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IPPR Economic Outlook, February 2007

Finding economic growth that responds to jobs is key public policy challenge

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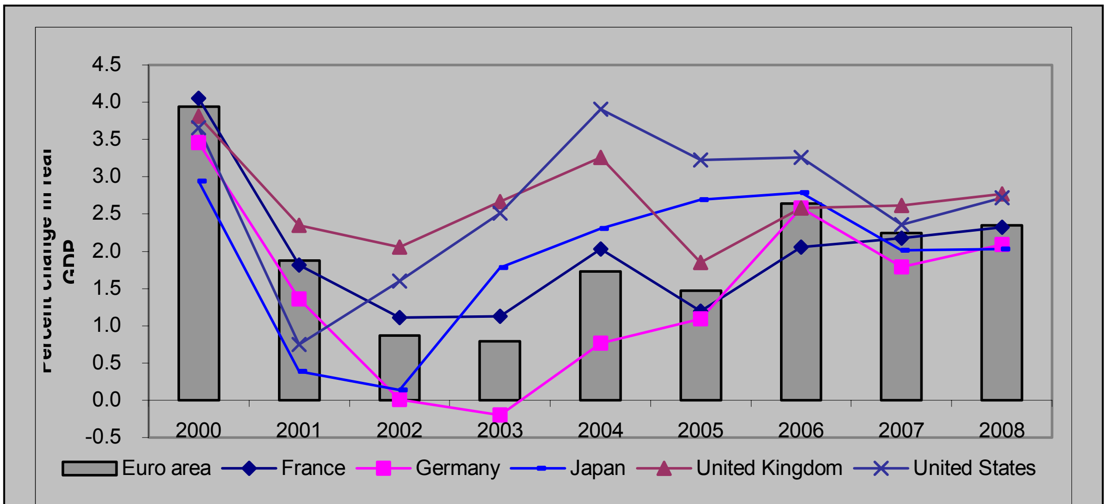
Growth expectations for both the Namibian and South African economy remain subdued for 2007, linked to the risk of interest rate hikes that may hamper domestic demand and investment as real interest rates are starting to peak. Similarly, most OECD economies are projected to grow less vibrantly relative to 2006. The policy challenge for Namibia is to create significant economic growth that leads to job creation. We find that employment growth does not respond in any meaningful way to real GDP between 1993-2004 – with an employment growth elasticity of 0.17%.

What's Inside?

International Growth Outlook

Economic growth expectations for most OECD economies remains subdued for 2007 and 2008 according to estimates by the OECD Centre. The graph below summarises these projections. The high-energy costs seems to have had minimal effect on a recovery in the Euro Area with the economic bloc growing at 2.6% in 2006 owing to growth in exports as well as corporate investment. Supported by a steady rise in consumption spending, the bloc is forecast to grow at a rather moderate pace in the range of 2.2% and 2.8% for this year and 2008. Nevertheless, the threat to the recovery would be an unchanged position with regard to structural rigidities that characterize some member countries. Indeed, such reform should put the bloc in a better position to deal with economic shocks. On the other hand, the slow down in housing prices owing to the tight monetary stance has not made matters any easier for the USA economy currently faced with a massive current account deficit which puts future growth prospects at risk. The growth outlook for the US economy is a mild 2.4% for 2007 and a 2.7% for 2008. Generally, most core economies in the OECD will experience an economic slow-down in 2007 followed by a projected mild recovery in 2008.

Figure 1: Growth outlook for core OECD economies



Source: OECD Economic Outlook

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South Africa Economic Outlook

It has been expected that the onset of inflation and the resultant monetary tightening would dampen consumer spending that has driven economic growth in the past three years. On the contrary, current evidence shows that consumers' appetite to spend has remained largely unaffected by the tight monetary policy. Results from monthly retail surveys by the Bureau of Economic Research (BER) have shown a significant growth of 13% in retail purchases for the month of October 2006. This resilience could be attributable to, on one hand a possible increase in consumers' real incomes and perhaps the use of savings given the period (festive season) in which the surveys were taken. Another important factor could be the perceptions of consumers regarding the current level of interest rates (13.75% prime rate) compared to 1998 when the prime-lending rate shot up to 25.50% and thus could feel at ease. Furthermore, while the inflation outlook remain on the upside there is sufficient support in fundamentals that the situation is largely in control by authorities. Oil prices have since stabilised on the lower side whereas the currency's volatility has been within acceptable levels. Indeed, latest figures show a reduction in producer prices whereas the consumer price index (excluding mortgage rates) for December 2006 stood at 5.0% and thus unchanged for three months in a row from October. Therefore, the future behaviour of consumers will in part depend on the extent to which these factors change. On the other hand, the pending infrastructure spending programmes linked to the 2010 World Cup and other projects will further boost consumption through employment creation and related demand for goods and services. As the table below shows, inflation is expected to peak this year before gradually easing off in the next two years accompanied by a relaxation of the monetary stance. Similarly, a mild slow down in real GDP is forecast in the current year before slowly picking up in the two years ahead. While these figures point to a rather favourable position for the economy, there remains an external risk in the form of a record current account deficit.

Table 1 Consensus of Independent Economic Forecasts for South Africa 2007-2009

	2007 (f)	2008 (f)	2009 (f)
Real GDP growth	4.3%	4.6%	4.9%
Inflation (average CPI-X)	5.3%	4.8%	4.6%
Repo rate (year end)	9.08%	8.04%	7.94%
Prime interest rate (year end)	12.58%	11.54%	11.37%
Exchange rate R/US$ (year end)	7.53	7.83	8.05

Notes: (f) Latest consensus forecasts
Source: http://www.ber.sun.ac.za/downloads/2007/consensus/reuters/reuters_jan07.asp

Growth Outlook for the Namibian Economy

Agriculture

The phenomenal run in meat prices seen for much of last year is expected to come to a halt as realignment in South Africa begins to set in. While prices of crops, mainly maize, have shown some resilience, the poor early rains experienced thus far will most likely result in a relatively poor harvest. The same could apply with respect to stock farming as farmers could see it more beneficial to rid themselves of some additional heads as a drought coping strategy. As a result, negative to low growth prospects are foreseen for this sector in the year. Though the sector contributes only about 6% to GDP (as of 2005), the impact thereof should be seen in the context of its contribution to employment representing close to 27% of the total workforce. As such, the expected decline will not only affect production but also aggregate demand in the economy.

Table 2 Real production and annual growth in agriculture

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Commercial (N$m)	602	519	489	495	648	589	723	755	681	753
% Growth	16.3	-13.8	-5.8	1.1	31.1	-9.2	22.7	4.5	-9.9	10.6
Subsistence (N$m)	403	407	420	514	408	310	252	255	338	375
% Growth	13.6	1.1	3.2	22.4	-20.7	-24.0	-18.6	0.9	32.7	11.0

Source: National Accounts 1996-2005, CBS

Fishing

A steady rise in fish prices, coupled with a relatively stable exchange rate and declining energy prices should have brought some relief to the ailing sector in the past year. On the negative side, it has become evident that environmental concerns present a significant challenge to the sector, especially the pelagic sub-sector where no single catch was recorded from the allocated quota in the previous year. The same could be said with regard to the prime hake sub-sector where there has been a significant reduction in quota allocations (see table 3 below). Though oil prices subsided in the past year, OPEC's decision to cut supply could potentially push-up energy prices once again and thus resulting in higher production costs given the sector's dependence on fuel. Altogether, growth prospects are fairly remote as the sector is expected to remain in a recovery mode.

Table 3 Total Allowable Catches

	2000	2001	2002	2003	2004	2005	2006
Pilchard	25,000	10,000	0	20,000	25,000	25,000	25,000
Hake	194,000	200,000	195,000	180,000	195,000	180,000	130,000
Horse Mackerel	410,000	410,000	350,000	350,000	350,000	350,000	360,000
Crab	2,000	2,100	2,200	2,000	2,200	2,300	2,400

Rock Lobster	35	400	400	400	420	420	420
Alfonsino	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Orange Roughy	2,400	1,875	2,400	2,650	2,600	2,050	1,100
Monk	N/A	13,000	12,000	12,500	12,000	11,500	9,500

Source: Ministry of Fisheries and Marine resources

Table 4 Real production and annual growth in fishing

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Fishing (N$m)	482	456	567	559	641	631	703	732	666	643
% Growth	-1.8	-3.6	21.9	-1.4	14.5	-1.5	11.4	4.2	-9.1	-3.4

Source: National Accounts 1996-2005, CBS

Mining

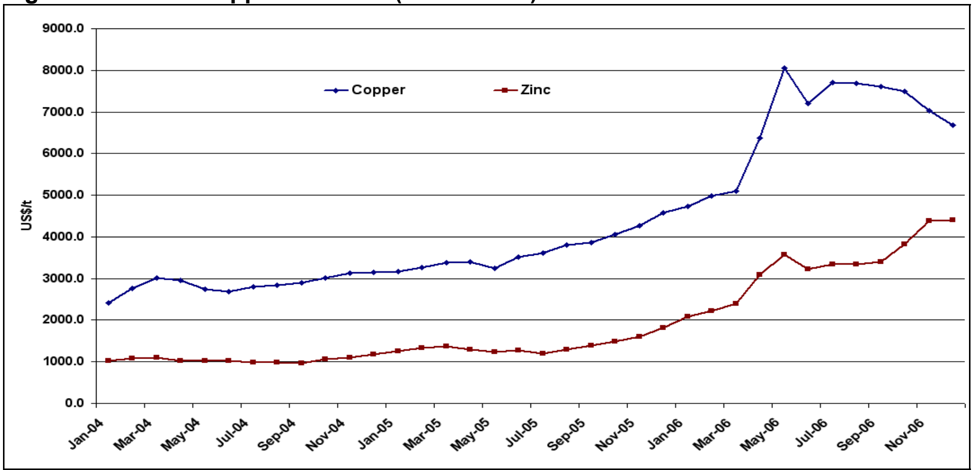
Current developments show that the mining sector will once again remain prominent despite metal prices that have been increasing at a decreasing rate (even a decline in the case of copper) towards the end of the past year. Contributing to this growth will be the expected increase in uranium production following the recent commissioning of the Langer Heinrich mine in early January, as well as an increase in diamond, copper and zinc production coupled with a relatively favourable exchange rate. On the other hand, remarkable growth in uranium prices (with January's average of US$70/lb, from US$37/lb a year ago) has since seen about 20 companies being granted exploration and prospecting licences in the country with two of these[2] in the process of undertaking environmental impact assessment (EIA) studies. Nevertheless, the sector still remains vulnerable to oil costs which could likely push up production costs.

Table 5 Real production and annual growth in mining

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Diamond Mining (N$m)	783	782	793	908	847	803	942	909	1,260	1,208
% Growth	2.6	-0.1	1.3	14.5	-6.7	-5.1	17.3	-3.5	38.6	-4.1
Other Mining (N$m)	317	363	324	303	343	314	355	328	426	450
% Growth	7.5	14.4	-10.8	-6.5	13.3	-8.5	-12.9	-7.5	30.6	5.0

Source: National Accounts 1996-2005, CBS

Figure 2 Price of Copper and Zinc (2004 - 2006)



Source: IJG Business Climate Monitor (2006)

Manufacturing

The fate of the textile industry remains uncertain with the special textile dispensation of the AGOA agreement coming to an end mid-year. Thus as from July this year, countries exporting apparels to the US market under the AGOA arrangement will no longer be allowed to source their input material from third party countries. Such a change is likely to raise the uncertainty regarding the residence of Namibia's top textile exporter, the Ramatex garment factory. Not helping matters will be the expected power cuts as Eskom battles to meet domestic demand which could impact on copper and zinc smelters as well as an expected decline in fish processing due lower catches in fisheries. Given such, the sector could be set for yet another tough year where negative growth is foreseen.

Table 6 Real production and annual growth in manufacturing

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Meat Processing (N$m)	128	92	99	111	101	107	109	97	88	95
% Growth	3.6	-28.3	8.0	12.6	-9.7	6.4	2.1	-11.6	-8.6	7.0
Fish Processing (N$m)	139	262	356	281	241	204	183	277	269	256

[2] These are UraMin Inc (Trekkopje deposit) and Forsys Metals Corp (Valencia deposit).

% Growth	-64.4	88.8	35.7	-21.1	-14.2	-15.3	-10.1	51.1	-3.0	-4.7
Other Food (N$m)	586	654	725	759	774	808	875	872	885	935
% Growth	8.7	11.5	10.9	4.7	1.9	4.4	8.3	-0.3	1.4	5.6
Other (N$m)	372	438	394	364	455	538	648	665	726	671
% Growth	-9.0	17.6	-10.0	-7.5	24.9	18.3	20.5	2.6	9.2	-7.6

Source: National Accounts 1996-2005, CBS

Water and Electricity

As predicted in last year's edition, the expiry of the Nampower - Eskom agreement in 2006 ushered in a new but less favourable contract. Faced with a higher than expected domestic demand, Eskom could no longer afford the luxury of exporting electricity at favourable terms. Among the significant changes is that Namibia is now at the mercy of Eskom with a contract that can be terminated at 24-hour's notice should the supplier be faced with critical shortages to meet its local demand. However, Eskom is set to commission 1050-mega watt-power stations in the Western Cape (among others) to offset peak demand during the approaching winter. Nevertheless, the early bouts of blackouts experienced early this year implies the situation remains unresolved. Such unpredictability means that Namibia remains very vulnerable to power cuts during the course of the year. Similarly, given the dependence of water supply on electricity coupled with the imminent drought, water supply will be largely affected. Therefore, low to moderate growth is expected for the sector.

Table 7 Real production and annual growth in electricity and water

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Electricity and water (N$m)	238	214	223	268	299	228	230	266	278	310
% Growth	-8.3	-10.1	4.3	20.2	11.5	-23.8	1.1	15.6	4.4	11.3

Source: National Accounts 1996-2005, CBS

Construction

The price war that ensued between Holcim and Cheetah Cement seems to have ended in the past year with retail prices now averaging N$55.00, way up from a low seen in late 2005 when prices were deliberately set in the mid N$20s. Furthermore, it is expected that high demand for both cement and steel in South Africa could push up building costs and thereby dampen demand for construction activities. However, the real danger emanates from the fact that virtually all four cement companies in South Africa (from where Namibia currently imports about 25 000 tonnes of cement a month) have to import extra volumes to augment local supply. Such practice brings to fore the impact of the exchange rate as prices are priced in US$ dollars. These developments should see the sector returning to negative territory this year after having had an uphill ride since 2003.

Table 8 Real production and annual growth in construction

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Construction (N$m)	416	367	423	364	344	527	459	564	570	588
% Growth	15.4	-11.8	15.3	-43.9	-5.4	53.1	-13.1	22.9	1.2	3.2

Source: National Accounts 1996-2005, CBS

Wholesale and retail trade

The cost-induced inflation that dominated the economy the past year is expected to ease. However, it is expected that the concomitant rise in interest rates should dampen consumer buying in the year ahead. Nevertheless, the customary resilience of the sector should see it remaining in positive territory where moderate to high growth is expected. Indeed, as seen in the table below, the sector has often withstood testing times including the high interest environment that spanned over six years from the late 1990s to the first three years of the new century.

Table 9 Real production and annual growth in wholesale and retail trade

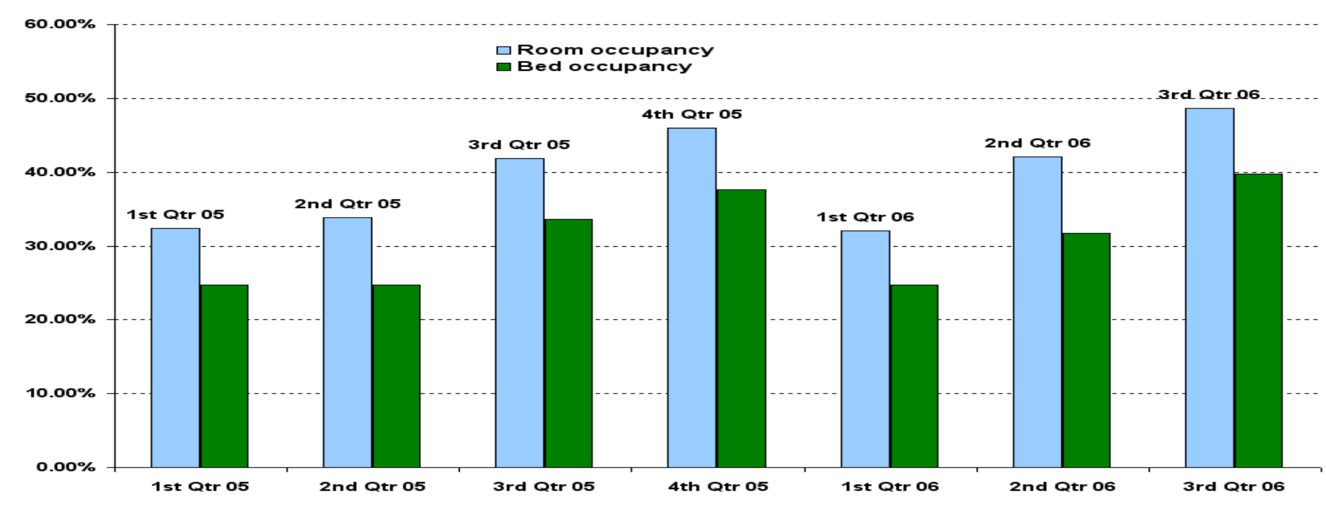
	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Retail and Trade (N$m)	1,179	1,248	1,336	1,380	1,455	1,496	1,607	1,674	1,801	1,942
% Growth	9.5	5.9	7.1	3.3	5.4	2.8	7.4	4.1	7.6	7.8

Source: National Accounts 1996-2005, CBS

Hotels and restaurants

A recovery witnessed in 2006 (Figure 4) should continue in the year ahead. Supporting this trend will be a rather stable exchange rate, lower energy prices and stability in the region.

Figure 3 Quarterly average room and bed occupancy at HAN members (2005-2006)



Source: Hospitality Association of Namibia

Namibia's Tourism Satellite Account in perspective

The results of a landmark study namely; the Tourism Satellite Account, commissioned early last year were finally presented to stakeholders in September 2006. The project looked at the "impact of travel and tourism on jobs and the economy" by examining not only the direct but also the indirect contribution of tourism sector to the economy as the sector is highly intertwined with almost all-economic activity. Illustrating this point, the study found that though the sector would directly account for 3.7% of GDP and 4.7% total employment in 2006, these shares would rise to 16% and 17.7% respectively if indirect contributions were included. The study further predicts that the sector would be contributing about 22.9% (both directly and indirectly) to the economy by 2016 and accounting for 20.7% of total employment. Two issues are noteworthy; firstly, the results show the latent contribution and importance of the sector to the Namibian economy, which might have been overlooked in the past. Secondly, the high integration of the sector could be cause for concern since it reveals the sector's sensitiveness to changes in the economy. Altogether, this calls for concerted efforts towards consolidating the sector particularly aimed at ways to mitigate shocks and fluctuations in the sector. On the negative side, given that only 2006 and 2016 years are included in the forecasts, the usefulness of the study as a monitoring and evaluation tool is limited. Similarly, the fact that the 2016 forecasts do not take into account the impact of the 2010 Soccer World and the African Nations Cup in neighbouring South Africa and Angola respectively should rank as a major drawback.

Transport and communication

An expected broadening of the customer base resulting from increased competition due to the launch of a second cellular network (Cell One) as well as new services offered by both MTC (credit card and 3G technology) and Telecom (Switch, ADSL and other technologies) should further see the post and telecommunication sub-sector registering higher growth. Nevertheless, the relatively restrictive monetary environment should be seen as a notable threat to demand for services. On the other hand, the impact of fuel costs will continue to exert pressure on the transport sub-sector, and thus low growth is expected.

Table 10 Real production and annual growth in transport and storage and post and telecommunications

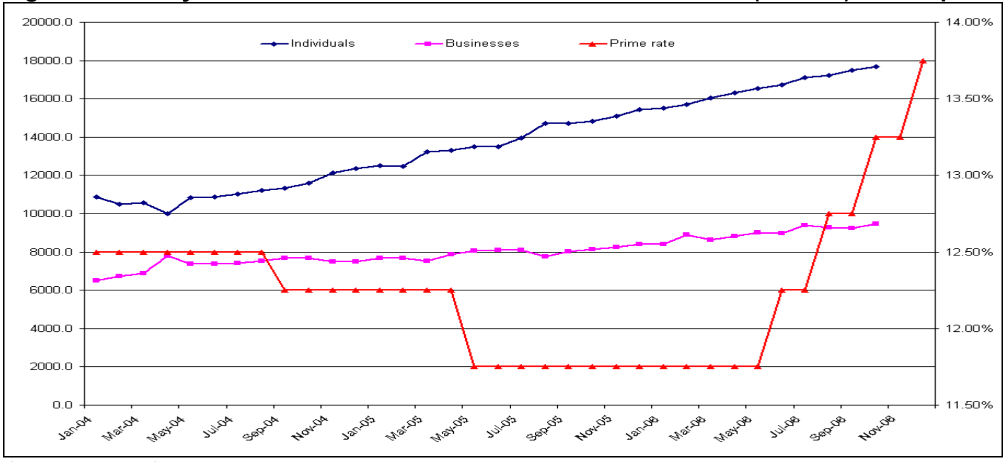
	1996	1997	1998	1999	2000	2001	2002	03	04	05
Transport and Storage (N$m)	655	673	533	631	671	725	837	753	816	835
% Growth	3.1	2.8	-20.8	18.4	6.3	8.1	15.5	-10.0	8.4	2.2
Post and Telecommunications	239	289	329	337	379	471	494	619	720	836
% Growth	10.7	20.8	14.0	2.3	12.4	24.3	5.0	25.2	16.3	16.1

Source: National Accounts 1996-2005, CBS

Financial intermediation

Unlike in previous years, no major losses are anticipated from floods this year and thus the insurance industry, which was hard hit in 2006, should see some relief. Similarly, the launch of new financing avenues and the continuous financial innovations should see the sector post significant growth in the year. However, though credit extended to both private individuals and businesses show no signs of declining (see graph below), increasing building costs as well as high property prices together with monetary tightening are foreseen as real threats to credit demand.

Figure 4 Monthly credit extensions of Namibia commercial banks (N$ '000) for the period 2004/06.



Source: Bank of Namibia (2006)

Table 11 Real production and annual growth in financial intermediation

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Intermediation (N$m)	380	423	450	461	489	498	514	564	646	788
% Growth	16.9	11.4	6.5	2.4	6.2	1.7	3.3	9.6	14.6	22.0

Source: National Accounts 1996-2005, CBS

Producers of government services

A windfall from the sale of equity, a 34% stake in MTC to a Portuguese firm, and other revenues should see the government meeting its forecast for a surplus in the ending financial year. Also, the expected growth in the mining sector as alluded to earlier, coupled with the current rush for uranium exploration could provide government with additional funds. On the other hand, the challenges of the education system and the need to stimulate employment creation will see government returning to the traditional norm of deficits in the next financial year. Currently, the newly created Ministry of Veterans Affairs has not yet pronounced itself with regard to activities and span of responsibilities to be undertaken once fully operational. In the same vein, the imminent energy crisis could induce government to up its investment into the envisaged Kudu Gas plant to which it has already committed resources during the previous budget with more resources likely to follow this year.

Table 12 Real production and annual growth in government services

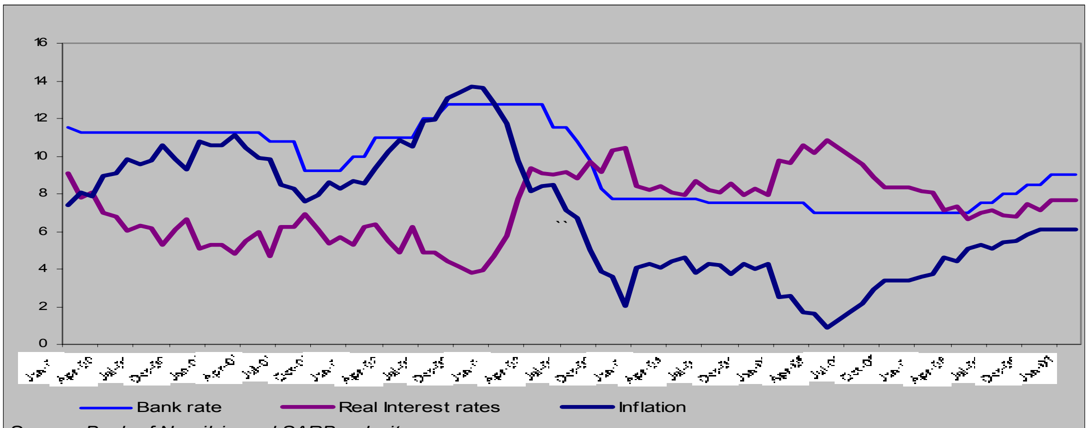
	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Government (N$m)	2,876	2,980	3,060	3,162	3,236	3,281	3,408	3,475	3,663	3,842
% Growth	3.5	3.6	2.7	3.4	2.3	1.4	3.9	2.0	5.4	4.9

Source: National Accounts 1996-2005, CBS

Price developments

It is almost unthinkable that not so long ago inflation rates were exceeding 10% (November 2002) with nominal interest rates hovering at similar levels. However, the beginning of 2003 saw a drastic fall in both nominal interest rates (bank rate) and the inflation rate. It is interesting to note that a trend reversal occurred in real interest rates (prime minus inflation) around the same time. The period of low inflation and interest rates halted during 2006, with the central bank raising interest rates on four occasions during 2006. Should current conditions persist, very little in the form of relief should be expected in the coming three quarters as authorities tread cautiously. Barring any pick-up in energy costs and a depreciating exchange rate, a mild relaxation in the monetary stance is foreseen in the fourth quarter.

Figure 5: Development in inflation and interest rates (Jan 2000 to Jan 2007)



Source: Bank of Namibia and SARB websites

Overall GDP growth
Once again the mining sector is expected to take centre stage, with support from financial intermediation and wholesale and retail trade sectors as well as the post and telecommunication sub-sector in driving economic growth this year. Not much will be expected from the fishing and hotels and restaurant sectors as they continue on the path of recovery, whereas the construction, manufacturing and agriculture will most likely experience some contraction. Overall the economy is foreseen to grow in the range of 3 – 3.5% for 2007. Of course, a growth rate of 3% is not going to have much effect on the employment front as discussed below.

Finding economic growth that creates jobs is a critical challenge for Namibia

Job creation has been one of the core development objectives since independence but it seems that we have very little to celebrate. The economy is projected to grow at around 3—3.5% for 2007. However, the Namibian economy has not been very good at creating jobs since independence according to several rounds of labour force and household surveys. For example, in 1993 of the total labour force of 521,821 only 350,280 were employed. More than a decade later, the labour force grew to 608,610 with only 385,329 people in employment. Moreover, the numbers of discouraged job seekers have increased from 87,143 in 1993 to 115,162 in 2004.

Despite economic growth of 60% between 1993 and 2004, employment only grew by 10%. This suggests that there is a mismatch between the type of growth we have experienced so far and job creation. We have calculated the target employment growth rates (TGR's) and employment absorption rates (EARs) as useful measures to assess and explain labour market performance and trends in the context of the expanding labour force. The target employment growth rate (TGRs) measures how fast employment should have expanded over a certain period to provide work for all new entrants to the labour market. This growth rate is independent of the rate or level of unemployment in the base year, because it captures the growth rate required to provide employment only to new entrants. The employment absorption rate on the other hand answers the question "by how much did employment growth miss the target growth rate?" In this instance we are simply comparing actual employment growth and the target rate. If all net labour force entrants are absorbed into employment, the EAR will be zero. Where only some net labour force entrants find jobs, the EAR is less than 100, while a reduction in the absolute level of unemployment is associated with an EAR greater than 100. How does the TGR and EAR for Namibia look like for the period 1993 to 2004 using the broad definition of unemployment?

Figure 6: Employment target growth rates and employment absorption rates, 1993-2004

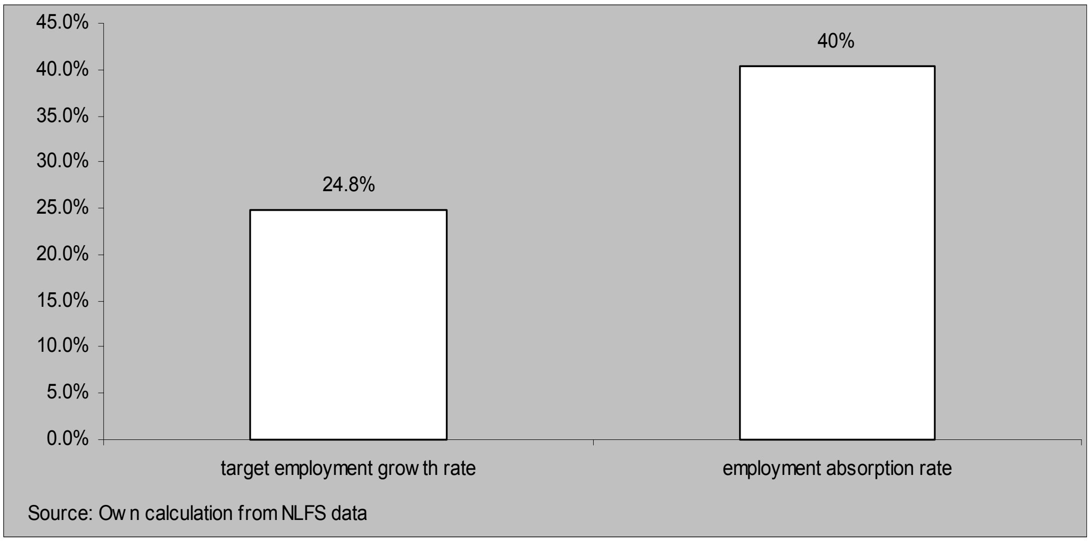


Figure 6 presents estimates of the TGR and the EAR for Namibia for the period 1993-2004. The TGR is estimated at 25% for this period, meaning that employment should have grown by 25% between 1993 and 2004 rather than the 10% with which it grew to provide jobs to all new entrants, thus keeping unemployment constant. This means that the EAR for the period under consideration was only 40%. These two measures show that employment growth has been insufficient to absorb new entrants.

The next measure is to see to what extent employment growth is responsive to economic growth. To this end we have calculated the elasticity of employment with respect to GDP growth. This measures the observed impact of GDP growth on employment growth. We find that employment growth is virtually non-responsive to changes in economic growth with an elasticity of 0.17%. This means that for every one percent rate of growth in GDP, employment grew by 0.17% between 1993 and 2004, all other things being equal.

Therefore a critical policy question is: "where has all the growth gone if not to creating jobs?" We believe that this should be a priority question all policy makers for 2007.

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