2

Economic overview

In brief

- Gross domestic product growth of 1 per cent is expected for 2017, up from 0.7 per cent projected in October 2017. Growth is forecast to reach 2.1 per cent by 2020.
- The economy has benefited from strong growth in agriculture, higher commodity prices and, in recent months, improving investor sentiment.
- The global economic recovery provides a supportive environment for South Africa to expand trade and investment, but domestic constraints that have reduced business confidence stand in the way of accelerated growth.
- In 2017, gross fixed-capital formation continued to decline and unemployment reached the highest level recorded since 2003. To boost capital expenditure and job creation, the upturn in confidence will have to be sustained.
- Government will implement structural reforms to promote investment by reducing policy uncertainty, and act decisively to strengthen governance and sound financial practices at state-owned companies.

Overview

South Africa's economic outlook has improved, with GDP growth of 2.1 per cent projected in 2020

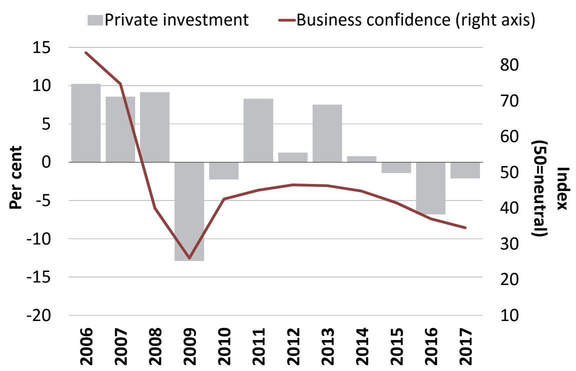
South Africa's economic growth outlook has improved in recent months, following a year marked by recession and policy uncertainty. GDP growth of 1 per cent is expected for 2017, up from 0.7 per cent projected in the 2017 *Medium Term Budget Policy Statement* (MTBPS), and is forecast to reach 2.1 per cent by 2020. The improved outlook flows from strong growth in agriculture, higher commodity prices and an incipient recovery in investor sentiment.

Although global risk factors remain elevated, the world economy continues to provide a supportive platform for South Africa to expand trade and investment. World economic growth is at its highest level since 2014 and continues to gather pace. GDP growth is rising across all major economies. The International Monetary Fund (IMF) forecasts global growth of 3.7 per cent in 2017 and 3.9 per cent in 2018.

South Africa has underperformed relative to peer countries

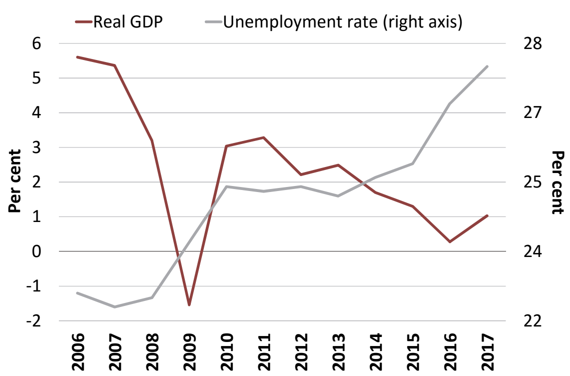
To create large numbers of jobs, build an inclusive and transformed economy and reduce inequality, South Africa needs a strong, sustained expansion. Yet in contrast to many of its developing-country peers, South Africa has experienced a period of protracted economic weakness, mainly as a result of domestic constraints. This is reflected in low levels of private investment, persistently high and rising unemployment, and declining real per capita income. These factors in turn have undermined the sustainability of the public finances and narrowed the scope for economic transformation.

Figure 2.1 Investment and business confidence



Source: Statistics South Africa and Bureau for Economic Research

Figure 2.2 GDP and unemployment



Source: Statistics South Africa

Structural reform, confidence, investment and jobs

Confidence and investment are mutually reinforcing. When businesses are confident about their growth prospects and certain about the policy environment, they invest and hire staff. In South Africa, private investment has been contracting since 2015, mainly as a result of low levels of business and consumer confidence. Growth has remained stuck below 2 per cent and unemployment remains high at 26.7 per cent. The National Development Plan (NDP) outlines the structural reforms required to boost investment, expand employment and remove constraints to economic growth.

Improved investor sentiment has led to stronger rand exchange rate and lower government borrowing costs

The 2018 Budget is introduced as government has an opportunity to reinforce confidence and contribute to a recovery in growth and investment. A renewed sense of optimism is driven by the expectation that government will finalise many outstanding policy reforms, act decisively against corruption, and swiftly resolve governance and operational failures at state-owned companies. Investor sentiment has improved, leading to a strengthening rand exchange rate and lower government borrowing costs.

South Africa's stable macroeconomic environment provides a strong platform to attract much-needed foreign savings that can fund additional investment. The country's prudent macroeconomic policies are highly regarded by international investors, as are its well-developed and well-regulated financial markets. Government remains committed to fiscal discipline, a flexible exchange rate and inflation targeting.

While macroeconomic policies provide a stable environment for growth, attracting higher levels of investment that create jobs requires government to finalise outstanding policy reforms.

Rejuvenating private investment will require policy reforms

Global outlook

The world economy continues to strengthen following a period of protracted weakness that began with the 2008 financial crisis. Global trade volumes are expected to grow by 4.7 per cent in 2017 – the highest growth rate since 2011. In developed economies, monetary policy remains broadly supportive of growth. The outlook for the euro area has strengthened, with improved growth outcomes for Germany, Italy and the Netherlands reflecting stronger domestic demand. Tax reforms, fiscal stimulus and higher external demand have bolstered the US economic outlook. The growth forecast for Japan has been revised up for 2018 and 2019, Chinese growth is expected to moderate to 6.4 per cent in 2019 and growth in India is expected to reach 7.8 per cent in 2019.

Table 2.1 Economic growth in selected countries

Region/country	2000-2008	2010-2016	2017	2018	2019
Percentage	Pre-crisis	Post-crisis	Average GDP forecast		
World	**4.3**	**3.8**	**3.7**	**3.9**	**3.9**
Advanced economies	**2.4**	**1.9**	**2.3**	**2.3**	**2.2**
United States	2.3	2.1	2.3	2.7	2.5
Euro area	2.0	1.1	2.4	2.2	2.0
United Kingdom	2.5	2.0	1.7	1.5	1.5
Japan	1.2	1.4	1.8	1.2	0.9
Developing countries	**6.5**	**5.4**	**4.7**	**4.9**	**5.0**
Brazil	3.8	1.4	1.1	1.9	2.1
Russia	7.0	1.8	1.8	1.7	1.5
India	6.8	7.3	6.7	7.4	7.8
Chile	4.8	3.9	1.4	2.5	2.7
Mexico	2.6	3.1	2.0	2.3	3.0
Indonesia	5.3	5.6	5.2	5.3	5.5
China	10.4	8.1	6.8	6.6	6.4
Sub-Saharan Africa	**5.9**	**4.5**	**2.7**	**3.3**	**3.5**
South Africa[1]	4.2	2.0	1.0	1.5	1.8

1. National Treasury forecast
Source: IMF World Economic Outlook, October 2017 and IMF World Economic Outlook Update, January 2018

Economic growth in developing economies is supported by external demand and a recovery in commodity prices. Growth in sub-Saharan Africa is projected to remain moderate at 2.7 per cent in 2017, increasing to 3.3 per cent and 3.5 per cent in 2018 and 2019 respectively. Continued slow growth in the region's two largest economies – Nigeria and South Africa – weighs on the outlook.

Risks to the global forecast include unsustainable asset prices and elevated indebtedness, particularly in China. As monetary policy in developed countries retreats from the exceptional measures adopted in the wake of the financial crisis, global financial conditions will tighten. Capital flows to developing countries may decrease as a result. The threat of rising protectionism could result in trade barriers that constrain

Risks to global forecast include unsustainable asset prices and elevated indebtedness exports, production and growth, while raising political and military tensions.

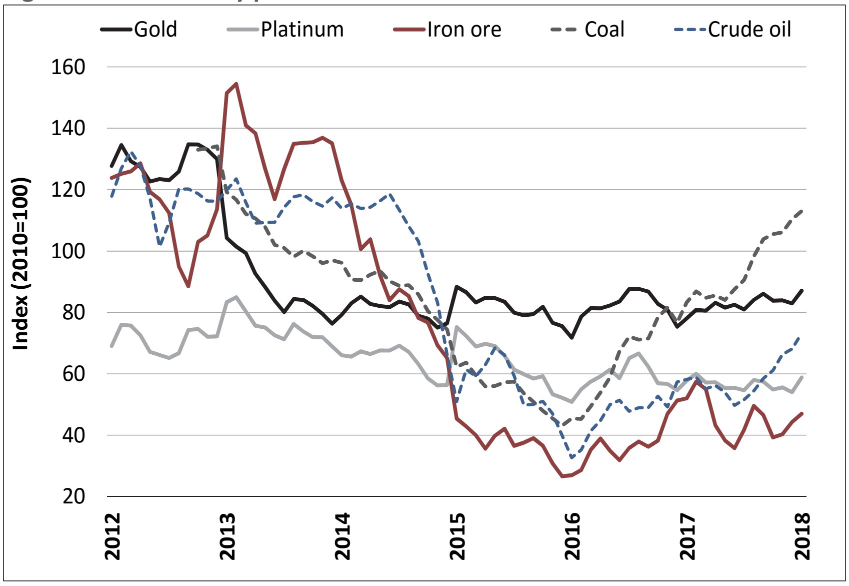
Commodity prices

Prices for crude oil, coal and iron ore have risen strongly over past year

Commodity prices have rebounded over the past year. In response to increased global demand and declining inventories, crude oil prices have risen appreciably, from US$47/barrel at the end of June 2017 to US$64/barrel at the end of 2017.

Non-oil commodity prices have recovered from the low reached at the end of 2015. Responding to higher demand from China and India, coal prices rose 45.1 per cent in 2017 compared with the previous year, reaching US$95/ton at the end of December 2017. Iron ore prices rose 20.4 per cent, from US$58/ton in 2016 to US$71/ton, also supported by stronger demand from Asia. Precious metals prices were mixed in 2017 compared with the prior year: platinum prices declined 3.8 per cent, while gold remained stable. These trends have resulted in an improved near-term outlook for commodity exporters such as South Africa.

Figure 2.3 Commodity prices*



**The coal index is only available from October 2012*
Source: Bloomberg and National Treasury calculations

Domestic outlook

GDP growth is expected at 1.5 per cent in 2018 and at 1.8 per cent in 2019

The South African economy is forecast to grow by 1.5 per cent in 2018 and by 1.8 per cent in 2019. On average, the growth outlook is 0.4 percentage points higher than projected in October 2017, mainly due to an expected increase in private investment as a result of improved business and consumer confidence.

Table 2.2 Macroeconomic performance and projections

	2014	2015	2016	2017	2018	2019	2020
Percentage change		**Actual**		**Estimate**		**Forecast**	
Final household consumption	0.7	1.7	0.8	1.3	1.7	1.9	2.3
Final government consumption	1.1	0.5	2.0	0.0	-0.3	1.2	1.4
Gross fixed-capital formation	1.7	2.3	-3.9	0.3	1.9	3.3	3.7
Gross domestic expenditure	0.6	1.8	-0.8	1.3	1.7	2.2	2.4
Exports	3.2	3.9	-0.1	1.5	3.8	3.4	3.5
Imports	-0.5	5.4	-3.7	2.7	4.4	4.6	4.5
Real GDP growth	**1.7**	**1.3**	**0.3**	**1.0**	**1.5**	**1.8**	**2.1**
GDP inflation	5.8	5.0	7.0	4.9	5.7	5.3	5.5
GDP at current prices (R billion)	**3 807.7**	**4 049.8**	**4 345.8**	**4 604.4**	**4 940.8**	**5 298.3**	**5 704.6**
CPI inflation	6.1	4.6	6.3	5.3	5.3	5.4	5.5
Current account balance (% of GDP)	-5.3	-4.4	-3.3	-2.2	-2.3	-2.7	-3.2

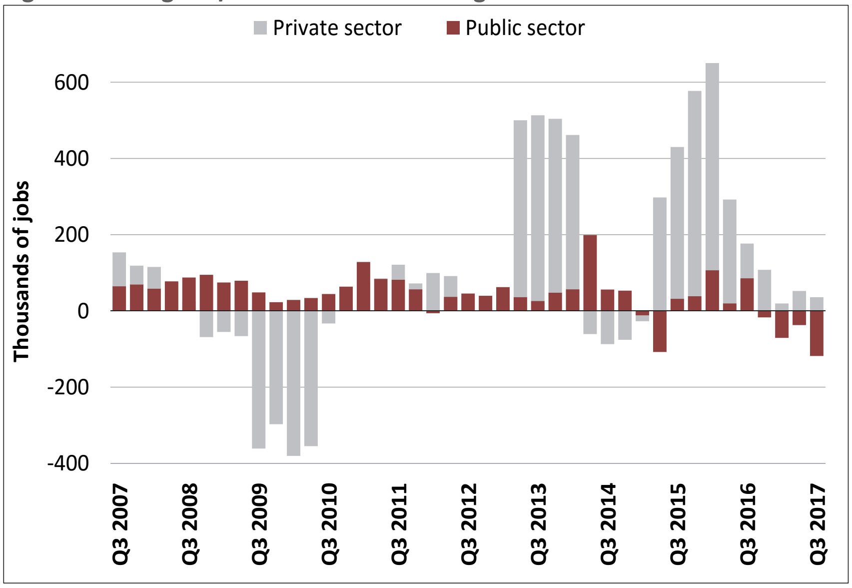
Source: National Treasury and Reserve Bank

Employment

South Africa's unemployment rate reached 27.7 per cent in the third quarter of 2017 – the highest rate since September 2003. Average formal non-agricultural employment declined by 0.4 per cent in the first three quarters of 2017 compared with the same period in 2016. Average employment in the public service, which accounts for about 21 per cent of total formal non-agricultural employment, contracted by 3.6 per cent in the first three quarters of 2017.

Unemployment rate reached 14-year high of 27.7 per cent during 2017

Figure 2.4 Job gains/losses in formal non-agricultural sector*



**Changes in employment relative to same period in prior year*
Source: Statistics South Africa

Private-sector job creation remains the only sustainable way to reduce unemployment. Labour relations have improved, but employment outcomes depend on a prolonged rise in confidence and investment. Since 2015, the private sector's contribution to job creation has fallen. Financial and business services, which account for the largest number of private-sector jobs, contracted by 0.3 per cent in the first three quarters of 2017. Over the same period, construction, which employs 7.9 per cent of private-sector employees, shrank by 1.4 per cent.

Household consumption

Spending on services grew by 2.3 per cent, but spending on durable goods declined by 0.3 per cent

Household consumption expenditure grew by 1.4 per cent in the first three quarters of 2017 compared with 0.7 per cent over the same period in 2016. Spending on services, such as education, grew by 2.3 per cent. Despite strong growth in the third quarter, durable goods expenditure declined by 0.3 per cent in the first nine months of 2017, compared with a larger contraction of 7.8 per cent over the same period in 2016.

Since peaking at 87.8 per cent in the first quarter of 2008, household debt as a percentage of household disposable income has continued to decline, reaching 72.5 per cent in the third quarter of 2017. Household consumption is projected to grow by 1.3 per cent in 2017, reaching 2.3 per cent in 2020 as employment growth accelerates, confidence improves and more favourable credit conditions boost purchasing power.

Investment

Private investment declining since 2015

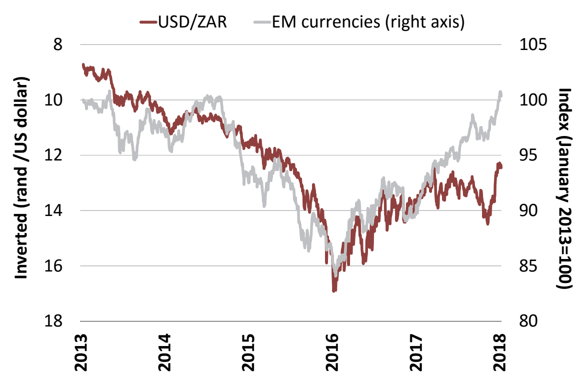
Real gross fixed-capital formation fell by 0.2 per cent during the first three quarters of 2017. Private investment, which accounts for about 60 per cent of total investment and has been declining since 2015, contracted by 2.1 per cent. Investment by public corporations contracted by 1.7 per cent during the first three quarters of 2017. Investment growth is expected to recover moderately, from 1.9 per cent in 2018 to 3.3 per cent in 2019. The ratio of investment to GDP was 19.5 per cent in 2016, well below the NDP target of 30 per cent of GDP by 2030. Boosting gross fixed-capital formation is critical to raise the economy's potential growth rate.

Exchange rate

Strengthening currency reflects investor reaction to political developments

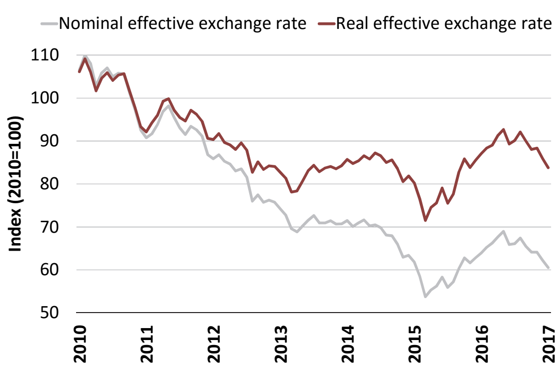
The rand strengthened by 10.6 per cent against the US dollar during 2017, reaching R12.38/US$ at year-end – a level last seen in June 2015. The currency's recent performance reflects investors' reaction to domestic political developments, as well as overall strength in developing-country currencies. These currencies benefited from US dollar weakness, the search for higher yields by international investors and rising global commodity prices.

Figure 2.5 Emerging-market currency performance



Source: Bloomberg

Figure 2.6 Effective exchange rate movements



Source: Reserve Bank

The real effective exchange rate depreciated by 5.9 per cent between January and November 2017. This indicates an improvement in South Africa's international competitiveness. Low inflation can help sustain these competitiveness gains.

Balance of payments

Current account deficit narrowed to 2.3 per cent of GDP in first three quarters of 2017

The current account deficit narrowed to 2.3 per cent of GDP during the first three quarters of 2017, from 3.8 per cent over the same period in 2016. This is largely due to a higher trade surplus, as South Africa's terms of trade – the ratio of export prices to import prices – improved in the first three quarters of 2017 relative to the same period in 2016. The deficit in 2017 is expected to average 2.2 per cent of GDP – the smallest since 2010. Since 2013, the current account deficit has steadily declined, largely as a result of slower import growth. As import growth accelerates and some terms of trade gains are reversed, the deficit is expected to widen to 3.2 per cent of GDP in 2020 in line with higher economic growth.

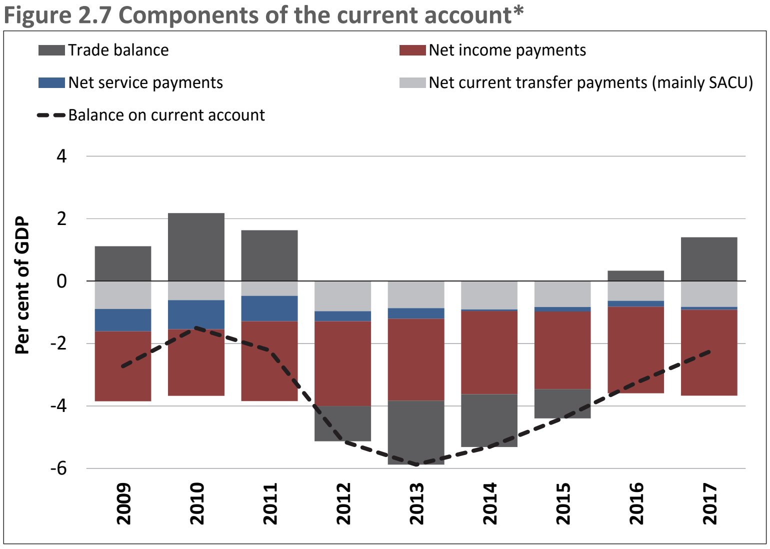
The value of total exports increased by 4.8 per cent in the first three quarters of 2017, while the value of total imports fell by 1.2 per cent. Certain agricultural exports have shown encouraging growth in recent years, particularly in new markets. The value of citrus exports to China, for example, increased by 59.2 per cent in 2017 compared with the prior year. Over the same period, the value of citrus exports to Asia as a whole grew 14.1 per cent, while exports to Europe increased 6.1 per cent.

In contrast, the value of manufacturing exports declined by 3.9 per cent in the first three quarters of 2017 compared with the corresponding period in 2016. Exports of vehicles, machinery, and food and beverages contracted.

Low domestic savings rate makes South Africa reliant on foreign inflows to fund investment

South Africa relies on foreign inflows to fund investment because of a low domestic savings rate, as shown by a persistent current account deficit. South Africa received capital inflows equivalent to 1.7 per cent of GDP in the first three quarters of 2017, compared with 4.9 per cent in 2016.

Figure 2.7 Components of the current account*



**Up to September 2017*
Source: Reserve Bank

In the first three quarters of 2017, net foreign direct investment outflows increased to R65.2 billion, compared with net outflows of R3.3 billion over the same period in 2016. This was driven by a large acquisition of foreign financial assets. Lower foreign direct investment increases the country's reliance on more volatile portfolio flows, which remained strong through 2017.

Inflation

Headline inflation declined to 5.3 per cent in 2017 from 6.3 per cent in 2016. Lower inflation is due to lower food and non-alcoholic beverage prices, which moderated from 10.5 per cent to 6.9 per cent, mainly as a result of the strong recovery in agriculture. Core inflation, which excludes price-volatile items such as food, fuel and electricity, declined to 4.7 per cent in 2017 from 5.6 per cent in 2016.

Headline inflation projected to remain at 5.3 per cent in 2018, partly due to tax increases

For 2018, headline inflation is projected at 5.3 per cent, which includes 0.6 percentage points added by tax proposals. Electricity inflation, which fell from 9.2 per cent in 2016 to 4.7 per cent in 2017, is expected to stabilise at about 3.7 per cent in 2018 following the regulator's approval of a 5.2 per cent Eskom tariff increase. The medium-term forecast assumes that electricity price inflation will not exceed 8 per cent.

The main risks to the inflation outlook remain a weaker-than-expected exchange rate, higher global oil prices and higher average wage growth.

Economic assumptions

The macroeconomic forecast is underpinned by a set of assumptions published in Table 2.3. The main revisions to the assumptions since the 2017 MTBPS forecast include upward revisions to global demand, higher commodity prices and a lower risk premium. Electricity inflation has been revised down following the recent tariff decision. Nominal government consumption and investment have been revised down to reflect expenditure cuts.

Table 2.3 Assumptions used in the economic forecast

	2015	2016	2017	2018	2019	2020
Percentage change	**Actual**		**Estimate**	**Forecast**		
Global demand[1]	4.2	4.1	4.4	4.4	4.3	4.3
International commodity prices[2]						
Brent crude oil (US$ per barrel)	52.7	44.2	54.8	66.5	63.2	60.4
Gold (US$ per ounce)	1 160.4	1 247.9	1 257.9	1 338.5	1 369.1	1 399.6
Platinum (US$ per ounce)	1 055.4	988.3	950.1	976.4	997.9	1 019.9
Coal (US$ per ton)	57.1	64.4	86.2	93.1	88.1	84.2
Iron ore (US$ per ton)	56.1	58.6	71.3	68.5	62.9	59.3
Food inflation	5.1	10.5	7.0	5.0	5.9	6.0
Electricity inflation	9.2	9.2	4.7	3.7	6.6	8.0
Sovereign risk premium (basis point)	2.9	3.4	2.7	2.7	2.4	2.3
Real public corporation investment	6.0	0.7	-0.3	1.5	3.1	4.5
Real private residential investment	8.4	-1.8	-0.8	-2.0	0.9	4.4

1. Combined growth index of South Africa's top 15 trading partners (IMF World Economic Outlook, October 2017 and IMF World Economic Outlook Update, January 2018)
2. Bloomberg futures prices as at 25 January 2018
Source: National Treasury

The current water crisis in the Western Cape will affect economic growth, although its impact is uncertain. Much depends on its duration, the extent to which specific catchment areas are affected and the success of mitigation measures.

Risks to the outlook

Although the growth forecast has improved relative to the 2017 MTBPS, there are major risks to the outlook. A sustained GDP recovery depends on extending the current upturn in business confidence. Continued policy and political uncertainty, and further deterioration in the finances of state-owned companies, remain the largest risks to the economic outlook. Other risks include:

- A further downgrade of South Africa's local-currency debt, resulting in the country's exclusion from the Citi World Government Bond Index. This would result in higher risk premiums and trigger some capital outflows, leading to an increase in borrowing costs, exchange rate depreciation and further deterioration in economic activity.
- A weaker-than-expected rand exchange rate or higher administrative price inflation (for example, water or electricity price increases). Higher overall inflation would reduce South Africa's competitiveness and negatively affect trade, and decrease the purchasing power of domestic consumers and businesses.
- A severe contraction in the Western Cape economy due to the water crisis, which would threaten employment in agriculture and tourism. Calculations by the National Treasury show that every 1 per cent contraction in the economy of the Western Cape subtracts 0.2 percentage points from overall growth.

Alternative scenarios

The National Treasury has modelled three alternative scenarios quantifying some of the risks to the baseline economic forecast.

In the first scenario, Moody's downgrades local-currency debt further. The risk premium – a measure of the extra return required by global buyers of South African bonds – increases by 100 basis points, or one percentage point, before returning to the baseline average in 2020. The impact on growth is largely reflected through higher borrowing costs, and lower investment and consumption. Growth slows to 0.7 per cent in 2018, 1.3 per cent in 2019 and 2 per cent in 2020.

In the second scenario, risks in the state-owned company sector materialise, prompting a fiscal crisis and a local-currency downgrade. The cost of borrowing increases by an average of 2.4 percentage points over the medium term. GDP growth contracts by 3.1 per cent and 0.3 per cent in 2018 and 2019, respectively, before recovering to 1.1 per cent by 2020.

The third scenario assumes that the increase in business confidence evident at the beginning of 2018 is maintained, global growth improves by an annual average of 0.5 percentage points, the risk premium is on average 50 basis points lower and bond yields decline by an average of 70 basis points. GDP growth accelerates to 2.1 per cent in 2018, 2.9 per cent in 2019 and 3.2 per cent by 2020, as higher income growth promotes stronger consumption and investment demand. Robust structural reforms, including changes to the business models of state-owned companies, bolster confidence and investment.

Sector performance

South Africa's muted economic performance over the past year was reflected across all major sectors, apart from agriculture and mining.

Agriculture

Agriculture grew strongly as production recovered from drought in summer rainfall regions

Real value added in the agriculture, forestry and fishing sector grew by 21.9 per cent in the first three quarters of 2017 compared with the same period in 2016, contributing 0.5 percentage points to overall GDP growth. Good summer rainfall led to a broad-based recovery in production following a severe drought, which caused agriculture to contract in 2015 and 2016. Maize production is expected to reach 16.7 million tons in 2017 – a 115.3 per cent increase from the 2016 crop. Soybean production is expected to increase by 77.4 per cent to 1.3 million tons.

Growth is expected to continue at a more moderate pace in 2018. Ongoing drought in the Western Cape – which contributes about 22 per cent of agricultural value-added and is a key producer of wheat, horticultural products and wine – will restrict growth in 2018.

Table 2.4 Sector growth trends

	2015	2016	2017			
Percentage change[1]			**Q1**	**Q2**	**Q3**	**Year[2]**
Agriculture, forestry and fishing	-6.1	-7.8	23.1	38.7	44.2	21.9
Mining and quarrying	3.9	-4.7	13.1	8.2	6.6	4.3
Manufacturing	-0.2	0.7	-3.7	1.5	4.3	-1.2
Electricity, gas and water	-1.5	-3.5	-4.8	8.8	-5.5	-0.6
Construction	1.7	0.7	-0.8	-0.3	-1.1	0.4
Trade, catering and accommodation	1.4	1.2	-5.9	0.6	-0.4	-1.0
Transport, storage and communication	1.1	0.4	-1.6	2.2	0.6	1.2
Finance, real estate and business services	2.8	1.9	-1.2	2.5	1.2	1.0
General government services	0.8	1.4	-0.7	-1.1	-0.7	0.1
Personal services	1.1	1.2	-0.1	1.3	0.9	1.1
GDP	**1.3**	**0.3**	**-0.6**	**2.8**	**2.0**	**1.0**

1. Quarterly numbers are seasonally adjusted and annualised
2. Up to September 2017
Source: Statistics South Africa

Mining

In the first three quarters of 2017, real value added in the mining sector grew by 4.3 per cent. Over this period, the sector contributed 0.3 percentage points to overall GDP growth. After a contraction in 2016, mining output is recovering, supported by higher commodity prices. Improved demand has boosted iron ore, manganese and chromium production.

Mineral sales increased by 9.4 per cent in the first nine months of 2017 compared with the same period in 2016, driven largely by coal and iron ore. Gold and platinum sales fell by 11.6 per cent and 3.4 per cent respectively over the same period, weighed down in part by a strong US dollar.

Policy uncertainty hinders investment in the mining sector

Despite improved performance in 2017, mining remains under pressure due to high operating costs and persistent policy uncertainty related to the Mining Charter and the Mineral and Petroleum Resources Development Amendment Bill.

The amendment bill was sent back to Parliament in January 2015 and its status has not been resolved. The Mining Charter, approved by Cabinet and gazetted in June 2017, has contributed to policy uncertainty. Both the charter and the outstanding amendment bill leave mining, oil and gas companies unable to accurately assess the expected return on their investments. According to the Fraser Institute's Mining Investment Attractiveness Index, South Africa ranked 74th out of 104 jurisdictions in 2016. The country is currently ranked 13th in Africa. Botswana, Ghana, Namibia, Tanzania and Uganda have more favourable mining policy environments than South Africa.

Real fixed investment in mining has been stagnant since 2008. As a result, growth in the volume of production of South Africa's key commodities, including iron ore, coal, gold and platinum, has underperformed compared to countries such as Chile, China, Canada, Australia and Russia.

Manufacturing

Real value added in manufacturing declined by 1.2 per cent during the first three quarters of 2017, reducing GDP growth by 0.2 percentage points. Poor performance was the result of weak domestic demand and low levels of business confidence. Production decreased by 1.4 per cent over the first three quarters of 2017. This was true across most subsectors, apart from food and beverages, and metals, which respectively grew by 0.8 per cent and 4 per cent over the year.

Electricity

Weak demand and independent power producer contributions enabled Eskom to ensure supply

Electricity sector output declined by 0.6 per cent in the first three quarters of 2017 compared with the same period in 2016. Low levels of demand, alongside contributions from independent power producers, have enabled Eskom to ensure continued supply. Two Eskom power station units – Medupi's unit 4 and Kusile's unit 1 – were brought into commercial operation in 2017, adding 794MW and 800MW respectively to the national grid.

Transport and telecommunications

Performance of the transport, telecommunications and storage sector remained flat over the year, growing by 1.2 per cent in the first three quarters of 2017 compared with the same period in 2016. The sector contributed 0.1 per cent to GDP growth. Declining external trade, low consumer demand and a decrease in manufacturing underpinned the subdued performance.

Construction

Poor performance of construction sector has serious implications for job creation

Growth in real value added in construction moderated to 0.4 per cent in the first three quarters of 2017. Civil construction investment growth slowed to 1.9 per cent. The FNB/BER Civil Confidence Index registered its lowest result in 17 years during the third quarter of 2017. Given that the construction sector has a high employment multiplier, its poor performance has serious implications for job creation.

Finance, insurance, real estate and business services

Growth in real value added by the finance, insurance, real estate and business services sector moderated to 1 per cent in the first three quarters of 2017 compared with the same period in 2016. The sector's contribution to growth decreased to 0.2 percentage points.

Growth in banking sector assets averaged 2.4 per cent in the first nine months of 2017 from an average of 9.8 per cent in the same period of 2016. Over the same period, growth in loans declined from an average of 8.8 per cent to 2.6 per cent. Despite the tough economic conditions and an evolving regulatory environment, the banking sector remains profitable and well capitalised. Impaired advances as a percentage of outstanding loans were 2.8 per cent in November 2017, a marked improvement from a high of 5.9 per cent in 2010.

Investment and transformation for inclusive growth

NDP's structural reforms focus on boosting employment, improving education and building state capability

Government's economic policy is focused on inclusive growth. The benefits of a growing economy should be shared more widely and more equitably through transformation and job creation. Government, the private sector and organised labour all play a part in creating decent and sustainable employment, supporting transformation and boosting productivity. In outlining a range of structural reforms needed to raise long-term economic growth, the NDP identifies three priorities:

- Raising employment through faster economic growth
- Improving the quality of education, skills development and innovation
- Building the capability of the state.

Progress in these areas requires a long-term coordinated effort, complemented by a number of steps being taken over the medium term.

Eliminating policy uncertainty to catalyse investment

Immediate measures are needed to establish policy certainty in key areas to rebuild trust and create an enabling environment for investment.

- In telecommunications, government will end the delay in licensing spectrum, which limits access to stable, affordable information and communications technology.
- Bottlenecks in finalising the Mineral and Petroleum Resources Development Act and the Mining Charter will be addressed to improve the attractiveness of the mining sector for investment.
- The Interim Rail Regulator is an important first step in building regulatory capacity. Government is finalising the Single Transport Economic Regulator Bill, which will improve efficiency in the transport sector.

Government's approval of six special economic zones to benefit from lower corporate tax rates for qualifying firms, and employment tax incentives for all workers, will encourage investment and help overcome inefficient spatial legacies in production. Recent amendments to the venture capital company tax incentive have resulted in investment of R650 million in qualifying small businesses – increasing the pool of funding available to support enterprise development.

Financial and governance reform at state-owned companies

Government is acting decisively to address financial and governance concerns at state-owned companies

State-owned companies operate network industries, such as electricity and transport, that underpin the country's economic growth potential. Government has renewed its commitment to address the financial and governance challenges in these companies. Cabinet has adopted a private-sector participation framework and government will review the funding models of state-owned companies. In considering the reforms necessary to return troubled institutions to financial health, government will consider inviting the private sector to take equity stakes in state-owned companies.

In January 2018, government appointed a new board at Eskom. It is expected to restore the electricity utility's operational viability and its financial stability. South Africa has excellent potential to generate electricity from renewable resources, the cost of which has fallen significantly in recent years. Eskom needs to adapt its business model to market competition, technological change and more efficient procurement arrangements. Partnerships with the private sector to strengthen the utility's capital structure will be explored. A strong and capable board and management team at Eskom will prepare the utility to adapt to these changes, building on South Africa's comparable advantages to generate cleaner, more affordable energy.

Partnerships for inclusive growth

Government, business and labour are working together to promote inclusive growth

Government will intensify its efforts to build durable partnerships with the private sector and labour to promote national development. These partnerships have already resulted in important initiatives:

- The CEO Initiative has developed a business-led fund supporting high-potential small and medium-sized enterprises, which has commitments of R1.4 billion to date. By June 2018, about R500 million is expected to be disbursed to the first round of enterprises. In addition, the Youth Employment Services Initiative aims to provide quality work experiences for vulnerable youth and is scheduled to begin operating in 2018. The pilot phase involves more than 20 of South Africa's largest companies.
- Government, business and labour are working within the National Economic Development and Labour Council to find ways to strengthen South Africa's investment ratings and promote faster growth.
- Legislation will be passed this year to enact the national minimum wage. Amendments to the Labour Relations Act (1995) will address wage inequality and help prevent prolonged industrial action.

Government's review of business incentives, which will be completed in 2018, aims to improve the contribution of incentives to investment and job creation.

Enabling economic transformation

A fundamental change in the systems and patterns of ownership and control that govern the economy can create opportunities for all South Africans to live productive, prosperous and dignified lives. Government continues to implement policies aimed at transforming the economy:

- Revised public procurement regulations came into effect in April 2017. These enable designated groups, including small businesses and those operating in rural and township economies, to participate more effectively in public procurement. The Public Procurement Bill, currently awaiting Cabinet approval for public consultation, will replace and improve on the revised regulations.
- The conclusion of the outstanding power-purchase agreements with independent power producers will bring benefits to the communities where those projects are located by creating an estimated 66 000 jobs and enabling investments of R55 billion.
- Government's Small Business and Innovation Fund, focused on providing support for entrepreneurs, will fund businesses in their start-up phases. The fund will also help to commercialise local innovation, with R1 billion allocated for 2019/20.
- The Financial Sector Code, gazetted in December 2017, aims to increase access to financial services for black South Africans – particularly low-income households. A R100 billion Black Business Growth Fund has been created through the code. Additional information on financial sector reforms appears in Annexure F.
- Government supports the expansion of competitive, affordable banking services, and recognises the value of digital banking services in this context. In 2017, the Reserve Bank granted three bank licences – two for banks with significant digital banking capabilities and one for a new digitally focused mutual bank. Progress has been made with the Postbank's licence.
- Efforts are under way, particularly in metropolitan cities, to promote increased investment in integrated transport, housing and related infrastructure. The Cities Support Programme's work on urban reform is discussed in Chapter 6.

Strengthening competition law to promote economic transformation

South Africa's economy has historically been characterised by concentration, cartels and price fixing in major sectors, making it difficult for small and new businesses to compete. Competition authorities have been successful in tackling anti-competitive practices covering a wide range of products, including bread, steel, cement, concrete, plastic pipes and HIV/AIDS drugs. Anti-competitive practices in banking and telecommunications have also been penalised. The World Economic Forum's *Global Competitiveness Report* 2017–2018 ranks South Africa 28th of 137 countries on the effectiveness of its anti-monopoly policy.

From its inception in 1999 to 2017, the Competition Commission has levied administrative penalties of about R6.4 billion against various firms. According to a 2016 World Bank report, the authorities' success in breaking up cartels in white maize, poultry, wheat and flour, and pharmaceuticals resulted in a reduction in overall poverty of 0.4 percentage points.

Proposed amendments to the Competition Act (1998), which would strengthen the competition authorities' powers, have been published for public comment. The amendments would enable the authorities to investigate the general state of a specific market, rather than the conduct of particular firms. In addition, they would obligate the authorities to consider structural issues of economic concentration and transformation when considering mergers and acquisitions, and in adjudicating abuse of dominance complaints.