

GDP comment

Recession exited, but growth remains soft

The South African economy came out of the technical recession in 2018Q3, in line with the general consensus. Stats SA reported that GDP expanded by 2.2% quarter-on-quarter (q-o-q), annualised¹, a robust recovery from an upwardly revised 0.4% (from -0.7%) contraction in 2018Q2. The Q3 print was somewhat better than the Bloomberg consensus expectation and our forecast of 1.9%. However, the figure came out quite a bit better than our forecast back in September which was for Q3 growth of 1.5%. Compared with the third quarter of 2017, GDP rose by a seasonally adjusted 0.6% year-on-year (y-o-y) with real growth amounting to only 0.8% in the first nine months of 2018. This is much weaker than the already subdued real growth of 1.3% recorded during 2017.

Table 1: Manufacturing and transport help GDP back into positive territory

Seasonally adjusted	q-o-q % (annualised)		y-o-y %	
	2018Q2	2018Q3	2018Q2	2018Q3
Agriculture	-31.9	6.5	-2.9	-9.6
Mining	8.1	-8.8	-0.4	-4.1
Manufacturing	0.6	7.5	0.4	1.3
Electricity	2.2	-0.9	-0.2	1.2
Construction	2.1	-2.7	-0.6	-1.0
Trade	-1.4	3.2	0.0	0.8
Transport	-4.9	5.7	-0.2	1.0
Financial	1.9	2.3	1.9	1.9
Government	-0.4	1.5	1.0	1.1
Personal services	0.8	0.7	1.1	0.9
GDP (total)	-0.4	2.2	0.6	0.6

Source: Stats SA

The high-frequency production and sales data from Stats SA, especially for manufacturing and the retail and wholesale trade sectors, had suggested a much improved GDP performance in Q3. However, one of the key uncertainties in the lead-up to the Q3 growth print was the extent to which the **agricultural sector** would recover from steep declines in the first half of the year. In the end, the recovery in agricultural value added was somewhat less than we assumed. However, the sector still recorded a healthy

¹ Unless stated otherwise, all of the quoted figures are measured q-o-q and at a seasonally adjusted and annualised rate.

quarterly increase (see Table 1 for the details) as delayed maize harvesting in the Northern Provinces and a sharply higher wheat crop in the South boosted output in the sector.

Of the other major sectors, the following stands out:

- The robust q-o-q growth in the **manufacturing sector** contributed most to Q3 GDP, adding 0.9 percentage points (% pts).
- At the other end of the scale, **mining** was the most significant drag on Q3 GDP, shaving 0.7% pts off overall GDP. The other laggards were the construction and electricity sectors.
- Relative to our expectations, a positive surprise was the strong growth in value added recorded for the **transport sector**. This added 0.5% pts to Q3 quarterly growth. Along with an improved performance from general government (driven by increased employment), this pushed **tertiary sector** growth up to 2.6% after a 0.4% contraction in 2018Q2.
- Compared to the growth signalled by Stats SA's monthly retail and wholesale trade data, growth in the **trade sector** (retail, wholesale, hotels and restaurants) came in lower than expected. However, the sector still contributed 0.4% pts.

Table 2: Strong export growth and inventory rebuild the key drivers of demand-side GDP recovery

Seasonally adjusted	q-o-q % (annualised)		y-o-y %	
	2018Q2	2018Q3	2018Q2	2018Q3
Private consumption	-1.1	1.6	1.4	1.2
Government consumption	0.8	2.2	1.3	1.5
Fixed investment	-0.7	-5.1	0.1	-0.6
Inventories (R bn)	-9.1	12.7		
Residual (R bn)	-1.6	1.8		
Gross Domestic Expenditure	-2.6	3.2	0.6	1.7
Exports	12.7	24.2	1.0	6.7
Imports	4.0	26.7	1.0	10.4
GDP (total)	-0.4	2.2	0.6	0.6

Source: Stats SA, BER calculations

Measured from the demand side, an expected rebound in **inventory investment** boosted the growth number. Stats SA mentioned that the build-up was mainly in the manufacturing and retail sectors. This was aided by an improved performance from **household** consumption expenditure and **government** consumption. A downside surprise was the weakness in **fixed investment**, driven by a quarterly plunge of more than 13% in public corporation capital formation. However, the investment weakness was broad-based with private sector capex declining for a third consecutive quarter. This corresponds with continued depressed levels of business confidence.

In line with the monthly international trade data, the import and export numbers suggest that the trade balance - and by implication the current account shortfall - deteriorated in 2018. This is despite a strong recovery in exports, which was outweighed by even faster import growth.

Subdued growth outlook, especially over the short term

It is important to appreciate that, until the SA Reserve Bank tells us otherwise, SA remains in the longest business cycle downswing on record (since 2013Q4) with annual growth below the estimated potential growth rate of the country. In other words, while it is positive news that the economy moved out of recession, growth momentum remains very weak.

The survey data already available for the fourth quarter does not inspire confidence for a growth acceleration in the final months of 2018. Business confidence deteriorated in 2018Q4 with the **RMB/BER Business Confidence Index** posting a marginal decline to 31. This means that roughly 70% of all respondents were unsatisfied with prevailing business conditions in the economy. Although confidence rose in three out of the five sectors surveyed, it remained below the neutral-50 mark in all of the sectors surveyed. Furthermore, despite a robust increase in November, the **Absa Purchasing Managers' Index** for the manufacturing sector averaged 46 in October and November, below the neutral 50-point mark and somewhat less than the average recorded for the third quarter. In addition, the **Agbiz/IDC Agribusiness Confidence Index** declined by 6 points to 42 in the fourth quarter. This is the weakest reading since 2009Q4.

Besides the subdued survey data, specific events are likely to curtail growth in Q4. For one, two of SA's leading gold mining companies have been hit by **labour unrest** in the last number of weeks. This is likely to prolong the weak activity levels in the mining sector. Perhaps of greater concern, depending on how prolonged the problem is, is the re-emergence of country-wide electricity **load shedding** in the past week or so. This has the potential to curb output towards the end of the year, and potentially beyond.

On a more positive note, the combination of a record petrol price decline in December and discounts related to Black Friday retail trading will hopefully provide some boost to festive season consumer spending. At the very least, these factors should help to shield consumers against the adverse impact of the 25bps lending rate hike announced at the end of November.

Previously, we had pencilled in a fairly robust Q4 GDP growth print of about 3% q-o-q. This now seems to be too high, putting downward risk on our already downbeat full-year 2018 growth forecast of 0.6%. However, the better-than-expected Q3 growth outcome and mild upward revision to the second quarter means that we remain comfortable with a 2018 real growth figure of 0.5 - 0.7%. For 2019, the length of time that load shedding remains a reality, the February Budget and the outcome of the May 2019 national elections are likely to be important drivers of confidence, private sector fixed investment and ultimately GDP growth. At this stage, we are sticking with a fairly subdued outlook of 1.5% real GDP growth for next year.

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