

BER Business Survey results show improvement in activity indicators despite weak confidence

- ***Introduction – confidence remains at low level***
- ***Activity indicators show more improvement than suggested by confidence***
- ***Employment creation remains fickle***
- ***Input cost and selling price indicators show inflationary pressures***
- ***Concluding remarks and implications***

Introduction – confidence remains at low level

A cornerstone of the BER's work over the years has been its regular business surveys. The BER's survey method is modelled on those of the Munich based IFO Institute and the European Commission. The survey data has a proven track record as exceptionally reliable – given the correspondence with the available formal statistics – and as leading economic indicators. The results reveal the direction of production, sales, selling prices, employment etc. before the release of official data and provide unique information such as confidence, rating of business conditions and respondents' expectations for the next quarter.

The aim of this note is to summarize some specific insights and trends observed in the current round of BER surveys¹ as a first indication of developments in the real economy during the fourth quarter. More detailed sectoral analyses are provided in the respective BER survey publications.

Business confidence as measured by the RMB/BER Business Confidence Index (BCI) remained more or less flat in 2011Q4 – declining by 1 index point (to reach 38), after falling a cumulative 16 index points in the second and third quarters. The concern was that any further weakening of confidence may signal further stalling of economic growth in the fourth quarter or even bring the sustainability of the economic upswing into question. However, although confidence remained low, fourth quarter results on balance sketch a more robust picture with respect to underlying business conditions. The disconnect between activity indicators and business confidence is most pronounced in the manufacturing sector, but is also evident in the motor trade survey results. On the other hand, confidence increased along with improvements in business conditions in the retail and wholesale sectors, while building sector confidence and activity levels remained low. Hence, although not necessarily suggested by the headline composite RMB/BER BCI at first glance, the data on balance suggests that GDP growth is likely to have accelerated during 2011Q4 after the Q2 and Q3 soft patch.

¹ Conducted between 17 October and 14 November.

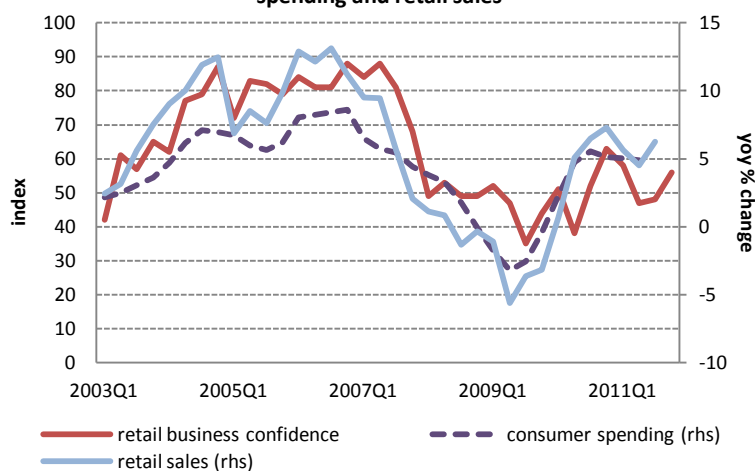
Activity indicators

One of the key positive signals from this round of BER business tendency surveys was the fact that the **retail** environment seems to be more resilient than expected. Growth in the volume of sales and orders placed continued to accelerate in 2011Q4, surprising respondents on the upside. Albeit that demand conditions were

already showing improvements during the third quarter, retailers were hesitant to expect the pace to continue into this quarter. After witnessing a sustained improvement, retail business confidence rose sharply from 48 to 56 index points during 2011Q4.

These results imply that the strong real growth (year-on-year) in official retail trade sales (averaging close to 6% in 2011Q3) and consumer expenditure is likely to continue in the fourth quarter.

Figure 1: Retail business confidence and growth in consumer spending and retail sales

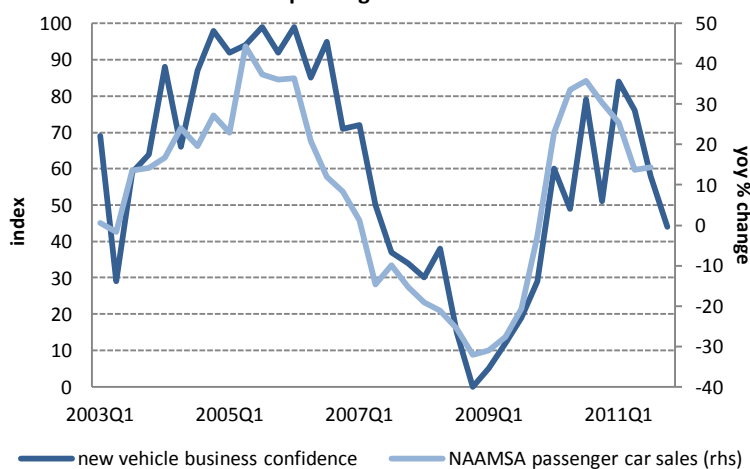


Source: BER; Stats SA; SARB

Consumer confidence remained relatively supportive of spending, with the FNB/BER Consumer Confidence Index (CCI) increasing by one index point to 5 in 2011Q4. Moreover, the components pertaining to the rating of own finances and the time to buy durable goods ticked up.

Naamsa reported a 19.8% increase in passenger car sales for October, and even though sales growth is expected to slow into the end of the year, the fourth quarter should record a solid average (following growth of 14.4% in the third quarter). Although the BER survey data also showed continued growth in units sold during 2011Q4, **motor trade** confidence fell from 58 to 44 index points (see Figure 2). The confidence decline might be an overreaction given that traders expected a more noticeable acceleration in the growth in units sold.

Figure 2: New vehicle dealers' business confidence and passenger car sales



Source: BER; Naamsa

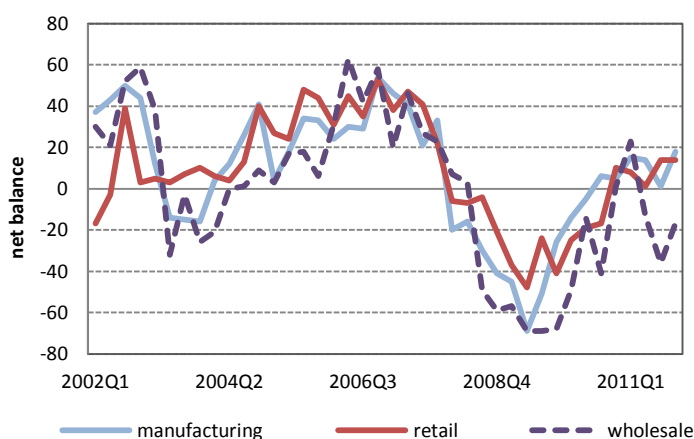
Although business conditions in the **wholesale** sector remain tough, the fourth quarter witnessed some improvements. Fewer wholesalers reported a deceleration in the growth in the volume of sales and orders placed. Wholesaler confidence rose from 31 to 38 index points.

Figure 3 plots the **manufacturing** domestic orders indicator against indicators for orders placed by retailers and wholesalers. Manufacturing order volumes seem to have benefitted from the sustained acceleration in the growth of orders placed by retailers and the increase in the orders placed indicator for the wholesale sector. In fact, the rise in domestic order volumes as reported by manu-

facturers is currently at a 4-year high. Exporters also indicated that export sales and order volumes were increasing at the fastest pace since 2003. It is likely that the weaker rand exchange rate leading up to and during the fourth quarter has impacted positively on the export performance of the sector (at least in some cases). The fact that respondents indicated a significant acceleration in the rate of increase in the average export selling price per unit of production substantiates this claim.

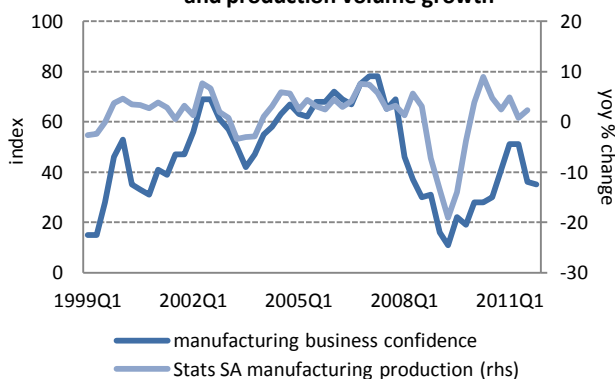
These improvements in demand stimulated production growth during the fourth quarter, albeit that some of the production indicator's increase might be due to a bounce back after the recent strike action. However, manufacturing business confidence remained low – declining by one index point to reach 35. One could argue that since late-2009, manufacturing business confidence has not been a good indicator of production.

Figure 3: Manufacturing domestic order volumes; retail and wholesale growth in volume of orders placed



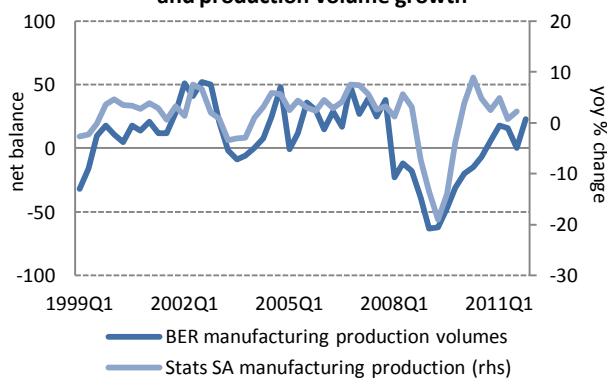
Source: BER

Figure 4: Manufacturing business confidence and production volume growth



Source: BER; Stats SA

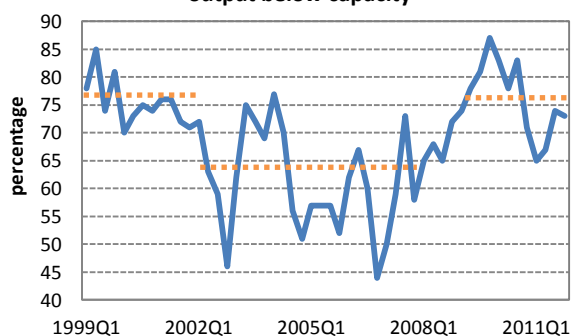
Figure 5: Manufacturing production volume and production volume growth



Source: BER; Stats SA

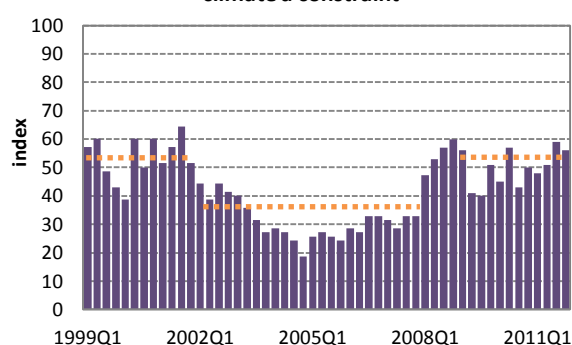
As shown in Figure 4, this argument was also relevant between 1999 and 2001. When the BER production indicator (net balance statistic) is considered, the downside risk for official manufacturing production growth is significantly less – see Figure 5. However, over the long term, manufacturing business confidence and production track each other closely.

Figure 6: Percentage rating present level of output below capacity



Source: BER

Figure 7: Percentage rating general political climate a constraint

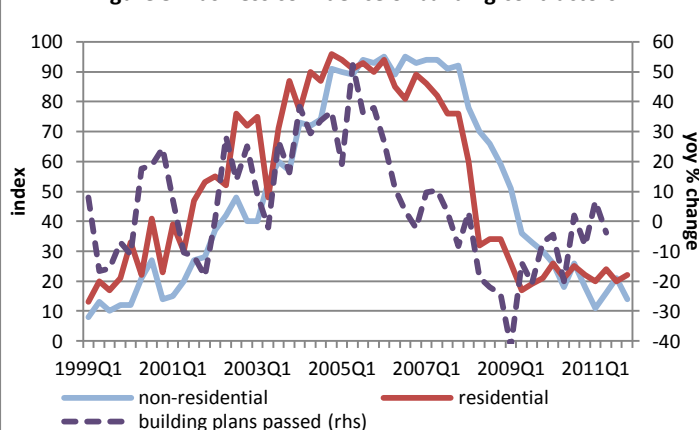


Source: BER

The discrepancies can to some extent be explained with reference to the broader economic landscape. Both these periods are at the start of an upward phase of the SA business cycle and followed international financial shocks. Hence, they are characterised not only by low capacity utilization (implying that manufacturers might still be unsatisfied with business conditions despite improvements in production – see Figure 6), but also by high levels of uncertainty (assuming manufacturers' rating of the general political climate as shown in Figure 7 as a crude proxy for uncertainty).

Building sector activity remained soft in 2011Q4, with non-residential building contractors reporting a further weakening in building activity and their confidence dropping from 21 to 14 index points. Business confidence of residential building contractors rose slightly to 22 index points, but remains low. There is evidence of a recovery slowly taking hold – if one goes by activity improvements early in the pipeline such as the rising trend in building plans passed (Figure 8). Both architects and quantity surveyors saw more projects progressing from sketch plan and working drawing stage to contracts awarded. Bar postponements, this recovery in contracts awarded

Figure 8: Business confidence of building contractors

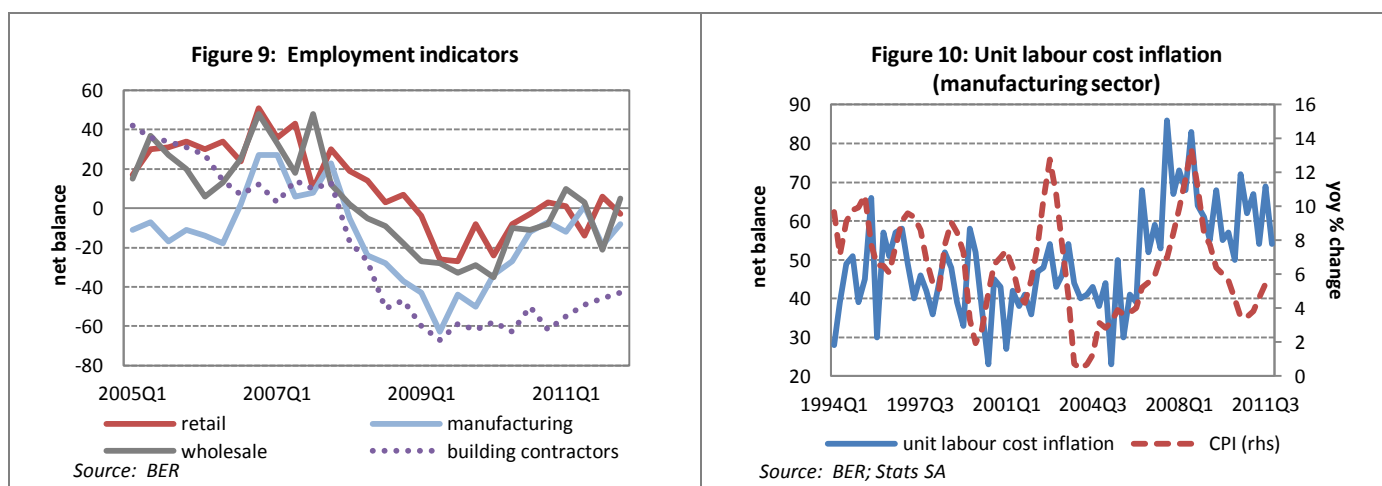


Source: BER; StatsSA

bodes well for the building industry – in particular the non residential sector which is one of the main users of these professional services. Furthermore, manufacturers and retailers of building materials reported improvements during the quarter, leading to a rise in the FNB/BER building confidence index from 23 to 29 points.

Employment

Employment creation remains highly fickle. As shown in Figure 9, the BER survey indicators for employment (barring that of the building sector which continues to underperform) are bounded around zero i.e. not showing any sustained increase in workers employed. The retail sector reported a deceleration in the growth of the number of people employed in 2011Q4, after being the only sector to report growth in employment during the previous quarter. On the other hand, the employment growth indicator for the wholesale sector recovered back to positive territory after dipping notably in the third quarter.



Employment conditions in the manufacturing sector also improved somewhat during 2011Q4. Manufacturers stepped up production by increasing the average number of hours worked per factory worker. Although an increase in the average hours worked bodes well for factory employment, relatively high unit labour cost inflation (compared to for example consumer price inflation as measured by the CPI – see Figure 10) as well as low capacity utilization are likely to make producers hesitant to expand their workforce before they witness a sustained improvement in demand.

Input cost and selling price indicators

Although cost pressures remain high, manufacturers reported a slight further deceleration in total unit cost inflation during the fourth quarter. Producers' domestic selling prices continue to rise at a slower rate than their

costs (respondents indicated that the rate of increase in their average domestic selling prices remained roughly unchanged), as has been the case from mid-2007 (Figure 11).

Results from the retail survey however show very sharp accelerations in average purchasing price and selling price inflation in 2011Q4 – Figure 12. The effect of the weaker rand exchange rate on imported consumer goods might be a specific factor at play. These results highlight the upside risks to the BER's forecast for CPI inflation which is expected to continue rising in the near term (after reaching 6% in October), but is projected to again dip below the upper level of the target band in 2012Q4.

Figure 11: Manufacturing input cost and selling price inflation

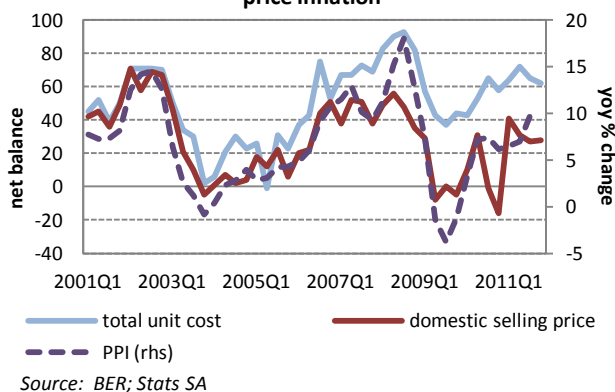
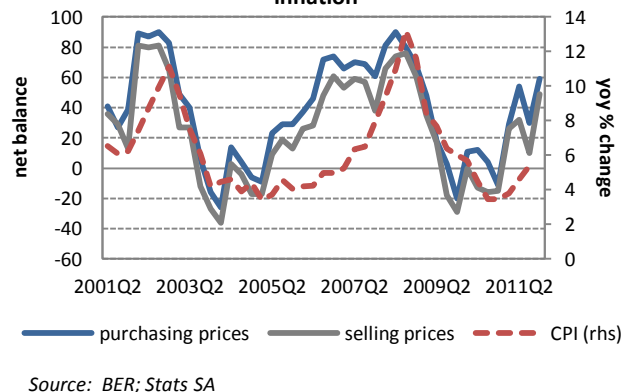


Figure 12: Retail purchasing and selling price inflation



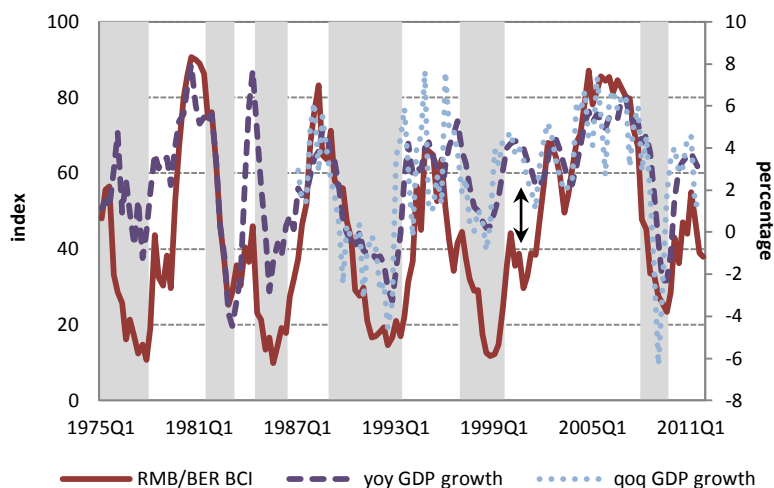
Concluding remarks and implications

The fact that business confidence remained roughly unchanged in 2011Q4 masks the more upbeat picture as painted by underlying activity indicators. The manufacturing sector is the main culprit in this regard, with demand and production indicators improving while confidence remains low. Although manufacturers expect the improvement in business conditions to continue, they are cautious with respect to the sustainability of the tempo of improvement. The November Kagiso Purchasing Managers' Index (PMI) saw a sharp drop (from 62.4 to 55.0) in the index for expected business conditions in 6-months' time, albeit that business activity increased further during the month – echoing the quarterly BER survey.

On balance, the survey results point towards an acceleration in GDP growth in 2011Q4 relative to the third quarter, while year-on-year growth is likely to slow further.²

² The RMB/BER BCI is technically more correlated with year-on-year GDP growth (with a correlation coefficient of 0.74 versus 0.55 for quarter-on-quarter seasonally adjusted and annualized).

Figure 13: Business confidence and GDP growth



Source: BER; SARB; Stats SA

As evident from Figure 13, the RMB/BER BCI is generally a useful leading indicator of GDP growth. The current slight discrepancy, with confidence remaining low while activity improvements accelerated during the quarter, reminds of the experience during the start of the previous upward business cycle phase (1999 to 2001) of the SA economy. As argued with respect to the manufacturing sector results, low capacity utilization and

high levels of uncertainty also characterized that period. Indeed, the fact that business confidence remains low highlights the downside risks to the growth outlook, particularly given the current global economic environment and threatening impact of the European crisis. Furthermore, it does not bode well for the already lagging recoveries in fixed investment and employment.

Christelle Grobler

Technical assistance: Ester Manefeldt

1 December 2011

Copyright and Disclaimer.

This publication is confidential and only for the use of the intended recipient. Copyright for this publication is held by Stellenbosch University. Although great care is exercised to record and interpret all information correctly, Stellenbosch University, its division BER and the author(s)/editor do not accept any responsibility for any direct or indirect loss that might result from accidentally inaccurate data and interpretations by third parties. Stellenbosch University further accepts no liability for the consequences of any decisions or actions taken by any third party on the basis of information provided in this publication. The view, conclusions or opinions contained in this publication are those of the author(s)/editor and do not necessarily reflect those of BER or Stellenbosch University.