Treasury bonds, pending the introduction of new series, reduced the flow of funds to the Post Office Savings Bank and other government savings facilities. Participation mortgage bond schemes did not, on balance, accept new funds because of a lack of demand for mortgage loans.

The large inflow of funds resulted in a lowering of most deposit and related interest rates, namely by one per cent in October 1978 and generally by one-half per cent in February and again in April 1979. The rate on ordinary savings accounts, however, was not reduced in either February or April. Other rates which remained unchanged were the rate on the newly introduced transmission deposit accounts and the rate on Defence Bonus Bonds.

Changes in longer-term funds invested with deposit-receiving and related savings institutions

	Year ended 30 June 1978		1979	
	R mill.	%	R mill.	%
Banking institutions	1 015	48,1	1 280	42,7
Building societies	661	31,3	1 376	45,9
Participation mortgage bond schemes	4	0,2	-23	-0,8
Post Office Savings Bank and National Savings Certificates	202	9,6	159	5,3
Other government savings facilities	228	10,8	208	6,9
Total	2 110	100,0	3 000	100,0

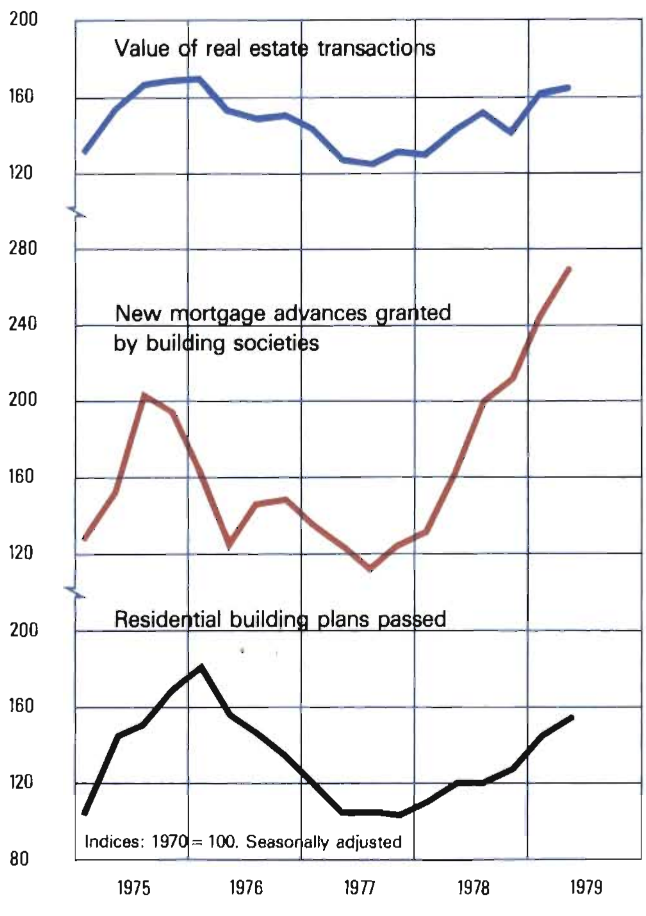
Transmission accounts were introduced in order to make a distinction between, on the one hand, "genuine savings accounts" which carry higher average balances and are subject to infrequent or limited withdrawals and, on the other hand, convenience salary or wage accounts which carry small average balances and are subject to frequent and regular monthly withdrawals. In view of the higher rate of turnover of funds in the convenience or transmission accounts, they are subject to higher liquid asset requirements than other savings accounts.

Slight recovery in mortgage and real estate markets

Activity in the residential mortgage market recovered slightly during 1978/79. The value of residential building plans passed increased from a monthly average of R50 million in the first half of 1978 to R54 million in the second half and R63 million in the first five months of 1979. In addition, building societies' mortgage loans outstanding rose by R705 million, or 11 per cent, during 1978/79, compared with R423 million, or 7 per cent, during the preceding year. Also indicating an accelerated rate of mortgage lending by building societies, the monthly average of gross mortgage loans granted increased from R161 million during the second half of 1978 to R200 million during the first half of 1979.

The availability of funds for mortgage lending nevertheless continued to exceed the demand for mortgage loans and the building societies had to increase their holdings of prescribed investments, consisting mostly of cash, deposits and public sector securities. These holdings rose by R692 million during 1978/79 and excess holdings over and above the legally required minimum amounted to R754 million, or 8,6 per cent of liabilities to the public, at the end of June 1979.

Fixed property market



Reductions in borrowing rates enabled the societies to reduce their home mortgage rates in October 1978 from a range of 10,5–12,0 per cent to a range of 10,0–12,0 per cent. In April 1979 the range was lowered to 9,5–11,5 per cent. Participation mortgage bond schemes also lowered their mortgage rates on new bonds, namely from 11,35 to 10,80 per cent in October, to 10,25 per cent in March, and 9,70 per cent in May. These reductions, however, had virtually no effect on the sluggish demand for participation bond finance.

A more distinct upward trend in the value of real estate transactions became evident during 1978/79. The value of transactions, which had declined by 8 per cent in 1977/78, increased by 16 per cent in the year under review.