Industrial Development Corporation

Your partner in development finance

Economic overview:

Recent developments in the global and South African economies

November 2018

Department of Research and Information

Contents

Highlights

- Citing the impact of the US-China trade war on the world economy, the International Monetary Fund (IMF) has lowered its projections for global growth to 3.7% for both 2018 and 2019. Nevertheless, the United States (US) economy continues to perform well, supported by the recent tax reductions as well as rising employment and wages. The US Federal Reserve has maintained the pace of monetary policy normalisation on the back of upward inflationary pressures.
- A weak expansion momentum is anticipated for the European Union as growth-suppressing risks loom large. These include, within the regional bloc itself, the showdown over Italy's budget and the possibility of a hard Brexit, while externally the intensifying protectionist trends in the global trading arena bring forth serious challenges.
- Among the BRICS economies, Brazil, Russia and South Africa are expected to continue experiencing low levels of growth for some time. Economic activity in China is already being affected by the trade war with the US, and the trend will intensify unless the two countries reach a compromise soon. China's growth is consequently anticipated to moderate over the forecast period. India, in turn, is expected to continue posting strong rates of economic expansion.
- A slowing Chinese economy, particularly industrial activity, is posing considerable downside risks across the commodities complex. The extent of downward price pressure may, however, be limited due to the countering effects of elevated crude oil prices and the Chinese authorities' efforts to support the domestic expansion momentum, among other factors.
- Sub-Saharan Africa's growth prospects remain positive, albeit modest. Relatively subdued growth rates in the region's two largest economies, Nigeria and South Africa, continue to hold back aggregate headline growth, despite a still supportive global environment characterised by firmer commodity prices and strong external demand. The pace of economic expansion in the region is expected to gather momentum from 2019 onwards, but an increasingly uncertain external backdrop is likely to keep growth below the 4% mark.
- The South African economy is expected to return to positive growth in the third quarter of 2018, following the technical recession recorded in the first half of the year. Higher output is expected in the manufacturing sector, whereas improved sales volumes in the retail and wholesale trade sector, alongside higher new motor vehicle sales, should also contribute to the economic recovery.
- Despite the anticipated rebound, the domestic economic environment remains challenging, as evidenced by low confidence levels in the household and business sectors. Local demand is still weak and external markets are being affected by US-led protectionism and tension. As such, the recovery is likely to be muted in the shorter-term, as alerted by the recent decline in the leading business cycle indicator.
- Although the South African economy created 92 000 additional jobs in the third quarter of the year, its labour absorption capacity is insufficient to absorb all new entrants into the market. Consequently, the unemployment rate remains very high, now measuring 27.5%.
- Government finances have worsened despite the continued commitment to fiscal consolidation. The main budget deficit is set to remain above 4% of GDP over the entire MTEF period to 2023, while the gross loan debt of government is projected to increase substantially towards 59.6% of GDP by 2023/24. The credit rating agencies

World GDP growth forecasts:

3.7% in 2018
3.7% in 2019

(IMF)

Sub-Saharan Africa GDP growth forecasts:

3.1% in 2018
3.8% in 2019

(IMF)

South Africa's unemployment rate:

27.5% in Q3 2018

(Stats SA)

South Africa GDP growth forecasts:

0.8% in 2018
1.6% in 2019

(IDC)

have expressed concern over the persisting structural constraints in the economy, which are negatively affecting its growth momentum and by, implication, the fiscal metrics. In its preliminary assessment of the October 2018 Mid-Term Budget Policy Statement, Moody's characterised such developments as "credit negative".

- Lacklustre growth of 0.8% is now projected for the South African economy in 2018, with a gradual improvement expected in subsequent years, taking the average growth for the period 2018-2023 to 2.3% per year. Although household spending is anticipated to be a key driver of growth, its contribution is likely to remain quite modest earlier in the outlook period. The rate of increase in private sector fixed investment should accelerate towards the later years, as improving demand conditions take utilisation of production capacity to significantly higher levels.

- The economic outcomes could, however, be significantly better if effectively enhanced by the ongoing Presidential initiatives, specifically the economic stimulus and recovery plan, the interventions delineated in the framework agreement reached under the auspices of the Presidential Jobs Summit, and the USD100 billion investment drive.

Implications for South African businesses

Implications of global economic developments

- Although the growth forecasts for the world economy have been moderated, global demand is expected to remain generally supportive of South Africa's export sector, especially in the short-term.

- Despite relatively robust rates of economic growth in more recent years, prospects for the US and Eurozone economies are not as favourable going forward, particularly from 2020 onwards. Combined, these two major export markets account for close to 30% of SA's total merchandise exports. Companies that are reliant on these external markets should thus follow developments closely and plan accordingly.

- The increasingly tense trading relations between the US and China have the potential to destabilise global trade flows and ultimately overall world growth. Weaker global growth and an increasingly challenging trading environment would affect many economies, including South Africa's, both directly and indirectly. It is therefore crucial that businesses monitor such developments attentively, identifying not only potentially negative implications but also export market development opportunities in a fast-changing world trade environment.

- Monetary policy tightening in advanced economies, led by the US, will continue to affect global capital and currency markets. On occasion, this will potentially re-direct capital flows away from emerging markets, in the process possibly weakening their currencies, raising inflationary outcomes and applying pressure on their monetary authorities to raise domestic interest rates. Emerging markets with large structural imbalances, including South Africa, are likely to be most affected.

- Economic activity is anticipated to recover in several African economies, which should result in increased import demand. Since the rest of the African continent is a leading market for South African exports, particularly manufactured goods, this could have positive implications for local exporters.

- Moreover, significant infrastructure investment is anticipated in several African countries. This should also have a beneficial impact on South African businesses, whose production activities are closely aligned with investment activity, as demand for materials and/or services (e.g. engineering and construction services) could rise substantially.

Implications of domestic economic developments

- On the domestic front, it is expected that as consumer confidence improves and employment levels increase, overall household consumption expenditure will gain momentum, particularly towards the latter part of the outlook period. This should provide business opportunities for many local companies whose production activities are linked to consumer spending.
- Although modest at present, private sector fixed investment is projected to pick up over the outlook period. This should have positive spin-offs for a range of supplier industries that focus on investment spending as an important driver/market for their own production activities. In light of the high import intensity generally associated with fixed investment activity in the South African economy, this should also create import replacement opportunities.
- Private sector fixed investment activity is likely to be enhanced by initiatives such as the economic stimulus and recovery plan, the action plans contained in the framework agreement reached under the auspices of the Presidential Jobs Summit, and the catalytic impact of the Presidential investment drive. These initiatives aim to create a more business friendly and enabling investment environment with the objectives of raising economic growth, creating employment and reducing poverty and inequality.
- The anticipated rebound in investor and business confidence following recent positive developments on the political and economic fronts should eventually be reflected in higher levels of fixed investment activity by the private sector. As utilisation of existing production capacity progressively increases, capital spending will eventually be required in a number of industries for the expansion of such capacity. Other than brownfield investment activity, greenfield opportunities are likely to be pursued by private players in a more conducive investment environment.
- Renewed commitments by government to enhance the localisation impacts of public sector procurement, including greater adherence to product designations, should translate into substantial benefits for many sectors/industries in the South African economy.
- South Africa’s growth prospects are set to improve over the outlook period, but a recovery in sentiment levels amongst businesses, investors and households will be key in this regard, so as to underpin higher levels of domestic demand, including fixed investment and household consumption expenditure.
- In the shorter-term, however, economic growth will remain subdued, with adverse implications for government’s fiscal consolidation and debt sustainability efforts. Moody’s has characterised such developments as “credit negative”.

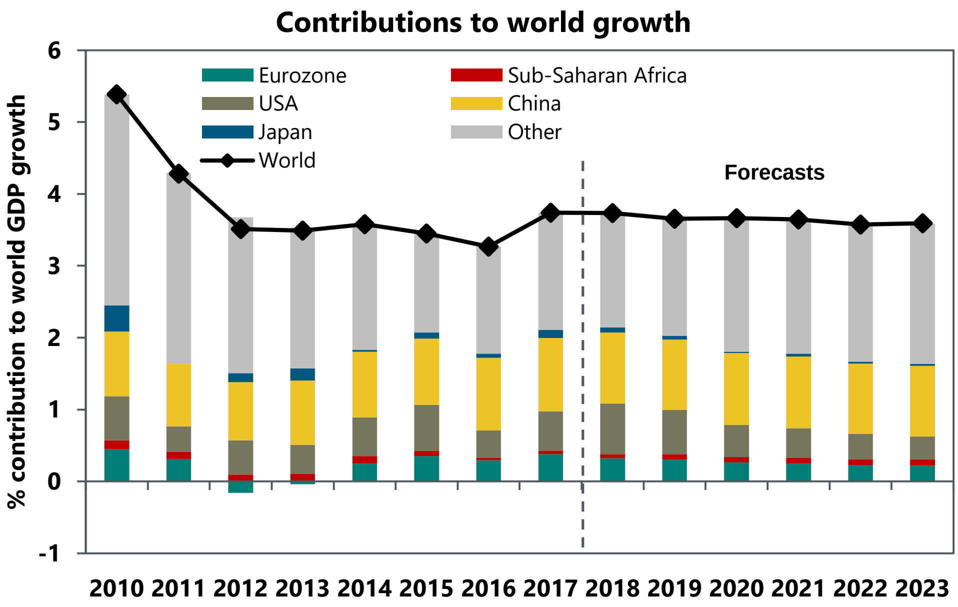
Global developments and outlook

Despite relatively robust performances by several of the world's larger economies, expectations are that such rates of expansion may not be sustained. In October 2018, the International Monetary Fund (IMF) revised its growth forecasts for the global economy down to 3.7%, for both 2018 and 2019, compared to the 3.9% projected in July 2018.

Global growth forecasts revised downward, risks remain considerable

Growth projections for the advanced economies have remained largely in line with previous expectations, pencilled in at 2.4% and 2.1% for 2018 and 2019, respectively. This may prove optimistic though, for the Eurozone economy is slowing at a faster than anticipated pace. The growth outlook for emerging and developing economies has deteriorated, with their collective output now projected to expand by 4.7% in both 2018 and 2019.

Figure 1: China and the US remain the main drivers of global growth



Source: IDC, compiled using IMF data

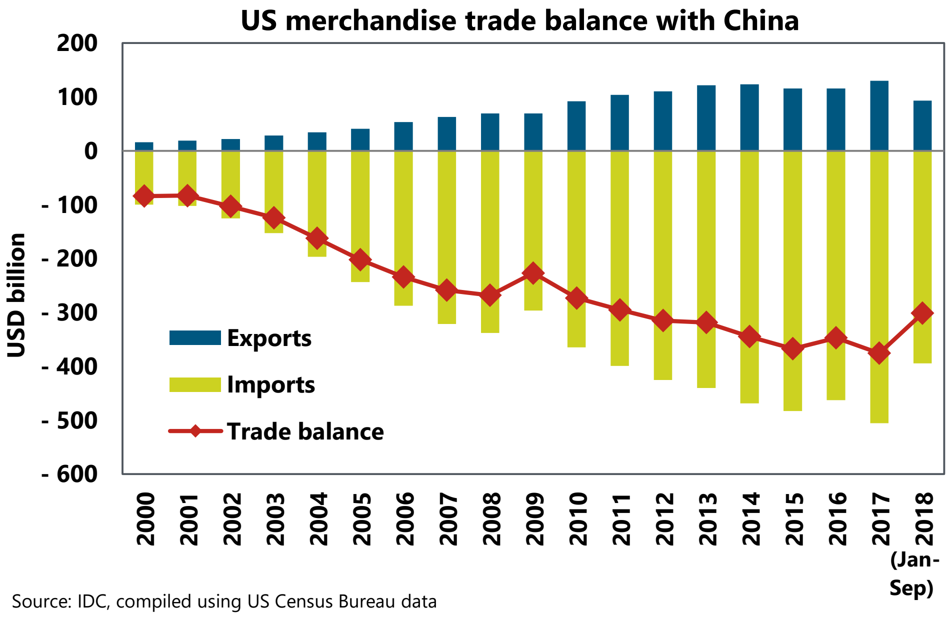
Economic growth in the Unites States (US) came in at 3.5% (quarter-on-quarter (q-o-q), seasonally adjusted and annualised rate (saar)) in the third quarter of 2018. Although still very strong, this rate of expansion was slightly lower than the 4.2% recorded in the second quarter. Despite this robust performance, there are signs that the US economy's expansion momentum is slowing.

US economic growth remains robust, although expected to slow in 2019

High levels of employment accompanied by significant wage increases are supporting strong growth in consumer spending. However, rising interest rates could weigh on future spending activity. Fixed investment expenditure contracted in the third quarter, potentially indicating that the impact of the corporate tax cuts on investment activity is falling short of the Trump administration's expectations, but also reflecting concerns over the effects of US trade policy.

The IMF projects US growth of 2.9% in 2018, slowing to 2.5% next year. The risks to these forecasts are tilted to the downside. The contraction in US exports during the third quarter provides an early indication of the negative implications of a US-China trade war. The conclusion of the US-Mexico-Canada (USMCA) agreement, which replaces the NAFTA agreement of 1994, however, alleviates some of the uncertainty over regional trade, which is crucial for business activity in the three North American economies.

Figure 2: Higher US tariffs set to narrow its trade deficit with China



Source: IDC, compiled using US Census Bureau data

World markets reacted positively to the US mid-term elections' results

Global equity and financial markets reacted positively to the outcome of the US mid-term elections, with sentiment towards emerging market (EM) assets also improving, as reflected by the appreciation of several EM currencies, including the rand. The positive reactions were largely based on expectations that economic policy-making and actions in the US could become somewhat less unpredictable. Although fiscal spending is subject to congressional oversight, the presidency has strong autonomy on international and trade policies.

Economic growth weakening significantly in the Eurozone

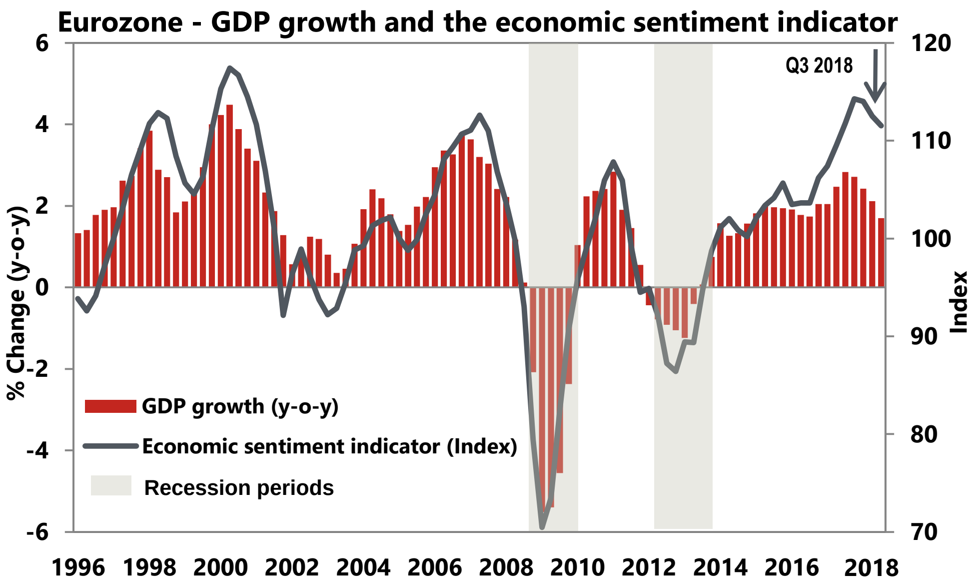
Economic conditions in the Eurozone deteriorated in the third quarter of 2018. Growth slowed to 0.6% (q-o-q, saar), from 1.8% in the previous quarter. This was partly attributable to weaker consumer spending and subdued industrial production activity. German vehicle manufacturers, for example, reduced production volumes as they ensured that vehicles adhered to newly introduced emission standards. The fragility of growth in the regional bloc supports the European Central Bank's (ECB) cautious approach to monetary policy, specifically the winding down of its quantitative easing programme and the start of interest rate normalisation.

The IMF revised its projections for output growth in the Eurozone to 2% in 2018, but left its forecast for 2019 unchanged at 1.9%. The bloc's future performance will be strongly influenced by both external and regional developments with respect to specific factors. Importantly, the trading relationship between the wider European Union (EU) and the US, particularly the use of trade protection measures, will be critical for production activity across several industries and countries.

In the EU, the Brexit issue remains a major source of uncertainty. Negotiations with the United Kingdom have not yet yielded an agreement on the relationship post-March 2019. Consequently, governments on both sides of the channel have started setting out guidelines for companies in case no agreement is reached, commonly referred to as a "hard Brexit".

Developments in Italy are also particularly concerning from the standpoint of currency bloc stability. In its recent budget proposals, the Italian government tested the EU rules and consequently met with opposition from Brussels. The Italian economy's stagnation in the third quarter of 2018 (growth rate of 0.1% q-o-q, saar) already undermines the premise of a stronger economic environment on which the budget proposals were predicated. Persistent concerns over Italy's structural challenges underpin increasing investor pessimism, leading to increased borrowing costs.

Figure 3: Weaker economic sentiment pointing to subdued Eurozone growth



Source: IDC, compiled using OECD and EC data

In China, economic growth slowed to 6.4% q-o-q (6.5% y-o-y) in the third quarter of 2018, slightly lower than the 6.8% recorded in the previous quarter. Slower rates of increase in consumer spending and infrastructure investment activity were countered to some extent by stronger export activity, possibly related to efforts to get products into the US market before the September tariff increases on around USD200 billion worth of Chinese exports. Chinese trade data for October further supports this view, as exports increased by 15.6% year-on-year. Imports into China rose 21.4% y-o-y, backed by the stimulus efforts of the Chinese government to limit the economy's slowing momentum.

The US-China trade war is showing signs of having an impact on the Chinese economy

Growth in credit demand remains weak despite the People's Bank of China's easing of its reserve requirements to encourage formal bank lending activities. The curtailment of credit demand growth could be related to concerns regarding the impact of the trade war on the Chinese economy, as well as continued efforts to clamp down on the lending activities of non-financial companies. The ability of the state to support growth through infrastructure development is becoming more constrained, especially at local government level.

The IMF kept its growth estimate for China in 2018 unchanged at 6.6% (6.9% in 2017), but lowered its 2019 projection to 6.2%, largely due to expected impacts of the trade war with the US. The structural changes currently underway in the Chinese economy are likely to curtail its medium-term growth prospects to some extent. However, this re-alignment is deemed necessary for the sustainability of growth in the long run.

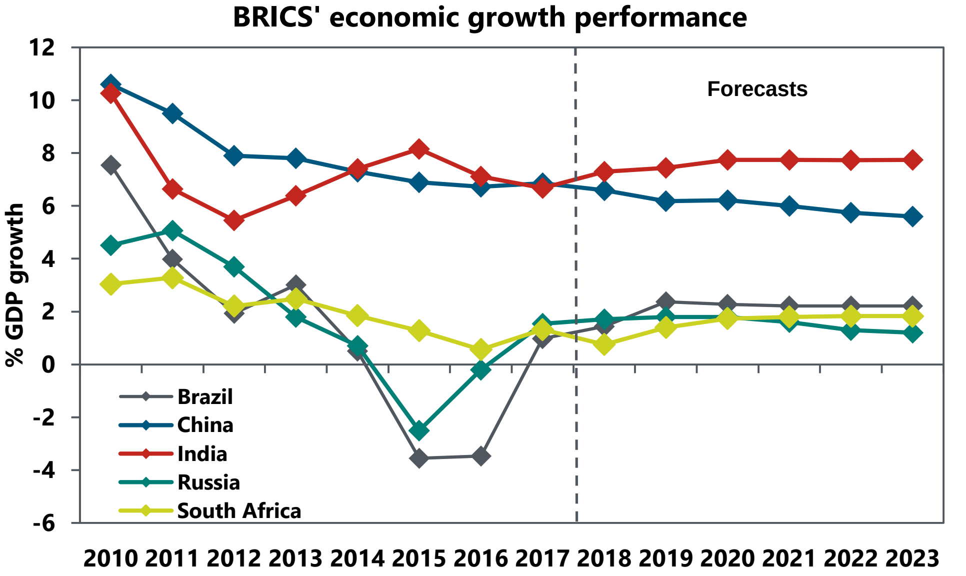
BRICS economies expected to post weak and/or declining growth rates, with India being the exception

The outlook for the Indian economy remains very positive, with growth projected to accelerate from 6.7% in 2017 to 7.3% in 2018, and to 7.4% next year. The ongoing reform programme is supporting investment activity as well as household consumption. The opening of the Indian economy to foreign companies is very gradual, providing the economy to adjust to the entrance of new players, while still supporting domestic enterprises. India remains vulnerable to rising commodity prices, especially oil, with recent price increases aggravated by a weaker currency expected to slow the economy's expansion momentum to some extent.

The Brazilian economy is still recovering from the recession it endured from 2015 to 2016. Growth is expected to improve slightly from the 1.0% recorded in 2017 to 1.4% in 2018. Newly elected President Bolsonaro sees the lowering of the country's debt burden and increasing international trade as critical for restoring economic growth. Efforts in this regard, combined with lower levels of state control over the economy and measures to address rampant corruption, could result in faster growth than is currently projected for 2019 (2.4%), although much will depend on the ability to deliver on the promises made during the electoral campaign.

Russia's improved economic performance has been supported by the recovery in oil prices, as the sanctions imposed by western countries continue to hamper production and investment activity. Domestic demand conditions are also improving as economic activity recovers, while monetary policy is expected to be relaxed as inflationary pressures recede.

Figure 4: Growth expectations for the BRICS economies below historical levels



Source: IDC, compiled from IMF data

Industrial commodities: global growth prospects highlight downside risks

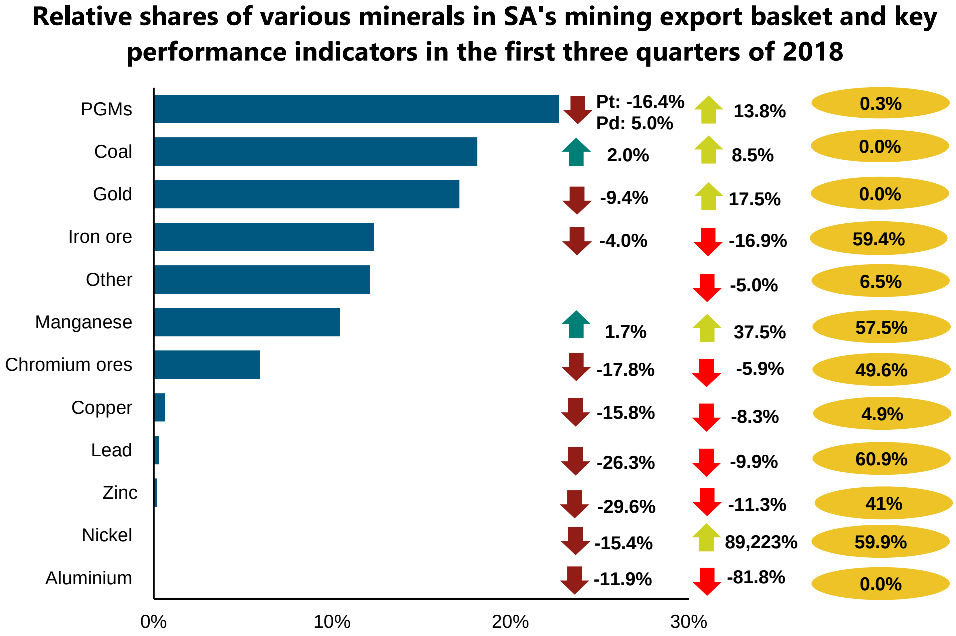
Downside risks for commodities have increased in the shorter-term

Industrial commodity prices have generally performed well since 2016, although platinum and iron ore are notable exceptions due to adverse supply-side dynamics. In most metal markets, resilient industrial productivity growth in China along with supply-side rationalization have tightened market balances, precipitating broad price recoveries across industrial commodities and base metals. However, this upward price momentum in the commodity complex has been halted since the second quarter of 2018, amidst escalating global macro-financial and geopolitical risks, which have also weighed on the outlook for the world economy.

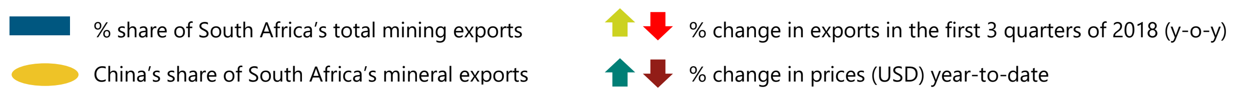
Emerging risks in the external economic environment, dominated by the US-led trade war, have noticeably weighed on China's economy, posing considerable downside risks across the commodities complex. Nevertheless, the prospects of steep declines in prices are being countered by elevated crude oil prices, which not only have anchored global inflation expectations, but also added to the marginal cost of production in individual industrial commodity markets – thus raising the perceived price floor in these markets.

While global manufacturing activity is still expanding, the downturn in China's manufacturing PMI in recent months to 50.2 in October, forewarns of downside risks to industrial commodity demand in the months ahead. China accounts for more than 50% of global industrial commodity consumption. In the current environment of softening demand growth, the industrial commodities that experienced supply-side gains during the recent commodity price recovery are likely to face the greatest downside risks.

Figure 5: The performance of South Africa's mineral exports was mixed in the first three quarters of 2018



Source: IDC, compiled using SARS and Bloomberg data



The commodities most at risk are those related to the steel value chain, as supply reform and capacity reductions in China are expected to impact negatively on commodities such as manganese, iron ore, coal, as well as hot-rolled coil steel itself. The manganese market recently experienced a surge in mine supply growth, while the iron ore market is anticipated to remain in surplus over the medium-term. Despite supply reforms in China, elevated steel-mill profit margins have kept production at relatively high levels, which should sustain the surplus in the global steel market for longer.

Commodities associated with the steel value chain are vulnerable over the medium-term

The extent of downward pressure may, however, be limited by recent pledges from Chinese authorities to support domestic growth, via both monetary and fiscal stimulus. This may tentatively support market sentiment for commodities across the steel value-chain as well as other base metals.

Chinese authorities' pledge to support growth may prevent steep declines in commodity prices

Strategically, tightening market balances due to supply-side constraints and robust demand support the medium- to longer-term outlook for base metals, particularly aluminium and copper. According to the key messaging expressed at the recent London Metal Exchange (LME) Week, the US-China trade war has not perturbed trading activity in key base metals (especially battery minerals in general), which supports a positive longer-term prognosis. The global vehicle electrification trend is, furthermore, expected to have a beneficial impact on the long-term outlook for copper, while aluminium consumption remains well supported by world trends across industrial applications to reduce weight.

Recent developments in and prospects for Sub-Saharan Africa

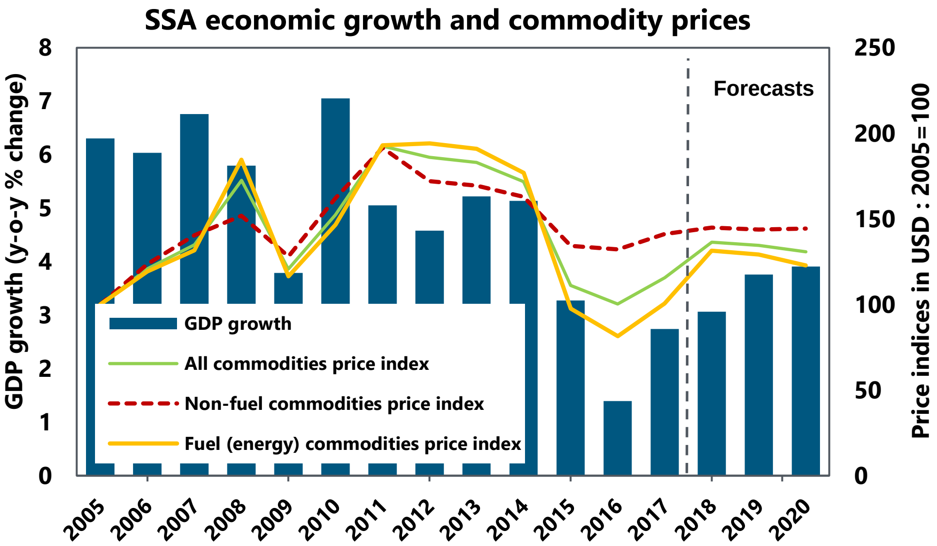
Growth prospects for the SSA region remain positive, albeit still tentative

Growth in Sub-Saharan Africa (SSA) depends, to a large extent, on developments in the economies of its key trading partners as well as in global commodity markets. As such, the past few years have been rather challenging, with the rate of expansion in the region's output slowing discernibly.

However, a modest improvement in SSA's growth is anticipated in 2018, albeit slower than previously projected. The outlook is supported by a firmer global economy, relatively improved commodity prices, favourable weather conditions and increased fixed investment activity, although the dynamics vary across countries. Nevertheless, persistent weaknesses in the region's major economies continue to pose serious challenges.

Weak growth projections for Nigeria (1.8%) and South Africa (0.8%) in 2018 undermine the overall growth projections for SSA as a whole, limiting it to 3.1%. The prospects for 2019 appear to be better, as growth of 3.8% is projected by the IMF. Excluding the impacts of Nigeria and South Africa, the growth projections for SSA improve to 4.6% and 5.4% in 2018 and 2019, respectively.

Figure 6: Growth recovery slower than previously anticipated in 2018



Source: IDC, compiled from IMF World Economic Outlook databases, October 2018

Economic activity in less resource-intensive economies such as Ethiopia, Rwanda, Côte d'Ivoire, Senegal and Kenya is likely to remain strong, supported by robust domestic demand, especially due to government-led infrastructure investments. These economies are expected to grow at an annual average rate of more than 6% over the three-year period to 2020. Among the resource-intensive (non-oil) economies, growth rates of over 6% are limited to a few, such as Ghana and Tanzania. Despite a modest recovery in international oil prices, the GDP growth of the oil exporters is likely to remain subdued at 1.6% and 2.4% in 2018 and 2019, respectively, albeit with some notable improvements in some countries.

An external environment that is becoming more uncertain could, however, dampen sentiment towards the SSA region. Relatively high debt levels, continued vulnerability to volatile conditions in global financial and commodity markets, alongside the adverse impact of the US-China trade war and wider geo-political risks could weigh on growth, trade and investment into the region. The IMF estimates that the impact of global trade disruption could result in a cumulative loss of GDP of approximately 1.5% between the period 2018 to 2021 for Sub-Saharan Africa.

Recent developments in the South African economy

Sectoral performance

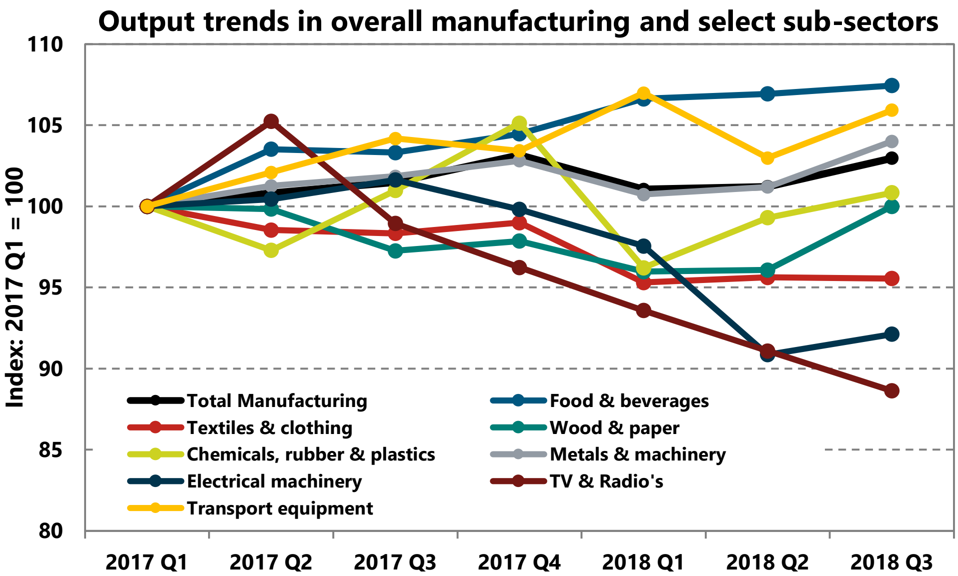
The South African economy is likely to have exited the technical recession experienced during the first semester of 2018, considering the available data for the quarter ending in September 2018. Recent high frequency data point to marginal recoveries in some key sectors of the economy. However, these do not indicate a strong rebound.

The South African economy may have emerged from the technical recession

The manufacturing sector recorded a fairly strong recovery in the third quarter of the year as its output increased by 7.1% on a quarterly basis, with a number of sub-sectors recording higher production levels. The transport equipment sub-sector saw its output rising at a rapid pace, and solid rates of expansion were also recorded by the sub-sectors producing chemicals, metals and machinery, wood and paper, furniture and other manufactured items. In turn, lower output levels were recorded by the sub-sectors manufacturing television and radios, non-metallic mineral products, as well as food and beverages.

Manufacturing sector posted a recovery in the third quarter

Figure 7: Manufacturing output rebounded, but challenges remain



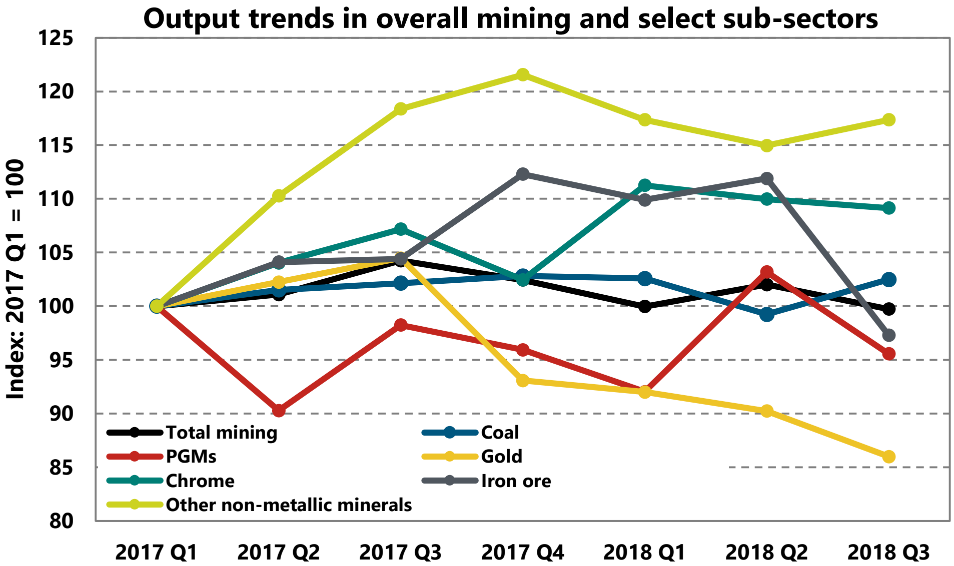
Source: IDC, compiled using Stats SA data

The manufacturing sector is, however, still taking strain in a difficult operating environment characterised by low confidence, weak domestic demand and increasingly challenging conditions in the global trading environment. Manufacturing business confidence, with a reading of 21 points for the quarter ended in September 2018, is at its third lowest level since 2009. Manufacturers' expectations regarding business conditions in 12 months' time fell sharply. Furthermore, the manufacturing purchasing managers' index (PMI) fell to a 15-month low of 42.4 points in October, worse than anticipated.

The output gains recorded by the mining sector in the second quarter of the year (8.4% growth q-o-q) were reversed by an 8.6% drop in its overall volume of production in the third quarter. Sharply lower output was reported by most mining sub-sectors, except for the segments mining coal and other non-metallic mineral products for their production levels increased.

Mining sector under severe strain

Figure 8: Mining output under pressure

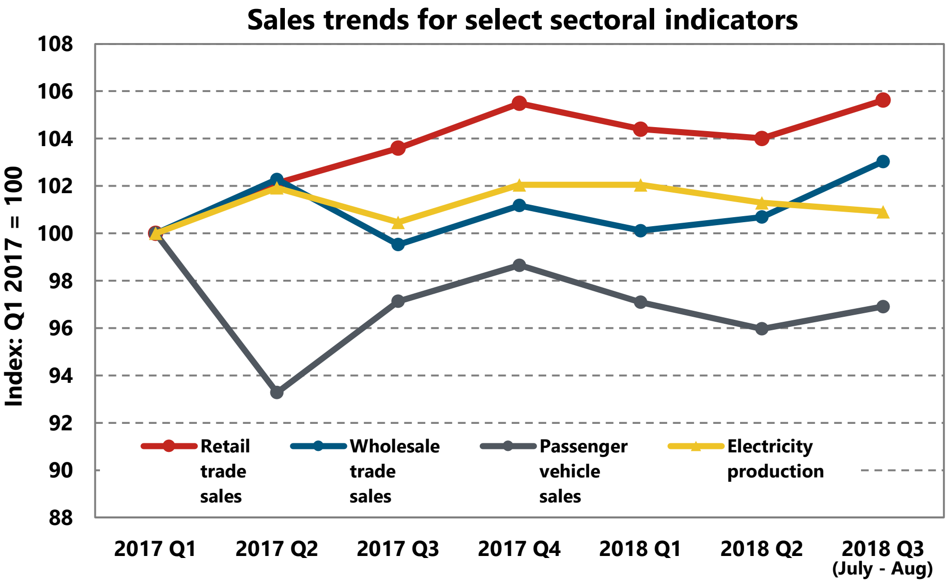


Source: IDC, compiled using Stats SA data

After a difficult first half of the year, the retail trade sector recorded a modest up-tick in sales volumes in the third quarter (based on data for July and August). Although households continue facing financial constraints, sales of new vehicles also rose modestly in the third quarter of 2018. Recent trends in both retail trade and passenger vehicle sales provide some optimism that the high levels of consumer confidence achieved in the first two quarters of the year may eventually feed into renewed spending by households.

In the light of the economy's poor performance, it is not surprising that lower electricity production has been recorded for the year to date. Moreover, Eskom is facing coal shortages at a number of its power stations. This is not only affecting electricity generation currently, but may also result in load shedding if the situation is not addressed in a decisive manner.

Figure 9: Services sectors showing a mixed performance



Source: IDC, compiled using Stats SA, SARB data

Employment trends

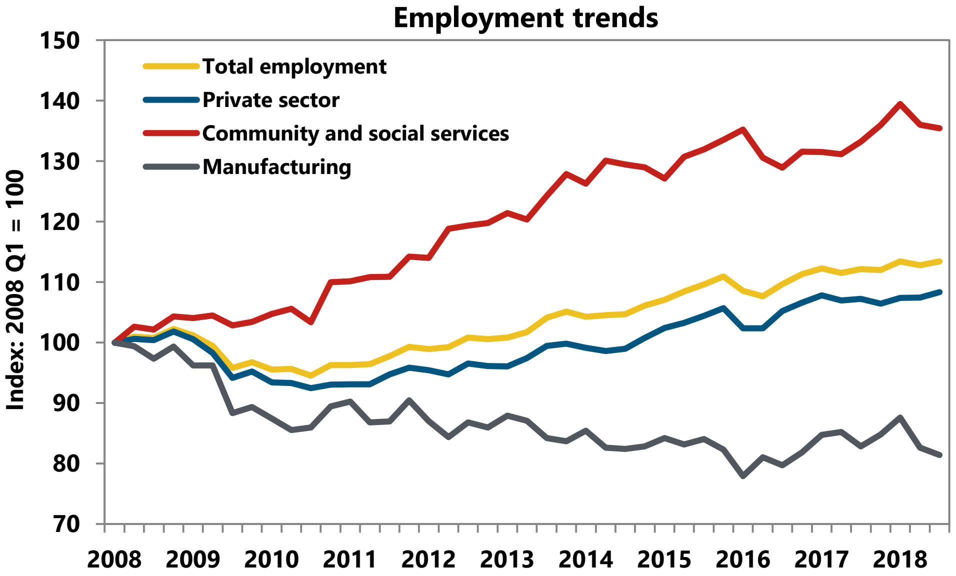
More jobs created, but unemployment rate still very high

The economy created 92 000 additional employment opportunities in the third quarter of 2018, thereby reversing the 90 000 job losses witnessed in the preceding quarter. Of concern is the fact that only the informal sector created jobs (188 000), while 65 000 jobs were lost in the formal non-agricultural sector. A further 30 000 job losses were reported by private households and agricultural sector employment fell by 1 000.

Employment intensity of the manufacturing sector on a decline

The manufacturing sector shed 25 000 jobs and is now employing almost 400 000 fewer people than at the start of 2008 (the most recent peak). Moreover, the sector's employment intensity (number of jobs per R1 million of real GDP) has been declining steadily for a prolonged period, reflecting its diminishing labour absorption ability in a highly competitive global manufacturing arena.

Figure 10: Gradual rise in total employment, but manufacturing still shedding jobs



Source: IDC, compiled using Stats SA data

South Africa has been grappling with high structural unemployment for many decades. The unemployment rate stood at 27.5%, or 6.2 million people without a job, in the quarter ending September 2018. Amongst the youth (15 to 34 years of age), the unemployment rate measured 39%, with just over 3.9 million young people unable to find employment.

The modest growth outlook for the economy will limit its labour absorption

Nearly 70% of the unemployed have been without a job for more than a year and, considering the limited skills in many cases, the chances of being re-employed in the formal sectors of the economy are possibly slim. Furthermore, considering the relatively subdued growth prospects for economy over the next couple of years, its labour absorption capacity will remain insufficient to meaningfully address the unemployment challenge at hand.

Fiscal performance

The fiscal metrics have worsened in a low growth environment

The October 2018 Medium Term Budget Policy Statement (MTBPS) reflected the impact of the economy's weak performance on government finances. Although government's commitment to fiscal consolidation and debt sustainability was reiterated, the fiscal metrics have deteriorated.

For the fiscal year to March 2019, revenue collections are now estimated to be R27.4 billion lower than budgeted, mainly due to higher VAT refunds of about R20 billion as government is attempting to reduce the backlog in this regard.

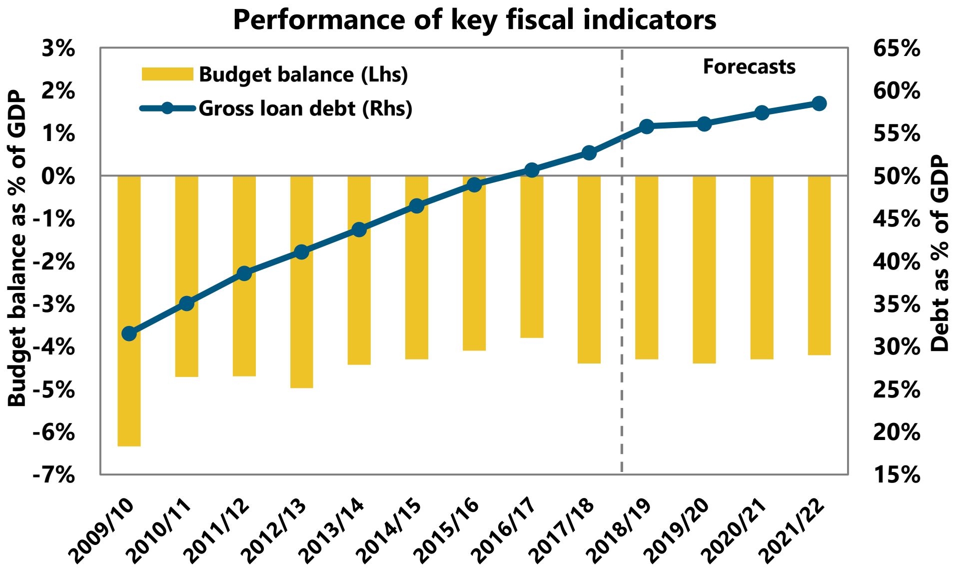
Fiscal deficit projections worse than anticipated

Partly due to the economy's growth projections having been downwardly revised, the main budget deficit to GDP ratio is projected to remain above the 4% level throughout the forecast period. The worsening fiscal situation is also partly due to above-budgeted salary increases over the next couple of years, whilst higher interest payments, which remain the fastest growing expenditure item, compound the problem.

Gross loan debt of government on a steep rising trend

The gross loan debt of government is projected to rise substantially in coming years to a level of R3.7 trillion by 2021/22, compared to the R2.8 trillion estimated in the 2018/19 fiscal year. As a ratio of GDP, the gross loan debt is expected to rise from 52.7% in 2017/18 to 58.5% by the end of the outlook period, stabilising at about 59.6% of GDP by 2023/24. Moody's has characterised such developments as "credit negative".

Figure 11: Worsening fiscal situation as the economy's weak growth takes its toll



Source: IDC, compiled using National Treasury data

Growth and employment enhancing initiatives led by the Presidency

Economic stimulus and recovery plan

In September 2018, President Cyril Ramaphosa announced an economic stimulus and recovery plan focused on implementing growth-enhancing economic reforms; reprioritising public spending to support economic growth and employment creation; establishing an infrastructure fund; addressing urgent matters in education and health; and investing in municipal social infrastructure.

This initiative aims to stimulate inclusive economic growth, catalyse investment activity and generate employment opportunities. It comprises interventions to support entrepreneurial development and training of the unemployed, assist small- and medium-sized enterprises, enhance localisation efforts associated with public sector procurement, and raise public sector spending on infrastructure development.

The Infrastructure Fund comprises a contribution from government of more than R400 billion over the next three years, which will be used to leverage funding from other sources, such as developmental finance institutions, multilateral development banks, as well as private lenders and investors. To ensure that infrastructure projects are implemented in a swifter, more cost-effective and developmental manner, particularly in terms of employment creation and localisation, the fund will be supported by a strong technical team in the Presidency.

Development finance will form an integral component of the economic stimulus and recovery plan.

Presidential Jobs Summit and framework agreement

At the Jobs Summit held on the 4th and 5th of October 2018, President Ramaphosa stressed the imperative of creating new jobs and retaining existing employment in the current economic environment.

According to the framework agreement reached between the government, business, labour and community constituencies of NEDLAC, businesses and government would establish, over the ensuing two months, rapid response teams of experts to assist businesses in crisis, with the modalities to be defined. The Training Layoff Scheme will be improved and revived. Funding and business turnaround expertise must be made available for distressed firms/sectors, with support from development finance institutions being key in this regard.

Stimulating demand for local products also forms an integral part of the framework agreement. Government committed to speeding up the process for the designation of products, including: the identification of possible products, assisted by a standing list of industry experts to support designation analysis; setting a timeframe of 30 days for National Treasury to finalise and issue circulars for designated products; capacity improvements at the South African Bureau of Standards; establishing a hotline to receive/deal with complaints on fraudulent claims regarding local content, flawed tender specifications and, among others, designations being ignored or circumvented. Furthermore, the Auditor-General will specifically include procurement practices in its audit scope for government departments.

Several private sector companies signed up commitments to buying local, and the business constituency will explore the creation of a b2b transparent procurement platform where firms can list their tenders and procurement requirements.

As part of the joint effort to mobilise finance for development on a much larger scale, the financial sector committed to invest R100 billion over five years in black-owned enterprises and firms empowered at Level 6 and above. The guidelines for disbursement of this funding are being developed by the Financial Sector Transformation Council and the DTI.

The financial sector and government also committed to working towards a single due diligence standard that is accepted by multiple financiers; developing interventions to "de-risk" industrial projects; implementing a guarantee facility to extend the term of financing provided to industrial projects, which will be funded by government; as well as creating sectoral/industry Enterprise and Supplier Development Funds. An Infrastructure Funding Task Team will be convened to develop infrastructure projects that crowd-in the private sector.

The social partners also agreed to undertake numerous interventions in various sectors identified as exhibiting significant growth and job creation potential. These include agriculture and agro-processing, manufacturing, mining, oil and gas, tourism and telecommunications.

The social partners also agreed to establish a Presidential Jobs Committee which will receive progress reports on and monitor the implementation of the interventions agreed upon, which aim to create an additional 275 000 direct jobs per year over and above the projections made in their absence.

Presidential investment drive and inaugural South Africa Investment Conference

The Presidential investment drive, which culminated in the inaugural South Africa Investment Conference held on the 26th of October 2018, represents a key milestone in national efforts to catalyse economic growth in a sustainable and more inclusive manner. The focus has been on addressing structural bottlenecks to capital investment as well as on enhanced dialogue with key stakeholders in order to resolve major challenges facing the business sector.

A new dawn as investment conference attracts huge interest

This investment drive entails an integrated, active and long-term investment mobilisation programme aiming to augment fixed investment spending in the South African economy by USD100 billion above baseline projections over the 5-year period to 2022. Although initially perceived as targeting international investment, the Presidential investment drive has had the unequivocal strategic objective of unlocking investment from domestic companies.

Investment potential can be unlocked through policy levers

Accordingly, efforts to date have centred on fast-tracking government processes to alleviate policy-induced uncertainty in key sectors of the economy, such as mining, telecommunications and tourism, as a basis to reverse the precipitous decline in domestic business confidence. Several sectoral policy challenges were either resolved ahead of the Investment Conference or addressed directly by the respective ministers through direct dialogue with potential investors.

The Presidential investment drive, which has also included domestic and international investment roadshows, has met with resoundingly positive responses from both the local and international business communities. R290 billion worth of investments were announced by companies in attendance at the highly successful South Africa Investment Conference 2018, where the country's compelling investment proposition was convincingly reiterated, as was the public sector's willingness to address structural bottlenecks. Improved investor confidence provides the foundation for higher and sustained economic growth over the medium- to longer-term.

SA economy set to benefit substantially from renewed investments going forward

Growth prospects for the South African economy

After a worse than anticipated performance in the first half of the year, IDC projections for real GDP growth in 2018 have been scaled down to 0.8%. It is, however, still expected that the pace of economic expansion will accelerate over the outlook period.

Subdued growth expected for 2018, rising thereafter

Growth in household spending is anticipated to pick up some pace on the back of gradually improving consumer sentiment, accommodative interest rates and job creation. However, limited growth in disposable income, rising costs of living and a reluctance to incur more debt will constrain the ability and willingness of households to meaningfully raise consumption spending.

Fixed investment activity is anticipated to increase at a progressively stronger pace as demand conditions improve and confidence levels rise, potentially being particularly robust later in the forecast period as utilisation of production capacity reaches high levels. Nonetheless, a substantially improved investment performance in the shorter-term is also possible, particularly in light of the major initiatives to stimulate economic growth, fixed investment activity and employment creation. Furthermore, such initiatives may result in substantially higher rates of growth in gross fixed capital formation than those currently forecast.

Private sector investment to gain a stronger momentum

Fiscal constraints are expected to limit the public sector's consumption and infrastructure investment expenditure throughout the outlook period. Government's fiscal consolidation and debt stabilisation efforts and outcomes will be closely monitored by the major credit rating agencies and the investor community.

Table 1: Outlook for the South African economy set to improve gradually

Key performance indicators for the South African economy

Variable (% change or % of GDP)	2014	2015	2016	2017	2018f	2019f	2020f	2021f
Real GDP growth and its components:								
Household consumption expenditure	0.8	1.8	0.7	2.2	1.8	1.9	2.6	2.8
Government consumption expenditure	1.7	-0.3	1.9	0.6	1.1	1.3	1.1	1.4
Gross fixed capital formation (GFCF)	0.7	3.4	-4.1	0.4	0.3	1.4	2.7	5.9
Exports	3.6	2.8	1.0	-0.1	1.4	3.0	3.2	3.6
Imports	-0.6	5.4	-3.8	1.6	3.0	3.7	3.7	4.2
GDP	**1.8**	**1.3**	**0.6**	**1.3**	**0.8**	**1.6**	**2.2**	**2.9**
Consumer price inflation	6.1	4.6	6.3	5.3	4.9	5.6	5.3	5.2
Current account balance (% of GDP)	-5.1	-4.6	-2.8	-2.4	-3.6	-4.0	-4.2	-4.1
GFCF as % of GDP	20.4	20.4	19.5	18.7	17.9	17.5	17.5	17.9

Source: IDC, compiled using SARB data, IDC forecasts

The potential implications of rising protectionism and tension in the global trading environment cannot be ignored, as it may affect the anticipated export performance, both positively and negatively, as well as import penetration due to trade diversion effects. A relatively weaker rand at present is likely to further enhance the price competitiveness of local exports. However, the currencies of other emerging markets have also depreciated considerably, in some instances to a greater extent than the rand, thus limiting the potential benefits to exporters.

Considering the relatively high import intensity associated with fixed investment activity in the South African economy, demand for imports is forecast to expand at a fairly robust pace. However, should government and state-owned enterprises succeed in maximising the localisation associated with public sector infrastructure investment and with the procurement of designated products, growth in imports may be lower than currently projected.

Department of Research and Information

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