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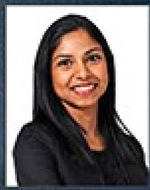
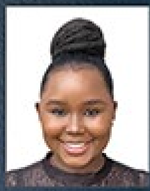
Herman van Papendorp
Head of Investment Research & Asset Allocation

Sanisha Packirisamy
Economist



Tshiamo Masike
Economic Analyst



Business pulse: Business confidence depressed at 30 points

Highlights

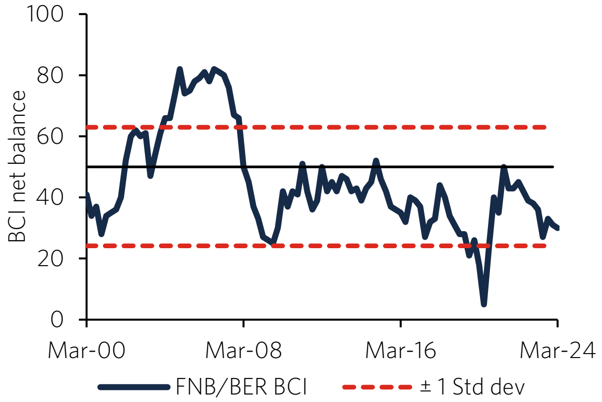
- The RMB/BER (Rand Merchant Bank/Bureau for Economic Research) Business Confidence Index (BCI) decreased further by one point to 30 in the first quarter of 2024, following a two-point decrease in the fourth quarter of 2023. The deterioration was mainly due to the decrease in retailer and manufacturer confidence but the rebound among new vehicle dealers prevented a more pronounced decrease in overall business sentiment.
- According to Statistics South Africa (Stats SA), seasonally-adjusted (sa) manufacturing production barely grew in the fourth quarter of 2023 (0.2 quarter-on-quarter (q/q)) and annual manufacturing production growth was weak (0.5% year-on-year (y/y)) in 2023.
- Seasonally-adjusted mining production was robust in the fourth quarter, registering an increase of 2.4% q/q but production contracted by 0.3% y/y in 2023. The biggest constraints facing the mining industry include loadshedding, logistics inefficiencies and soft commodity prices. These factors are expected to continue to place downward pressure on the industry.
- According to Stats SA, retail, wholesale and motor trade sales shrunk in the fourth quarter of 2023 as well as annually in 2023 relative to 2022.
- Seasonally-adjusted retail trade sales were down 0.4% q/q in the fourth quarter of 2023 and 1% lower in 2023. We expect consumers' financial position to improve somewhat in 2024 which could be supportive of retail trade sales. However, consumers face an elevated debt burden and additional tax payments through bracket creep, capping the potential boost to retail sales.
- On a quarterly basis, seasonally-adjusted motor trade sales fell marginally by 0.5% q/q in the fourth quarter. Annually, motor trade sales dropped by 1.8% y/y in 2023 largely due to a decrease in used vehicles sales.
- The construction industry performed poorly in the fourth quarter and cumulatively for 2023 with the real value of building plans passed and completed both down by nearly 20% annually. The improvement in the building confidence index for the third consecutive quarter is suggestive of better constructive activity but maintain a cautious view of the sector.
- The sentiment of agribusinesses was depressed in the fourth quarter of 2023. This mirrors the multiple headwinds experienced in the agricultural space last year. 2024 may see some improvement but there are still constraints (e.g. loadshedding, logistical inefficiencies, drier weather conditions) that could dampen production growth.
- According to the 2024 Allianz Risk Barometer, loadshedding is the most prominent risk facing SA businesses. Only 8% of the global surveyed respondents cited blackouts as a risk which highlights the severity of this issue domestically.

- **Prevailing depressed business confidence is a dampener on economic growth prospects because it could lead to reduced investment, lower production, and a decline in employment. Nevertheless, we expect economic growth to pick up slightly to 1% in 2024 from a lacklustre 0.7% (expenditure method) in 2023 and increase to 1.7% in 2024 on the expectation of a further alleviation in the energy crisis.**

70% of businesses are pessimistic about prevailing business conditions

Business confidence, measured by the RMB/BER BCI, declined slightly by one point from 31 in the fourth quarter of 2023 to 30 in the first quarter of 2024. At this level, more than two-thirds of businesses are not satisfied with the prevailing business conditions. The deterioration comes against a backdrop of improved loadshedding which suggests that logistics and other constraints are weighing on business sentiment.

Chart 1: BCI drops further into contractionary territory



Source: Global Insight, BER, Momentum Investments

Retailers expressed the biggest decline in sentiment (13-point drop to 34) which partially offset the 15-point gain in the fourth quarter of 2023. The BER/RMB notes that business profitability was under pressure and likely contributed to the downbeat sentiment of retailers.

Manufacturers also expressed lower sentiment with the subindex dropping from 26 in the fourth quarter of 2023 to 21 in the first quarter of 2024. This does not bode well for the already subdued manufacturing production growth rate especially considering RMB's comment that manufacturers were "more downbeat about investment and business conditions going forward".

The lower sentiment of retailers and manufacturers outweighed the 10-point rebound in confidence levels of new vehicle dealers. However, the confidence levels of new vehicle dealers remained depressed at 16 and are the lowest among the surveyed respondents. The new vehicles sector is bearing the brunt of the high interest rate environment and financially-stretched consumers.

Sentiment of building contractors and wholesalers was largely unchanged increasing by one point each in the first quarter to 42 and 37, respectively.

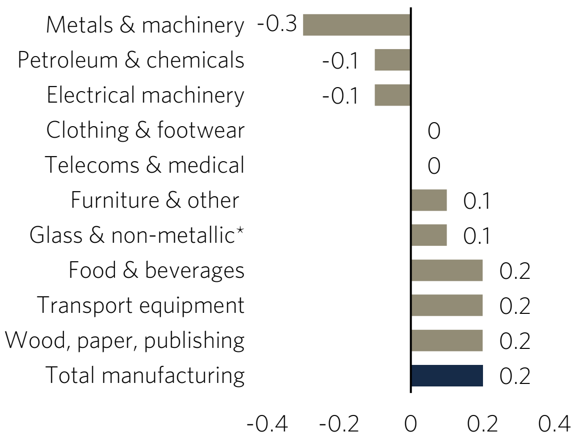
Manufacturing production stagnated in Q4 2023

As reported by Stats SA, growth in seasonally-adjusted manufacturing output in the fourth quarter of 2023 was slightly up by 0.2% q/q following a contraction of 1.1% q/q in the third quarter. This corresponds with the negligible contribution of manufacturing to GDP in the fourth quarter.

Manufacturing activity in the fourth quarter was dampened by lower growth in December (0.7% y/y) compared to 2.3% y/y in October and 2.5% y/y in November. Five of the ten manufacturing categories contracted in December, namely telecommunications (10.8% y/y), motor vehicles (8% y/y), electrical machinery (7.8% y/y), glass and non-metallic mineral products (4.8% y/y) as well as clothing and textiles (4.6% y/y).

The categories that detracted from manufacturing output in the fourth quarter were metals and machinery (detracting 0.3 percentage points), petroleum and chemicals (0.1 percentage point) and electrical machinery (0.1 percentage point). The remaining seven categories had a positive but small contribution (see chart 2).

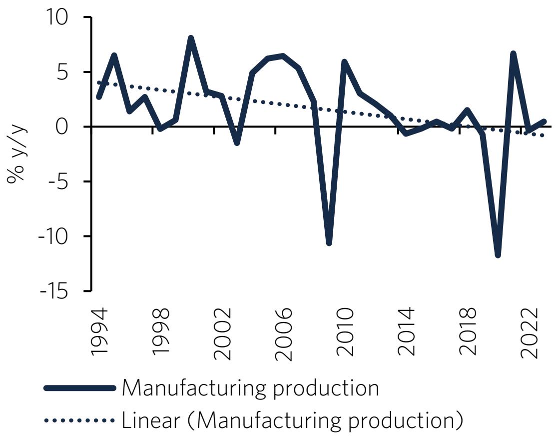
Chart 2: Manufacturing output grew marginally in Q4 2023, %q/q



Source: Stats SA, Momentum Investments
** Glass & non-metallic mineral products*

On a yearly basis, manufacturing production grew by 0.5% y/y in 2023, up from negative 0.4% in 2022 but below the long-term average of 1.6%. As illustrated in chart 3, growth in manufacturing output is on a downward trajectory.

Chart 3: Manufacturing output growth on a downward trend

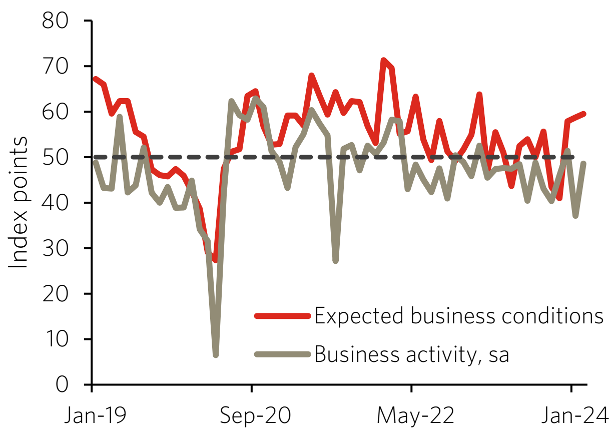


Source: Global Insight, Stats SA, Momentum Investments
Data until 2023

A policy brief published by the University of Johannesburg attributes the decline in manufacturing production to various factors categorised on a macro-, meso- and micro-level. On a macro-level, "the global and national policy shifts, currency fluctuations, import tariffs, inflation rates, manufacturing incentives, and labour regulation" are factors contributing to the decrease in manufacturing production. On a meso-level, the identified factors include "the quality of industrial estates, transport infrastructure, digital connectivity, and living environments for employees". On a micro-level, "energy and water supply, management, technical staff and worker quality, capital availability, and labour relations" are some of the factors cited.

The structural decline in the manufacturing industry has negatively impacted economic growth and employment. According to Stats SA, almost 309 000 jobs have been lost in the manufacturing industry between 2005 and 2021 and the industry's contribution to economic growth has declined from 23.1% in 1993 to 13.2% by 2021.

Chart 4: Manufacturing business activity subindex improves in the first quarter



Source: Global Insight, Stats SA, Momentum Investments
Data until February 2024

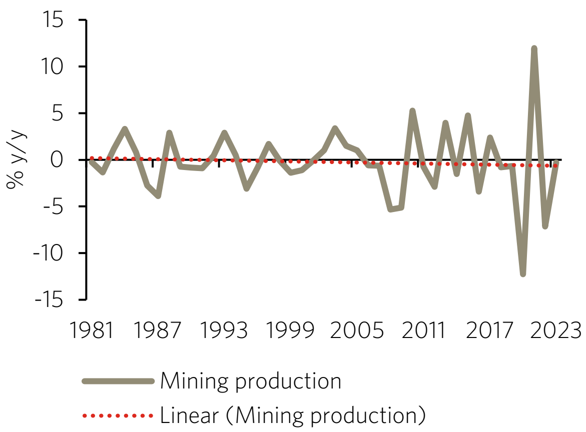
The ABSA Purchasing Managers Index (PMI) dropped by 7.3 points to 43.6 in January 2024, which was the lowest point since May 2020, but picked up to 51.7 in February. The rebound in February was due to a reversal in the subindices which decreased in January. These subindices were new order sales, business activity (see chart 4), inventories and purchasing commitments. The subindex measuring expected business conditions six months' time increased slightly from 58.7 in January to 59.5 in February. In our view, manufacturing growth will remain subdued in 2024.

Mining production contracted marginally in 2023

Seasonally-adjusted mining output grew by 2.4% q/q in the fourth quarter of 2023, contributing positively to the fourth quarter GDP print. The biggest contribution stemmed from PGMs (8.2% q/q, contributing 2.1 percentage points) and coal (5.3% q/q, contributing 1.3 percentage points). Nickel and diamonds also performed well in the fourth quarter, growing by 16% q/q and 9.6% q/q, respectively.

Annually, mining production fell marginally by 0.3% y/y in 2023 following a larger contraction of 7.1% y/y in 2022 (see chart 5). On a longer-term horizon, mining production levels are largely stagnant.

Chart 5: Long-term mining production largely stagnant

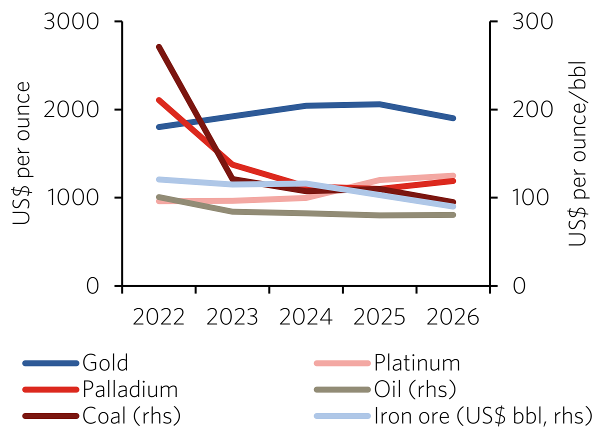


Source: Global Insight, Stats SA, Momentum Investments

Diamond production fell significantly by 39% y/y in 2023, followed by strong growth of 57% in 2022. The production of diamonds has historically been volatile. Some factors influencing the volatility are price changes, demand, consumer preferences and macro-economic conditions According to the *Wall Street Journal*, there is growing demand for lab-grown diamonds made with renewable energy. In addition to the sustainability appeal of lab-grown diamonds, they are cheaper (80% less than a mined diamond). As reported by *CNN*, sales for lab-grown diamonds were up 38% y/y in 2022 and they represent just over 17% of the overall diamond market. The growing popularity of lab-grown diamonds could contribute to falling prices and reduced demand for mined diamonds, subsequently resulting in lower domestic production in the future.

Risks facing the mining industry include loadshedding, logistics inefficiencies, soft commodity prices (see chart 6) and the energy transition agenda. These factors will likely be negative for production growth, employment, economic growth and government tax revenue. As reported by *IOL*, the Minerals Council of SA made a remark at the 2024 African Mining Indaba conference that the platinum industry could shed between 4 000 to 7 000 jobs due to rising costs, falling commodity prices and the move toward electric vehicles. In the 2024 February Budget Review, Treasury noted that provisional mining corporate tax collections were 50.4% lower in the first 10 months of 2023/24 compared to a year ago as a consequence of lower commodity prices.

Chart 6: SA's key export commodity prices stabilising at weaker levels



Source: Bloomberg (19 February 2024), Momentum Investments
Forecasts until 2027

In the 2024 State of the Nation Address, the government announced the following initiatives to support the mining industry:

- Modernisation of the mining rights licensing system.
- The launch of an exploration fund to support emerging miners and exploit new mineral deposits.
- Tackling illegal mining.

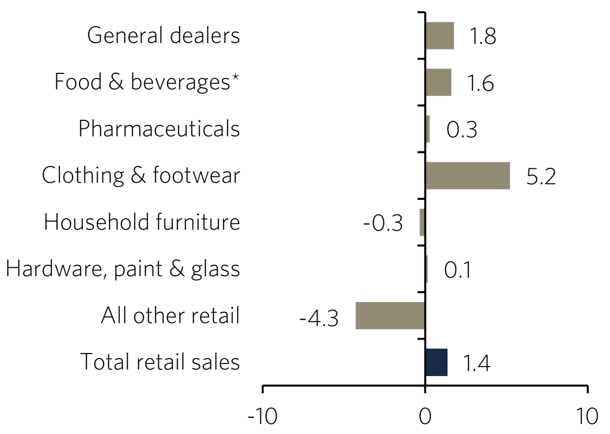
Trade sales fell in Q4 2023

According to Stats SA, retail trade sales, wholesale trade sales and motor trade sales shrunk in the fourth quarter of 2023 and as well as annually in 2023 relative to 2022.

Seasonally-adjusted retail trade sales were down 0.4% q/q in the fourth quarter of 2023 despite strong growth of 2.7% y/y (nsa) in December. The contraction in the fourth quarter was broad-based with five of the seven retailer categories recording negative growth. The largest negative contributor was clothing and footwear retailers (negative 1.5% q/q, detracting 0.3 percentage points).

Seasonally-adjusted retail trade sales were up 1.4% m/m in December, better than in November (1.1% m/m) and October (negative 1.7% m/m). The largest contributor to the increase in December was clothing and footwear retailers (see chart 7). The last time December growth was this high was in December 2015.

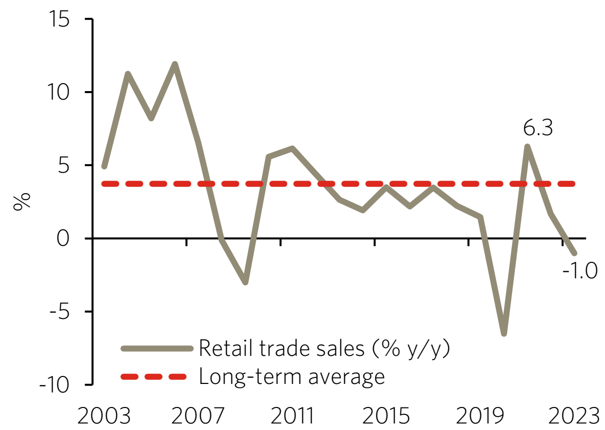
Chart 7: Retail sales growth in December, % m/m



Source: Global Insight, Stats SA, Momentum Investments
** Food and beverages in specialised stores*

On a y/y basis, retail trade sales dropped by 1% in 2023 (see chart 8), reflective of the financial strain endured by consumers during the year. Six of the seven retail categories recorded negative growth with the exception of strong growth by clothing and footwear retailers. We expect some reprieve for consumers in 2024 due to falling inflation, which will lift real wage growth, and expected interest rate cuts, which can alleviate consumer debt burdens. This may provide some support to retail trade sales but it might not be significant given still elevated consumers' debt levels and higher tax burden following no adjustment to tax brackets in the February 2024 national budget.

Chart 8: Retail trade sales fell by 1% in 2023



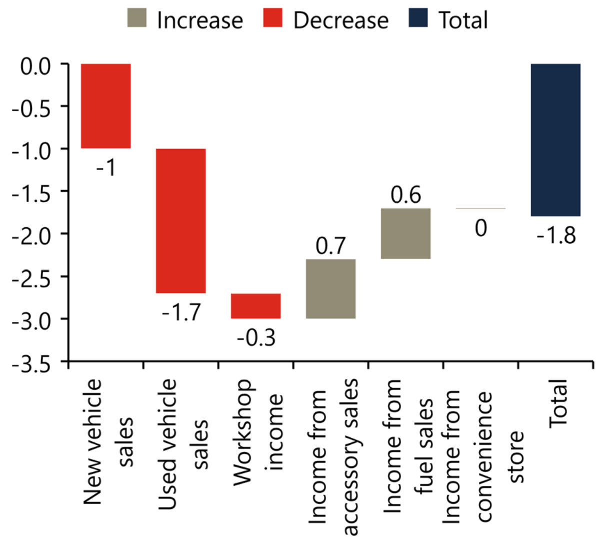
Source: Global Insight, Stats SA, Momentum Investments

Seasonally-adjusted wholesale trade sales dropped by 4.8% q/q in the fourth quarter of 2023. Over the quarter, December wholesale trade sales were 4.3% m/m lower. The rebound of 5.6% m/m in November offset the contraction of 5.6% m/m in October.

Relative to 2022, real wholesale trade sales were down 3.1% y/y in 2023 (worse than negative 0.3% y/y in 2022).

On a quarterly basis, motor trade sales fell marginally by 0.5% q/q in the fourth quarter. Annually, motor trade sales were down 1.8% y/y in 2023. The annual decrease was primarily due to used vehicle sales (negative 8.1% y/y, detracting 1.7 percentage points) and new vehicle sales (negative 4%, detracting one percentage point) as seen in chart 9. The decline in second-hand vehicle sales may be attributed to the reported shortage of used vehicles in the first half of 2023 which led to a substantial increase in prices (*TimesLive*).

Chart 9: Contribution of motor trade sales in 2023, a percentage point



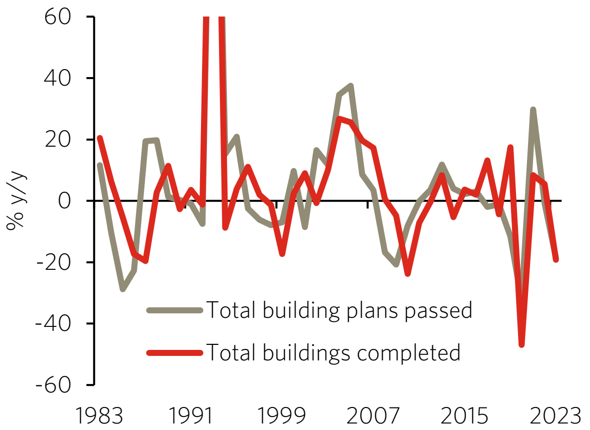
Source: Global Insight, Stats SA, Momentum Investments own calculation

The contraction in motor trade sales in 2023 follows growth of 3.9% y/y in 2022 and 11.7% y/y in 2021 which was largely driven by higher sales of new vehicles. Robust growth in 2021 was due to the economy re-opening from the COVID-19 lockdown restrictions. According to Naamsa (the Automotive Business Council), new vehicle sales were down 1.7% y/y in February 2024 year-to-date weighed down by passenger vehicles (negative 4% y/y). Light commercial bakkies and mini buses as well as heavy trucks and buses recorded positive growth over the same period. The Automotive Business Council highlights that weak economic growth estimated for 2024 is a risk for new vehicle sales. Furthermore, the upcoming election could spur uncertainty which could be a further dampener on new motor sales. However, the council is hopeful that easing inflation, expected interest rate cuts and an improvement in the electricity and logistics domains could be supportive of new vehicle sales.

Lack of demand a key constraint in the residential building sector

Building statistics published by Stats SA were depressed in 2023 with the total value of building plans passed (in real terms) falling by 18% y/y relative to 2022. The total value of buildings completed (real) was down 19% y/y over the same period (see chart 10).

Chart 10: Marked decline in the value of building plans passed and completed in 2023

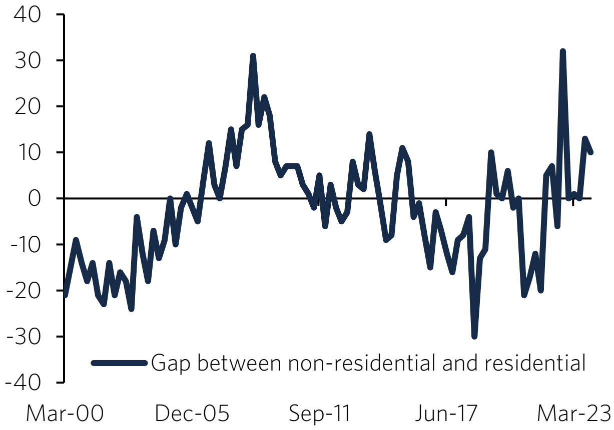


Source: Global Insight, Stats SA, Momentum Investments
Y-axis truncated at 60%. Maximum growth for total building plans passed and completed = 190% y/y and 194.7% y/y, respectively, in 1993

The largest contributor to the decrease in the value of building plans passed during 2023 was residential buildings (negative 23.1% y/y). The value of completions was lower mainly due to additions and alterations (negative 42.7% y/y). The decrease in additions and alterations is an indication that the boom in pandemic renovations has ended.

The value of building plans passed for non-residential buildings in 2023 also contracted but marginally in comparison to the other building categories. According to the BER construction survey results, respondents in the non-residential sector were more optimistic (54%: Q4 2023) than respondents in the residential sector (44%: Q4 2023) as seen in chart 11. A higher share of respondents (76%: Q4 2023) in the residential space identified insufficient demand as a constraint compared to 62% among non-residential respondents.

Chart 11: Respondents in the non-residential space more optimistic than those in the residential space



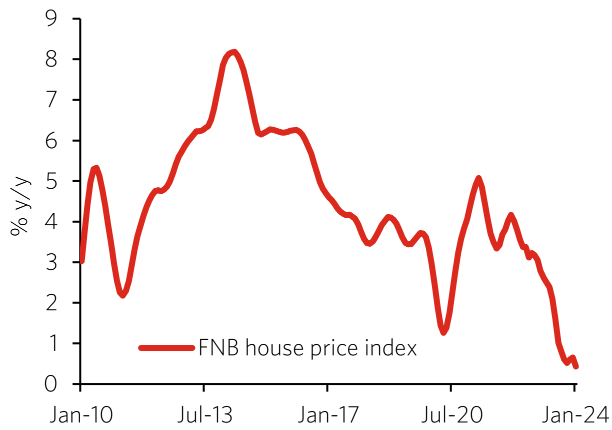
Source: BER, Momentum Investments
Data until fourth quarter of 2023
Positive = Respondents in the non-residential space are more optimistic
Negative = Respondents in the residential space are more optimistic

On a quarterly basis, the real value of building plans passed was marginally higher (1.1% q/q, sa) in the fourth quarter of 2023 and the value of buildings completed was 5.3% q/q higher.

The nine-point improvement in sentiment expressed by respondents in the building sector to 43 in the fourth quarter of 2023 is encouraging for the construction sector especially because it marks the third consecutive quarterly increase and 43 is the highest point since the fourth quarter of 2015. However, more than half of the respondents are still not satisfied with prevailing business conditions. FNB/BER notes the following concerns for the construction sector:

- Fundamentals in the residential sector (e.g. weak house price growth as seen in chart 12) suggests near-term strain in the residential space.
- Elevated interest rates are a hindrance for buildings in the pipeline proceeding to the construction phase.
- Economic growth is expected to be weak in 2024.

Chart 12: House price growth on a steady decline post-pandemic



Source: Iress, Momentum Investments

Sentiment of agribusinesses was downbeat in Q4 2023

Business confidence in the agriculture industry was weak in the fourth quarter of 2023 with the Agbiz (Agriculture Business Chamber) confidence index dropping by 10 points from 50 in the third quarter to 40 in the fourth quarter of 2023. This is the lowest point since the second quarter of 2020. Agbiz notes that confidence was dampened by logistical constraints, deteriorating municipal services, rising geopolitical uncertainty and power cuts.

The biggest decline was recorded in the capital investments subindex from 73 points to 43 points in the fourth quarter. Agbiz attributes this to a decrease in expenditure on agriculture equipment and machinery over the past few months. The general economic conditions and the general agriculture conditions subindices fell by 16 points each to 10 and 40, respectively, in the last quarter of 2023.

The downbeat sentiment of agribusinesses correlates with the headwinds experienced in the agriculture industry in 2023 from animal diseases to adverse weather conditions and structural constraints among other factors.

The volume of agriculture production fell significantly by 12.2% y/y in 2023 from an increase of 0.9% in 2022. There is a possibility of better agricultural activity in 2024. This will likely be driven by fewer irrigation disruptions on the back of fewer power cuts and a recovery from the Avian flu outbreak. El Niño has, as anticipated, been better than in previous years (e.g. 2015) which would be supportive of agricultural activity. However, less rainfall in February is a potential risk. Agbiz highlights further risks to this industry, including poor municipal performance, poor road conditions, crime, logistical constraints and loadshedding.

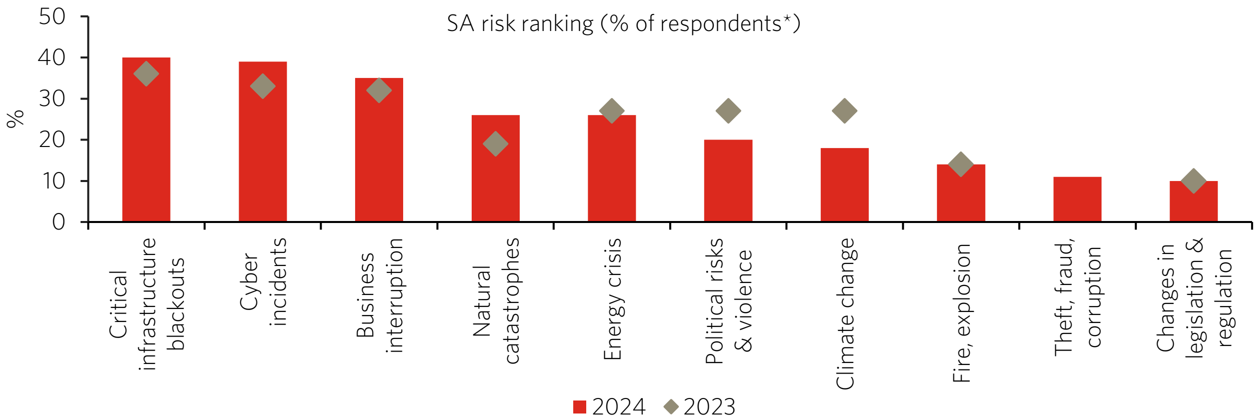
Loadshedding deemed as the highest risk facing businesses in SA in 2024

In the 2024 Allianz Risk Barometer, an annual corporate risk barometer, SA businesses ranked critical infrastructure blackouts as the top risk for the second consecutive year. While blackouts are not unique to SA, they are less of a concern globally with only 8% of the 3069 surveyed respondents citing blackouts as a risk globally.

The top three global risks in 2024 are cyber incidents (e.g. ransomware attacks, data breaches and IT disruptions), business interruptions (including supply chain disruptions) and natural catastrophes. The risk of cyber incidents and business interruptions ranked second and third in SA's perspective.

Political risks and violence as well as climate change have decreased in ranking in SA despite the upcoming 2024 general elections. Theft, fraud and corruption were introduced as a new risk category in 2024 (see chart 13).

Chart 13: 40% of respondents view critical infrastructure blackouts as a risk in SA



Source: Allianz Commercial, Momentum Investments

** There were 179 respondents in 2024 (124 in 2023). Figures don't add up to 100% because respondents choose up to three risks*

The survey for the 2024 barometer was conducted between October and November 2023. During this time, the duration and intensity of loadshedding were lower than in the preceding four quarters however, it was still significant. Furthermore, the country experienced a rise in logistical challenges which explains why more businesses (40% for 2024) noted critical infrastructure blackout as a risk compared to 36% in the previous year. Logistics constraints also partly explain the rise in business interruption.

EskomSePush data and anecdotal evidence point to a reduction in loadshedding in the first quarter of 2024 thus far. We expect this trend to continue and result in less intense loadshedding in 2024 relative to 2023 on the back of an increase in Eskom's electricity generation capacity due to maintenance and repairs. This would be supportive of business activity and economic growth. On the freight logistics front, the congestion experienced at the Durban port toward the end of 2023 has been largely cleared and government is implementing measures to improve the efficiency of the logistics network. Moreover, the appointed leadership of Transnet is receptive to working with the National Logistics Crisis Committee (NLCC) which is encouraging.

Key risks in the logistics and electricity sectors include:

- Unplanned outages from plant breakdowns
- Insufficient electricity transmission capacity. 14 000 kms of transmission lines need to be built over the next 10 years to accommodate renewable energy.
- Theft, vandalism, and sabotage.
- Ageing equipment.
- Maintenance backlogs. Traxtion Africa indicates that the maintenance spending backlog in rail infrastructure between 2012 and 2023 is estimated to be R30 billion.

Implementation of structural reform could provide much needed upward impetus in sentiment

Depressed business confidence in more than two-thirds of businesses is a dampener on economic growth prospects. Weak business sentiment could lead to reduced investment, lower production and a decline in employment opportunities (or even job losses). Furthermore, this introduces further strain on government's financial position.

In our view, the implementation of plans that government has developed to address power outages and logistics inefficiencies has the potential to boost business confidence and economic growth.

We expect economic growth to pick up slightly to 1% in 2024 from a lacklustre 0.7% (expenditure method) in 2023 and increase to 1.7% in 2024 on the expectation of a further alleviation in the energy crisis.