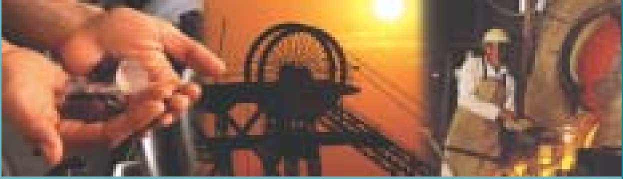


Economy

South Africa has achieved a level of macroeconomic stability not seen in the country for many years. Such advances create opportunities for real increases in expenditure on social services, and reduce the costs and risks for all investors, laying the foundation for increased investment and growth.

The economy is stronger than at any time in the past 20 years. It expanded by about 5% in 2005 and continued growth at about 5% a year over the period ahead is anticipated.

Business confidence remains strong, investment and employment creation are gaining momentum, and inflation and interest rates remain moderate.

Accelerated and Shared Growth Initiative for South Africa (AsgiSA)

Government's AsgiSA aims to ensure that economic growth is accelerated to at least 4,5% in the next five years (2005 to 2009) and about 6% between 2010 and 2014. This will assist in halving unemployment and poverty by 2014.

AsgiSA includes developing infrastructure to upgrade and build railway lines, harbours, ports and roads from 2005 to 2009.

With South Africa's unemployment rate at 26,7% by February 2006, the infrastructure programme is geared towards creating and sustaining jobs.

Overall government expenditure for infrastructure spending totals some R410 billion between 2007 and 2010. Of this, about 40% will be spent by public enterprises, mostly Eskom (R84 billion covering energy generation, transmission and distribution) and Transnet (R47 billion, of which R40 billion will go towards harbours, ports, railways and petroleum pipelines).

Airports Company South Africa will spend R5,2 billion, which includes airport improvement and the Dube Trade Port, while R19,7 billion will go towards water infrastructure.

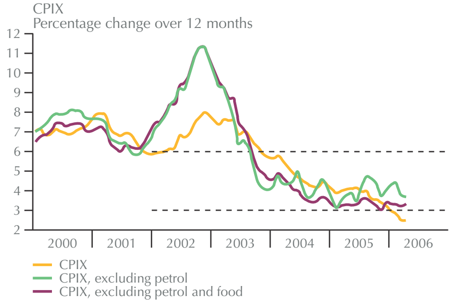
Because South Africa will host the 2010 Soccer World Cup, existing stadiums will be improved or new ones built, and an investment will be made in the environment around stadiums and access to these venues.

Joint Initiative for Priority Skills Acquisition (Jipsa)

On 27 March 2006, Deputy President Phumzile Mlambo-Ngcuka launched Jipsa, the skills empowerment arm of AsgiSA.

AsgiSA has identified six factors that constrain economic growth. One of these is the shortage of skilled labour.

Jipsa is a two-tiered structure comprising a joint task team and technical working group. The joint task team has the task of unblocking the acquisition of targeted skills, overseeing the work of Jipsa and ensuring that it delivers on its mandate of acquiring scarce and priority skills in the shortest possible time, building partnerships with different institutions and ensuring that Jipsa initiatives are sustainable.



Source: *Quarterly Bulletin*

Based on AsgiSA's priorities, Jipsa's work areas are:

- high-level world-class engineering and planning skills for the network, transport, communications and energy industries
- city, urban and regional planning and engineering skills desperately needed by South African municipalities
- artisan and technical skills, with those needed for infrastructure development enjoying priority
- management and planning skills in education, health and in municipalities
- teacher training in Mathematics, Science, information communications technology (ICT) and language competence
- specific skills needed by priority AsgiSA sectors starting with tourism- and business-process outsourcing and cross-cutting skills needed by all sectors, especially financial and project managers
- skills relevant to the local economic development needs of municipalities, especially developmental economists.

Jipsa will support citizens who are trapped in the Second Economy, giving them a chance to participate in the First Economy and in the growing South African economy in general. Jipsa aims to boost empowerment through education.

Domestic output

Real domestic production responded positively to the growth in real expenditure and registered a growth rate of 4,9% in 2005. This not only compares favourably with the growth in real gross domestic product (GDP) of 4,5% recorded in 2004, but is also the highest growth rate since 1984.

On a quarterly basis, real economic growth lost some momentum in the second half of 2005 and decelerated from an annualised rate of 4,2% in the third quarter of 2005 to 3,3% in the fourth quarter. The diminished performance in the final quarter of 2005 mainly reflected a decline in the real value added by the primary sector and slower growth in the real value added by the secondary sector.

For 2005 alone, the tertiary sector experienced the strongest growth among the major production sectors. Within the tertiary sector, the finance sector registered the highest rate of increase in real value added, consistent with the increase in the real value added by securities dealers throughout 2005. In the primary sector, agriculture output increased in 2005, following a contraction in 2004. The increase in real value added in mining was maintained at 3% in 2005 alone. Real value added by the secondary sector expanded by roughly 4% during 2005, after recording a rate of 5% in 2004.

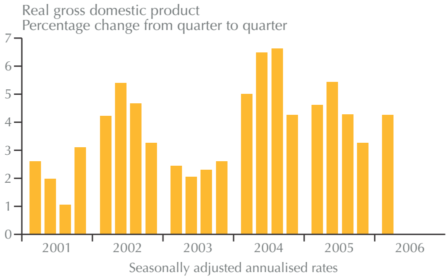
Domestic expenditure

Within an environment characterised by rising income and the lowest inflation and nominal interest rate levels encountered in more than 20 years, all the major components of real domestic final demand rose strongly in 2005.

Growth in aggregate real gross domestic expenditure slowed considerably from an annualised rate of 7,4% in the third quarter of 2005 to 3,9% in the fourth quarter. A substantial slowdown in the pace of inventory investment more than countered a marked acceleration in real domestic final demand – real final consumption expenditure by households and by general government, and real gross fixed capital formation. The level of real gross domestic expenditure was 3,9% higher in 2005 than in 2004.

Growth in real final consumption expenditure by households accelerated from 6,1% in the third quarter of 2005 to an annualised rate of 6,8% in the fourth quarter. The buoyancy in consumer spending was also reflected in a year-on-year growth rate of 6,9% in 2005 compared with a growth rate of 6,5% recorded in 2004.

Nevertheless, growth in real household expenditure for 2005 amounted to 7% compared with an increase of 6,5% in 2004. This



Source: South African Reserve Bank

was the highest annual growth rate in real consumption expenditure by households registered since 1981.

Factors that underpinned strong household spending in 2005 included:

- an increase of 6,6% in real household disposable income in 2005, partly due to wage settlements that remained above the contemporaneous inflation rate and income tax rates, which were lowered marginally
- the ratio of debt-service payments to disposable income that remained relatively low throughout 2005 at 6,6%
- the high levels of consumer confidence recorded in 2004, previously observed in 1997
- the wealth effects arising from the exceptional increase in property and other asset prices.

Price inflation

In recent years, there has been remarkable progress in lowering South Africa's inflation rate to levels more consistent with those of its main trading partners.

Overall consumer price inflation decelerated markedly from a high of 9,2% in 2002; to 5,8% in 2003; 1,4% in 2004; and 3,4% in 2005, which was the lowest rate of increase since 1962. The year-on-year rate of increase in the consumer price index (CPI) for metropolitan and other urban areas, less mortgage interest cost (CPIX), decelerated to within the inflation target range of 3% and 6% in the 30 consecutive months to February 2006.

During the recent period, price inflation decreased mainly due to the substantial appreciation in the Rand's exchange rate since the second half of 2002. Additional factors that contributed to the drop in inflationary pressures were:

- the consistent application of prudent fiscal and monetary policies
- low increases in food prices over an extended period
- a progressive deceleration in inflation expectations.

A further moderation in price inflation in South Africa was prevented recently in line with mounting concerns in the international community over the inflationary effects of the increase in commodity prices, particularly crude oil.

Year-on-year CPIX inflation rose from 4% in December 2005 to 4,3% in January 2006 and 4,9% in February 2006. Contributors to the last figure included annual increases in the price indices for transport, food, medical care and health expenses, and housing, excluding the interest rate on mortgage bonds.

The annual rate of increase in food prices was 4,4% in January 2006 and 4,7% in February 2006.

Year-on-year headline inflation or the CPI was 4% in January 2006 and 3,9% in February 2006.

Exchange rates

The weighted average of the Rand, which appreciated by 11,7% between the end of December 2003 and the end of December 2004, depreciated by 2% between the end of December 2004 and the end of December 2005.

The decline in the external value of the Rand coincided with a widening in the deficit on the current account. The trade weighted exchange rate of the Rand displayed notable fluctuations during 2005, having depreciated by 9% during the first half of the year before recovering nearly all the lost ground during the second half.

The external value of the Rand strengthened by 1,8% and 0,3% in January and February 2006 respectively before depreciating by 1,1% in March. From the end of December 2005 to the end of March 2006, the nominal effective exchange rate of the Rand appreciated by 1%.

Foreign trade and payments

Strong domestic production and expenditure in 2005 were accompanied by buoyant demand for imports.

For the year as a whole, the volume of merchandise imports rose by 11%. Over the same period, merchandise export volumes expanded by 8,5%, consistent with the solid performance of the world economy. Both the trade deficit and the deficit on the service income and current transfer account widened in 2005, resulting in a deficit on the current account of the balance of payments amounting to R64,4 billion from R47,5 billion in 2004. As a ratio of GDP, the deficit rose to 4,2% in 2005.

The value of merchandise exports which increased by 8,7% in 2004 advanced by 13,8% in 2005. This increase could be partly attributable to higher volumes of exported goods, which amounted to 19,9% of GDP. The increase of 4,7% in the Rand prices of merchandise exports following the vigorous surge in international commodity prices also boosted the earnings of South African exporters.

The value of mining products, and agricultural and manufactured goods rose by 18,9%, 11,4% and 11,2% respectively. Increases were most noted in the subcategories for mineral products, platinum-group metals, machinery and electrical equipment, vehicle and transport equipment and chemical products.

The widening of the current account deficit in 2005 was also caused by a further decrease of 5,8% in the value of net gold exports from R28,7 billion in 2004 to R27 billion in 2005. The lower value of net gold exports resulted from a decline of 12,5% in the volume of gold exported. This drop was, however, partially offset by an increase in the price of gold. Despite the appreciation of the external value of the Rand in 2005, the average realised Rand price of gold increased by 7,5% after having decreased by 4,5% in 2004. On the London market, the average fixing price of gold rose by 8,7% from US$409 to US$445 over the period.

South Africa recorded substantial inflows of capital on the financial account of the balance of payments during 2005. An inflow amounting to R98,4 billion was recorded during the year, which was the highest annual inflow ever recorded in a calendar year.

Trade relations

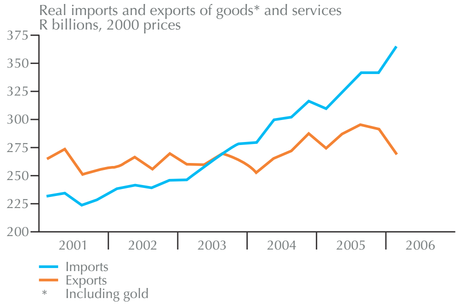
Internationally, open economies with an export base perform much better in terms of economic growth than closed economies. Increasingly, production is becoming globally integrated, and South Africa forms a vital part of international supply chains.

Therefore, dismantling barriers to trade, especially those faced by South African exporters, is a critical component of any economic strategy that promotes sustainable growth.

Africa's economic development

South Africa's global economic strategy focuses on Africa and a strong development agenda. Partnerships with countries on the continent are therefore considered vital and strategic. South Africa's economy is inextricably connected to that of the southern African region, and its success is linked to the economic recovery of the continent through the New Partnership for Africa's Development (Nepad).

Africa is an important market for South African exports. In 2003, about 23% of South Africa's exports were destined for the continent. There was a huge increase in imports from the continent. In 2003,



Source: *Quarterly Bulletin*

only 4% of total imports came from Africa. However, this increased to 40% in 2004.

This trade imbalance has largely been offset by South Africa's investment on the continent, aimed at infrastructural projects designed to enhance the productive capacities of African economies. Besides forging bilateral trade and economic relations, the Department of Trade and Industry is committed to increasing South Africa's involvement in large capital projects on the continent. The following areas have been prioritised:

- infrastructure and logistics (roads, ports, etc.)
- energy and ICT
- water and waste management
- transport
- construction
- oil and gas infrastructure
- agri-business
- mining
- human resource development.

During meetings of the World Economic Forum for southern Africa, the formation of a business forum for southern Africa was announced (a joint initiative between the Department of Trade and Industry and the private sector). It was established to take advantage of investment opportunities in the region.

The department, through Trade and Investment South Africa, has established trade- and investment-promotion offices in Egypt, Nigeria, Ghana, Kenya, Ethiopia, Tanzania, Zimbabwe, the United Arab Emirates, Saudi Arabia and Angola to facilitate trade and investment flows. More were expected to be opened.

New Partnership for Africa's Development

The Department of Trade and Industry provides supportive services to Nepad, which has a critical role in accelerating trade and economic development on the continent to alleviate poverty, which is Nepad's primary objective.

The department aims to contribute to the Nepad agenda by mobilising the necessary support from relevant stakeholders internally and externally, and providing leadership and strategic guidance on trade and economic issues. It also contributes to the national project co-ordinated through the African Renaissance Cluster on the formulation of a national response to Nepad through the Nepad Implementation Strategy of South Africa.

Southern African Development Community (SADC)

The SADC comprises Angola, Botswana, the Democratic Republic of Congo, Lesotho, Malawi, Mauritius, Mozambique, Namibia, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe. Madagascar submitted an application for membership during the SADC Heads of State Summit, held in Mauritius during August 2004, and was granted permanent membership in August 2005.

Since attaining democracy in 1994, South Africa has put regional integration by SADC member states on the top of its foreign economic agenda. This approach follows from the belief in the economic benefits that can be brought to all member states by closer economic co-operation in the region. To support this approach, South Africa has reviewed its trade relationship with other SADC members, adopted the SADC Trade Protocol, promoted investment by South African firms in the SADC and helped to facilitate greater volumes of trade by South Africa and other SADC members.

Europe

Trade relations with Europe, particularly with the European Union (EU), are pivotal to South Africa's economic development. The Trade, Development and Co-operation Agreement with the EU forms a substantial element of South Africa's reconstruction and development efforts.

Europe remains South Africa's largest trading region and source of investment. In 2005, Europe accounted for 38,9% (R116,94 billion) of South Africa's total exports, and 40,3% (R140,448 billion) of its total imports. During the same year, the EU accounted for the bulk of this trade, with exports to the EU reaching R106,465 billion in 2005 (up from R93,426 billion in 2004), and imports reaching R128,360 billion in 2005 (up from R121,064 in 2002).

Six European countries are among South Africa's top 10 export destinations, and four European countries are among the top 10 countries from which South Africa's imports originate. In 2005, South Africa's imports from Germany, South Africa's largest source of imports, totalled R49,197 billion. The United Kingdom (UK) remains South Africa's largest export destination in Europe. Exports to the UK amounted to R32,377 billion in 2005.

The formal, non-agricultural sectors created 158 000 jobs in 2005, a 2,2% improvement on 2004, bringing the number of people employed in the formal economy, excluding farming, to 7 255 million in 2005, compared with 7 097 million in 2004.

United States of America (USA)

The USA is South Africa's number-two trading partner in terms of total trade (the sum of exports and imports) recorded in 2005. Exports to the USA increased marginally in nominal terms from R30 billion in 2004 to R31 billion in 2005. Imports from the USA also recorded a paltry increase in nominal terms from R26 billion to R27 billion from 2004 to 2005. Since 2000, the trade balance has been in South Africa's favour, with the trade surplus increasing in nominal terms from R3,5 billion to R4,1 billion between 2000 and 2005.

South Africa is a beneficiary of the USA's Generalised System of Preferences (GSP), which grants duty-free treatment for more than 4 650 products, and benefits from the Africa Growth and Opportunity Act (AGOA), which was promulgated in May 2000. In terms of the AGOA, 1 783 more products were added to the existing GSP product list. Although the AGOA was initially due to lapse in 2008, the US Government met African countries' requests for it to run to 2015 under what is called the AGOA III amendments.

The AGOA also allows duty-free entry of clothing and selected textiles into the USA, subject to certain criteria and policy reforms.

Canada

Canada is South Africa's second-largest trading partner in North America. Since the lifting of sanctions in 1994, bilateral trade between South Africa and Canada increased from R904 million in 1993 to R4,7 billion in 2005.

The number of South Africans with incomes below R250 per month declined from 18,5 million in 2000 to 15,4 million in 2004, while those with higher incomes rose from 26,2 million in 2000 to 31 million in 2004. Between 1994 and 2004, and mostly within the period 2000 to 2004, the real income of the poorest 20% of South Africa's population increased by 30%.

South Africa benefits from Canada's General Preferential Tariff (GPT). GPT rates range from duty-free to reductions in the Most Favoured Nation rates. South Africa also has a memorandum of understanding (MoU) with Canada relating to the export of clothing and textile products to that country. It allows a certain amount of South African clothing and textile products to enter the Canadian market at a better than Most Favoured Nation rate. The Trade and Investment Co-operation Arrangement, signed in 1998, enhances bilateral and trade investment.

Latin America

South Africa's major trading partners in Latin America are Brazil, Argentina, Chile, Mexico, Colombia and Peru. Most trade is with Brazil and Argentina, which are members of the Mercusor trade bloc. A framework agreement committing South Africa and Mercusor to a free trade agreement was signed in 2000. However, as a first step towards achieving this goal, the parties signed a preferential trade agreement (PTA) in December 2004. Upon ratification by all signatories, the PTA will offer businesses from both sides preferential access to a broad range of product lines. Trade between South Africa and Mercusor grew substantially from R2,7 billion in 1994 to R14,5 billion in 2005. South Africa recorded a trade deficit of about R8,5 billion against the bloc for 2005. From 2002 to 2005, about 62,5% of total trade between South Africa and Mercusor was with Brazil.

South and south-east Asia and Australasia

India is a key partner for South Africa in South Asia and total trade has been increasing rapidly since 1994. According to the latest figures, two-way trade between the two countries reached R14,42 billion in 2005. South Africa and India are fostering closer economic ties through initiatives such as the Joint Ministerial Commission and the India-South Africa Commercial Alliance.

South Africa co-operates with India in areas of common interest in the World Trade Organisation and other fora, and works closely in the India-Brazil-South Africa (IBSA) Forum. IBSA is not only an economic initiative but also an undertaking by countries with shared interests in a multilateral system that equitably addresses political, social and economic matters. South Africa and India co-operate in the G20, a grouping of developing countries that seeks to address developmental challenges in the global economic system.

Bilateral trade with south-east Asia, particularly the Association of South-East Asian Nations (Asean) members, increased rapidly from a low base from 1990. Asean presents South Africa with a potential market in excess of 520 million people. South African total trade with Asean totalled R25,72 billion in 2005, and is set for continued growth. Within Asean, key partners for South Africa include Singapore, Thailand, Indonesia, Malaysia, Vietnam and the Philippines.

North-east Asia

Economic and trade relations between South Africa and the People's Republic of China have grown rapidly since the formal establishment of diplomatic relations. Total trade grew from R5,3 billion in 1998 to R40,2 billion in 2005.

Japan is South Africa's largest trading partner in Asia and became the country's primary export partner in 2005 with total trade reaching R56,9 billion in 2005.

Australia is another important market for South Africa with total trade reaching R17,05 billion in 2005.

Economic transformation

Small is big

Government's National Strategy for Small Business aims to boost small enterprises, equalise income and wealth and create long-term jobs. Fostering entrepreneurship among women is a particular focus.

Developing small, medium and micro enterprises (SMMEs) has attracted increasing attention in South Africa in recent years, as an engine for general economic growth, and for employment creation and equity acceleration.

The Department of Trade and Industry launched the Small Enterprise Development Agency (Seda) in December 2004.

Seda, which provides non-financial support to small and medium enterprises (SMEs), was formed by merging the Ntsika Enterprise Promotion Agency and the National Manufacturing Advisory Centre. It aims to:

- improve geographic outreach
- achieve the desired impact on small enterprises
- provide a single access point for small enterprises
- be inclusive of all relevant stakeholders
- leverage resources in service delivery
- optimise resource usage
- align government's service-delivery strategy coherently.

National Empowerment Fund (NEF)

The NEF was established by the NEF Act, 1998 to promote and facilitate economic equality and transformation. The fund received R150 million in 2004/05 and R400 million in 2005/06.

The NEF leverages its funding by setting up strategic alliances with other private-sector financial institutions to further increase funding for Black Economic Empowerment (BEE).

It operates at several different levels, providing finance and business support to rural women and fledgling entrepreneurs, and large-scale financial support to BEE groups.

The fund's new products and services include the Group Entrepreneurial Schemes Division (loans and equity finance to BEE SMEs from R250 000 to R10 million), Market Making (finance for larger BEE transactions in capital markets, warehousing and strategic projects) and BEE Retail Investment (promoting historically disadvantaged individuals' savings and access to listed equities through new product offerings in design phase).

The NEF partners business organisations that focus on serving women. It deploys its resources to optimise the empowerment dividend to government and provides pre- and post-investment management assistance.

The NEF's funding comprises a hybrid of loans and equity, and is designed to lower the cost of capital for BEE participants. This approach to BEE funding is aimed at overcoming existing funders' traditional risk aversion.

Industrial Development Corporation (IDC)

In forming SMEs, the IDC has an increasingly important role in supporting and assisting with venture capital. The IDC has three operational and client-oriented divisions, namely Services Sectors, Industrial Sectors and Projects.

IDC collaboration with the EU and the European Investment Bank on the Risk Capital Facility enabled it to reach more black-empowered SMEs. This facility was used in 15% of IDC deals.

Some of the highlights in 2005/06 included the following:

- 26 000 jobs created through financing activities
- competitive financing for development schemes of R1 billion
- 69% of the total number of approvals were for SMEs
- R370 million of approvals would directly benefit townships mainly through investments in telecommunications, food-retail industries and tourism
- increased strategic focus on maximising development impact in rural and regional development
- 150 financing approvals to the amount of R4,2 billion.

Business Partners Limited

Business Partners Limited is a specialist investment group, providing customised investment, mentorship and property-management services to SMEs in South Africa.

In March 2006, Business Partners launched two new specialist investment funds, the Business Partners Empowerment Fund and the Business Partners Tourism Fund. Business Partners will be investing R6,6 billion into entrepreneurial enterprises over the next five years.

During its first 25 years of existence, Business Partners invested R6,9 billion into the country's SMEs. A further R6,6 billion was invested through Business Partners' three geographical investment funds, as well as through a number of specialist funds, some of which are joint ventures with government bodies and other organisations. These include the Business Partners-Khula Start-Up Fund and the Business Partners Umsobomvu Franchising Fund.

State-owned enterprises (SoEs)

The Department of Public Enterprise is responsible for overseeing SoEs, to ensure that they:

- facilitate economic growth by locating them in optimal industry structures and ensuring the efficiency of their operations and the economic effectiveness of their investment programmes
- play a leadership role in the economy in terms of corporate governance and the implementation of national policy
- catalyse sector and regional economic development opportunities.

Expanded Public Works Programme (EPWP)

The EPWP celebrated its first anniversary in April 2005. It is the largest job-creating initiative to be undertaken by government.

The EPWP is operational in all nine provinces. Projects include the construction of rural or low-volume roads, water and sanitation trenches and sidewalks.

South Africa has a significant small business sector with some two million small businesses representing 98% of all firms. Collectively, small enterprises employ 55% of the country's labour force and contribute about 43% to the total wage bill. However, 87% of small businesses are survivalist, with the great majority being black-owned and 41% owned by women.

The Company Registration Index shows that the share of business held by small firms is increasing. In the 2006 calendar year alone, by the end of May 2006, the Companies and Intellectual Property Registration Office had recorded 19 050 company and 88 086 close corporation registrations. This represented an annual increase of 2,7% and 13,7% respectively.

Registrations of co-operatives totalled 4 843, representing an annual increase of 207%.

Overall, new registrations are in the business services, trade and financial sectors, followed by community and social services and the construction industry.

In addition, government will increase spending on the maintenance of schools, clinics and other government buildings. EPWP projects will also be launched in the area of home-based care for people affected by HIV and AIDS, childcare projects, and in environmental projects like LandCare and clearing alien vegetation from river banks.

By June 2006, the EPWP was on course to deliver on its mandate. It had surpassed its employment-creation targets across four

Trade unions in South Africa

Year	Registered trade unions	Trade union membership	Registered employers	Bargaining councils
2001	485	3 939 075	265	73
2002	504	4 069 000	270	62
2003	369	3 277 685	239	56
2004	341	3 134 865	229	58
2005	335	2 935 864	226	58

Source: Department of Labour

sectors, with more than 301 000 work opportunities created. On average, 52% of beneficiaries were female and 38% youths.

The greatest number of job opportunities were created in KwaZulu-Natal, which had 66 317 beneficiaries, of which 33% were youths and 0,3% were people with disabilities. The province also had the highest number of female beneficiaries in the country at 62% and, at R126 million, the highest wage payout.

Of the youths employed by the EPWP, 51% were in Mpumalanga, 48% in the Free State, 46% in Gauteng, 44% in North West and 40% in the Western Cape.