Contents

Highlights ........................................................................................................................................... 1
Implications for South African businesses ........................................................................................... 2

Global developments and outlook ......................................................................................................... 4
Sub-Saharan Africa: Growth outlook and South African direct investment ........................................ 8
Recent developments in the South African economy .......................................................................... 11
Growth prospects for the South African economy .................................................................................. 17
Economic overview

Highlights

- The world economy’s expansion momentum is slowing more than previously anticipated. The International Monetary Fund (IMF) is projecting global economic growth of 3.3% for 2019, down from 3.6% in 2018. At the regional level, only Sub-Saharan Africa (SSA), as well as South and Central America are expected to post faster rates of expansion in 2019 compared to last year.

- Concerned with possibly weaker growth prospects while inflation remains generally below targeted levels, central banks in most advanced economies, including the United States (US), have paused their monetary policy tightening actions.

- The trade war between the US and China recently escalated after President Trump raised tariffs on USD200 billion’ worth of Chinese imports to 25%. The Chinese authorities have since retaliated by increasing tariffs by as much as 25% on US products totalling USD60 billion in import trade. Such developments will have adverse repercussions for both economies and the world at large.

- The industrial commodities complex has experienced relative price stability since the start of 2019, precipitated by improved investor risk appetite due to an anticipated resolution to the US-China trade spat, as well as improved manufacturing activity in China. However, the prognosis for industrial commodity prices is being constrained by geopolitical risks and by the recent deterioration in US-China trade relations.

- Although improving, the economic outlook for SSA remains relatively modest, with growth rates of below 4% projected for the next five years. Excluding South Africa and Nigeria, the regional economy is expected to grow at sturdy rates of around 5% in 2019 and 2020. Robust performances are anticipated from Rwanda, Ethiopia, Côte d’Ivoire, Ghana, Senegal, Uganda and Kenya.

- South African direct investment in the rest of the African continent has grown exponentially since the advent of democracy in 1994, but the pace of expansion tapered off after 2015 as economic conditions deteriorated domestically and growth moderated in the SSA region.

- After a dismal performance in 2018, the South African economy continues to face serious challenges, with various sectors under severe strain. In the first quarter of 2019, output levels were sharply lower in key sectors such as mining and manufacturing, affected by weak demand conditions and recurring interruptions in electricity supply. The difficult consumer environment was reflected in a steep drop in sales volumes of new passenger vehicles as well as in lower retail trade sales in real terms.

- Total employment in the domestic economy fell by 237 000 (quarter-on-quarter) in the first quarter of 2019, taking the unemployment rate to 27.6%, from 27.1% at the end of 2018. Substantial job losses were reported by several sectors, particularly construction, finance and business services, community and social services, as well as the embattled mining sector. Manufacturing sector employment, however, increased by 14 000 on a quarter-on-quarter basis.

- The outcome of the national elections held on May 8th could have a decisive impact on investor, business and consumer confidence, potentially leading to a sharp rebound if followed by effective action with regard to structural reforms aimed at boosting economic growth, greater policy certainty and coherence, increased localisation associated with public sector procurement and infrastructure development, concerted efforts to tackle the challenges at the power utility, Eskom, and visible progress in the fight against corruption. This could result in substantially increased production activity, fixed investment and employment creation.
Economic overview

• Growth prospects for the South African economy are expected to improve gradually over the five-year outlook period. GDP is forecast to expand by 1.5% in 2019, with the growth momentum projected to accelerate towards 3.2% by 2022. Household consumption expenditure will be a key driver of economic growth, whereas fiscal constraints are likely to curb government expenditure. Although fixed investment spending by the private sector is expected to remain relatively subdued in 2019, it could be bolstered by rising sentiment on the back of the implementation of pro-growth and business-friendly reforms following the election outcomes. The anticipated slowdown in economic growth in some of South Africa’s key trading partners could, however, have unfavourable implications for the country’s export performance.

Implications for South African businesses

Implications of global economic developments

• Slowing growth in China, the US and Germany, which are South Africa’s three largest trading partners at the individual country level, may constrain the performance of export-oriented businesses in the mining and manufacturing sectors.

• The escalating trade war between the US and China, alongside renewed threats of US protectionist measures being imposed on specific imports from the European Union, are raising risks (displacement of South African exports in existing external markets and import competition in the local market) as well as presenting export opportunities for the manufacturing, mining and agriculture sectors due to trade diversion effects.

• The postponement of Brexit to the end of October 2019 prolongs the uncertainty not only for the British and European Union economies, but also for their trading partners, such as South Africa, for they are likely to be directly and/or indirectly affected in the process. In the interim, companies based in or highly exposed to the United Kingdom are increasingly implementing contingency strategies, with potential implications (both positive and negative) for South Africa’s export sector.

• The improved outlook for Sub-Saharan Africa (SSA) bodes well for South Africa’s export sector. The rest of the African continent has become the leading global destination for South African exports at the regional level, having claimed a 26.5% share in the overall merchandise export basket and just over 39% of total manufactured exports in 2018. However, South African producers have, to-date, hardly tapped the export market development potential in the region’s fastest growing economies, specifically Rwanda, Ethiopia, Côte d’Ivoire, Ghana and Senegal, thus presenting significant opportunities.

• Notwithstanding the positive prospects for the SSA region, there are considerable risks at the individual country level. These include debt sustainability challenges in a number of countries such as Mozambique, Zimbabwe, Zambia and Sudan; vulnerability to adverse developments in commodity markets where resource-reliant African exporters are concerned, with their performance being strongly correlated to developments in the Chinese economy; and the trade diversion effects of increasing protectionism in the world trading arena, which may displace South African export products from existing African markets.

• The pause in monetary policy normalisation in major advanced economies, especially the US and the Eurozone, has prompted renewed flows of capital to emerging markets. In the short-term, such inflows could support emerging market currencies,
including the rand. However, due to their short-term nature, they could also result in significant currency volatility in future.

- US dollar weakness on the back of unaltered or potentially lower US policy rates would be largely supportive of industrial commodity prices as well as precious metals.

- Financial market jitters have recently resurfaced due largely to a spate of negative developments in the global arena, particularly the escalating trade war between the US and China, as well as substantial higher geopolitical risks due to increased tension between the US and Iran, among other factors. Such developments are affecting the performance of listed equities, particularly resource-based companies as well as those with significant exposures to the most affected world markets.

**Implications of domestic economic developments**

- The national election’s outcomes are expected to strengthen President Ramaphosa’s economic reform and stimulus agendas. Clear signs of a swift and effective roll-out of such reforms will be crucial for a substantial rebound in confidence levels amongst businesses, investors and households, setting the foundation for a virtuous cycle of growth, investment and employment creation.

- Private sector fixed investment could rebound strongly in a more business-friendly environment. This is based on the assumption of a significant turnaround in business and investor sentiment in anticipation of improving prospects for the South African economy. Businesses that are reliant on the investment cycle should pay close attention to economic developments and plan accordingly so as to take advantage of emerging opportunities in an improved investment climate.

- In the meantime, considering that many industries in the domestic economy currently have spare production capacity, fixed investment activity is likely to be of a maintenance and upgrading nature earlier in the forecast period. However, expansionary investments are expected to gradually gain momentum.

- In light of the limited fiscal space of general government, as well as the financial constraints and operational challenges experienced by a number of state-owned companies, infrastructure spending by the public sector is likely to remain constrained for some time. This could have continued adverse implications for the construction sector and respective suppliers, among other potentially affected industries. Effective efforts to enhance the localisation benefits of public sector procurement would, however, be a powerful mitigant in this regard.
Global developments and outlook

The world economy’s expansion momentum is slowing more than previously anticipated. The International Monetary Fund (IMF) is now projecting global economic growth at 3.3% for 2019, down from the 3.6% growth achieved in 2018. A relatively synchronised slowdown is expected around the globe, with the regional exceptions being Sub-Saharan Africa as well as South and Central America, for these regions should post improved economic performances in 2019 relative to last year.

Preliminary growth data for the first quarter of 2019 in the United States (US), China and the Eurozone were reasonably robust. However, the headline numbers mask underlying challenges that may constrain the ability of these economies to maintain their growth momentum over the remainder of the year. Concerned with possibly weaker growth prospects while inflation remains generally below targeted levels, central banks in most advanced economies, including the US, have paused their monetary policy tightening actions.

*Figure 1: Global growth to moderate in the short-term, recovering thereafter*

The US economy expanded by 3.2% (quarter-on-quarter, seasonally-adjusted and annualised rate) in the opening quarter of 2019, a recovery from the 2.2% recorded in the previous quarter. Although overall growth remains strong, both the pace of increase in and level of inventories point to a potential slowing in coming quarters. Furthermore, activity levels in the US have been fuelled by substantial tax reductions and higher fiscal spending. The beneficial transmission effects are, however, largely reflected in the economy’s growth rates hitherto.

Also concerning is the fact that personal consumption expenditure in the US increased by only 1.2% in the first quarter, while overall spending on durable goods declined. The weakness in US consumer spending is surprising given unemployment at 50-year lows and wage growth in excess of 3%, while inflation has remained below 2% in recent months.
Concerns over a possible recession in the US were prompted by the inversion of the yield curve on US government bonds (i.e. short-term interest rates being higher than long-term interest rates), for such a development had preceded recession periods in the past. However, this appears to be an overly pessimistic view, for slower growth is a more probable outcome. The IMF projects a moderation in US economic growth to 2.3% and 1.9% for 2019 and 2020, respectively, from 2.9% last year.

Although the impact of the trade spat with China on the US economy has been modest thus far, production costs, exports and investment activity have started being affected by higher tariffs and the associated policy-related uncertainty. Furthermore, hopes of a trade deal being concluded by mid-May were scuppered by President Trump raising tariffs on USD200 billion worth of Chinese imports from 10% to 25% on the 10th of May, after accusing China of reneging on previous commitments during the negotiation process.

The Chinese authorities have since retaliated by increasing tariffs by as much as 25% on USD60 billion worth of import products from the US. Tariffs on imports of US cotton, machinery and grains were raised from 10% to 25%, hitting directly on America’s agricultural heartland, while imports of US-produced aircraft parts, optical instruments and furniture will now face 20% duties upon entering the Chinese market, from 10% previously. The escalating trade war will have adverse repercussions for both economies and the world at large.

The most recent reading of the World Trade Indicator, released by the World Trade Organisation (WTO), came in at 96.3, the lowest since March 2010 (a reading below 100 indicates that global trade growth is set to be below the medium-term trend). Prevailing weakness in world trade is attributable not only to increasing protectionism and escalating tension, but, among other factors, also to the difficulties experienced by Germany’s automotive sector as new emissions standards impacted on vehicle production in the latter part of 2018 and early in 2019.

**Figure 2: World trade under pressure as trade tensions take a toll**

The trade war with the US is impacting on the Chinese economy, which expanded by 5.6% in the first quarter of 2019 (quarter-on-quarter, seasonally-adjusted and annualised rate), down from the 6% achieved in the final quarter of 2018. Encouragingly though, year-on-year growth in manufacturing output improved to 6.5% in the first quarter of 2019, from
Economic overview

5.7% in the preceding quarter. The Chinese authorities continue to provide substantial stimuli to sustain the economy’s growth momentum in the face of increased adversity.

In the Eurozone, the recent improvement in German industrial production supported the upturn in regional growth to 1.8% (q-o-q, seasonally-adjusted, annualised rate) in the first quarter of 2019, from 0.9% and 1.2% in the third and fourth quarters of 2018 respectively. The recovery was further supported by the emergence of the Italian economy from a technical recession. However, growth prospects for the Eurozone remain subdued, with key risk factors including continued uncertainty regarding Brexit, which has been postponed to 31 October 2019, and the threat of US tariff increases on motor vehicle exports.

Sustained weakness in the Eurozone economy, alongside low inflationary pressures, prompted the European Central Bank (ECB) to remove its guidance on possible interest rate increases, while reactivating the targeted longer-term refinancing operations (TLTRO-III) in an effort to stimulate lending activity by financial institutions across the regional bloc.

Although recent growth data from the US, China and the Eurozone (which collectively account for around half of global GDP) have been relatively positive, the outlook remains somewhat downbeat. The prognosis is supported by the Brookings-Financial Times’ Tracking Indexes for the Global Economic Recovery (TIGER), which indicate that although confidence levels remain in positive territory in advanced economies, they have fallen steeply in recent times. The trend has been even more unfavourable where emerging markets are concerned, with sentiment already in negative territory.

**Figure 3: Confidence levels have fallen as global headwinds are mounting**

Turkish remains at the forefront of emerging market concerns, with the IMF projecting a 2.5% contraction in GDP in 2019.

In India, the run-up to the six-week long election process provided a modest boost to overall economic activity as the government provided some fiscal stimulus to attract voters. The Indian economy is anticipated to sustain its growth trajectory, with the IMF forecasting 7.3% and 7.5% growth for 2019 and 2020, respectively. Should Prime Minister Modi and his
political allies obtain an outright majority in the Indian national election, this could provide the platform needed to roll-out the required economic reforms over the next five years.

In Brazil, the election of President Bolsonaro raised hopes that much needed reforms would be effected, supporting the recovery from the recession that gripped the country in 2015 and 2016. Although this optimism is reflected in the IMF’s growth forecasts for the Brazilian economy, at 2.1% and 2.5% for 2019 and 2020 respectively, signs of infighting in the Bolsonaro administration are prompting concerns that such reforms could stall.

Prospects for the Russian economy remain subdued, with growth of 1.6% and 1.7% projected by the IMF for 2019 and 2020, respectively. This lukewarm outlook is premised on continued US sanctions against Russia and a large number of its prominent business people, as well as threats of weaker global economic conditions suppressing commodity prices, especially those of crude oil.

**Industrial commodities: Relative stability in prices, but risks still abound**

The industrial commodities complex has experienced greater price stability since the start of 2019, after a volatile performance in the fourth quarter of 2018.

**Figure 4: Relative commodity price performance and China’s manufacturing PMI**

Economic growth in China, which accounts for approximately 50% of global demand for industrial commodities, is being buoyed by several growth-supportive policies. Consequently, China’s manufacturing PMI is once again above the 50-index-points threshold, reversing investors’ expectations of a steep downturn in demand for industrial commodities, which were prevalent throughout 2018. However, according to the most recent data releases, retail sales growth is at its lowest since 2003 and industrial production activity has also slowed, indicating that the Chinese economy remains vulnerable and that additional policy stimulus may be required in the months ahead to avert further downside risks. Furthermore, the lifting of industrial output restrictions imposed in China during the winter season provides a supportive context for the base metals’ complex in general, as well as for the commodities associated with the steel value chain, which have recorded weak expansion in primary supplies.
Economic overview

Among the base metals, the copper and aluminium markets are expected to record sustained deficits due to global supply chain constraints and are well positioned to benefit from a recovery in manufacturing activity in China. The collapse of the tailings dam at Vale’s Feijão operation in Brazil, which led to the suspension of 5% of global iron ore supply capacity, is expected to result in a market deficit in 2019. This should be supportive of iron ore prices in the months ahead.

The prices of industrial and energy commodities that have experienced expanded global supply, such as manganese and thermal coal, should remain under pressure. The downside risks for thermal coal prices are being exacerbated by uncertainty surrounding China’s coal import policies, as well as by increasing renewable energy generation in Europe.

The upside potential for crude oil prices is being limited by tepid growth in global demand and by the potential future supply responses of OPEC+ to geopolitical disruptions, especially the impact of US sanctions on Iran, which should displace more than 1.5 million barrels per day from the global oil market, but also heightened conflict in Libya and Venezuela.

While commodities have, over the year-to-date, been supported by improved sentiment among global investors and by a more dovish approach by the US Fed to monetary policy, the recent deterioration in US-China trade relations is again likely to weigh on China’s growth prospects and reflate downside risks across global industrial commodity markets.

Elevated global macro-financial and geopolitical risks could lead to investment flows into precious metals, especially if unaltered policy rates in the US weigh on the dollar. A steep market deficit supports the outlook for palladium, while growing industrial demand and constrained supply growth limit the downside risks for platinum prices.

Sub-Saharan Africa: Growth outlook and South African direct investment

Sub-Saharan Africa (SSA) is still expected to post a moderate recovery in overall economic growth from 2019 onwards, largely on the back of gradual improvements in activity levels in some of the region’s larger economies, particularly South Africa and Nigeria, alongside relatively faster growth in most of its non-resource intensive economies.

Figure 5: Wide variations in SSA’s economic performance

Average annual GDP growth forecasts (2019-20) for the fastest growing economies in Sub-Saharan Africa and growth forecasts for the region’s three largest economies

Source: IDC, compiled using IMF data (April 2019)
The IMF projects growth of 3.5% for the SSA region in 2019, and 3.7% for 2020. However, these aggregate figures mask wide disparities at the individual economy level. Economic conditions are likely to remain relatively subdued in its three largest economies – namely Nigeria, South Africa and Angola – although gradually improving. Excluding South Africa and Nigeria, the region’s economy is expected to grow at a sturdy 5.0% rate in 2019 and by 5.1% in 2020. Robust performances are anticipated from countries such as Rwanda, Ethiopia, Côte d’Ivoire, Ghana, Senegal, Uganda and Kenya, which are not reliant on oil and metals exports.

However, the external environment is becoming less favourable, while fiscal and debt sustainability risks remain very high in certain countries and climate-related shocks are intensifying, as recently observed in Mozambique and, to a lesser extent, in Zimbabwe and Malawi. Such factors could undermine the region’s economic prospects.

A less supportive external environment and a moderation of economic growth in the region would likely affect capital flows into the African continent, including foreign direct investment (FDI) flows, which have struggled to reach the USD58 billion level recorded in 2008.

South African foreign direct investment in the rest of the Africa

South Africa has, over the years, become an increasingly important source of FDI in the African continent. Its direct investment stock in the rest of the continent totaled R338.2 billion as at 31 December 2017 (latest available data), compared to less than R10 billion in the late 1990s. As such, South Africa ranks amongst the world’s top five sources of FDI in Africa.

South African direct investment in the rest of the continent has grown exponentially since the advent of democracy in 1994, but the pace of expansion tapered off after 2015 as economic conditions deteriorated domestically and growth moderated regionally. Furthermore, South Africa’s FDI assets in the rest of Africa represented only 9.9% of its overall FDI assets globally in 2017, down from a ratio of just over 23% in 2011.

Figure 6: South African direct investment in the rest of Africa has grown exponentially

South Africa’s direct investment in the rest of Africa and relative shares of select host countries

Source: IDC, compiled using SARB data
Investment activity was historically concentrated in other member states of the Southern African Customs Union (SACU), mainly due to their geographical proximity as well as strong commercial and cultural connections with South Africa. However, the outward investment momentum also gained strength elsewhere in the Southern African Development Community (SADC) region during the 1990s, and subsequently moved progressively further afield to other parts of the continent. Mauritius is host to over 40% of South Africa’s FDI on the continent, reflecting the island nation’s attractive tax environment which makes it an investment platform of choice for many South African investors targeting regional opportunities.

Figure 7: The distribution of South Africa’s direct investment assets in the rest of Africa is relatively concentrated

Historically, South African investments on the continent have been mainly of a market- and resource-seeking nature, having been largely concentrated on the telecommunications, retail and wholesale, as well as mining sectors. However, it has diversified to a significant extent in more recent years, also encompassing investments in manufacturing operations and in other services sectors, including infrastructure and construction-related developments.

The South African private non-banking sector has been responsible for the largest share of direct investments into Africa, accounting for 76.1% of the total in 2017. Many of these were realised through mergers and acquisitions. Total direct investments by the domestic banking sector represented 18.2% of the total, while investments by South African public corporations accounted for only 5.7%. The latter have been declining in the past few years, possibly not only reflecting the financial challenges faced by several of these entities, but also shifts in their strategic focus towards the South African market.

FDI flows into Africa from the world at large are expected to increase on the back of improving economic conditions in various African countries. However, these could be tempered by risk factors such as adverse geopolitical developments, rising protectionism and escalating trade tensions between the world’s largest economic powers, which should affect production activity, trade flows and investment activity worldwide. In addition, tax reforms in the United States, which is one of the principal sources of FDI into Africa, may also affect its outward investment activity.
Economic overview

Recent developments in the South African economy

With the national and provincial elections behind us, the stage is set for follow-through on governmental commitments to structural reform, policy alignment and certainty, prudent macroeconomic management and the fight against corruption. The vigour and swiftness of their roll-out will be a major determinant of the economy’s performance for the remainder of the year and over the outlook period, for they will influence sentiment amongst households, businesses and investors. Considering the base set by the economy’s weak performance in the first quarter of 2019, a rapid turnaround in confidence levels is crucial.

Domestic economic conditions reflecting widespread challenges

After a dismal performance in 2018 (gross domestic product increased by a mere 0.8% in real terms), the South African economy has continued to face serious challenges since the start of 2019.

As illustrated in Figure 8, in the first quarter of the year output levels were sharply lower in key sectors such as mining and manufacturing. These were affected by generally weak demand conditions both domestically and globally, but also by extended and recurring interruptions in electricity supply as Eskom resumed “load-shedding” to prevent a collapse of the national power grid. The difficult consumer environment, in turn, was reflected in the steep drop in sales volumes of new passenger vehicles as well as in lower retail trade sales.

Considering that the manufacturing; mining; trade catering and accommodation (which includes motor trade); and electricity sectors account for around 35% of overall GDP, the economy is likely to have contracted in the first quarter of 2019. Such a contraction is estimated at 0.5% on a quarter-a-quarter, seasonally-adjusted and annualised basis.

Figure 8: Sharply lower output or sales volumes in key sectors of the economy

![Graph showing growth in select key economic indicators](image)

Source: IDC, compiled using SARB, Stats SA data

Manufacturing output fell by 9.1% in the first quarter of 2019 (refer to Figure 9), thereby posing a major drag on overall GDP growth. Several consumer-oriented manufacturing sub-sectors reported lower output levels relative to the previous quarter, such as those producing televisions, radios and professional equipment (-13.1%); as well as furniture (-3.5%). Energy-intensive sectors such as chemicals, rubber and plastics (-10.3%); wood,
paper and printing (-13.2%); as well as metals and machinery (-12.5%) were significantly impacted by the interruptions in electricity supply. Moreover, weak investment activity continued to affect demand for building materials such as non-metallic mineral products (e.g. cement, tiles and bricks).

In contrast, output levels increased considerably in the sub-sectors producing transport equipment, which includes motor vehicles, parts and accessories (+16%); food and beverages (+10.1%); and, among others, clothing, textiles, leather and footwear (+16.8%).

**Figure 9: Manufacturing output under strain in key sub-sectors**

The manufacturing sector’s poor performance is of concern, for it has strong linkages with supplier and supporting industries across the South African economy. At the broad sector level, the manufacturing sector has the highest GDP multiplier (4.00), while it ranks second in terms of employment multipliers. Its employment multiplier of 5.02 implies that every single direct job in the manufacturing sector creates and/or sustains an additional 4.02 jobs elsewhere in the economy. Similarly, for every R1 million of GDP in the manufacturing sector, a further R3 million of value added is created across the entire supply chain in all sectors whose production activities benefit from the manufacturing sector’s demand.

Furthermore, the sector’s relative contribution to overall GDP has declined over time, as illustrated in Figure 10. From being the largest of the ten broad sectors of the South African economy in 1994 (21% of overall GDP at basic prices), the manufacturing sector currently ranks in fourth position, with its contribution to total GDP having fallen to 13.2% by 2018. From a global perspective, the share claimed by South Africa’s manufacturing sector has largely followed the trend observed in developed economies, and is presently well below those of eastern and south-eastern Asia economies (excluding China), for which the ratio stood at 23.6% by 2017.

According to recent surveys, South African manufacturers have become more pessimistic about expected business conditions in 12 months’ time, thus indicating that production activity may remain weak for some time. Their expectations regarding export volumes over the next 12 months have also deteriorated due to unfavourable developments in the world trading arena.
Economic overview

Mining production fell by 12.7% in the first quarter of 2019 (quarter-on-quarter, seasonally-adjusted and annualised rate), as shown in Figure 11. This was the worst quarterly decline in four years, reflecting the generally unfavourable operating environment for the mining sector at large.

The mining sector continues to face a difficult operating environment.

Lower output was recorded in the large iron ore, platinum group metals (PGMs) and coal mining sub-sectors, although smaller sub-sectors such as those mining diamonds, chrome and manganese also reported lower volumes. Gold output recovered modestly in the first quarter of 2019, after a significant drop in the preceding quarter. The output of the sub-sectors mining copper and other mineral products expanded at a robust pace.

The South African mining sector has now been under considerable strain for more than a decade. Excluding gold, which is in long-term decline, domestic mining output has only managed to expand by 0.7% per annum, on average, over the past 10 years. Consequently,
Economic overview

its overall employment has fallen sharply over time, standing at approximately 450 000 in 2018, about 85 000 fewer than in 2012.

Going forward, activity in the mining sector may be constrained by the global slowdown. In addition, the steep hike in domestic electricity tariffs will raise the costs of doing business, with serious consequences for many of the marginal and loss-making mining operations. Such factors could affect the sector’s overall production, exports and investment activity, with adverse effects on labour-absorption.

Further drop in employment

Overall employment in the South African economy declined by 237 000 (q-o-q) in the first quarter of 2019, taking the unemployment rate to 27.6%, from 27.1% at the end of 2018 (refer to Table 1). The construction sector reported a loss of 142 000 jobs as its employment fell to a four-year low. Substantial job losses were also reported by finance and business services, community and social services (which includes government), as well as by the embattled mining sector.

Although the manufacturing sector managed to increase its workforce by 14 000 people, this is still 69 000 fewer than for the same period in 2018. Higher employment levels were also recorded by sectors such as transport; trade, catering and accommodation; and utilities (i.e. electricity, gas and water supply).

The number of discouraged work-seekers (part of “not economically active” population) increased by 156 000, while the labour absorption rate (i.e. number of working-age population that are employed) decreased further to 42.6%. Of major concern is the fact that 69% of the unemployed have been without a job for more than one year. Considering the fact that the economy has become more technologically advanced in its production and operating methods, whereas many of the unemployed lack the required skills, their chances of being re-employed in the formal sectors of the economy are quite low.

Table 1: Labour market reflecting a worrying trend

<table>
<thead>
<tr>
<th>Labour market indicators</th>
<th>Number ('000s)</th>
<th>Change in '000s (q-o-q)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population (15 to 64 years)</td>
<td>38 283</td>
<td>149.4</td>
</tr>
<tr>
<td>Labour force</td>
<td>22 492</td>
<td>-175.7</td>
</tr>
<tr>
<td>Unemployed</td>
<td>6 201</td>
<td>61.5</td>
</tr>
<tr>
<td>Unemployment rate (%)</td>
<td>27.6</td>
<td>0.5</td>
</tr>
<tr>
<td>Not economically active</td>
<td>15 791</td>
<td>325.1</td>
</tr>
<tr>
<td>Employed:</td>
<td>16 291</td>
<td>-237</td>
</tr>
<tr>
<td>Agriculture</td>
<td>837</td>
<td>-12.1</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>417</td>
<td>-20.1</td>
</tr>
<tr>
<td>Utilities (electricity, gas &amp; water)</td>
<td>1 780</td>
<td>13.9</td>
</tr>
<tr>
<td>Construction</td>
<td>1 339</td>
<td>-142.5</td>
</tr>
<tr>
<td>Trade, catering &amp; accommodation</td>
<td>3 345</td>
<td>25.0</td>
</tr>
<tr>
<td>Transport</td>
<td>1 025</td>
<td>59.2</td>
</tr>
<tr>
<td>Finance &amp; business services</td>
<td>2 516</td>
<td>-94.3</td>
</tr>
<tr>
<td>Community services (incl. government)</td>
<td>3 574</td>
<td>-49.9</td>
</tr>
<tr>
<td>Private households</td>
<td>1 301</td>
<td>-31.2</td>
</tr>
</tbody>
</table>

Source: IDC, compiled using Stats SA data
**Economic overview**

**Consumer environment**

South African households have been facing a difficult environment for quite some time. Subdued growth in real disposable incomes, high levels of indebtedness and tighter lending practices by the financial sector, rising living costs (e.g., fuel, electricity tariffs) and concerns over employment prospects are affecting their discretionary spending. The net wealth of households as a ratio of disposable incomes declined to 367.4% in 2018, the lowest in five years, while the household savings-to-disposable income ratio deteriorated further in 2018.

These factors contributed to the sharp drop in consumer confidence in the first quarter of 2019, to a reading of just 2 points, from the all-time highs of 26 points at the start of 2018 (refer to Figure 12). Credit extended to households has declined in each of the past five years, with some recovery at the beginning of 2019, as shown in the chart below.

The consumer environment is expected to remain fairly challenging in the months ahead, affecting the ability and willingness of households to raise consumption spending.

*Figure 12: Subdued demand for household debt*

**Business confidence**

Overall business confidence has been at low levels for more than 11 years and fell further in the first quarter of 2019 to a reading of just 28 points (refer to Figure 13). Business confidence was well below the crucial 50-point mark for all the sectors surveyed by the Bureau for Economic Research (BER).

The highest reading was reported for the textiles, clothing, leather and footwear sector at 42 points, whereas the lowest pertained to furniture and other industries, at zero. Confidence levels amongst manufacturers fell by 10 points over the 12 months to the opening quarter of 2019 to a reading of 25 points, one of the lowest readings since the 2009 economic recession.

Factors at play included weak domestic demand; the adverse impacts of load shedding on business activity; prolonged labour strikes in the gold mining sector and threats of industrial action in other mining sectors; policy uncertainty (e.g., renewed calls for land expropriation without compensation); as well as the global economic slowdown, which may further limit export opportunities.
Economic overview

However, the outcome of the recent national election could have a decisive impact on investor, business and consumer confidence, potentially leading to a sharp rebound if followed by effective action with regard to structural reforms aimed at boosting economic growth, increased localisation associated with public sector procurement and infrastructure development, concerted efforts to tackle the challenges at Eskom, and visible progress in the fight against corruption and state capture. This would eventually result in increased production activity, fixed investment and much needed employment creation.

Figure 13: Business confidence still on the decline in a difficult operating environment

Merchandise trade performance

Having ended 2018 on a strong note, with a trade surplus of R14.6 billion in the fourth quarter of the year, the opening quarter of 2019 saw a sharp reversal in South Africa's balance of trade as a R4.1 billion deficit was recorded. However, this was an improvement if compared to the deficit of R19.1 billion recorded in the first quarter of 2018.

Figure 14: Trade balance worsened as manufactured exports disappointed

Source: IDC, compiled using SARB, BER data

Source: IDC, compiled using SARS data
Whereas gold exports plummeted by 26.9% (year-on-year), mining exports were boosted by solid increases in iron ore (+52.8%), PGM (23.2%) and, to a lesser extent, by other mining exports (e.g. chrome, copper, manganese) (+18.7%). On the import side, demand for crude oil, which accounted for about 80% of all mineral imports in the first three months of 2019, decreased by 16.2% on the back of lower international oil prices.

The mining sector’s trade surplus thus increased by R16.4 billion to R71.5 billion over the 12 months to the first quarter of 2019. This higher trade surplus was the main contributor to the lower trade deficit in the first three months of the year, as illustrated in Figure 14, if compared to that for the same period of 2018. On a quarterly basis, however, the trade surplus of the mining sector decreased slightly by R3.4 billion, due to lower exports.

Manufactured exports increased by 7.5% (year-on-year), largely supported by a strong performance by the transport equipment sector (including motor vehicles, parts and accessories), and by higher exports of chemicals, rubber and plastic products. Imports of manufactured goods, in turn, increased by only 4.5% over the same period. Consequently, the trade deficit for the manufacturing sector remained almost unchanged compared to a year earlier, at just over R84 billion, but widened by R14.6 billion relative to the final quarter of 2018.

South Africa’s balance of trade is expected to remain under pressure during the course of 2019. Slower global growth and the destabilising effects of the escalating trade war between the US and China on world trade flows may affect the domestic export sector’s performance. Import demand, in turn, is likely to be relatively constrained by subdued consumption and investment spending domestically.

Growth prospects for the South African economy

Despite a very poor start to the year, with real GDP estimated to have contracted by 0.5% during the first quarter, economic activity is likely to rebound over the remainder of 2019. Overall GDP growth is forecast at 1.5% for the year as a whole (refer to Table 2).

South Africa’s growth prospects will, however, hinge on the extent of a turnaround in confidence levels among households, businesses and investors.
The outcomes of the national elections held on 8 May 2019 provide a significant degree of comfort that President Cyril Ramaphosa will have the necessary support and mandate to implement his pro-growth reform agenda, as outlined in the State of the Nation Address. These include reforms aimed at accelerating inclusive economic growth and creating jobs; improving the education system and skills development; stepping up the fight against corruption and state capture; and strengthening the capacity of the state to address the needs of the people.

Effective efforts to ensure fiscal consolidation and debt sustainability, which will essentially also encompass decisive interventions to address the prevailing challenges facing key state-owned companies, will also be key to the economic recovery process. Limited fiscal space in a low-growth environment will continue to weigh on government finances for some time, thereby constraining both its consumption and capital expenditure.

The consumer environment is, however, expected to remain challenging for some time, thus impacting on the ability and willingness of households to increase expenditure in a meaningful manner. Nonetheless, consumer confidence should recover gradually over the outlook period, thereby permitting a progressive improvement in household consumption spending, albeit well short of the expansion rates achieved during the consumer boom of the early 2000s.

South Africa’s export performance is expected to improve over the outlook period. This is based on the assumptions that export market development efforts will intensify, that global demand will remain reasonably sturdy and that commodity markets will remain fairly supportive of mining sector exports.

Subdued demand conditions and surplus production capacity in many sectors of the economy will continue to adversely affect private sector fixed investment expenditure earlier in the outlook period. However, as demand conditions recover, overall investment spending should gain momentum and gradually shift towards expansionary investments.

### Table 2: South Africa’s economic growth expected to improve over the outlook period

<table>
<thead>
<tr>
<th>Variable (% change or % of GDP)</th>
<th>2016</th>
<th>2017</th>
<th>2018</th>
<th>2019f</th>
<th>2020f</th>
<th>2021f</th>
<th>2022f</th>
<th>2023f</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Real GDP growth and its components:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Household consumption expenditure</td>
<td>0.6</td>
<td>2.1</td>
<td>1.8</td>
<td>1.7</td>
<td>2.0</td>
<td>2.5</td>
<td>3.2</td>
<td>3.1</td>
</tr>
<tr>
<td>Government consumption expenditure</td>
<td>2.2</td>
<td>0.2</td>
<td>1.9</td>
<td>1.2</td>
<td>1.3</td>
<td>1.6</td>
<td>1.8</td>
<td>1.9</td>
</tr>
<tr>
<td>Gross fixed capital formation (GFCF)</td>
<td>-3.5</td>
<td>1.0</td>
<td>-1.4</td>
<td>1.1</td>
<td>2.7</td>
<td>5.3</td>
<td>6.1</td>
<td>6.5</td>
</tr>
<tr>
<td>Exports</td>
<td>0.4</td>
<td>-0.7</td>
<td>2.6</td>
<td>2.7</td>
<td>3.0</td>
<td>3.1</td>
<td>3.2</td>
<td>2.6</td>
</tr>
<tr>
<td>Imports</td>
<td>-3.9</td>
<td>1.0</td>
<td>3.3</td>
<td>3.1</td>
<td>3.5</td>
<td>4.1</td>
<td>4.2</td>
<td>4.0</td>
</tr>
<tr>
<td><strong>GDP</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Consumer price inflation</td>
<td>0.4</td>
<td>1.4</td>
<td>0.8</td>
<td>1.5</td>
<td>2.0</td>
<td>2.6</td>
<td>3.2</td>
<td>3.1</td>
</tr>
<tr>
<td>Current account balance (% of GDP)</td>
<td>6.3</td>
<td>5.3</td>
<td>4.6</td>
<td>4.9</td>
<td>5.3</td>
<td>4.9</td>
<td>4.6</td>
<td>4.7</td>
</tr>
<tr>
<td>GFCF as % of GDP</td>
<td>-2.9</td>
<td>-2.5</td>
<td>-3.5</td>
<td>-3.3</td>
<td>-3.6</td>
<td>-4.0</td>
<td>-3.7</td>
<td>-3.3</td>
</tr>
<tr>
<td><strong>Import growth</strong></td>
<td>19.4</td>
<td>18.8</td>
<td>18.2</td>
<td>17.6</td>
<td>17.6</td>
<td>18.0</td>
<td>18.4</td>
<td>18.9</td>
</tr>
</tbody>
</table>

Source: IDC, compiled using SARB data; IDC forecasts

Import growth is expected to rise as South Africa is highly dependent on key imported items such as machinery and equipment, crude oil, refined petroleum products, as well as parts and accessories for motor vehicles. Nevertheless, considering the relatively modest domestic demand conditions anticipated through most of the outlook period, growth in...
imports will be contained, thereby alleviating pressure on the current account of the balance of payments.

The rand is expected to strengthen to some extent vis-à-vis the US dollar and euro over the five-year outlook period. Relative rand appreciation alongside the absence of significant demand-pull inflationary pressures throughout the forecast horizon, are likely to translate into moderate average rates of consumer price inflation well within the target band set by the South African Reserve Bank. In the absence of major cost-push risks (for example, extraordinary hikes in electricity tariffs), the Monetary Policy Committee is expected to leave the repurchase (repo) rate unchanged throughout the period.

Among the key risks to the economic outlook summarised in this section of the report are the financial and operational challenges at Eskom, with government having to embark on decisive plans to swiftly implement a restructuring plan to ensure reliable and affordable electricity supply.