



## Middle East and Africa: Economic Review July 2010

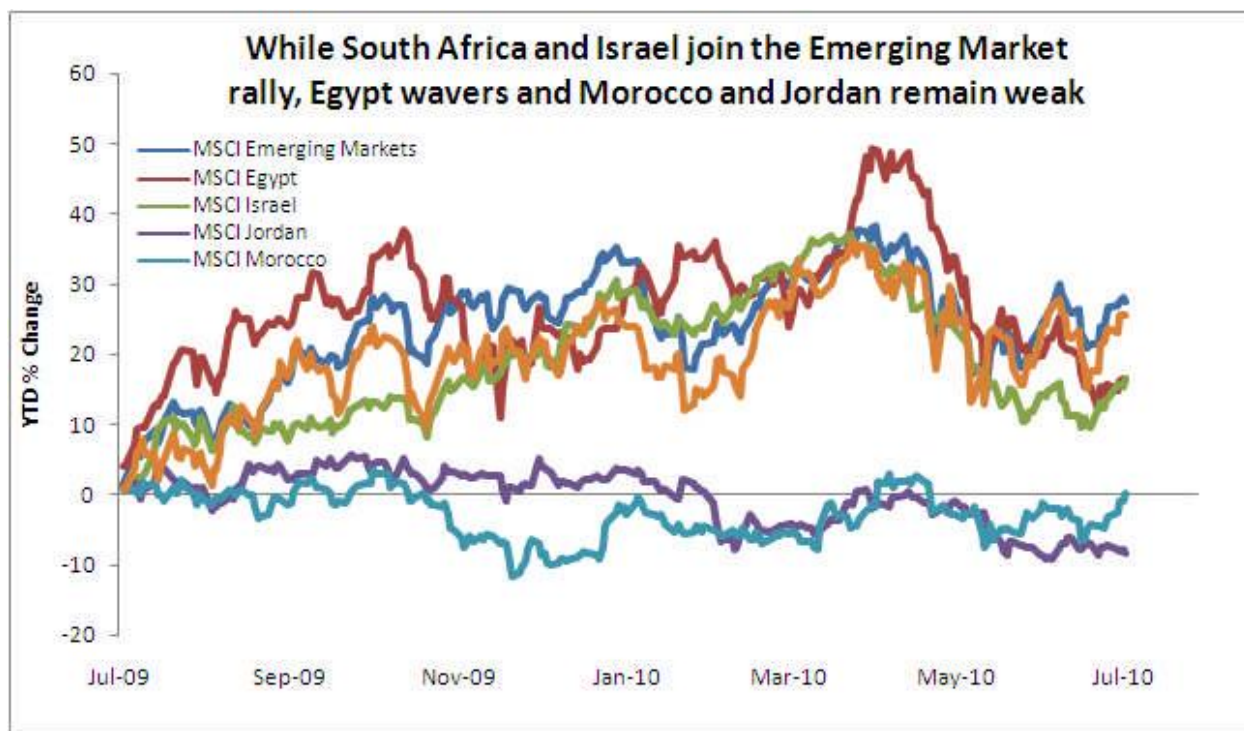
**T**he OECD has suggested that South Africa must ramp up its manufacturing output and strengthen its exports to achieve healthy economy growth, while ensuring that the rand not appreciate further. The recommendations followed the country's recent poorer showing in manufacturing, with the PMI dropping below 50 for the first time in eight months in June.

As well, Israel is suffering from a sliding PMI due to sluggish domestic and international demand. Falling to one of the lowest levels globally, the country's PMI dipped to 46% in June.

In contrast, Jordan's exports have shown an increase of 52.6% in the first five months of 2010. Also bringing cheer, Jordan's budget deficit dropped sharply. This was not the case in Morocco, where the budget deficit climbed compared to last year.

### At a Glance

- **South Africa:** To achieve economic growth and battle unemployment, the OECD has suggested that South Africa boost its manufacturing output and exports, and prevent the rand from strengthening further.
- **Israel:** The government has passed a dual-year budget for 2011 and 2012, with spending slated to rise by 2.7%.
- **Egypt:** Urban inflation climbed to 10.7% in June due to a rise food and beverage prices.
- **Morocco:** To improve social policies and good governance, Morocco and the EU have entered into a cooperation agreement worth \$749 million.
- **Jordan:** Jordan's exports to the EU have risen by 52.6% in the first five months of the year, with Italy being its biggest buyer followed by Romania.



### South Africa: OECD advises South Africa to step up exports

In its recent survey, the Organization for Economic Cooperation and Development (OECD) recommended that South Africa must better its exports and prevent the rand from further strengthening, in order to achieve long-term economic growth, which includes job creation. According to Angel Gurría, the OECD Secretary General, “the economy is still around 3% below potential, and will probably take at least 3 years to reach potential.” Currently, the rand is standing strong at around 7.60 to the dollar, after appreciating nearly 30% in 2009.

The OECD also noted that unemployment is one of the major issues facing the country. Although the jobless rate in South Africa had reduced in recent years, it still remained above 20%, and by the first quarter of 2010 it had soared to more than 25%. Encouragingly, there was a pull back in the jobless surge in May as finance and community services perked up, and with this, unemployment declined by 6.2% and by a further 0.26% in June. But the OECD estimated that an economic growth rate of 5% has to be achieved before there is a discernible change in

unemployment figures. “The overarching challenge for South Africa is to boost its trend growth rate and thereby create jobs,” the OECD pointed out.

What’s more, a slowdown in South African manufacturing year-on-year in May pointed to another task at hand. Though factory production increased by 7.9% year-on-year in volume terms in May, it was still a decline compared to a rate of 8.6% in April. The contraction continued into June, with the Purchasing Managers Index (PMI) dropping below 50 for the first time in eight months. The index dipped to 48.4 from 51.1 in May, indicating a loss of momentum in manufacturing, which accounts for 15% of the economy.

**Consumer Price Inflation (CPI) inched down in May to 4.6% year-on-year** compared to 4.8% in April, due to a lowering of food prices. This is the fifth straight month that inflation has stayed within the target range of 3% to 6%. Labor unions have long demanded the government avoid setting such a target range because it has led to higher interest rates that have affected the poor. In defense, South African Finance Minister Pravin Gordhan stated that as a result of the measure, investor confidence has been boosted and options have been provided for the central banks during times of crisis. “Our inflation-targeting framework has proven itself in the past as a valuable signal for credible policy,” Gordhan insisted in a written statement to the Parliament.

On a positive note, **South Africa’s trade gap declined sharply by \$39.9 million in May** as exports showed a rise of 6.8% compared to April. Imports, on the other hand, increased 3.1% in May compared to the previous month.

### **Israel: Government passes dual-year budget**

The Knesset has passed the dual-year budget for 2011 and 2012 following the same pattern that it had followed for 2009 and 2010. Constant disagreements over the budget in the past have led to the forming of the dual-year budget plan, a practical alternative for the Israeli government. Dominique Strauss-Kahn, the Managing Director of the International Monetary Fund (IMF) has agreed that a dual-year budget leads to “stability and long term planning.”

**The new budget will increase government spending by 2.7%, with the budget deficit expected to be 3% in 2011 and 2% in 2012.** While indirect taxes will be raised, defense spending will be tempered to allow unrestricted movement of funds for social and welfare programs targeting education and economic growth. To reach the proposed budget deficit, the defense budget will be slashed by \$700 million and taxes will be raised by \$1.4 billion in 2011 and by another \$881 million in 2012.

**Inflation slowed down to an annualized 2.4%, its lowest level since October 2007,** falling well within the government’s target between 1% and 3%, according to the Central Bureau of

Statistics. Israel's Central Bank is thus expected to maintain the benchmark interest rate at 1.5% for August.

Meanwhile, the PMI tumbled 2.1% in June to 46% from 48% in the previous month, reaching one of the lowest levels globally thanks to a slowing of trade activity post Greek debt crisis. Israel's PMI has plunged 16.5% since November 2009 to reach below 50%, the dividing line between contraction and expansion, due to waning domestic demand, sluggish exports and slowing industrial production.

**Overall exports slumped an annualized 11% in the second quarter of 2010 after rising an annualized 8.3% in the first quarter.** Exports in June totaled \$4.4 billion, a dip of 1.2% compared to May. Imports, on the other hand, stood at \$4.9 billion showing a small rise of 0.2% compared to the previous month. Israel's trade deficit in June amounted to \$500 million, with the increase in imports pointing to Israel's economic slowdown.

Due to this deceleration, Israel's GDP expanded only by an annualized 3.4% in the first quarter, a slower rate compared to 4.4% in the previous quarter. Israel had rebounded from the global financial crisis powered by its exports, which make up 50% of its GDP. However, with the ongoing European crisis and the depreciation of the euro, Israeli exports have been hit hard.

On the employment front, the National Insurance Institute has noted that there has been a 24% drop in jobless claims in the first half of 2010, although it doesn't point to a lessening in unemployment figures. "Despite the steady decrease in jobless claims, as evident from the past six months, we still have high unemployment rates," points out Social Affairs Minister Isaac Herzog.

Encouragingly, tourism has been robust as a record 1.6 million tourists visited Israel in the first half of 2010, a 39% rise year-on-year. The Ministry of Tourism estimates that income from tourism has touched \$1.55 billion during this period, which is 35% higher than the first half of 2009. The Ministry, though, is remaining cautious. "The increase in incoming tourism during the first half of this year should not be taken for granted. It is the result of massive investment in marketing activities around the world with significant budgets," said Stas Mizezhnikov the Minister of Tourism.

### **Egypt: Inflation increased to 10.7%**

In Egypt, annual urban inflation increased up to 10.7% in June mainly due to a rise in food and beverage prices, which account for more than 40% of the inflationary basket. Urban inflation has

in fact been on the wane since February, and this marks its first rise. However, Producer Price Inflation (PPI) sharply fell 9.9% in May from 15.8% the previous month.

**Suez Canal revenues shot up 10% year-on-year to \$383.7 million in June.** But when seen on a month-on-month basis, revenues from the canal declined in June by nearly \$11.3 million compared to the previous month. Revenue from the canal is expected to improve in the coming months as the general trading scenario improves.

Poverty stood at 22.5% in 2005 and continues to be one of Egypt's most crushing problems. The government is targeting a reduction in the poverty rate by 18% in the year 2010-2011. Reducing poverty is but one part of a development plan being chalked out by the government, which will also urge for social programs that aim to bridge the gap between rural and urban areas.

**Egypt's budget deficit stands at 8.3% of the GDP,** which is below the government's target of 8.4%. State revenues for the fiscal year 2009-2010 are \$47 billion while expenditures amounted to \$64.3 billion.

### **Morocco: Morocco enters into a cooperation program with the EU**

Morocco has signed a cooperation program worth \$749 million with the EU to be implemented between 2011 and 2013. Aimed at forwarding social policies, promoting the environment and good governance, the program's goal is to strive for an all-encompassing development of Morocco. Of the allotted amount, \$149 million will be earmarked for developing rural areas and medical aid.

Environment has also become a concern in Morocco, which recently opened a sprawling wind farm worth \$300 million. Located near Tangiers, it is now Africa's largest wind farm containing 165 turbines with a production capacity of 140 MW. But it doesn't stop there. The wind farm is "part of a global project estimated at \$3 billion. It will be completed in 2020" according to Yamsmina Benkhadra, Morocco's Minister of Energy and Mining.

As forecasted, **Morocco's budget deficit should stay within the expected limit of 4% of the GDP,** despite a soaring fuel subsidy bill due to higher oil prices. To cope with the fuel bill other costs will be cut. "We will ... take measures in the second half to reduce the state's cost base and remain confident of maintaining the deficit at around 4%," said Economy and Finance Minister Salaheddine Mezouar. However, the budget deficit this year is higher compared to 2.2% last year, with the government spending more to stimulate the economy by slashing taxes and increasing wages.

Thanks to a healthy wheat harvest for two years in a row, the economy has kept from slowing down too much. Exports, though, still act as a deterrent to Morocco's pace of growth as Europe, the country's chief export destination, continues to struggle in its economic recovery. Exports did register a 12.4% growth in the first five months of the year mostly due to strong phosphate products sales, but other sectors lagged behind.

**Consumer prices went up 1.9% year-on-year in June** due to a spike in food, clothing and transportation prices. But core CPI, which excludes the volatility of these factors, rose 0.5% year-on-year in June.

### **Jordan: Exports to EU increased by 52.6%**

Jordan's exports to the EU shot up 52.6% in the first five months of the year compared to the same time in 2009, amounting to \$106.4 million. Italy was the biggest buyer of Jordanian goods followed by Romania. Exports to the Americas also showed an increase compared to last year in the first five months, totaling \$351 million. Jordan's imports from the EU, on the other hand, dropped 7% in the first five months of the year to \$1.1 billion.

**Jordan's budget deficit reduced drastically in the first five months of 2010 to \$193 million**, as the government halted non-essential capital spending. In contrast, in the same period in 2009, the deficit had hit a record \$490 million or 9% of the GDP, as the strain of the global financial crisis took its toll on foreign cash flows, remittances and domestic demand. This year, the government plans a host of austerity measures in a bid to trim its budget deficit to 6.3%. Already, the government has slashed civil service pay and debt servicing, with total expenditures falling 8.3% year-on-year and capital expenditures declining sharply by 45%.

Meanwhile, the trade deficit broadened by 11.5% to \$2.99 billion from January to May year-on-year, chiefly due to a high oil bill. Total imports increased 7.2% during this period year-on-year to \$5.7 billion, spurred by increasing oil prices and consumption. Jordan's crude imports, mostly sourced from Saudi Arabia, surged 49.5% compared to 2009. Exports rose by 3% year-on-year to \$2.8 billion.

Domestic and foreign debt is on a continuous rise. Total debt rose 2.4% to \$13.9 billion at the end of May year-on-year. Public debt now forms 56.2% of the projected GDP in 2010, tumbling from an earlier figure of 59.4% in 2009. But as the recession continues to clamp down on foreign aid and local revenue, total debt is expected to hit a record \$14 billion this year, flirting close to the legal limit of 60% of the GDP.

**The CPI climbed 5% in the first six months of 2010 year-on-year** driven by price rises in commodities, transportation and fuel. A month-on-month increase of 0.3% was noted in June due

to a spike in the prices of food items and other products, while on an annualized basis the CPI stepped up by 5.3% in June.

Unemployment eased its pressure on the Jordanian economy in the second quarter year-on-year, touching 12.2% from April to June 2010 compared to 13% during the same time last year. The jobless rate stood at 12.4% in the first quarter of this year.

**On the positive side, tourism revenues shot up by 24% in May** year-on-year generating around \$264 million. In the first five months, tourism witnessed a phenomenal growth of 30% reaching \$1.2 billion compared to \$960 million in 2009 during the same period. 

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