

# World Economic Situation and Prospects

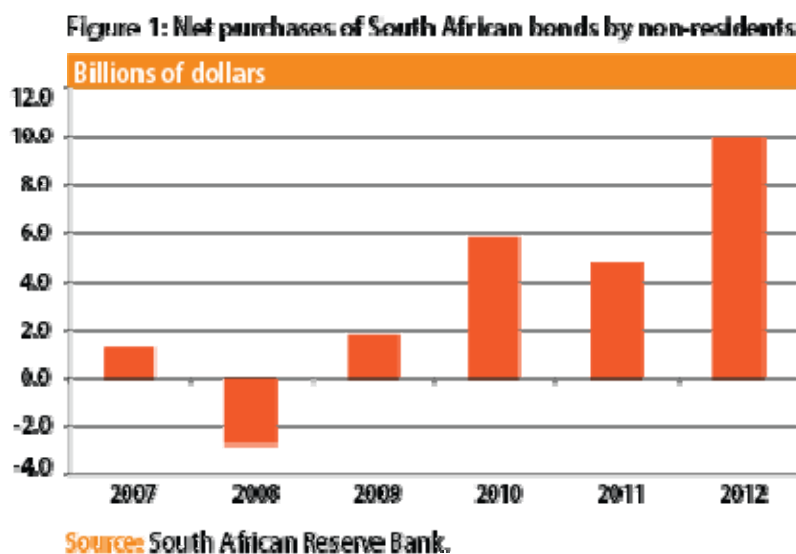
## Weekly Highlights

Prepared by: Matthias Kempf

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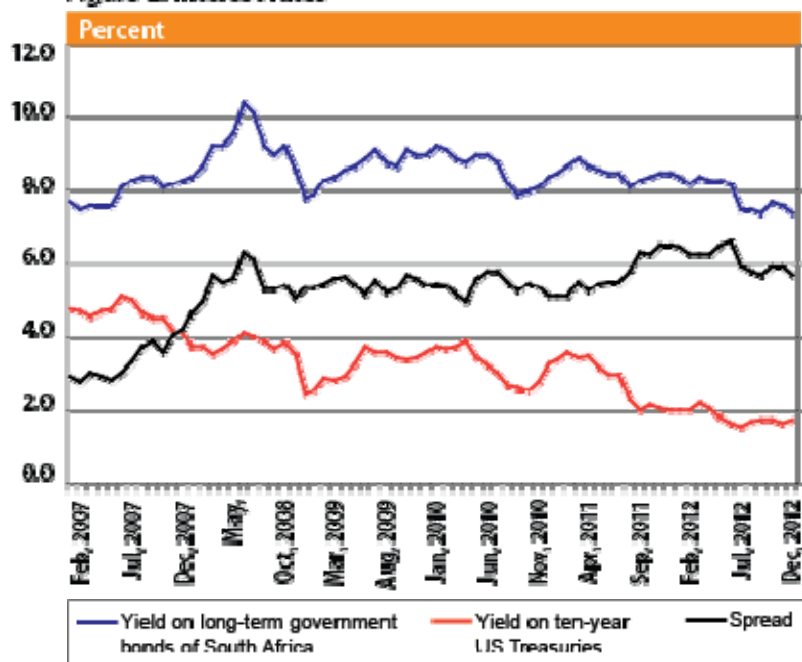
### South Africa: strong bond investment inflows in 2012

Net purchases of South African bonds by non-residents more than doubled in 2012 from the previous year, reaching the equivalent of \$9.9 billion (figure 1).



There are a number of reasons for these increased capital inflows. First, widening spreads paid on South African long-term debt (figure 2) made investments relatively more attractive. However, a cut in the South African policy interest rate by 50 basis points to 5 per cent in July 2012 also prompted a fall in bond yields and a sideways movement in spreads. Second, even with a flat trend in spreads, investors still found a strong rationale for increasing their bond exposure in the continued yield compression in advanced economies. The return on the ten-year United States Treasury bond fell below 2 per cent during the course of 2012, increasing the pressure for investors to search for higher yields elsewhere. Third, the inclusion of South Africa as the first African market in Citigroup's World Government Bond Index in October 2012 provided additional impetus to demand for South African bonds, especially from institutional investors.

Figure 2: Interest rates



Sources: South African Reserve Bank, J.P. Morgan Chase.

Looking ahead, bond investment inflows are expected to face a number of headwinds. The violent strikes in the mining sector last year illustrated various underlying social and economic problems. This pertains for example to inequality as well as unemployment, which stands at more than 24 per cent. Moreover, a more pronounced loosening in fiscal policy during the next budget year would also hold the potential of dampening the allure of investing in South African debt. This, in turn, could put further pressure on the South African rand, which has already depreciated by 5.6 per cent against the dollar since the fourth quarter of 2012.