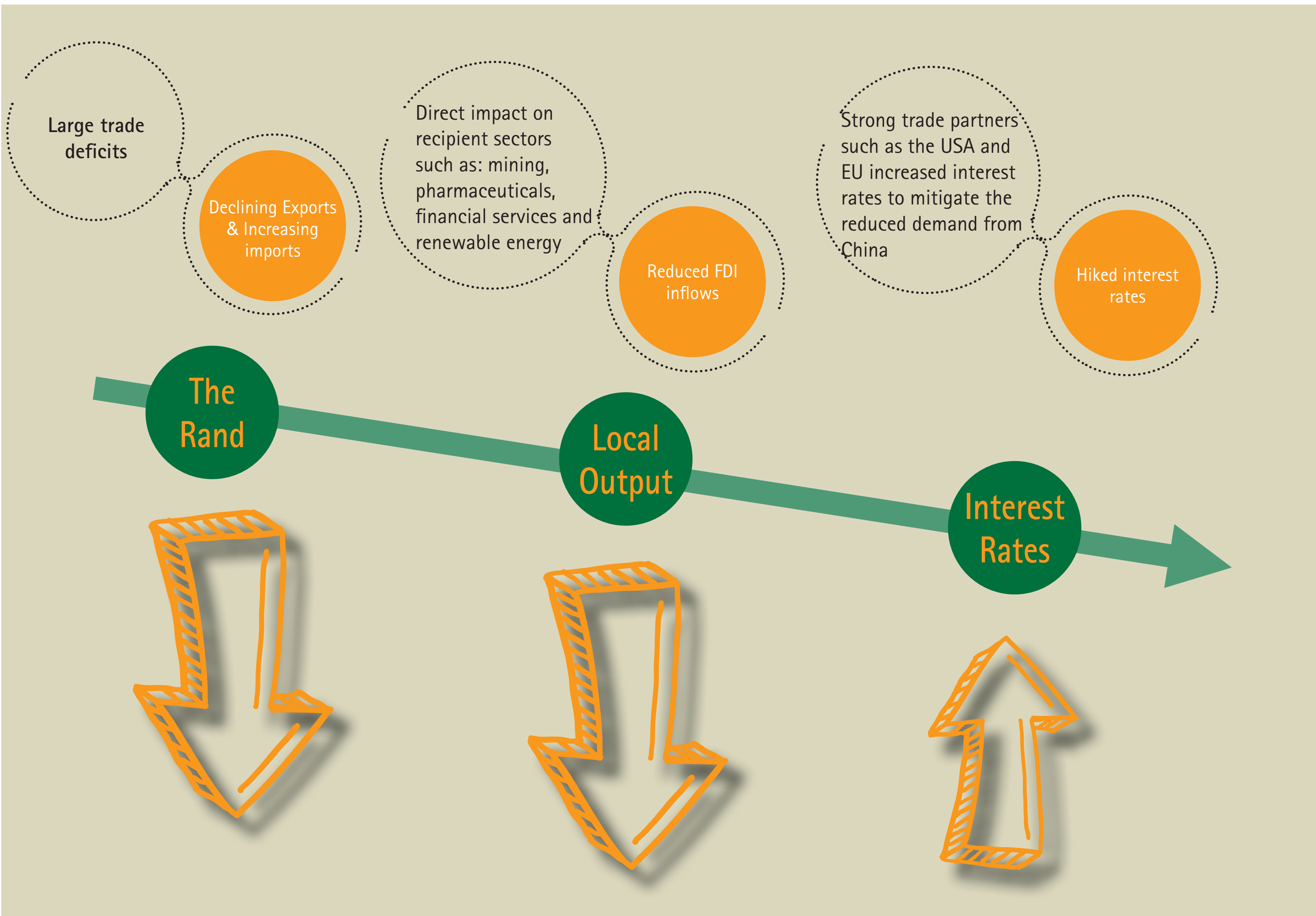
OVERVIEW OF THE ECONOMIC ENVIRONMENT

South Africa's economy grew by 1.3% in 2015, lower than the 1.5% growth experienced in 2014. Globally, the 2015 economy was characterised by relatively weak growth in GDP. Uncertainty over emerging economies, fuelled by the global slowdown in growth as well as decreases in commodity prices had a negative impact on the South African economy. An economic slowdown in China was largely responsible to lowered demand for South Africa's commodity exports. Furthermore, interest rate increases in developed countries such as the USA seeking to normalise their economies, resulted in a capital flight from African and Asian markets as investment capital anticipated relatively better returns in the USA.

Figure 1: Impact of global market volatility on SA economy



Locally, the main contributor to the slowdown was in the agricultural sector which saw severe drought conditions contracting the sector by 8.4%, reportedly the largest annual fall in agriculture since 1995. Another sector that experienced a negative growth rate was the electricity, gas and water supply industry which shrank by 1%.

Growth in manufacturing was minimal, expanding by a mere 0.1%. Whilst other sectors recorded growth figures of less than 2%, the finance industry experienced growth levels of 2.8%. The highest growth recorded was in the mining sector which saw the industry expand by 3%. This growth was however a result of increased activity in the platinum mining sector following the low base created in 2014 when a crippling strike resulted in diminished production. Combined with a volatile currency that has seen a severely weakened Rand exchange rate, these dynamics have only served to reduce investor confidence.

Indicator 2015 (avg.)	% Rate	% Change from prior year
Unemployment	24.5	0.2 ↑
Inflation	4.6	(1.5) ↓
Real GDP growth	1.3	(0.2) ↓
Real GDP per capita	0.48	(0.44) ↓

The economic downturn has had a negative impact on the performance of enterprises that cannot be ignored. Rising interest rates, ever-increasing input costs and a significant decline in spending threaten the profitability and sustainability of many enterprises. A weaker rand does not bode well for importers, whilst those operating in mining and steel manufacturing will no doubt be impacted by the slowdown in these sectors. The weaker exchange rate may also not necessarily spell an advantage for exporters as rising supply-side costs (notable examples being electricity and water) erode any exporting gains.

Analysts report that SMEs are likely to bear the brunt of the contracting economy. More businesses are struggling and this has been all too clear at the NEF as we witness increased distress in our current investees, resulting in potentially good business ideas losing their commercial viability. Management continues to dedicate its efforts towards vigilant monitoring of the portfolio and implementing various interventions in order to stabilise businesses in distress.

Economic analysts paint a subdued picture for South Africa's growth prospects in the next decade with the GDP growth rate forecast to reach 2.2% per annum by 2025. In the absence of radical interventions, South Africa will thus continue to fall short of NDP targets of 5.4% growth rate.

This poses a challenge to the NEF as a DFI with a clear mandate to drive economic transformation in alignment with the goals of the NDP. As a funder with a strictly black economic empowerment focus the NEF seeks to address market inefficiencies where private capital may be unwilling or unable to bear the risk of providing capital to black business that may be considered high risk – an increasing reality faced by black enterprises operating under the current economic climate.

In order to continue supporting current and future investees, as well as making a meaningful contribution to government's transformation agenda, the NEF is strategically positioning itself to not only identify but also take advantage of opportunities for growth. Government sponsored programmes such as the newly established Black Industrialists Programme as well as Operation Phakisa present opportunities for the NEF to expand its activities to tap into sectors that stand to benefit from these programmes. Other developments in the economy which may present as challenges have produced opportunities for entrepreneurs. An example is the electricity supply crisis which has spurred a growing need for alternative energy sources, giving way to opportunities for emerging gas fuel wholesalers and retailers to tap into both local and continental African markets.

The NEF also recognises the country's high unemployment rate as an obstacle toward real transformation and is proud of the progress it continues to make towards the creation and support of employment opportunities. The NEF therefore prioritises the maximisation of the empowerment dividend through targeted investment activities.

As we inch forward towards the greater goals of our national transformation agenda, it is crucial to highlight that the development space is however not only the ambit of the state or DFIs but big business too has a role to play in advancing inclusive growth.

> *"For the financial year 2015/16, the NEF has approved a total of one hundred and twenty-seven (127) transactions worth R1.2 billion. One hundred and twenty (120) transactions worth just over R1 billion were committed, and total disbursements amount to R819 million."*
>
> *Performance Review, NEF Integrated Report 2016*