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South Africa: Foreign trade alert

Trade surplus surprises

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What is the latest? In a surprise turn of events, the trade account registered a surplus in May for the first time since December 2006. The trade deficit closed during the month and recorded a surplus of R2.019bn from April's deficit of R1.456bn. The surplus was driven by a 2% m/m increase in exports to R41.456bn in May from R40.656bn in April. Fifteen of the 23 export categories reflected increases in May with large gains reported in the following categories: vegetable products (R0.622bn), vehicles, aircraft and vessels ((R0.987bn) and other unclassified goods (R0.545bn). Exports of base metals and articles thereof and mineral products declined by R0.638bn and R0.725bn, respectively (see Table 1 overleaf). And in an unexpected fashion, imports declined to its lowest level since December 2006 to R39.437bn in May from R42.112bn in April. The decline in imports translates into a monthly fall of 6.4%. Eighteen of the 23 import categories reflected decreases during the month with substantial declines emanating from the following categories: machinery and mechanical appliances (R1.327bn), base metals and articles thereof (R0.621bn) and original equipment components (R0.640bn) (see Table 2 overleaf). The year-to-date trade deficit of R19.725bn is R14.291bn lower than the corresponding 2008 year-to-date deficit.

Our view: The past three months have surprised markets with a turnaround in the trade deficit from the previously large deficits recorded. The average trade deficit in the three months to April was R0.874bn compared to an average trade deficit of R8.729bn in the three months to January. This, however, is not to say that trade deficits of this nature (i.e. the recent three months) is likely to continue for the remainder of the year. And as May's data reflected, the volatility of the trade data is plentiful and the pendulum can swing in either direction given the economic circumstances during the month. However, the economic developments thus far signals that further trade deficits are on the horizon and that May's unexpected surplus may be a temporary reprieve. That said, the slowdown in internal domestic demand is gathering pace, as confirmed by this morning's credit data. Furthermore, the current strength of the currency is not likely to support exports to the same degree as it has been, while imports are likely to continue to reap the benefits of rand strength. In May, the rand strengthened by 65c (on average) against the dollar, by 38c (on average) against the pound and by 51c (on average) against the euro. June saw a further strengthening of the rand against the dollar, which could weigh on the performance of exports in June. Furthermore, higher rand commodity prices lifted the import bill during the month and the oil bill in particular.

Trends to be aware of: The recent release of the South African Reserve Bank's *Quarterly Bulletin* revealed significant trends to keep a watchful eye on. There was little surprise when the data broke newswires that the deficit on the current account as a percentage of GDP widened to 7% in Q1 2009 from 5.8% in Q4 2009. Of significance with regards to the number was the impact from the trade deficit – the core reason behind the widening of the current account deficit. It has become common reason that the global downturn holds the trump card in the contraction of global trade volumes resulting particularly from a decline in the demand from the world's advanced economies. While many emerging markets are not suffering the same fate as their western counterparts, the effects of a deceleration in global demand are sparing few markets from a contraction in trade. In South Africa, merchandise exports volumes declined by a much sharper-than-expected 21% in Q1 2009 compared to a decline of 6.3% in Q4 2009. Despite mild gains in export prices in Q1, owing to a moderate increase in most industrial commodities, these were insufficient to offset the substantial decline in particularly manufacturing and mining export volumes. As a result, the value of exports declined by 19.4%.

Imports were on the same war path, but were left less wounded. Merchandise imports fell by 13% in Q1 2009 from Q4 2008, owing to a 5% decline in the prices of merchandise imports and an 8.4% contraction in import volumes. The decline was impacted largely by the relatively low international price of crude oil, despite the Organisation of Petroleum Exporting Countries' (OPEC) initiatives to scale down production. However, recent rand strength is likely to support import volumes, despite generally weaker demand. The decline in domestic demand for intermediate and consumer goods imports have translated into a lower import penetration ratio (i.e. the value of real merchandise imports relative to gross domestic expenditure) of 24.4% in Q1 relative to 26.8% in Q4; robust capital spending is likely to keep imports relatively buoyant as has been the case for the past few months, despite recessionary conditions.

Risks: The outlook for exports is feeble and is at risk of receiving knocks from the continued weakness in the global economy. Continued systemic risks have not disappeared and the global economic recovery is no longer guaranteed. The recent debates of green shoots sprouting may still be alive, but it is unlikely at this stage that blooms will occur in the near future. Furthermore, there are differing views with regards to whether the global economy is improving, or whether the stabilisation and return to trend growth is imminent. Uncertainty in the global economy is therefore manifesting in declining global trade volumes, South Africa included.

That said, with the sheer size of global destocking having already taken place, it is plausible to argue that the bulk of the negative knock-on effects on South Africa's exports have already taken place. As such, the rate of decline in SA exports may start running out of steam. We will closely monitor these trends in so far as reducing the size of expected deficits this year. On a more positive note there has been evidence of improved appetite for emerging market assets. The MSCI Emerging Market equity index increased by 1.6% last week. This, combined with emerging market currency gains against the dollar, is supportive of emerging markets stepping out of the global economic recession sooner than the developed world. However, the strength of the domestic currency (the dollar lost 2.7% ground against the rand in the past week alone) could place a ceiling on the ability of exports to recover from what could be a more prosperous year should the developing world step out of the rut.

Outlook: The trade account, in an unexpected turn of events, registered a surplus of R2.019bn in May from April's trade deficit of R1.456bn as exports reversed some of the declines that we have become accustomed to of late. Furthermore, and unexpectedly, imports declined to its lowest level since December 2006. While this may lift sentiment that the string of trade deficits may just be behind as, it might not be wise to count your chickens before they hatch. Economic developments thus far this year are pointing the needle to further declines in exports, by as much as 10%, which casts doubt on whether further surpluses are in the pipeline.

Table 1: Selected SA export categories – May 2009

Category	Rm	% of total	% y/y
Total	**41 456.8**		**-26.8**
Precious stones/metals	10 152.8	24.5	-25.5
Base metals	5 468.2	13.2	-59.7
Mineral products	8 001.8	19.3	-6.6
Chemical products	2 092.3	5.1	-20.8

Source: SARS

Table 2: Selected SA import categories – May 2009

Category	Rm	% of total	% y/y
Total	**39 437.2**		**-31.9**
Machinery	11 205.3	28.4	-27.1
Transport equipment	3 034.5	7.7	-46.1
Chemical products	3 836.5	9.7	-25.5
Mineral products	8 887.4	22.5	-28.2

Source: SARS

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Lesotho	**Ghana**	**Mozambique**	**Nigeria**
Namibia	**Malawi**	**Uganda**	**Tanzania**
Swaziland	**Mauritius**	**Zambia**	**Zimbabwe**

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