Impact of the financial crisis on South Africa

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Introduction

- The worst impact of the crisis is associated with:
  - Structural industrial weaknesses – result of development centered around mining and mineral sectors
  - Continued reliance on mining & minerals exports
  - Recent growth can be compared to US debt-driven, consumption led growth and increased investment in services sectors, such as finance and retail
  - Speculative asset bubbles in real estate and finance & increased construction and car sales
- Central to continued weaknesses is the role of the financial sector which has emulated the behaviour of US financial institutions in increasing leverage and misallocation of capital in SA economy.

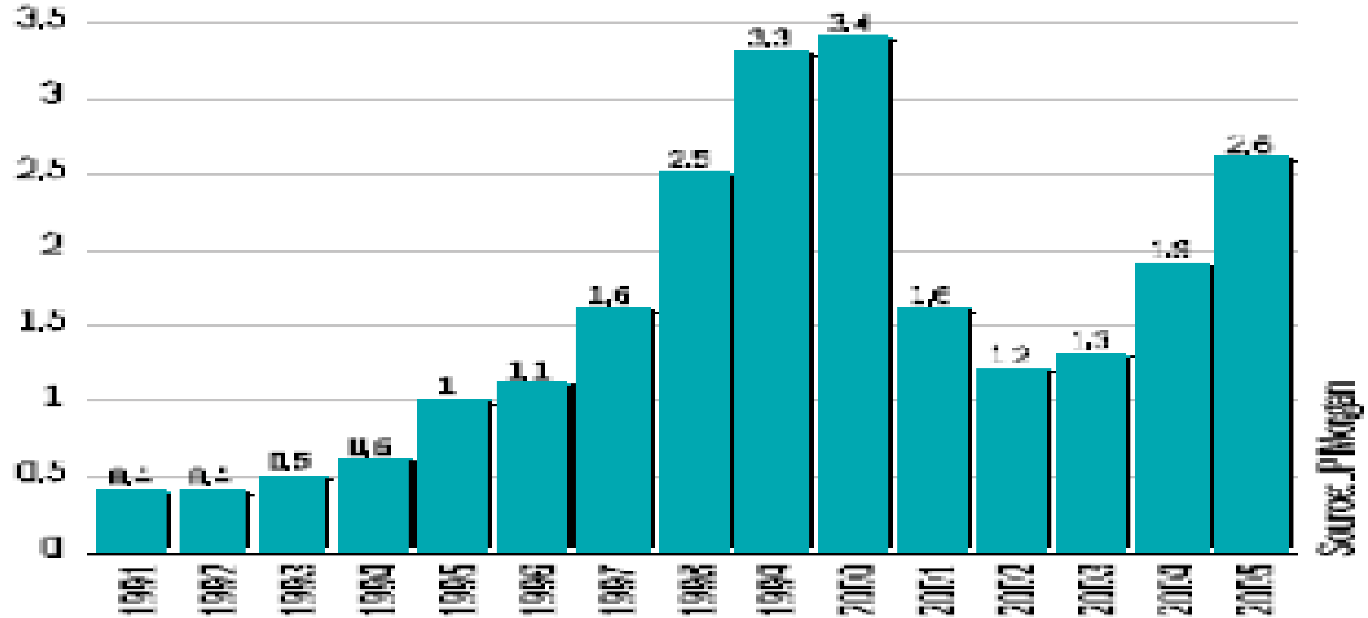
Serious problems existed before crisis

- The South African economy had an unemployment crisis and poor industrial performance before the crisis.
- These economic problems are a legacy of past economic and industrial development
- They are related to the industrial structural weaknesses of the economy.
- These problems have been exacerbated by recent debt-driven and consumption led economic growth and have intensified as a result of the global financial crisis.
- Uncertainty capital flows to developing countries during the crisis increases the fragility of the financial sector because of large trade deficit.

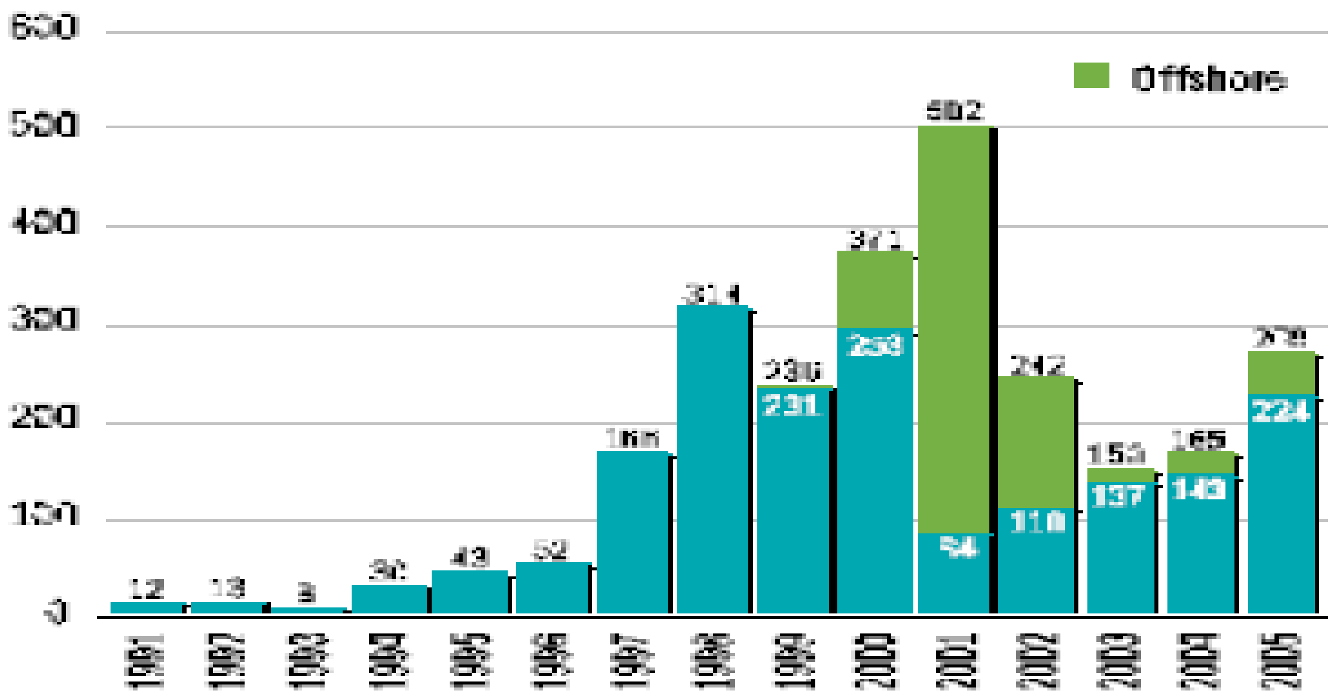
Corporate restructuring

- Massive global levels of M&As and global corporate restructuring, which increased global concentration
- SA large corporations restructured
  - Impact of democratic change & capital flight
  - Impact of shareholder value movement & the global corp. restructuring
  - Many of largest corporations listed abroad and increased international operations
  - Dependence on mining & minerals grew
  - Restructuring negative for industrial diversity

GRAPH 1: WORLD-WIDE MERGERS (US$ trn)

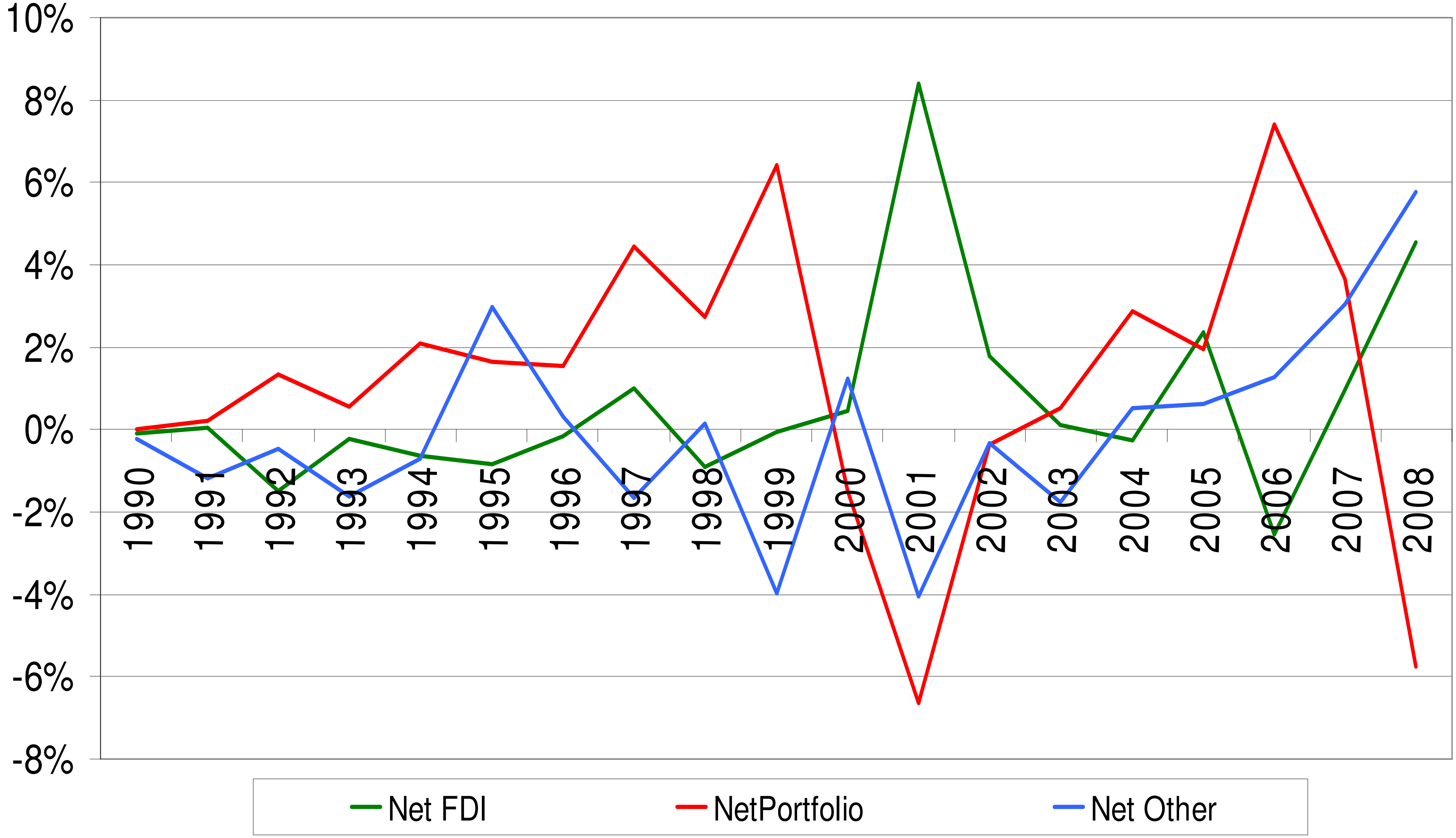


GRAPH 2: TRENDS IN SOUTH AFRICAN MERGER & ACQUISITION ACTIVITY (Rbn)

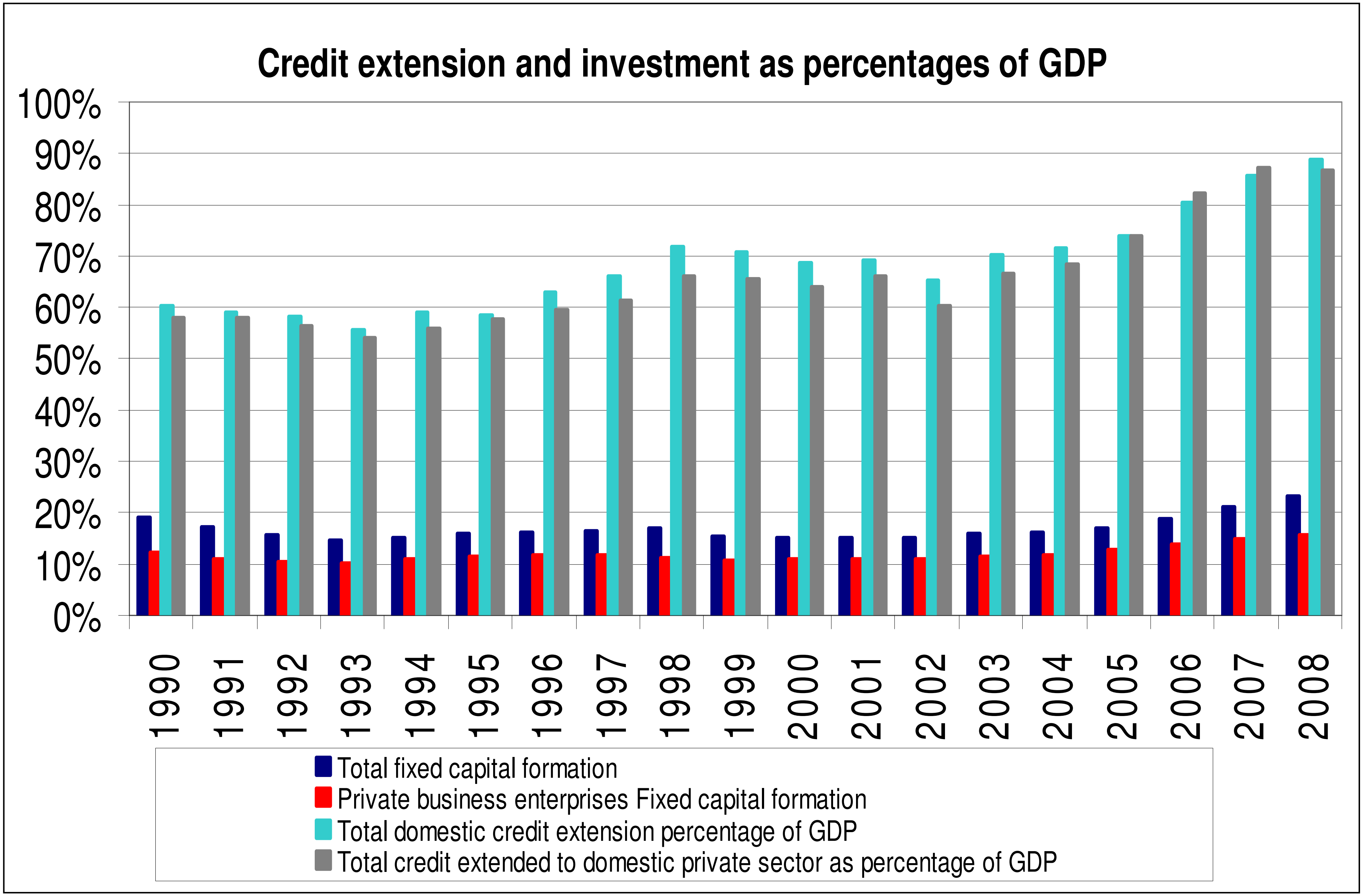


Source: Ernst & Young

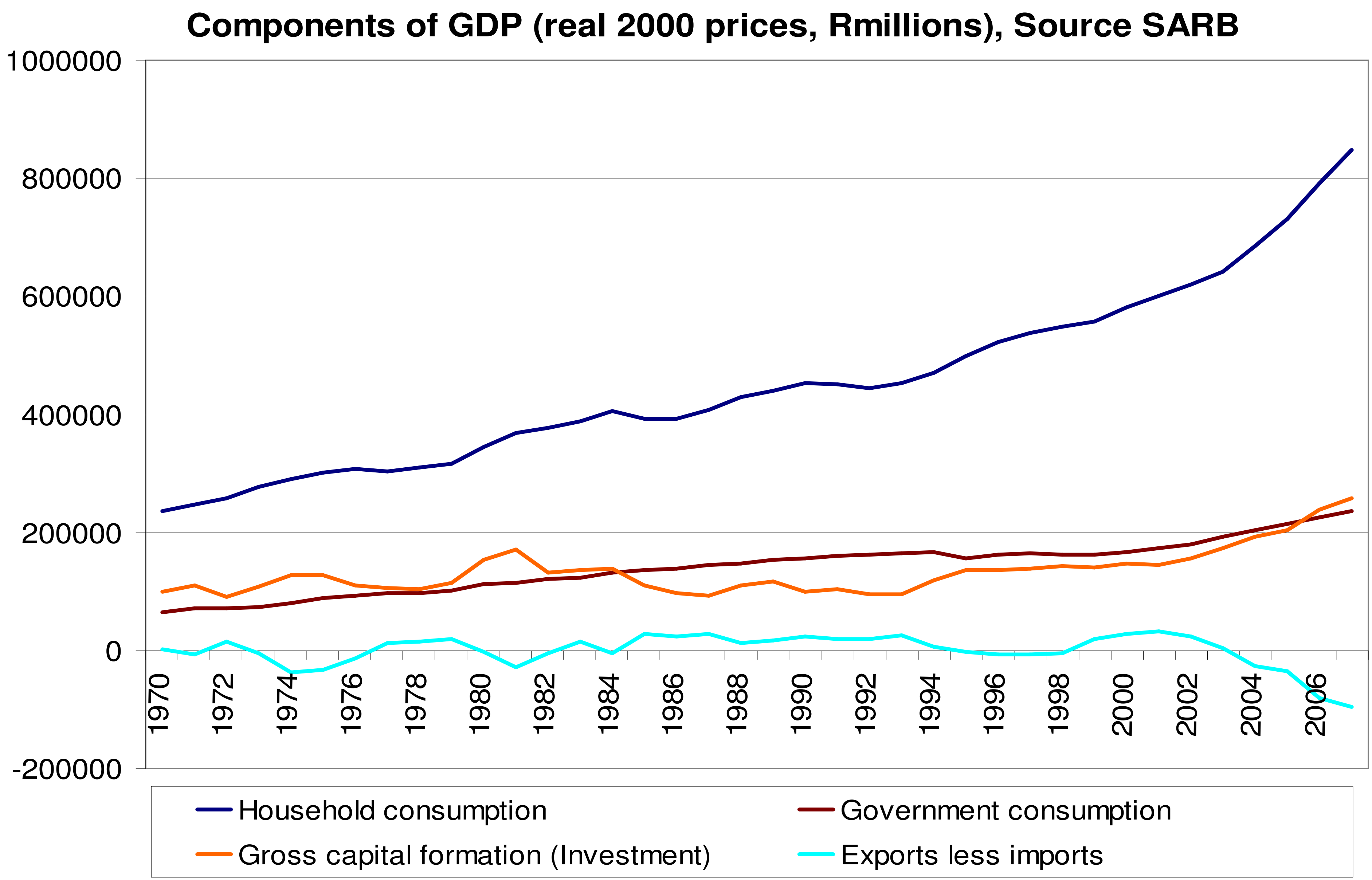
Net Capital flows (percentage of GDP)



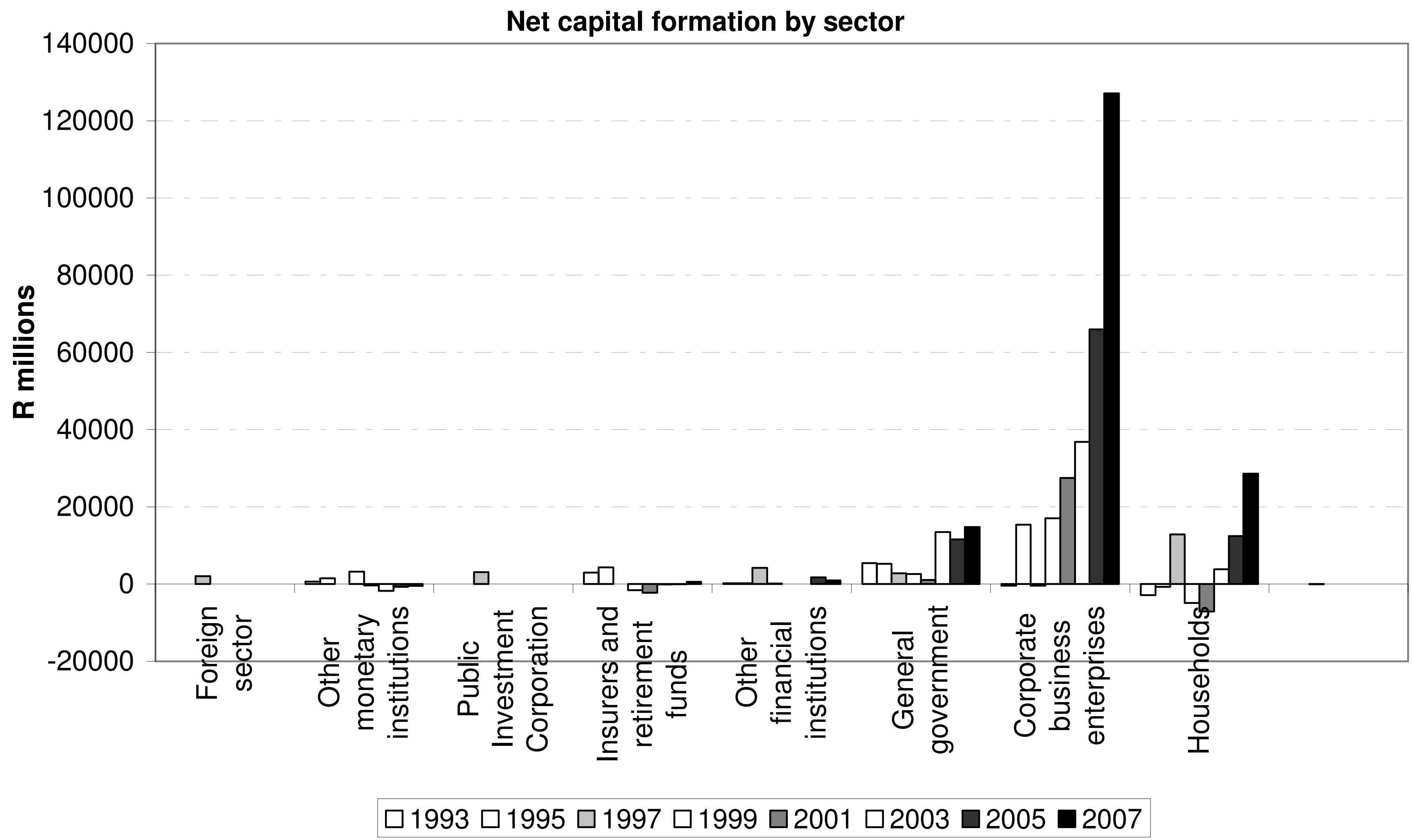
Credit extension to Private sector increased about 22% from 2000-08 BUT Private business investment increased by only 5%



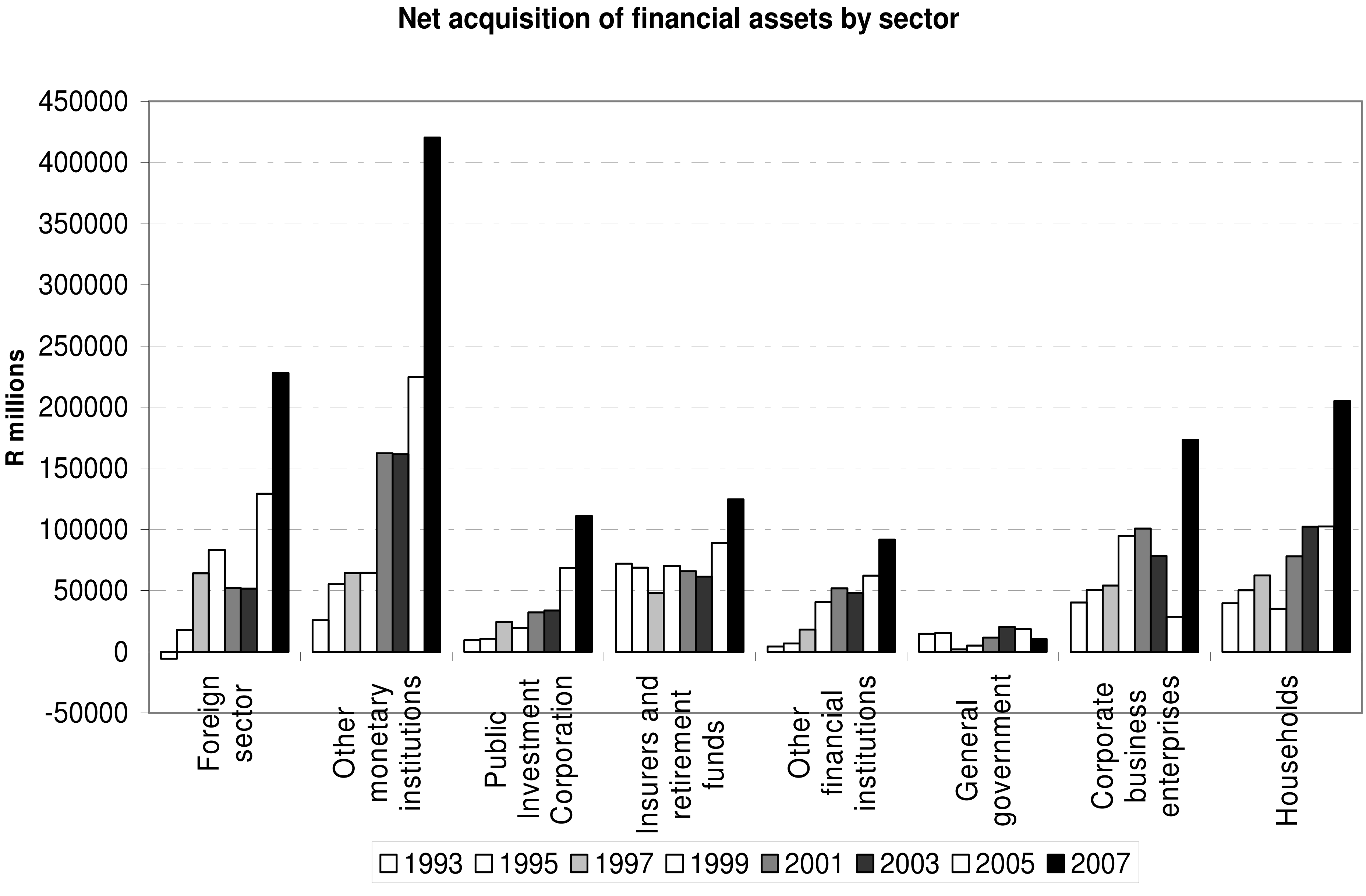
Growth in household consumption



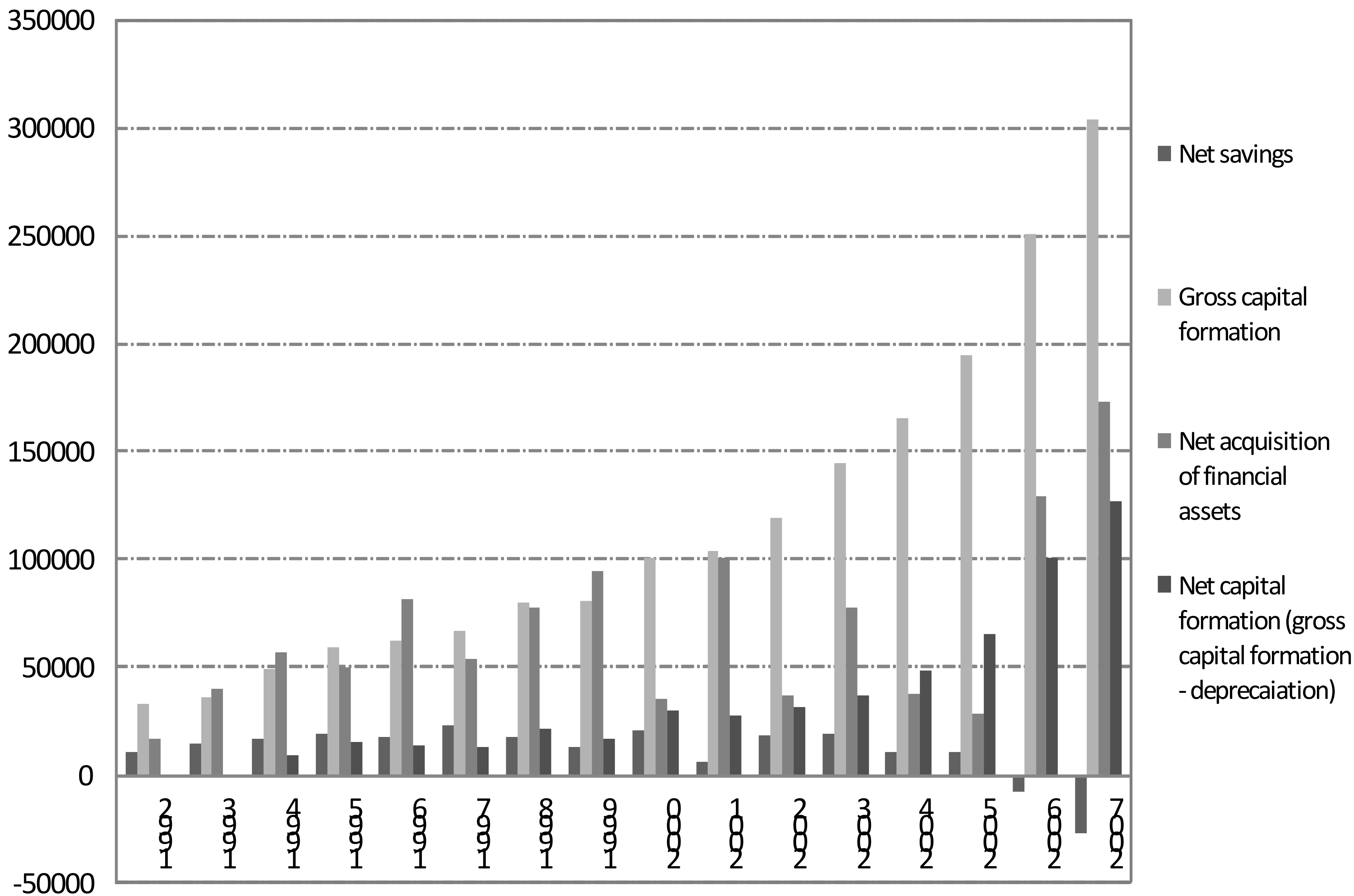
Capital flows to fixed investment (after depreciation)



Capital flows to financial assets

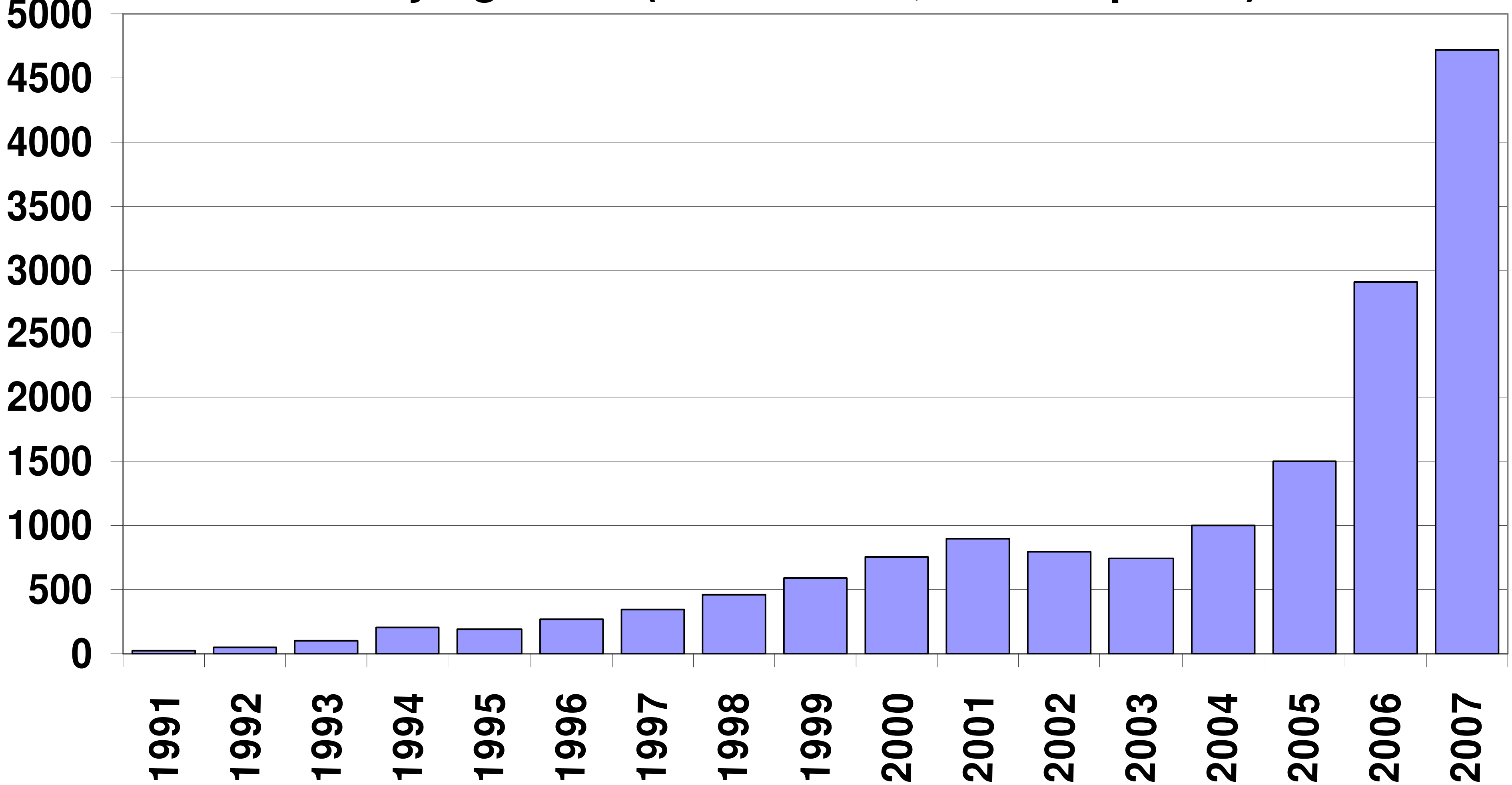


Sources and uses of capital in coporate business enterprises



Increased use of derivatives: increase financial systemic risks in SA

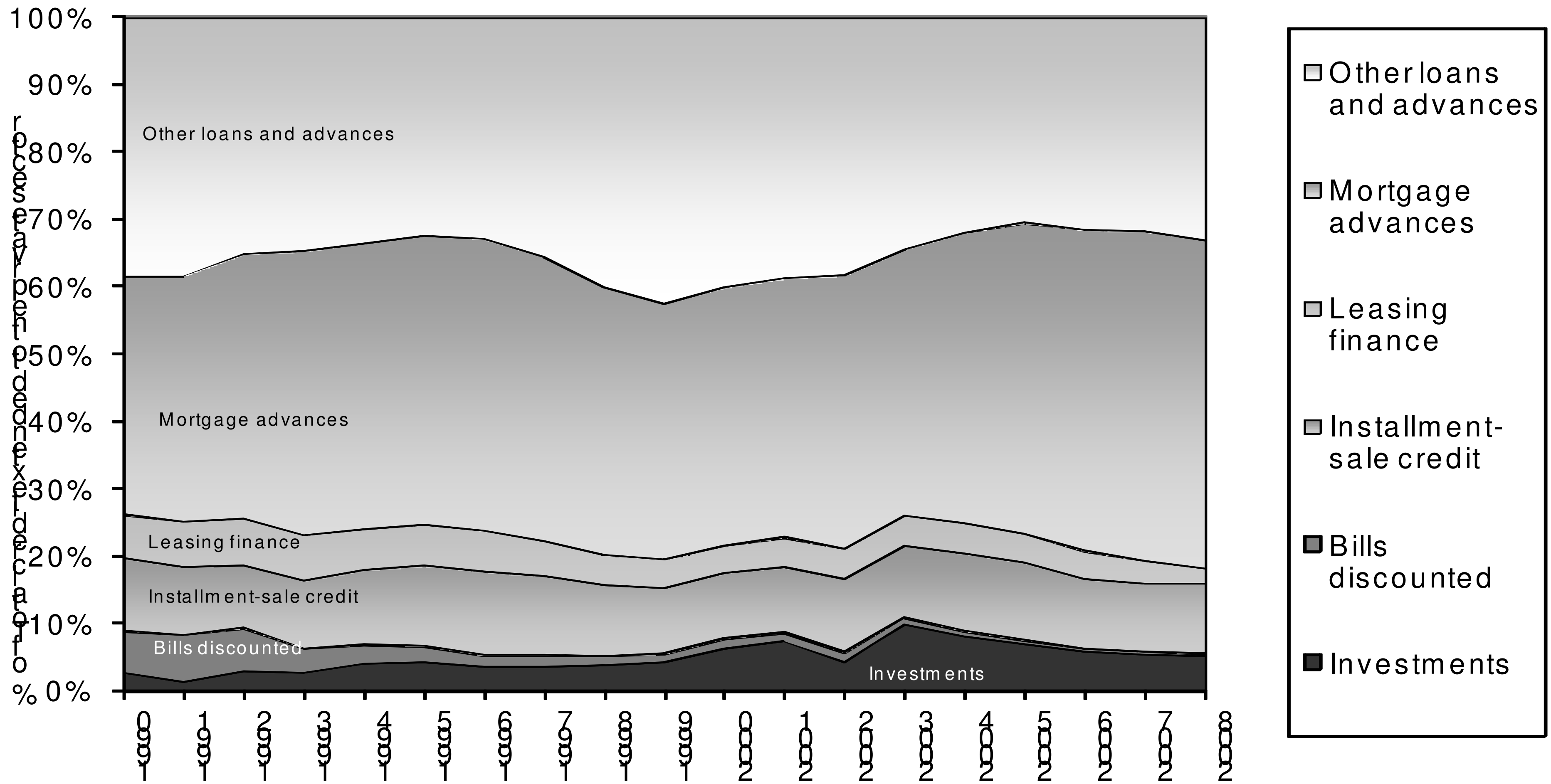
Derivative market - futures contracts :
Underlying value (in R billions, current prices)



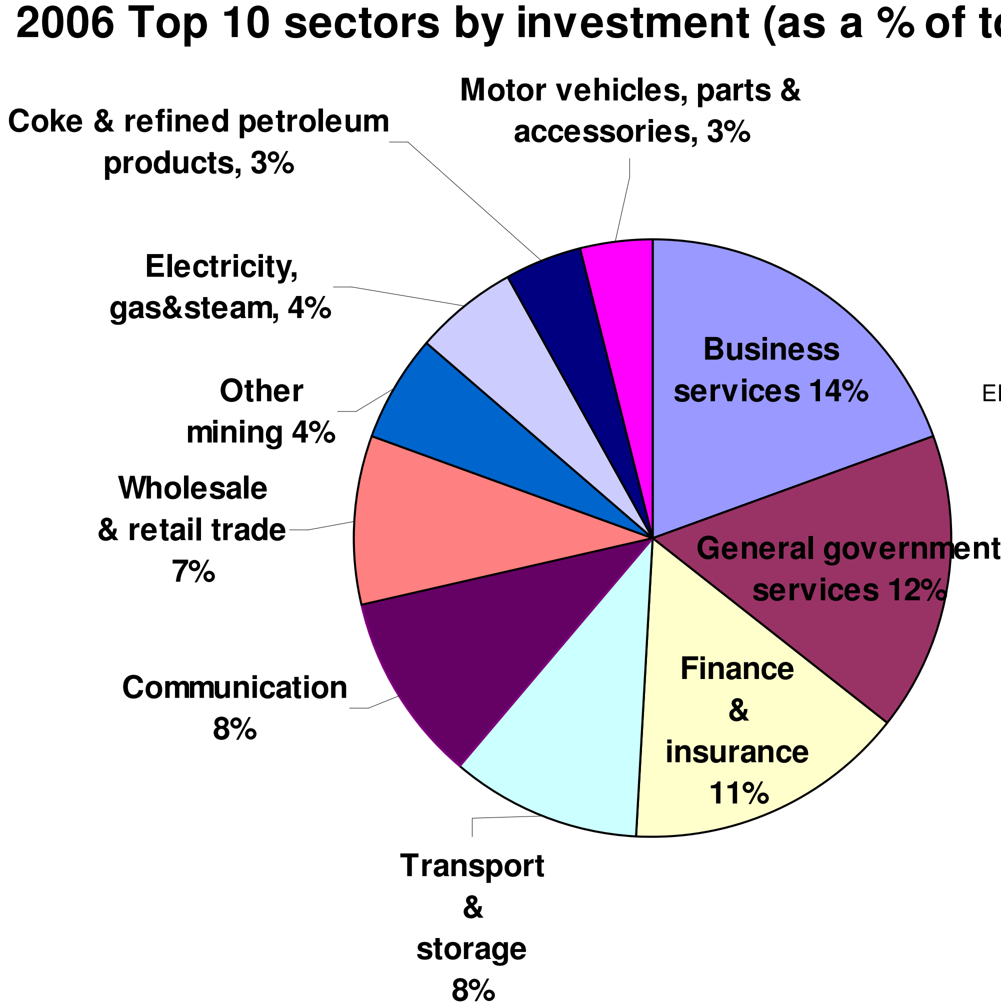
Allocation of capital by private sector:

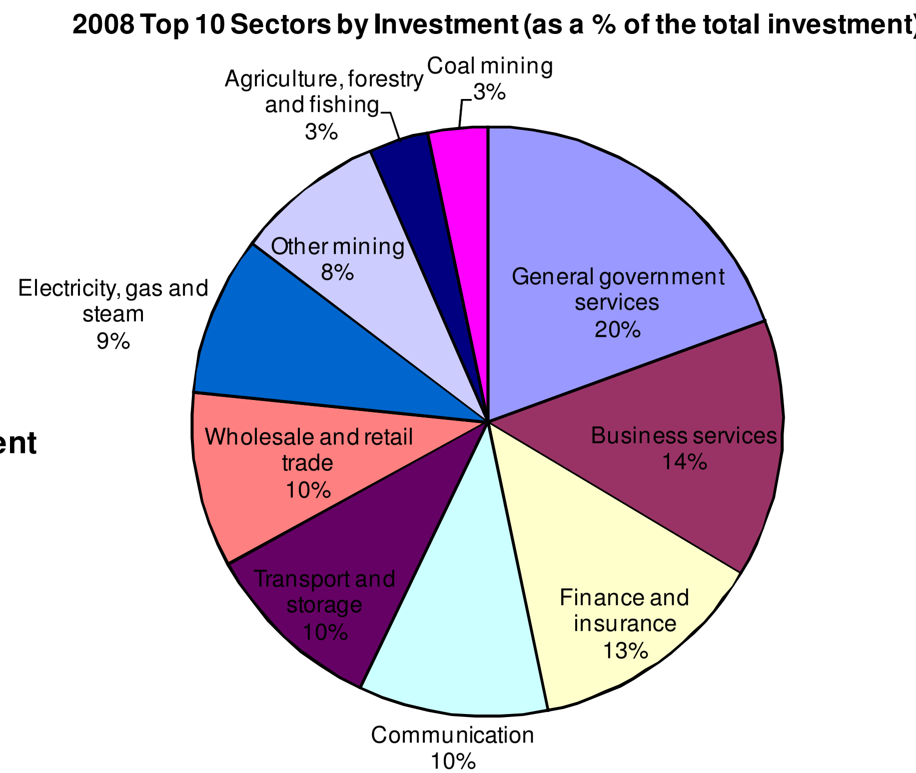
- mostly for credit cards, car finance &mortgages;
- mostly for short-term and collaterised debt

Private Sector Credit Extension by all Monetary Institutions

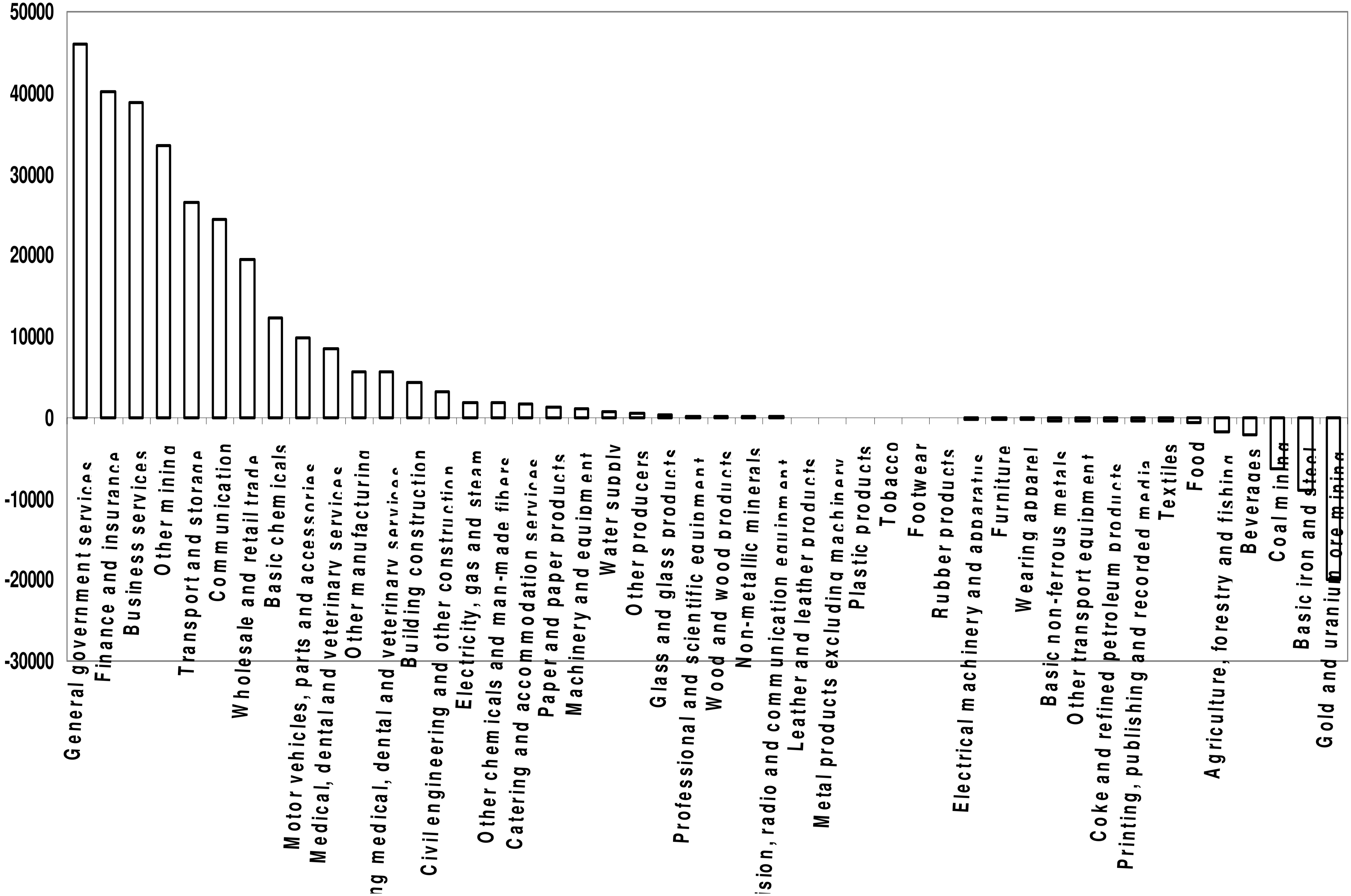


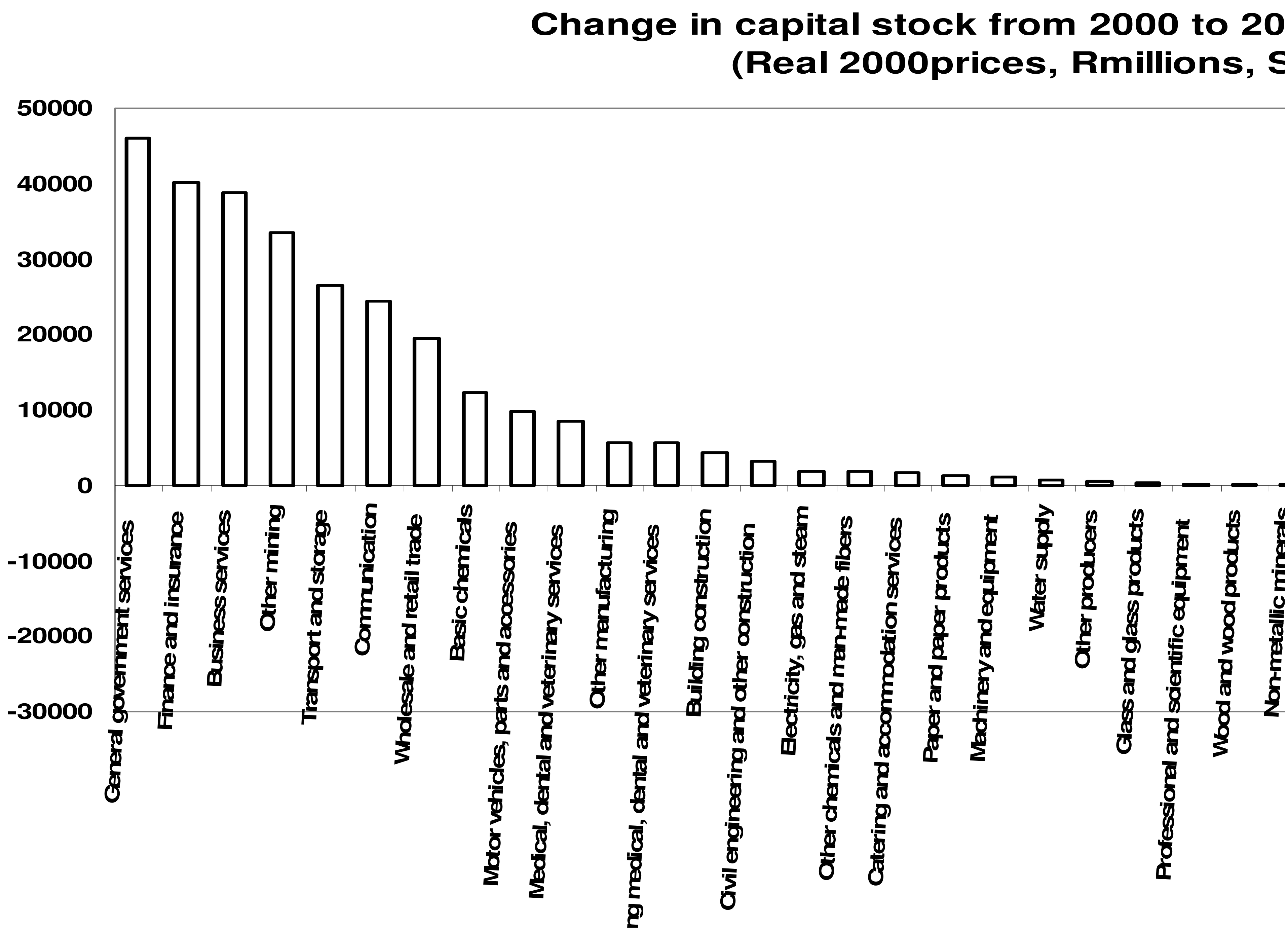
And, even fixed investment is misallocated





Change in capital stock from 2000 to 2006 for all economic sectors
(Real 2000prices, Rmillions, Source: Quantec)




Change in capital stock from 2000 to 20
(Real 2000prices, Rmillions, S
50000
40000
30000
20000
10000
0
-10000
-20000
-30000
General government services
Finance and insurance
Business services
Other mining
Transport and storage
Communication
Wholesale and retail trade
Basic chemicals
Motor vehicles, parts and accessories
Medical, dental and veterinary services
Other manufacturing
ng medical, dental and veterinary services
Building construction
Civil engineering and other construction
Electricity, gas and steam
Other chemicals and man-made fibers
Catering and accommodation services
Paper and paper products
Machinery and equipment
Water supply
Other producers
Glass and glass products
Professional and scientific equipment
Wood and wood products
Non-metallic minerals

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Rmillions, Source: Quantec)