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Economy Watch – July 2018

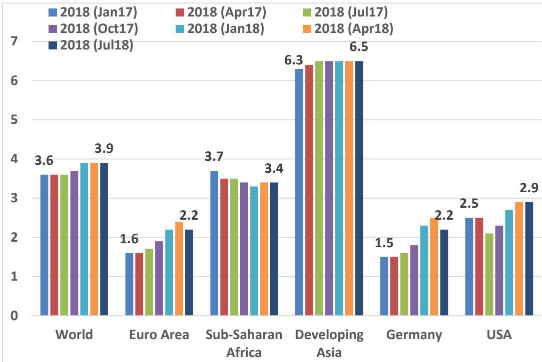
The International Monetary Fund (IMF) has maintained its **global economic growth outlook** for 2018 and 2019 at 3.9% in the World Economic Outlook update of July 2018. While the outlook has not changed since the beginning of this year, it is up by 30 basis points compared to the 3.6% forecast a year ago in July 2017 for 2018. Although the global outlook remained unchanged, some **countries and regions face more headwinds** than expected in earlier forecasts. Growth in the **Euro area** is projected to expand by 2.2% this year and by 1.9% in 2019, which is 0.2 and 0.1 percentage points lower than previously estimated. While the **German economy** is not expected to perform as strongly as initially expected during this year - the forecast has been lowered by 30 basis points to 2.2% - the outlook for next year was slightly revised upward by 0.1 percentage points to 2.1%. Similarly, economic prospects for **France and Italy** are a little bit more overcast and adjusted to 1.8% and 1.2% respectively – down also by 30 basis points.

While the **Chinese economy** is expected to grow by 6.6% and 6.4% this and next year respectively, which is supported by a growth rate of 6.7% for the second quarter 2018, growth in **India** is anticipated at 7.3% - down from 7.4% at the beginning of this year and forecasts made last year of 7.7% - and at 7.5% in 2019 – down from 7.8%. **Brazil**'s growth prospects were revised downward by 0.5 percentage points to 1.8% this year, but maintained at 2.5% for next year. **Russia**'s economy is expected to expand by 1.7% and 1.5% in 2018 and 2019 respectively as previously projected. Likewise, the outlook for the **US economy** remained at 2.9% and 2.7% for the two years respectively.

Sub-Saharan African economies are projected to grow by 3.4% this year while picking up to 3.8% in 2019, which indicates an upward revision by 0.1 percentage points. The **Nigerian** economy is expected to grow by 2.1% and 2.3% respectively and hence cementing its place as Africa's largest economy, since the **South African** economy that follows on rank two, is anticipated to expand by 1.5 and 1.7%. The projection remained unchanged from the April forecast, but is much more positive than anticipated in January 2018 – 0.9% for both years.

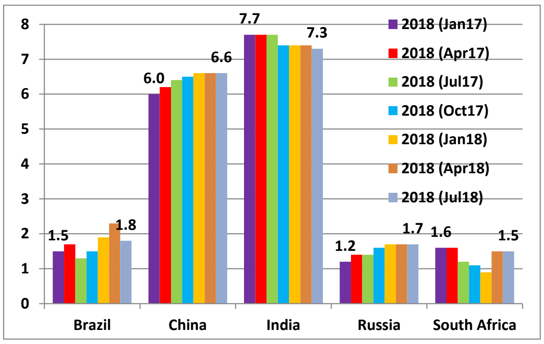
Growth prospects for emerging market economies including African economies are in part **supported by higher commodity prices** and in particular higher oil prices (see below) unless internal political factors hinder economic progress in countries such as Brazil and Venezuela. There are, however, **downside risks** mainly because of destructive decrees from the US administration including the imposition of **additional tariffs** on imports from various countries. The US **withdrawal from the Iran deal** and the renewal of sanctions that will affect companies from other countries as well have resulted in upward pressure on oil prices. The resulting uncertainties regarding global trade and adherence to multilateral, rules-based trade arrangements will delay investment decisions and hamper growth prospects. These uncertainties are further compounded by a lack of progress regarding **Brexit**. It remains unclear whether a trade agreement can be reached before the withdrawal becomes effective, whether a new trade deal will cover all goods or even include services (the backbone of the UK economy),

Global economic outlook for 2018 in per cent for selected countries and regions



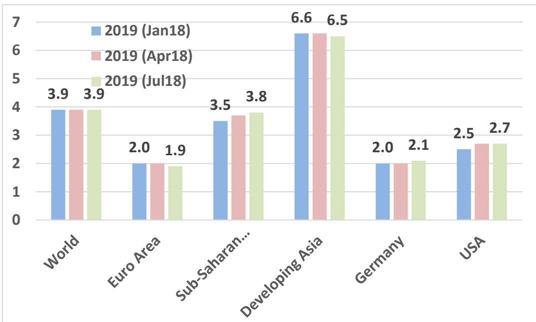
Source: IMF, World Economic Outlook July 2018

Economic outlook for BRICS countries for 2018 in per cent



Source: IMF, World Economic Outlook July 2018

Global economic outlook for 2019 in per cent.

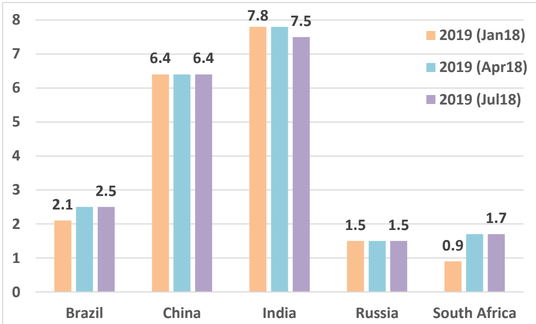


Source: IMF, World Economic Outlook July 2018 how the border issues in Ireland and between Gibraltar and Spain can be solved, etc.

Additional tariffs will hurt producers and consumers everywhere, increase prices and eventually inflation and could **result in further monetary tightening**, which in turn increases the costs of investments financed through loans and dent the appetite for investment. The uncertainties have already resulted in **funds being moved out of emerging market economies** and invested in particular in the USA, which leads to the depreciation of their currencies vis-à-vis the US dollar (USD). Some emerging economies have reacted and increased interest rates in order to create a more attractive environment for financial investors and to counter inflationary pressure caused by the currency devaluation and rising oil prices. The **depreciation** has hit the **Argentine peso, the Turkish lira and the Brazilian real** especially hard – depreciation by over 20% and 10% and 10% respectively. But the South African rand has also not been spared the consequences (see below).

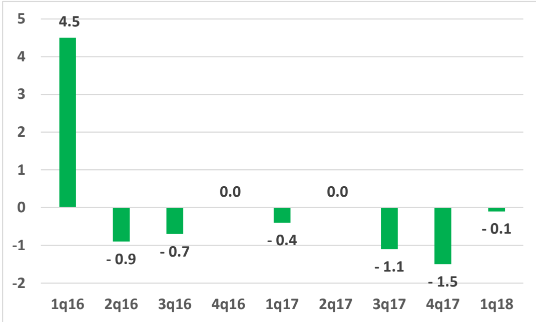
The **Namibian economy** shows signs of recovery. Initial data for the first quarter 2018 indicates an economic contraction of 0.1% on a year-on-year basis, which is slightly better than the decline by 0.4% during the first quarter 2017 and contractions of 1.1% and 1.5% in the third and fourth quarters of 2017 respectively. After contracting during each quarter in the past two years, the **construction sector** started 2018 with positive growth of 23.7%. The strong growth needs to be seen against a low base in 2017 due to continuous declines in value added. Real value addition of the construction sector amounted to NAD1,289 million, which remains one of the lowest since 2013 with the exception of 2017. Value addition in the **mining sector** expanded by 4.7%, which together with the performance of the construction sector, has benefited the **transport sector** that grew by 2.5%. The **manufacturing sector** contracted by 2.1% mainly caused by a decline in the processing of non-metallic minerals and base metals. Below average rainfall in the first quarter of the year resulted not only in a strong increase of live animals being exported, but also an increase in meat processing (growth of 11.2%). Value addition in the **hotel and restaurant** sector dropped by 5.3%.

Economic outlook for BRICS countries for 2018 in per cent



Source: IMF, World Economic Outlook July 2018

Quarterly growth figures for selected Namibian sectors in per cent



Source: Namibia Statistics Agency, 2018, Gross Domestic Product – First Quarter 2018.

After steady declines starting in the second half of 2014, **oil prices** have begun to **rebound** since the second half of 2017. Oil prices dropped from a quarterly **average of USD109.69** per barrel (bbl) for crude Brent oil in the second quarter of **2014** to a low of **USD33.84** / bbl during the first quarter of **2016** where after prices recovered, but remained below USD50.00 / bbl for the rest of 2016. Prices passed the USD50.00 per barrel mark in August 2017 and briefly touched the USD80.00 per barrel mark in the second half of May 2018. Since then prices have weakened slightly and closed the **second quarter 2018 on an average of USD74.53** per barrel – the highest quarterly average since the first quarter of 2014. Average quarterly oil prices increased by between 5.1% and 17.9% on a quarter-to-quarter basis since the second half of 2017 and by between 13.8% and 50.4% on a year-on-year basis.

Oil prices in USD per barrel (Europe Brent), Jan 2012 to Jul 2018

Sources: US Energy Information Administration (EIA) daily data.

The recovery of oil prices was supported by **production cuts** that were agreed between **OPEC member states and non-OPEC member states**, in particular Russia. Rising tensions in the Near and Middle East, from Syria to Yemen, further pushed prices up temporarily. While oil prices remain below levels of above USD100.00 seen between 2011 and 2014, the pace of price increases has stoked **fears about a global economic slow-down**, since producers and consumers had barely time to adjust to the rising price levels. This in turn resulted in **calls** for OPEC and non-OPEC member states **to increase production** in order to rein in rising prices. The withdrawal of the USA from the Iran deal, its re-introduction of sanctions with effect of August 2018 and its call to stop buying oil from Iran with effect of November 2018 has again put upward pressure on oil prices aided by the turmoil in Venezuela. **Saudi Arabia** reportedly heeded calls from Washington to increase output beyond the agreed-upon levels in order to counter upward price pressure, which would not bode well for the US Republican Party's chances of winning the mid-term elections later this year. The rivalry between Saudi Arabia and Iran has certainly contributed to the decision to increase output, which has led to **prices dropping to USD71.03**/bbl.

As usual, **higher prices provide incentives** for other producers to increase output. According to Baker Hughes rig count, the monthly average number of international **oil rigs** (excluding Canada and the USA) increased by 11% between June 2016 and June 2018. Canadian and US shale oil producers have responded to rising prices by significantly **increasing the number of oil rigs** from 27 and 417 to 86 and 861 respectively amounting to increases of 219% and 106% for Canada and the USA. The monthly average for Canada, however, covers a steep increase between the middle of June to the middle of July resulting in 139 oil rigs operating on 13 July 2018. Of course, the production capacity of the rigs matter as well, but it is expected that the impact of the growing number of oil rigs and increased output will contain oil prices. The IMF projects oil prices to **average USD59.00 per barrel** in the medium term.

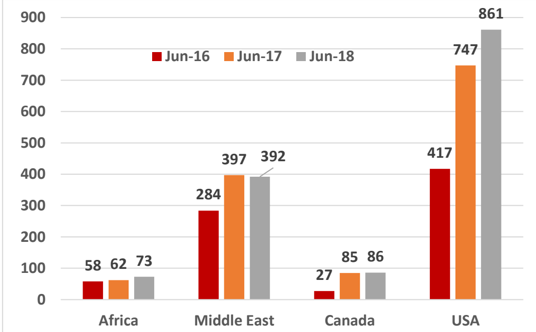
The **depreciation** of the Namibia dollar vis-à-vis the US dollar since 2011 led to rising oil prices in the domestic currency even when international oil prices dropped. 2015 was the exception, but oil prices in NAD terms dropped by only 42.0% compared to 2016, while oil prices in USD terms declined by 50.7%. In 2017, the **appreciation** of the NAD versus the USD **cushioned Namibian consumers and producers** against rising oil prices. Oil prices in NAD rose by 4.8% compared to oil price increases of 15.7% in USD terms.

However, oil price fluctuations in NAD did not always result in similar changes of **fuel prices**. The steep drop in oil prices during 2015 was only partially passed on to the motorist. While oil prices declined by 42%, petrol and diesel prices were reduced by 12.5% and 15.5% respectively, since Government used the opportunity of low oil prices to increase the transport levy and Road Fund Administration levy by 10 cents per litre each and the industry margin by 12 cents per litre. The lower oil prices in 2015, however, cushioned customers in 2016 when diesel prices still dropped (by 3.9%) and petrol prices increased only by 0.7% compared to a rise in oil prices by 10.6%.

The **adjustment** in TransNamib's bulk fuel rail rate in July 2018 by between 10 cents and 29 cents per litre pushed fuel prices to **levels last seen** in the second quarter of **2014**. Motorists in Windhoek pay NAD12.72 per litre for petrol, which amounts to an increase by 12.4% compared to a year ago and exceeds petrol prices in 2014 when they stood at NAD12.51 per litre. Diesel prices increased to NAD13.11 per litre for 50ppm resulting in an increase by 22.4% compared to July 2017. They, however remained slightly below prices between March and June 2014 of NAD13.15 per litre. Motorists, however, have been spared steeper price increases, since Government decided to use the National Energy Fund to absorb for the time being under-recoveries that ranged between 45.3 cents per litre for diesel 50ppm and 52.6 cents per litre for petrol. Unless oil prices drop below the average price in June of USD74.40 per barrel and the currency remains stable, motorists can expect more price hikes. Since fuel prices account for **9% of the consumption basket** that determines the **inflation rate**, the current fuel price increases will result in a higher inflation rate.

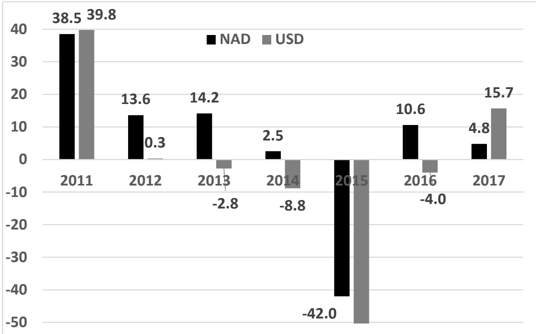
However, it is not only the direct impact of fuel price rises on the consumer, but also **second-round effects** through producers that face higher input costs. According to information from the Social Accounting Matrix 2013, the fishing sector is most affected by rising fuel prices, since fuel accounts on average for

Oil rig count for selected countries and regions: Monthly averages for June 2016 to June 2018



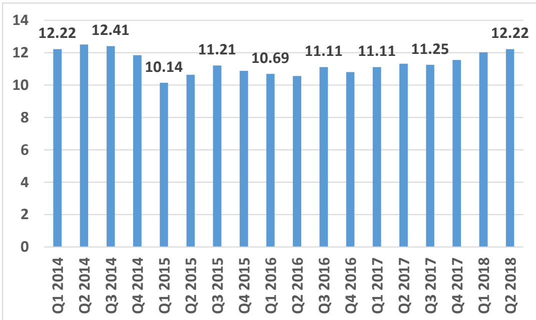
Sources: Baker Hughes Rig Count

Oil price changes compared to previous year in USD and NAD, 2011 to 2017.



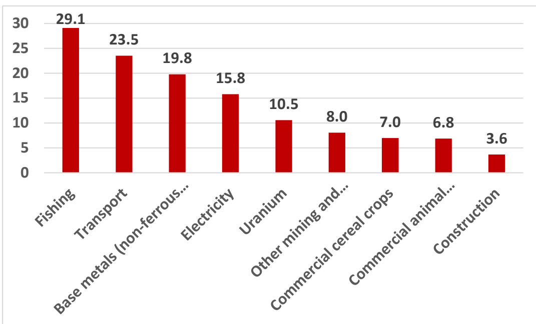
Sources: Authors' calculation based on EIA daily data.

Quarterly average pump prices for Petrol 95 (Windhoek) per litre, 1q2014 to 2q2018.



Sources: Authors' calculation based on MME monthly data.

Share of fuel over total input costs for selected sectors in per cent.



Source: Social Accounting Matrix 2013

29% of input costs. Fuel contributes about 24% to total input costs of the transport sector, 20% to base-metal (copper, zinc, etc.) mining, 16% to electricity generation and 11% to uranium mining. It can be expected that increasing input and transportation **costs will be passed on to the consumer**.

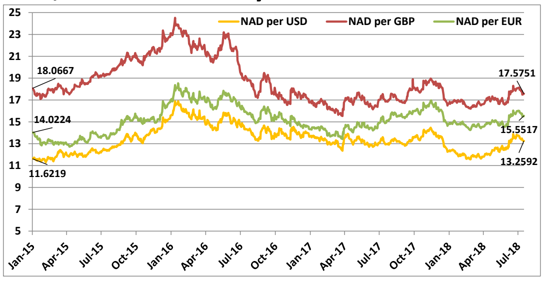
The **Namibia dollar (NAD) has depreciated** since the beginning of the year against currencies such as the USD, British Pound (GBP), EUR and Japanese Yen (JPY) as well as against BRIC currencies with the exception of the Brazilian Real (BRL). As explained above, uncertainties created by the imposition of tariffs by the US administration on products ranging from solar panels to steel and the retaliation by affected countries across the world, as well as uncertainties surrounding the exit of the UK from the EU has resulted in increased risk aversion and the shifting of funds from emerging markets to – in particular – the US. Monetary tightening in the US because of strong economic growth, historically low unemployment and hence rising inflationary pressure (supported by price increases of imported products owing to the introduction of new tariffs) is expected to result in two or three interest rate increases this year, which will increase the attractiveness of the USD for financial investment. The European Central Bank is expected to reduce its bond-buying programme significantly by the end of this year and most likely raise interest rates in the middle of 2019.

In contrast, the **South African Reserve Bank** and the **Bank of Namibia** have lowered the repo rate since June 2017 by 50 and 25 basis points to 6.50% and 6.75% respectively in order to stimulate economic growth. Combined with weakening currencies, it makes the countries a less favourable destination for portfolio investment. The **NAD depreciated** most against the JPY (8.3%), followed by the USD (7.9%), GBP (6.0%) and EUR (5.7%) by the 17th of July. BRIC currencies have also been affected by the shift in investor sentiments. The NAD depreciated by 5.4% against the Chinese Yuan (CNY), but only by 1.2% against the Indian Rupee (INR) and 0.2% against the Russian Rouble (RUB). The Brazilian Real performed poorly due to uncertainties surrounding the upcoming elections, which resulted in the appreciation of the NAD vis-à-vis the BRL by 7.5%.

Zinc prices continued the strong recovery over the past decade into the first quarter of 2018, but have weakened during the second quarter to below quarterly averages in the previous two quarters. **Copper prices** also performed well during the first quarter but remained below levels seen until the third quarter of 2014. Both base metals lost some ground during the second quarter trading at an average quarterly price of USD3,111 per tonne for zinc and USD6,871 per tonne for copper. This trend has continued in July. Zinc prices dropped by 23% since the beginning of the year to USD2,547.50 per tonne, while copper prices weakened by 14% to USD6,141.00 per tonne. **Uranium prices** remained low at USD22.85 per pound – a decline by 3.8% since January 2018, but an improvement of 12% compared to July 2017. The low uranium price has resulted in the Langer Heinrich Uranium mine being put on care and maintenance. **Gold has not** benefited from current uncertainties and traded at USD1,241.70 per ounce on 13 July 2018 - 3.8% lower than at the beginning of 2018.

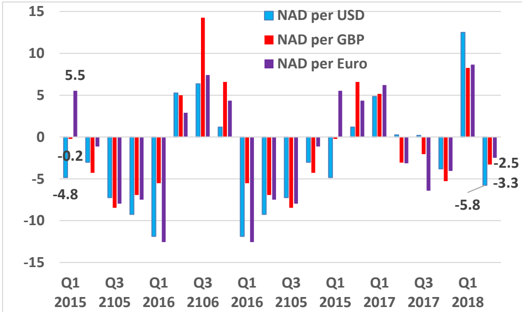
Prices for **white maize** have increased this year by 6.8% to NAD1,998 per tonne, while **wheat prices** rose by 9.4% to NAD4,040 per tonne on 17 July 2018. However, compared to prices a year ago, maize and wheat prices moved in opposite directions: Maize prices increased by 12.4%, while wheat prices decreased by 10.9%. Future prices at the South Africa Future Exchange suggest price increases by 5.2% (white maize) and 2.3% (wheat) until December 2018.

Exchange rates – NAD per USD, GBP and EUR, Jan. 2015 to July 2018



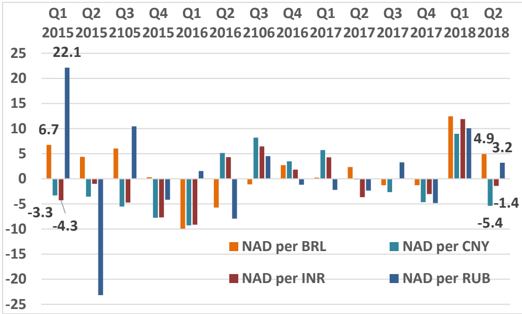
Sources: Authors' calculation based on SARB daily data.

Quarter on quarter changes – NAD per USD, GBP and EUR, 1q 2015 to 2q2018



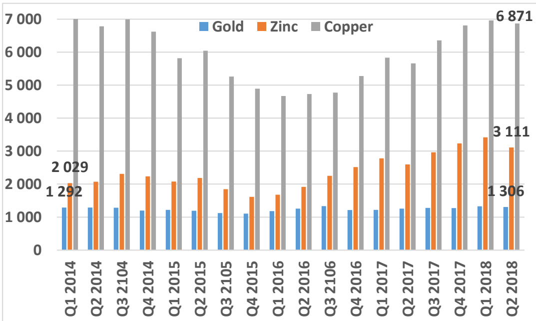
Sources: Authors' calculation based on SARB daily data.

Quarter on quarter changes – NAD per BRL, CNY, INR and RUB, 1q 2015 to 2q2018



Sources: Authors' calculation based on SARB daily data.

Average quarterly prices in USD per ounce (Gold) and per tonne (Zinc, Copper)



Sources: Authors' calculation based on LME and World Gold Council daily data.

Economy Watch Namibia is compiled by IPPR Research Associate Klaus Schade (economist@ippr.org.na) and is financially supported by the Hanns Seidel Foundation (HSF). Economy Watch can be downloaded from www.ippr.org.na or www.hsf.org.na.