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TRENDS, DEVELOPMENTS AND DATA

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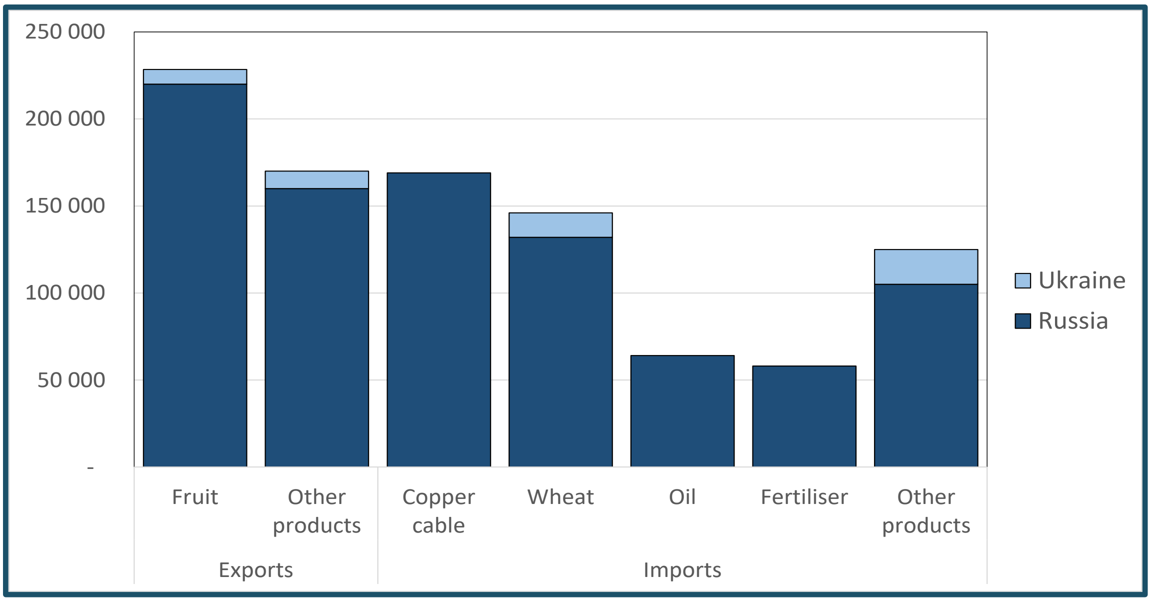
# Briefing Note 1: The Ukraine war and the South African economy

The war in the Ukraine has vastly increased uncertainty for the global economy, and consequently for South Africa.

The war itself will have limited impact on trade because South Africa has only very limited economic ties to Russia and Ukraine. But it has already led to extreme volatility in commodity prices, affecting both export products and as well as petroleum, wheat and fertiliser imports. It seems likely to disrupt international capital markets as well. In the longer run, it may prove a significant drag on growth in the global North, which is still South Africa's main export market.

Direct trade with Russia and Ukraine together accounted for less than 1% of South Africa's total imports and 0.5% of exports in 2020. A third of imports from Russia were copper cable in 2020, with wheat, petroleum and fertilisers making up most of the remainder. South Africa accounted for 0.16% of Russian exports, but 3% of its exports of copper cables. South African imports from Ukraine were far smaller, and consisted principally of wheat and other agricultural products. South Africa bought less than 0.1% of Ukrainian exports. It exported mostly fruit to both countries, with capital equipment for mining and mineral products (mostly manganese to Russia and chrome to Ukraine) following at a considerable distance. (Graph 1)

**Graph 1. South African trade with Russia and Ukraine by major commodity in thousands of US dollars in 2020**




*Source:* Calculated from ITC. Trade Map. Interactive dataset. Accessed at www.trademap.org in March 2022.

The data on trade understate the impact of the war on South Africa because Russia and, to a lesser extent, Ukraine account for a significant share of trade in some major commodities.

Russia produces over 10% of world petroleum exports, with a slightly higher share for fertiliser. Russia and Ukraine together supply around a fifth of international wheat exports. If the war cuts into their ability to produce or trade in these products, international prices could rise substantially. That would ultimately affect both economic growth and household consumption in South Africa.

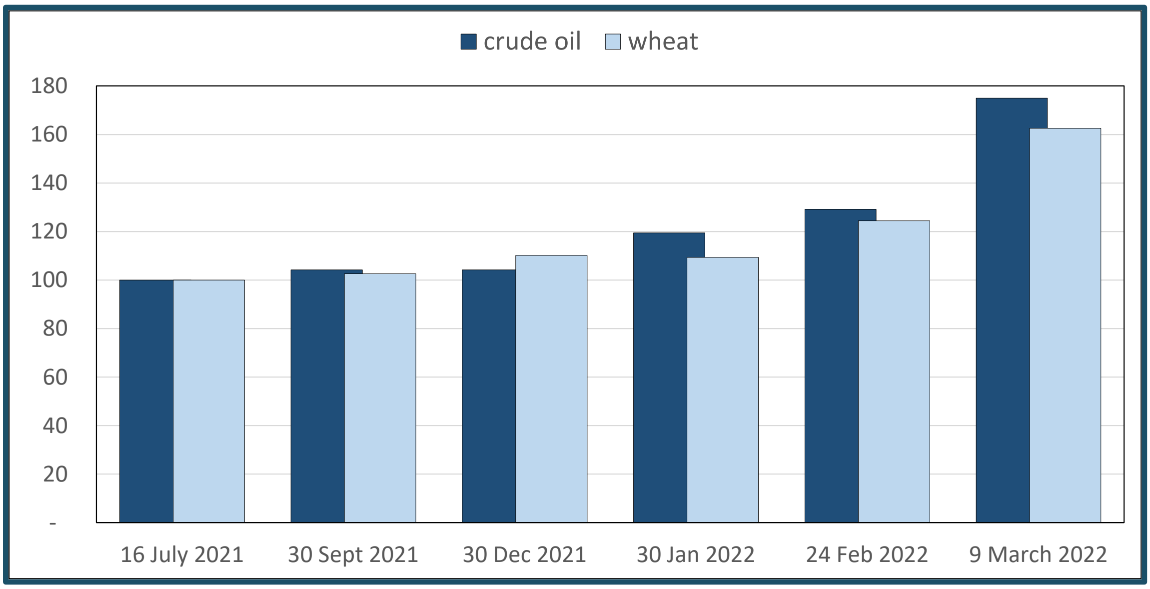
In 2021, oil comprised 17% of all South African imports. Wheat and fertiliser were much smaller, but higher prices could disproportionately affect food security and production. Foreign wheat meets around 40% South African demand, but in most years makes up less than 1.5% of total imports.

South Africa also imports around half of all the fertiliser used, although it contributes only 0.7% of all imports. In the past year the unit price of imported fertiliser already doubled, even before the invasion. Fertiliser accounts for around a tenth of production costs in local agriculture, so rising prices can have significant implications for food prices.

A more immediate impact has occurred through the destabilisation of global commodity prices. As noted (see **Error! Reference source not found.**), all of South Africa's main mineral exports have seen an extraordinary spike in prices since the rumours of war began.

A similar hike also affected petroleum and wheat, as the following graph shows. Prices have risen particularly quickly since the initial attack on 24 February. That said, the war itself has not yet significantly constrained supply of any of these commodities. The increases reflect uncertainty about the potential impacts of the war much more than actual changes in market supply and demand.

**Graph 2. Indices of international prices of petroleum and wheat from 16 July 2021 to 9 March 2022 (16 July 2021 = 100)**




*Source*: Calculated from Trading Economics. Commodity prices. Interactive dataset. Accessed at https://tradingeconomics.com/commodities on 9 March 2022

The panic and speculation due to the war have disrupted already extraordinarily volatile commodity and capital markets. The war profoundly intensified global economic uncertainty from the pandemic, which had already caused huge price swings over the past two years. More fundamentally, over the past 15 years or so commodity markets have been enveloped in the asset bubble that emerged from persistent low interest rates and the shift to defined-contribution retirement saving in the global North. These developments have been associated with increased synchronisation across commodities. Even after less than three weeks, the war in Ukraine has deepened both the ups and the downs.

As of mid-March, the ratings agencies had begun to warn that Russia might be unable to meet its debt. Sanctions have cut it off from its reserves, held predominantly in Western currencies, as well as major global payments mechanisms and financial institutions. If Russia defaults, it could lead to higher interest rates for all emerging economies, including South Africa. Foreign debt already absorbs a significant share of South Africa's budget, so that could mean an even starker squeeze on government spending.

In the longer run, if the war expands to Europe or interrupts its energy supplies, global growth will slow down. That will inevitably undermine South Africa's recovery from the pandemic. The European Union remains South Africa's largest market, absorbing almost 20% of exports in 2021. Moreover, both the United States and China rely on it for both export demand and high-tech inputs. As a result, a serious European slowdown will constrain virtually all of South Africa's trade and financial relations.

Hopefully, Russia will realise the immense costs of continuing with the conflict and withdraw sooner rather than later. In that case, the damage to the global economy will remain moderate – although the people of Ukraine will still face the pain of reconstructing their shattered cities and their lives.