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Economic overview:

Recent developments in the South African economy and drivers of growth over the medium-term

May 2016

Department of Research and Information

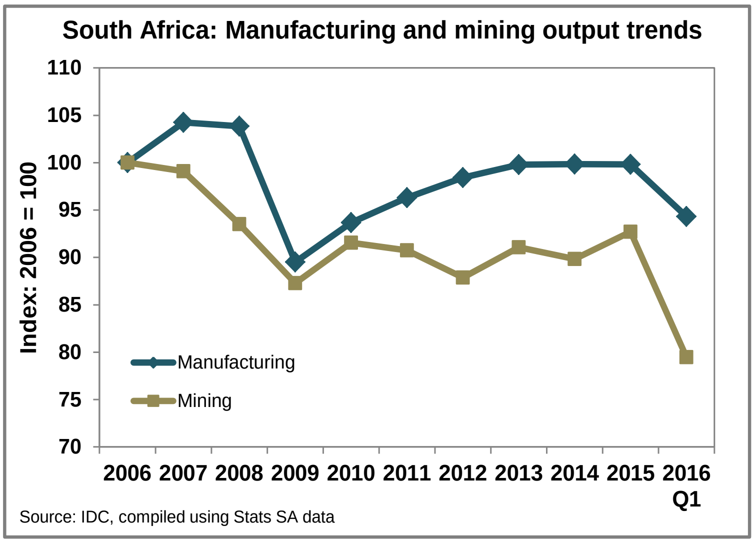
RECENT ECONOMIC DEVELOPMENTS

The global economy continues to face significant headwinds and is struggling to attain a higher growth trajectory. Amongst the advanced economies, the growth momentum is being sustained in the United States, the United Kingdom and the Eurozone, while Japan continues to report sporadic contractions. However, the growth trend continues to slow in the emerging/developing world, with China being the principal contributor, followed by Brazil and Russia. India is the notable exception. The International Monetary Fund has lowered its projections for world GDP growth yet again to 3.2% for 2016 and to 3.5% for 2017.

Lacklustre global economic growth and fundamental imbalances continue to weigh on the outlook for industrial commodity prices over the short- to medium-term. While a recovery in global investor appetite for riskier asset classes and US dollar weakness have, more recently, supported a recovery in commodity prices from heavily oversold levels, the balance of risks is tilted towards continued weakness in the short- to medium-term. The large market supply excesses that are expected to persist over the next two years at least, as well as tepid demand-side conditions across the commodities complex, imply that price recoveries should be viewed as transitory.

Continued signs of resilience in the US economy may culminate in a resumption of US Fed policy rate increases possibly towards the end of 2016 and into 2017, which would renew downward pressure on commodity prices. However, over the longer-term, supply-side adjustments and gradually improving demand conditions should support price recoveries. Global equity markets have posted some gains since the very bearish start to 2016, but remain highly volatile.

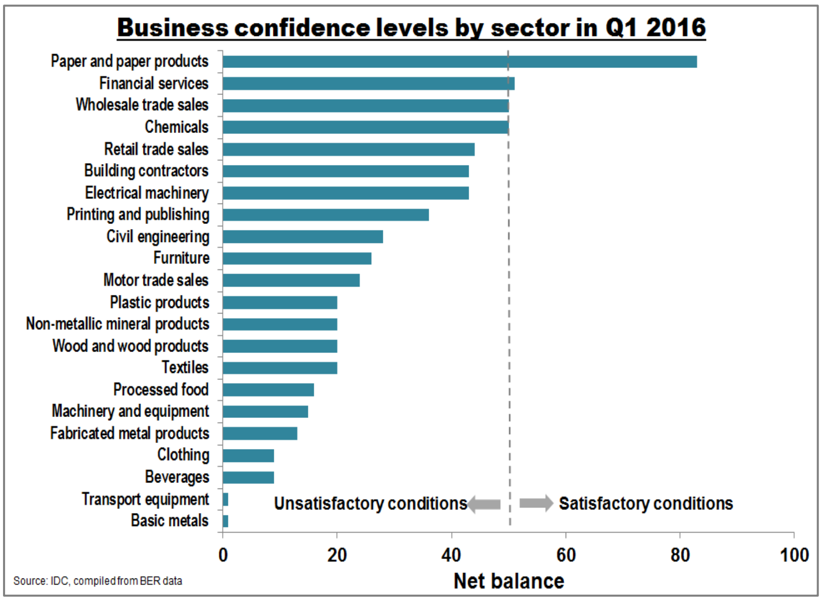
Adversely affected by both domestic and external factors, the growth performance of South Africa's economy is still trending downward. Due to the devastating drought the maize crop is projected at 7 million tons for 2016, or 30% lower than the 9.96 million estimated for 2015. Other farming segments, including livestock, have also been harshly affected.



Mining production fell by 11.2% in the first quarter of 2016 compared with the same period last year. Although statistical factors played a significant role in this regard, all mining sub-sectors with the exception of coal and gold mining recorded lower output levels on a quarter-on-quarter basis.

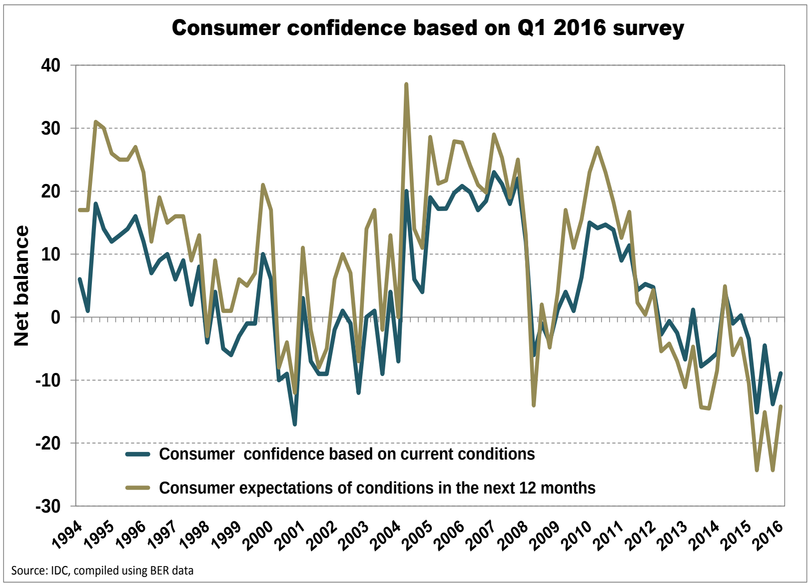
Manufacturing output contracted by 0.8% over the year to the first quarter of 2016. However, conditions appear to be improving in manufacturing, as the sector's PMI reached 54.9 (a 32-month high) in April 2016.

Business confidence is at the lowest level (36 index points in the 1st quarter of 2016) in almost six years. In relative terms, conditions appear to be reasonably satisfactory in the financial services and wholesale trade sectors, as illustrated. The same cannot be said about retail traders, motor traders and building contractors. With the stark exception of the paper and paper products industry, which views current trading conditions as highly satisfactory, low business sentiment is still being observed across most other manufacturing sub-sectors. Many are already in recession.



The unemployment rate rose sharply to 26.7% in the 1st quarter of 2016, from 24.5% in the 4th quarter of 2015. Some 355 000 jobs were lost across a number of sectors on a quarter-on-quarter basis. The manufacturing sector recorded 100 000 job losses and the trade sector shed 119 000 jobs, with seasonal factors playing a part. The number of unemployed individuals increased by 521 000 to 5.71 million, also reflecting a considerable number of entrants into the labour force.

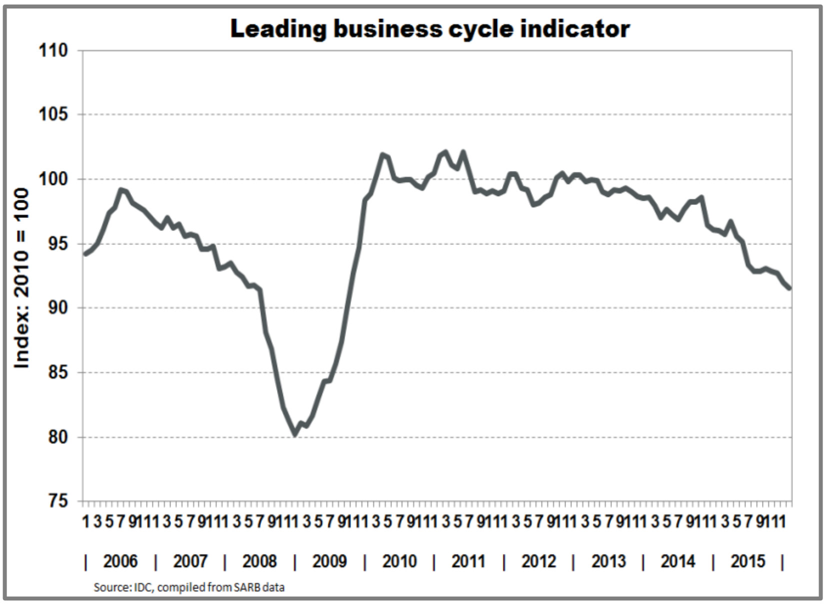
The environment remains largely unfavourable for South African consumers, who expect conditions to worsen over the next 12 months. The continued decline in new vehicle sales in the first four months of the year attests to this. The financial health of households is of particular concern in light of higher interest rates and poor employment prospects. According to the South African Reserve Bank, the household debt-service risk index is still within the high-risk range.



The decision taken by Moody's to keep South Africa's credit rating unchanged at Baa2, with a negative outlook, surprised the market positively. However, the rating agency raised its concerns over the downside risks to economic growth and fiscal stability. The adverse trends in business and consumer confidence, alongside the poor performance of the agriculture, mining and manufacturing sectors in the first quarter of the year, reflect the generalised weakness in the economy at the present time and the challenges lying ahead.

DRIVERS OF GROWTH IN THE MEDIUM TERM

The growth outlook for the South African economy has deteriorated substantially as both domestic and external factors are taking their toll. The leading business cycle indicator, which provides an indication of economic conditions in about 6 months' time, has dipped sharply over the past two years. At 91.6 index points in February 2016, it has fallen to its lowest reading since October 2009. This provides advance warning of a difficult year ahead.



The economy is therefore expected to grow only marginally in 2016, with the momentum rising modestly over the next two years. The rates of increase in household consumption expenditure and government spending will be initially weak, while fixed investment is forecast to contract marginally in 2016. Export growth is projected at 3.8% for 2016, accelerating in subsequent years as the global economy potentially resumes a higher growth trajectory.

At a broad sector level, it is projected that the goods-producing sectors - agriculture, mining and manufacturing - will record contractions in real value added during 2016, albeit to varying degrees, while fairly modest rates of expansion are anticipated for most other sectors.

Real GDP growth and outlook at broad sector level (% change per annum)

Economic sector	2010	2011	2012	2013	2014	2015	2016f	2017f	2018f
Agriculture, forestry & fishing	-0.3	1.3	0.6	1.5	5.6	-8.4	-7.6	3.4	5.4
Mining & quarrying	5.3	-0.7	-2.9	4.0	-1.6	3.0	-2.9	0.1	1.6
Manufacturing	5.9	2.9	1.9	0.7	0.0	0.1	-0.1	1.4	2.9
Electricity, gas & water	2.4	1.4	-0.1	-0.6	0.0	-1.0	-0.5	2.1	4.1
Construction	0.7	0.4	2.1	2.7	2.9	1.9	0.4	1.3	3.4
Trade, catering & accommodation	4.4	3.8	3.6	1.9	1.3	1.4	1.0	1.1	2.5
Transport, storage & communication	1.7	3.0	2.5	2.0	2.3	1.4	0.5	0.9	2.2
Finance, insurance & business services	1.2	4.1	3.0	3.0	2.2	2.8	1.9	2.0	3.6
Community, social & personal services	0.4	2.4	2.1	1.8	1.4	1.1	1.0	1.2	2.0
General government	2.7	4.5	3.6	3.1	3.0	0.9	1.1	0.6	1.0
Total GDP growth	**2.9**	**3.0**	**2.2**	**2.3**	**1.6**	**1.2**	**0.4**	**1.2**	**2.6**

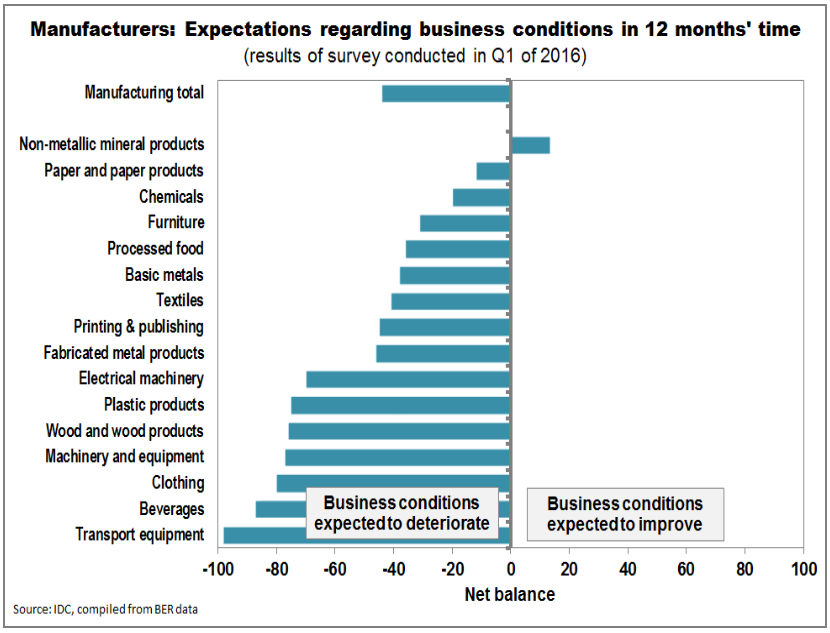
Source: Stats SA (historical data); IDC forecasts

The devastating drought will be affecting agriculture production across various farming segments, including crops, livestock farming and the horticultural sector. Maize production has been estimated to drop sharply by almost 30% to 7.05 million tons for 2016, whilst other summer crops are also expected to be much lower than in the previous year. However, as climatic conditions improve, a strong rebound in agricultural output could be expected.

The mining sector could still be facing very difficult conditions, at least in the short term, despite the recent recovery in commodity prices. A continued growth moderation in the Chinese economy is likely to affect its demand for South African mineral commodities and there is no certainty that commodity prices are on a sustained rebound. The strong up-tick in growth in mining output experienced in 2015 is expected to be reversed in 2016, as the 2015 growth rebound was mainly due to technical factors and not reflective of demand conditions. In addition, gold production is forecast to continue on its long-term declining trend and remaining a drag on overall mining output.

Having already experienced two consecutive years of stagnant output growth, the manufacturing sector is expected to face yet another difficult year. On the domestic front, household spending will be under severe strain, whilst real fixed investment outlays by the private sector and public corporations is projected to contract, thereby impacting on demand for manufactured goods. Furthermore, operational challenges such as rising cost pressures and infrastructure related problems (e.g. electricity supply) could still be affecting production.

The difficult operating environment is reflected in low levels of business confidence, with the majority of manufacturing sub-sectors being of the view that business conditions will remain unsatisfactory during the course of 2016. The only exception is the sector producing non-metallic mineral products, which has a positive outlook according to the recent Bureau of Economic Research survey.



For the manufacturing sector at large, investment in machinery and equipment is expected to decline in 2016, as demand remains weak and surplus production capacity still exists. This could be affecting much needed employment creation. There is, however, some light at the end of the tunnel as manufacturers expect an improved export performance on the back of a weaker rand. After recovering considerable ground vis-à-vis the US dollar and the euro from early February to end April, the rand lost some ground in recent weeks on the back of renewed risk aversion towards emerging markets. The production benefits potentially associated with a weaker exchange rate environment are not yet being fully realised, as South Africa’s export performance is being hampered by subdued demand conditions in key external markets for manufactured goods and commodities. The situation is, however, expected to improve over the medium- to long-term.

Growth drivers: Household consumption spending to provide limited impetus

Overall household consumption spending is expected to grow by a mere 0.3% in 2016 and 1.2% in 2017, which is significantly slower than in previous years, before recovering to 2.2% in 2018. As household spending accounts for around 60% of national GDP, it is a major driver of economic activity. Spending on durable goods is expected to contract over the next two years, while semi-durable spending is projected to remain weak. However, demand for services and non-durable goods are expected to continue to report relatively robust growth over the three-year horizon.

Given the current environment, household spending will be under strain for some time, particularly so for the durable and semi-durable categories.

Growth in household consumption expenditure by type of spending category

Consumer spending category	2014	2015	Average annual growth forecasts: 2016 to 2018
	% growth per annum		
Durable goods:	**5.3**	**1.6**	**-0.9**
Furniture, household appliances, etc	5.5	2.3	2.3
Personal transport equipment	5.0	0.5	-2.6
Recreational and entertainment goods	6.5	4.4	1.2
Other durable goods	3.9	2.4	1.9
Semi-durable goods:	**3.2**	**3.5**	**1.5**
Clothing and footwear	3.3	3.2	1.6
Household textiles, furnishings, glassware, etc	4.3	5.0	1.5
Motor car tyres, parts and accessories	0.2	3.2	1.1
Recreational and entertainment goods	2.1	2.6	1.3
Miscellaneous goods	4.5	3.7	0.7
Non-durable goods:	**0.8**	**1.1**	**1.2**
Food, beverages and tobacco	1.0	1.4	1.4
Household fuel and power	0.2	-2.4	0.3
Household consumer goods	0.8	2.6	1.2
Medical and pharmaceutical products	1.5	2.1	2.5
Petroleum products	-0.4	0.9	0.3
Recreational and entertainment goods	1.9	1.5	1.3
Services:	**0.5**	**1.6**	**1.6**
Rent	0.5	1.1	1.3
Household services, including domestic servants	0.5	0.9	0.7
Medical services	2.1	2.2	2.9
Transport and communication services	2.2	0.2	2.0
Recreational, entertainment and educational services	0.4	-0.1	0.5
Miscellaneous services	-2.4	4.6	1.6
Total household expenditure	**1.4**	**1.6**	**1.2**

Source: SARB data (historical); IDC forecasts

Consumers are expecting the domestic economic situation to remain very difficult throughout 2016, whilst their own financial position is also not in a good standing at present. Consumer confidence remained low in the first quarter of 2016 across all income categories. Consumers across all population groups indicated that it was not an opportune time to buy durable goods, with potentially adverse implications for sectors producing items such as motor vehicles, furniture and household electronics, among other durable goods.

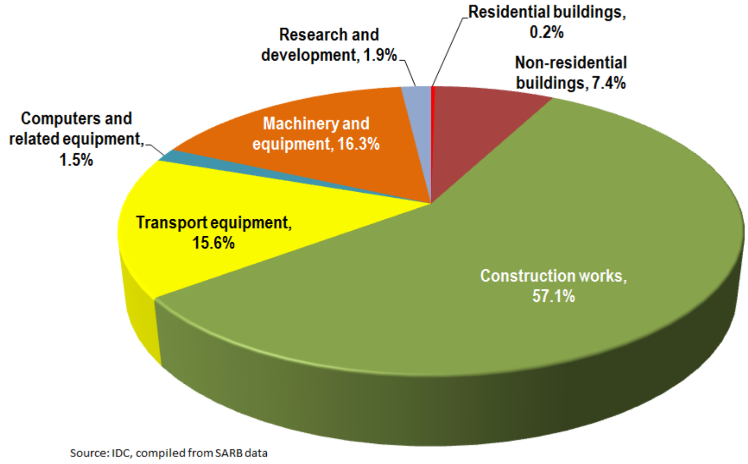
The relatively more positive outlook for certain services sectors was highlighted earlier in this report. As such, sectors that are expected to benefit from the spending structure of households include business services; finance and insurance; wholesale and retail trade, as well as communication. Increased pressure on companies throughout the economy to reduce their cost base could intensify the trend towards outsourcing certain non-core functions, with these functions being fulfilled by companies that are largely classified as providers of business services.

In turn, the manufacturing and motor trade sectors reported the lowest business confidence levels, with the weak spending on durable goods being clearly reflected in the extremely low confidence levels reported by the motor trade sector.

Growth drivers: Public sector investment and consumption expenditure

The large scale infrastructure development programme being rolled out by the public sector is having a profound impact on the economy. The government and public corporations spent R1 619 billion on infrastructure over the past seven years and a further R865 billion will be spent during the next three fiscal years to 2018/19. This expenditure will have a substantial impact on the economy by addressing the infrastructure related bottlenecks - particularly electricity, transport and logistics - currently hindering its growth potential. Increased electricity generation capacity as various units of Ingula, Medupi and Kusile come on stream from 2016 to 2018, will alleviate the supply-side constraints to a significant extent and encourage investment activity.

Composition of public sector infrastructure expenditure in 2015



Source: IDC, compiled from SARB data

Moreover, this expenditure will continue to generate additional value added (GDP) and employment throughout the economy. The impact of this substantial build programme could be increased even further in light of government's policy of increased localisation to be associated with its capex spending. In addition, the increased focus being given to a range of designated products for public sector procurement could have a positive impact on production activities in these specific sectors.

Public sector procurement: Industries, sectors and sub-sectors that have been designated for local production with minimum local content thresholds

	Minimum threshold for local content		Minimum threshold for local content
Various:		**Rail rolling stock and components:**	
Buses (bus body)	70%-80%	Diesel locomotives	55%
Textile clothing leather and footwear	100%	Electric locomotives	60%
Canned / processed vegetables	80%	Electric Multiple Units (EMU)	65%
Set top boxes	30%	Wagons	80%
Electrical and telecom cables	90%	Assembly of locomotives and EMU	100%
Valves products actuators	70%	Car body	100%
Conveyance pipes	80% -100%	Bogie	100%
		Coupling equipment	100%
Electricity infrastruture related:		Suspension	100%
Steel power pylons	100%	Heat ventialtion and air conditioning	60% - 70%
Monopole Pylons	100%	Braking system	70% - 80%
Steel substation structures	100%	Alternators	90% - 100%
Powerline hardware	100%	Traction motors	65% - 80%
Street light steel poles	100%	Electric systems	80% - 90%
Steel lattice towers	100%		
Canned / processed vegetables	80%	**Furniture products:**	
		Office furniture	85%
Pharmaceutical products:		School furniture	100%
OSD tender	70% (volumes)	Base and mattress	90%
Family planning tender	50% value		
		Working vessels/ boats (all types):	
Solar water heaters:		Vessels / boats	60%
Solar Water Heater tanks / geysers	70%	Components	10% -100%
Solar Water Heater collectors	70%		
		Transformers and shunt reactors:	
Residential electricity meters:		Class 0, 1 and 4	10% - 90%
Prepaid electricity meters	70%	Components and conversion activities	50% - 100%
Post-paid electricity meters	70%		
SMART meters	50%		

Source: the dti

Looking ahead, the public sector infrastructure build programme can result in a large number of jobs being created and/or sustained in various sectors of the South African economy. For the period 2016/17 to 2018/19, overall infrastructure investment spending by the public sector is projected to average R288.5 billion per annum. Considering that a large portion of the goods and services required in this build programme will be sourced from local companies, it is without any doubt that the economy-wide benefits associated with the infrastructure roll-out could indeed be fairly substantial.

We have estimated that 614 000 employment opportunities (directly and indirectly), on average per annum over the three-year period, may be associated with this public sector infrastructure spending. In terms of GDP, estimates are showing that an average of about R216 billion per annum (both directly and indirectly), may possibly be linked to such investment spending over the aforementioned period.

Key sectors estimated to benefit from the public sector infrastructure investment programme over the period 2016/17 to 2018/19

Economic sector	Economy-wide impact: Average annual impact (direct and indirect)	
	GDP (R million)	Employment (number)
Construction	72 088	191 634
Finance & business services	46 652	131 607
Trade, catering & accommodation	29 027	98 031
Transport, storage & communication	16 404	18 216
Community & social services	7 257	64 076
Electricity & water supply	5 336	2 475
Base metals and fabricated metal products	5 194	20 777
Other non-metallic mineral products	4 103	11 083
Petroleum products, chemicals, rubber & plastic	4 103	6 319
Wood, paper, publishing & printing	3 643	8 510
Total (incl. other)	**216 436**	**614 205**

Source: IDC calculations

Growth drivers: Export markets present significant expansion potential

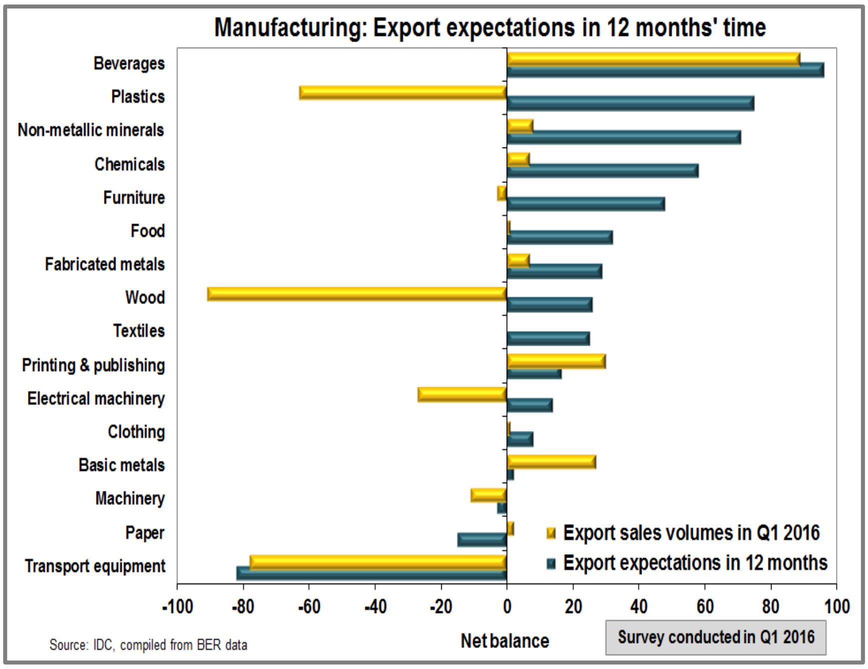
Export demand in global markets is an important driver of performance for many goods producing as well as services sectors, especially when trading conditions remain quite subdued in the local market.

Exports have played an increasingly important role in the South African economy, with their contribution to national GDP having risen over time. After recording an all-time low of 20.7% in 1992, the export-to-GDP ratio increased to 30.9% by 2015. Merchandise exports totalled R1.0 trillion last year, with R610 billion pertaining to manufactured exports and R336 billion to mining exports.

The impact of exports on the local economy is substantial. We have estimated that, due to manufacturing exports alone, domestic value add (GDP) amounting to almost R140 billion was generated directly within the manufacturing sector itself in 2015, whilst through linkages with other sectors the total impact on GDP rises to R580 billion.

In terms of employment creation, more than 816 000 direct jobs are estimated to be linked to merchandise exports, with the number rising to about 2.66 million if all indirect effects are included. It is estimated that almost 24% of all formal sector employment and 26.5% of GDP in 2015 was associated with merchandise exports.

Looking ahead, the majority of manufacturers are expecting higher export volumes in the next 12 months. Although a weak rand can play an important role in improving the price competitiveness of local products, export-oriented enterprises should focus on process and productivity improvements, economies of scale, as well as on product and market development. Since the manufactured export basket is highly concentrated, a diversification of product offer and external markets is imperative to make the economy less vulnerable to developments in specific global markets.



The remainder of this section of the report highlights the key global trading partners, both African and non-African, which are anticipated to make significant contributions to South Africa's export growth over the next three years. The selected countries accounted for 52% of South Africa's exports in 2015.

The sectors highlighted in the following table are those that recorded positive average annual growth in exports over the two-year period ending in 2015 to the respective non-African region/countries. Only the 10 largest are illustrated, ranked from highest to lowest in terms of the average annual exports for the five years ending 2015.

Anticipated high performance SA sectors (10 largest) as exporters to select key non-African trading partners

EU EU import growth forecasts 2016-18: • Eurozone: 4.1% p.a. • UK: 3.6% p.a. SA exports to EU in 2015: R212.3bn SA exports to EU, average 2011-15: R171.1bn p.a.	– Motor vehicles, parts & accessories – Platinum group metals mining – Basic iron & steel products (esp. ferromanganese, ferrochrome, stainless steel) – Agriculture (esp. grapes, oranges, mandarins, apples, pears) – Basic chemicals – Processed food – Other chemicals & man-made fibres – Paper & paper products – Coke & refined petroleum products – Other transport equipment (esp. aircraft components)	**China** China import growth forecast 2016-18: 1.2% p.a. SA exports to China in 2015: R92.1bn SA exports to China, average 2011-15: R95.6bn p.a.	– Other mining (esp. manganese, chrome & zirconium) – Basic iron & steel products (esp. ferrochrome) – Basic non-ferrous metal products – Paper & paper products – Agriculture (esp. wool, edible nuts, oranges) – Processed food – Beverages (esp. wine) – Other chemicals & man-made fibres (esp. reaction initiators, accelerators, & catalysts) – Textiles (esp. of fine animal hair such as angora wool) – Leather & leather products

Anticipated high performance SA sectors (10 largest) as exporters to select key non-African trading partners (continued)

USA		Japan	
USA import growth forecast 2016-18: 4.8% p.a. SA exports to USA in 2015: R76.6bn SA exports to USA, average 2011-15: R66.4bn p.a.	– Motor vehicles, parts & accessories – Platinum group metals – Basic iron & steel products (esp. ferrochrome, ferromanganese) – Basic chemicals – Other mining (esp. diamond & titanium) – Basic non-ferrous metal products – Other chemicals & man-made fibres (esp. pharmaceuticals, soaps and detergents) – Agriculture (esp. edible nuts, oranges, mandarins, vegetable seeds) – Processed food – Coke & refined petroleum products	Japan import growth forecast 2016-18: 1.7% p.a. SA exports to Japan in 2015: R50.5bn SA exports to Japan, average 2011-15: R51.8bn p.a.	– Motor vehicles, parts & accessories – Basic non-ferrous metal products – Basic iron & steel products (esp. ferrochrome) – Wood & wood products – Processed food – Beverages (esp. wine) – Paper & paper products – Metal products (excl. machinery) – Furniture (esp. vehicle seats) – Leather & leather products

Source: IDC analysis, compiled using IMF and SARS data

Notwithstanding the headwinds facing a number of countries in Sub-Saharan Africa (SSA), particularly those dependent on exports of energy resources and other commodities, a number of African markets are expected to provide further opportunities for various export-oriented sectors of the South African economy. The SSA countries selected for our analysis are expected to record an average annual rate of increase in import volumes of more than 4% per annum over the period 2016-18 (according to IMF forecasts); are also sizeable markets for South African exports – that is, South Africa exported at least R2 billion worth of goods to the selected SSA countries in 2015; and, in order to focus on the larger markets, only those with overall imports valued at USD5 billion and above in 2015 are illustrated.

Guided by these parameters, the Top 10 South African export oriented sectors that may benefit from growth in import demand in the selected SSA markets are indicated in the following table. These sectors exhibited positive export growth into these markets over the past two years and are ranked, from highest to lowest, in terms of average annual exports for the five years ending in 2015.

Anticipated high performance SA sectors (10 largest) as exporters to Sub-Saharan African countries expected to post high import growth over the period 2016-18

Botswana		Mozambique	
Botswana import growth forecast 2016-18: 9.8% SA exports to Botswana in 2015: R52.7bn SA exports to Botswana, average 2011-15: R44.7bn p.a.	– Other mining (esp. non-ferrous metals and diamonds) – Machinery & equipment – Processed food – Motor vehicles, parts & accessories – Other chemicals (esp. soaps, pharmaceuticals, pesticides) – Agriculture – Metal products (excl. machinery) – Electrical machinery & equipment – Wearing apparel – Basic chemicals	Mozambique import growth forecast 2016-18: 25.0% SA exports to Mozambique in 2015: R28.2bn SA exports to Mozambique, average 2011-15: R24.1bn p.a.	– Processed food – Machinery & equipment – Basic iron & steel products – Motor vehicles, parts & accessories – Other chemicals(esp. soaps and paints) – Metal products (excl. machinery) – Electrical machinery & equipment – Agriculture, forestry & fishing – Basic chemicals – Paper & paper products

Anticipated high performance SA sectors (10 largest) as exporters to Sub-Saharan African countries expected to post high import growth over the period 2016-18 (continued)

DRC

DRC import growth forecast 2016-18: 9.7%

SA exports to DRC in 2015: R11.0bn

SA exports to DRC, average 2011-15: R10.8bn p.a.

- Coke & refined petroleum products
- Basic chemicals
- Other chemicals (esp. soaps, detergents, paints, pesticides)
- Processed food
- Other mining (esp. stone and salt)
- Television, radio & communication equipment
- Agriculture & fishing
- Textiles
- Other transport equipment (esp. railway locomotives and ship building and repairs)
- Paper & paper products

Nigeria

Nigeria import growth forecast 2016-18: 6.9%

SA exports to Nigeria in 2015: R8.0bn

SA exports to Nigeria, average 2011-15: R7.5bn p.a.

- Basic chemicals
- Basic iron & steel products
- Other chemicals (esp. paints pharmaceuticals, pesticides)
- Processed food
- Machinery & equipment
- Agriculture, forestry & fishing
- Television, radio & communication equipment
- Electrical machinery & equipment
- Other transport equipment(esp. ship building, boat repairs, motor cycles)
- Professional & scientific equipment

Kenya

Kenya import growth forecast 2016-18: 5.2%

SA exports to Kenya in 2015: R8.0bn

SA exports to Kenya, average 2011-15: R6.8bn p.a.

- Motor vehicles, parts & accessories
- Other chemicals(esp. pharmaceuticals, soaps, paints)
- Machinery & equipment
- Basic chemicals
- Agriculture & forestry
- Coal mining
- Processed food
- Beverages
- Professional & scientific equipment
- Other transport equipment (railway locomotives)

Tanzania

Tanzania import growth forecast 2016-18: 5.0%

SA exports to Tanzania in 2015: R6.2bn

SA exports to Tanzania, average 2011-15: R4.8bn p.a.

- Basic iron & steel products
- Machinery & equipment
- Motor vehicles, parts & accessories
- Other chemicals(esp. soaps, pesticides pharmaceuticals)
- Metal products (excl. machinery)
- Electrical machinery & equipment
- Basic chemicals
- Other transport equipment(esp. railway locomotives, ship building, boat repairs)
- Processed food
- Beverages

Ghana

Ghana import growth forecast 2016-18: 4%

SA exports to Ghana in 2015: R4.0bn

SA exports to Ghana, average 2011-15: R3.6bn p.a.

- Machinery & equipment
- Metal products (excl. machinery)
- Electrical machinery & equipment
- Processed food
- Basic chemicals
- Basic iron & steel products
- Paper & paper products
- Plastic products
- Professional & scientific equipment
- Textiles

Mauritius

Import growth forecast 2016-18: 4.5%

SA exports to Mauritius in 2015: R3.4bn

SA exports to Mauritius, average 2011-15: R2.7bn p.a.

- Processed food
- Coal mining
- Agriculture & forestry
- Other chemicals (esp. pharmaceuticals, soaps, pesticides)
- Motor vehicles, parts & accessories
- Machinery & equipment
- Coke & refined petroleum products
- Basic iron & steel products
- Basic chemicals
- Metal products (excl. machinery)

Source: IDC analysis, compiled using IMF, UNCTAD and SARS data

Sectors expected to contribute most to overall growth in the medium-term

In identifying and ranking the sectors that may deliver the largest contributions to what is likely to be a modest economic growth performance over the next three years, the projected rates of expansion for each individual sector were utilised, based on the performance of key growth drivers, as well as their relative shares in national GDP. Consequently, a fast growing, but relatively small sector may not necessarily feature amongst the largest contributors. Conversely, a larger sector that is expected to turn out a modest, but nevertheless significantly above average growth performance may rank among the top 15 contributors to overall growth, as listed in the table below.

15 sectors expected to contribute the most to overall economic growth over the period 2016-2018, and their key drivers

Economic sector	Contribution to growth	Key drivers of sector growth			
		Domestic demand drivers			*External demand drivers*
		Households	Corporates	Public sector	
Top services sectors:					
Business services					
Finance & insurance					
Wholesale & retail trade					
Communication					
Civil engineering & other construction					
Transport & storage					
Electricity, gas & steam					
Top manufacturing and mining sectors:					
Processed food					Mainly rest of Africa, EU
Coal mining					Mainly India, EU, rest of Africa
Motor vehicles, parts & accessories					Mainly EU, USA, rest of Africa
Metal products, excluding machinery					Mainly rest of Africa
Petroleum products					Mainly rest of Africa, EU
Machinery & equipment					Mainly rest of Africa
Plastic products					Mainly rest of Africa
Chemical products (e.g. pharmaceuticals)					Mainly rest of Africa, EU

Relative contribution to growth:

Strong ⟷ **Weak**

Source: IDC Research and Information

As illustrated, services sectors are projected to make the largest contributions to growth over the next three years, with weak domestic and/or global demand for manufactured goods and mining products generally being constraints to medium-term growth in these sectors. There are, however, some exceptions. The agriculture sector's output, in turn, will continue being harshly affected by the severe drought in the near-term. Although the El Niño weather phenomenon may have peaked and better rainfall could possibly be expected in the forthcoming season, the dire financial position of the farming community will impact on their planting decisions in the shorter term.

The business services sector is almost entirely dependent on the domestic market as only a very small share of its activity is reliant on foreign demand, with the latter anticipated to be rather subdued over the outlook period. The household sector is a substantial user of business services and, therefore, the challenging consumer environment will impact on demand for business services. However, as indicated earlier in the report, the anticipated rates of increase in household spending on specific services items, although modest, may be relatively more favourable than for non-durable, semi-durable and particularly durable goods. Corporate demand supports the bulk of the activities of the business services sector and is projected to continue being the main driver of its performance over the next three years.

Similarly, corporate sector demand will underscore the anticipated levels of activity in the finance and insurance sector, while gradually improving household spending should support retail trade growth, particularly later in the forecast period. Although the communications sector is forecast to expand at a relatively good pace over the outlook period, specifically at an average rate of 2.1% per year, its contribution to overall economic growth is projected at only 0.06 of a percentage point due to the sector's fairly small 2.8% share of national GDP (based on 2015 statistics).

Considering that construction work comprises around 57% of public sector expenditure, the R865 billion that government and public corporations will be spending on infrastructure development over the next three fiscal years will continue driving the performance of the civil engineering sector. The value added by the electricity, gas and steam sector is expected to increase significantly as from 2017 due to the commissioning of various units of Eskom's new power plants.

Reflecting the competiveness of the domestic food processing sector on the global stage, South Africa exports food products to many countries, including all those highlighted in the previous section. Demand from South African households and external markets should underpin a relatively good contribution from this sector to overall economic growth. The sector is also expected to benefit from a normalisation of climatic conditions and agricultural input prices later in the forecast period.

The coal mining sector will benefit from the country's expanding electricity generation capacity as various units of Medupi and Kusile come on stream from 2017 to 2018. Furthermore, Eskom recently announced that it would be undertaking continued maintenance on its older generation power plants instead of moth-balling them, and that it has entered into five-year contracts with coal mining companies to accommodate its future input requirements. On the export front, the growth potential is quite limited outside of the Indian and a few African markets, considering the over-supply situation in China.

South Africa's automotive sector has long received a substantial measure of state support and has gained global recognition for the build quality of its vehicles. The ability of the sector to compete in world markets is attested by the fact that its vehicles are exported to advanced economies such as the EU, USA and Japan, as well as to other African markets. The increased participation of the domestic automotive industry in the global supply chains of multinational motor vehicle manufacturers is yielding significant benefits, especially since local household demand for vehicles is expected to remain rather subdued in the short- to medium-term. Corporate demand for commercial vehicles is projected to be relatively stronger over the next three years.

Benefitting from continued policy support through the Automotive Production Development Programme (APDP), the automotive industry is expected to record increased investment activity. At the recent launch of the 8th iteration of the Industrial Policy Action Plan (IPAP), Minister Rob Davies announced that a post-2020 Automotive Master Plan is being developed so as to guide support for the sector beyond the APDP. The entire automotive industry will be analysed in the process so as to include light, medium and heavy vehicles, as well as motorcycles.

Although the growth trajectory of passenger vehicle exports is largely pre-determined at the global headquarters of original equipment manufacturers (OEMs), the local content of domestically produced vehicles is expected to increase over time. An expanding and export-oriented components' manufacturing segment is also likely to participate increasingly in global value chains. The motor vehicle and parts sector is projected to grow at an average of 2.7% per year, contributing roughly 0.03 of a percentage point to national economic growth over the next three years.

Moreover, the importance of the motor vehicles, parts and accessories sector lies in its strong inter-industry linkages with numerous suppliers of goods and services in the economy. Through these linkages, this sector is a key driver of production activity and job creation in many of its supplying industries such as metal fabrication, electronics, plastic products, textiles (seats) and rubber, among others.

The metal products (excluding machinery) sector is expected to benefit significantly from public sector procurement. The impact will be indirect through the demand from the corporate sector as a supplier to the state and public corporations, as well as directly via numerous product designations. Other African markets should also provide a significant source of demand through exports.

Domestic corporate demand for machinery and equipment is expected to remain modest over the forecast period, supported mainly by spending for maintenance and upgrading purposes rather than expansionary investments. However, fixed capital formation by the business sector should respond positively to the increased availability of electricity later in the forecast period. This should permit a revival of investment in greenfield and brownfield projects, as well as attract foreign direct investment, with positive implications for the machinery and equipment sector.

Public sector demand for machinery and equipment is expected to emanate mostly from state-owned enterprises, as capital spending by general government will remain constrained for some time by fiscal challenges. Exports of machinery and equipment to the rest of Africa, which consist largely of mining and agricultural machinery, are likely to continue accounting for a considerable and growing share of overall demand.

The plastics industry has strong linkages with most sectors of the economy as its products have a very wide range of applications. As such, demand pull from both the relatively faster growing as well the lagging sectors underpin its projected growth performance and respective contribution to overall economic growth. The anticipated increase in the value added by the industries manufacturing chemical products is largely underscored by the expected performance of the pharmaceuticals segment, with government procurement, household consumption spending and exports as the key drivers.

Should the rates of growth of the catering and accommodation sector and/or of the agriculture, forestry and fishing sector exceed current projections, either or both of these two sectors could feature amongst the Top 15, potentially replacing the chemical products and/or the plastics industries in the rankings.

Department of Research and Information

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