



Business pulse: Firms are cautiously optimistic

Highlights

- Business sentiment improved by a marginal three points to 38 in the third quarter of 2024 according to the Rand Merchant Bank (RMB)/ Bureau for Economic Research (BER) Business Confidence Index (BCI).
- The changes in the BCI sub-components were a mixed bag. New vehicle dealers recorded a 17-point improvement which was the main factor driving the BCI increase. Retailers also expressed higher confidence levels (six points higher) while building contractors and wholesalers recorded a decline in sentiment. Manufacturers' sentiment was unchanged in negative territory.
- According to Statistics South Africa (Stats SA), seasonally adjusted (sa) retail trade sales expanded in the second quarter, with a broad-based increase across the seven retailers.
- The two-pot retirement reform will benefit retail trade sales but this will likely be short-lived in our view. A more sustainable recovery in the retail sector will likely follow from interest rate cuts and contained inflationary pressures. Employment would also need to increase more meaningfully.
- Mining production was weak in the first half of 2024, declining by 1.7% quarter-on-quarter (q/q) in the first quarter and a further 0.8% q/q in the second quarter.
- The mining sector report for 2022 published by Stats SA highlights the importance of Platinum Group Metals (PGMs) in the mining sector. In 2022, PGMs accounted for the biggest share of total mining income. The industry's share of total mining income grew significantly between 2012 and 2022 while gold and most of the other minerals accounted for a smaller share over that period. PGMs also accounted for the largest share of total mining employees in 2022 but this share has decreased over the past 10 years.
- As such, the threat of the rise in electric vehicles (EV) which do not require PGMs is a concern but PGMs are classified as a critical mineral, which means the clean energy transition provides an opportunity for PGMs.
- Manufacturing production, reported by Stats SA, expanded by 1.1% q/q in the second quarter. While manufacturers' sentiment was unchanged in the third quarter, RMB indicates that fewer manufacturers were concerned about the general political climate posing a constraint to investment.
- The agriculture sector experienced a tough second quarter with production down 2.1% q/q and sentiment, measured by the Agricultural Business Chamber of SA (Agbiz)/ Industrial Development Corporation's (IDC) Agribusiness Confidence Index, down to 38 (the lowest level since the third quarter of 2009). Volatile weather patterns are likely to continue driving inconsistent activity in the agricultural sector.
- Structural reform is gaining momentum. In the third quarter, The SA National Water Resource Infrastructure Agency (NWRISA) Bill was signed into law and the National Transmission Company of SA (NTCSA) commenced

operations. Maintaining the reform momentum has the potential to boost business confidence and fixed investment.

- Despite the formation of a government of national unity (GNU), firms appear cautious about the economic outlook, registering only a slight improvement in sentiment levels that remain below neutral. In our view, further proof that economic reforms are being effectively implemented will raise sentiment levels in time, lifting growth in the outer years of the forecast horizon.

New vehicle dealers propel BCI higher, but overall sentiment remains depressed

Business sentiment, measured by the RMB/BER BCI, improved from 35 in the second quarter to 38 in the third quarter of 2024, the highest level since the fourth quarter of 2022. While this is a positive development, sentiment remains depressed, with more than 50% of the respondents being unsatisfied with prevailing business conditions for three consecutive years (see chart 1).

We do, however, observe that the BCI has likely bottomed out at 27 in the second quarter of 2023. The GNU coupled with a more reliable energy supply will likely support ongoing improvement in sentiment. RMB highlights that the third quarter BER results mark the first survey since the formation of the GNU and that respondents were “more upbeat about business conditions going forward”.

Chart 1: Small improvement in business sentiment but remains in negative territory



Source: Stats SA, Momentum Investments
Data until September 2024

The changes in the BCI sub-components were mixed. New vehicle dealers and retailers recorded an improvement in sentiment while building contractors and wholesalers recorded a decline in confidence levels. Manufacturers’ sentiment was unchanged at 28 following a seven-point increase in the second quarter.

New vehicle dealers drove up the BCI through a 17-point improvement in sentiment to 27. Nevertheless, new vehicle dealers remain the most pessimistic sector. The anticipated reduction in interest rates and the moderation in vehicle inflation will help this sector going forward. The inflation rate of vehicles came down to 4% year-on-year (y/y) in July 2024 from a recent peak of 8.4% y/y in September 2023.

Following a five-point improvement in sentiment to 39 expressed by retailers in the second quarter, this sector recorded a further six-point improvement to 45 in the third quarter of 2024.

Building contractors were more pessimistic. This sector’s confidence index decreased by six points to 41 in the third quarter, wiping out the five-point gain in the second quarter. RMB notes that the residential sector is under pressure.

Lastly, wholesalers recorded a two-point decrease in confidence to 51 in the third quarter. Despite this decrease, this is the only sector where more than 50% of the respondents are satisfied with prevailing business conditions.

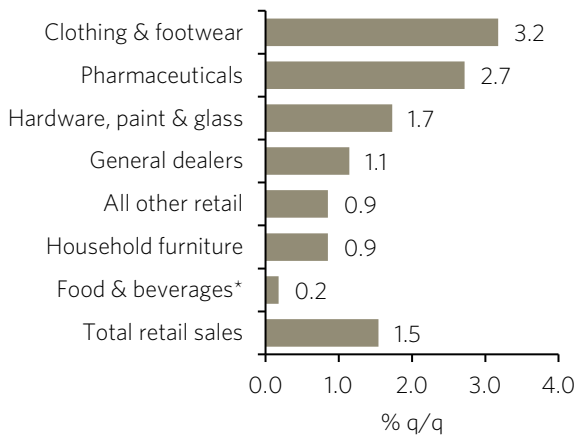
Boost on the retail sector from the pension reform is expected to be short-lived

Seasonally-adjusted retail trade sales rebounded to 1.5% q/q, in the second quarter of 2024 from negative

0.3% q/q in the first quarter. Positive growth was recorded across all seven retailers with strong growth in

clothing and footwear (albeit from a very low base), and pharmaceuticals (see chart 2). The increase in retail trade sales in the second quarter was the strongest since the first quarter of 2022.

Chart 2: Broad-based expansion in retail trade sales in Q2 2024



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

The implementation of the two-pot retirement reform will provide some support to the retail sector in the coming quarters. The extent of the boost will be determined firstly by how consumers split their withdrawals (between debt repayments and

consumption expenditure) and secondly by how they split the portion allocated for consumption expenditure. For instance, given strained consumer finances, consumers may prioritise spending on necessities. We will likely see a tick-up in durable goods and services especially given that Black Friday sales and the festive season are around the corner.

In our view, the impact of the pension reform on retail trade sales will likely be short-lived. A more sustainable recovery in the retail sector will likely follow from interest rate cuts and inflation remaining close to the mid-point of the target as this will increase households' disposable income across the board (i.e. not just among those who have pensions to withdraw from). Furthermore, job growth is a key element to a sustainable increase in the retail sector.

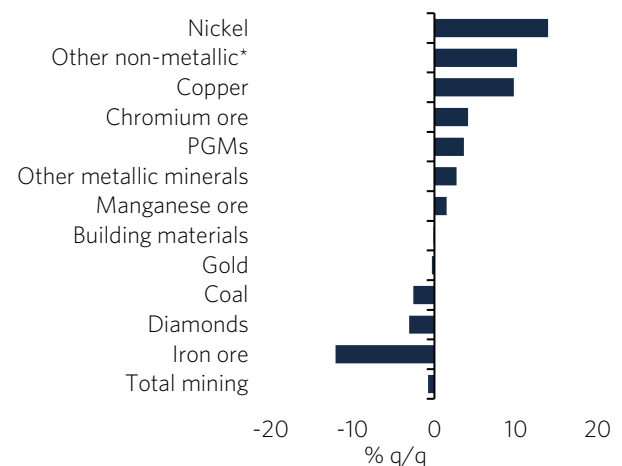
The second quarter services survey published by the BER indicated improvement in sentiment across all the respondents (hotels and restaurants, transport and storage, real estate and business services). A sharp increase was recorded in real estate (from 14 to 41). This was possibly influenced by the expectation of interest rate cuts. Hotels and restaurants maintained the highest confidence levels at 64 in the second quarter.

Uncertain future for PGMs

Production in the mining sector declined by 0.8% q/q, sa in the second quarter, detracting from economic growth. This follows a contraction of 1.7% q/q, sa in the first quarter of the year which means mining production was weak in the first half of 2024.

Most of the mineral groups (seven out of 12) recorded positive growth in production in the second quarter but large production decreases in iron ore (negative 12.1% q/q, detracting 1.6 percentage points) and coal (negative 2.6% q/q, detracting 0.7 percentage points) weighed on overall mining production (see chart 3). PGMs were the biggest positive contributor where an increase of 3.6% q/q translated to a 0.9-percentage point contribution but nickel outperformed all the mineral groups with production growing by 13.9% q/q.

Chart 3: Iron ore detracted the most from mining production in Q2 2024



Source: Stats SA, Momentum Investments
 * Other non-metallic minerals

The mining industry report for 2022 published by Stats SA highlights the important role of PGMs in the mining sector.

In terms of total mining income, PGMs accounted for the biggest share (41.2%) in 2022 followed by coal and lignite (21.9%). Between 2012 and 2022, PGM's share of total mining income grew significantly, while gold and most of the other minerals accounted for a smaller share over that period (see chart 4). The increase in income from PGMs may be attributed to growing demand from China and stricter emission regulations which necessitated more demand for PGMs in the automotive industry, among other reasons.

Chart 4: PGMs contributed the most to total mining income in 2022



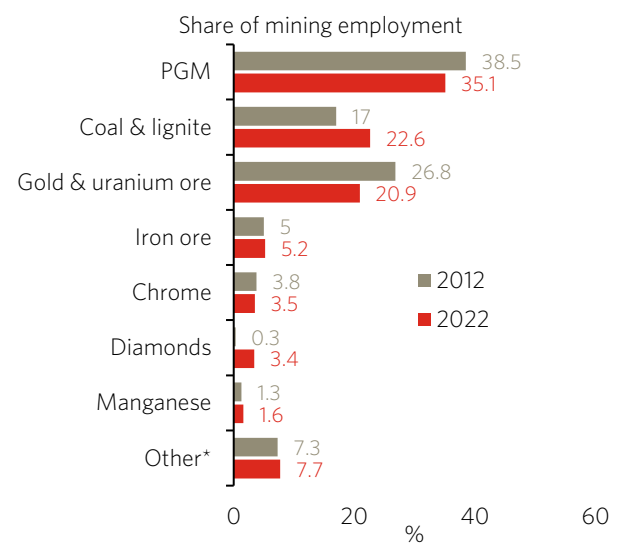
Source: Stats SA, Momentum Investments
 * Other includes limestone and limeworks, dimension stone, extraction and evaporation of salt, other mining activities, other stone quarrying, other chemical and fertiliser minerals, other minerals and materials not elsewhere classified

One of the key themes that emerged at the commodities conference held by the SA Reserve Bank (SARB) in August 2024 was uncertainty about the PGM industry going forward. This largely stems from the transition to EV cars which do not require PGMs. However, the conference also flagged future opportunities for PGMs because they are regarded as critical minerals for clean energy transition.

The PGM industry is not just important from an income perspective but it is also a big employer in the mining sector. According to Stats SA, 35.1% of people in the

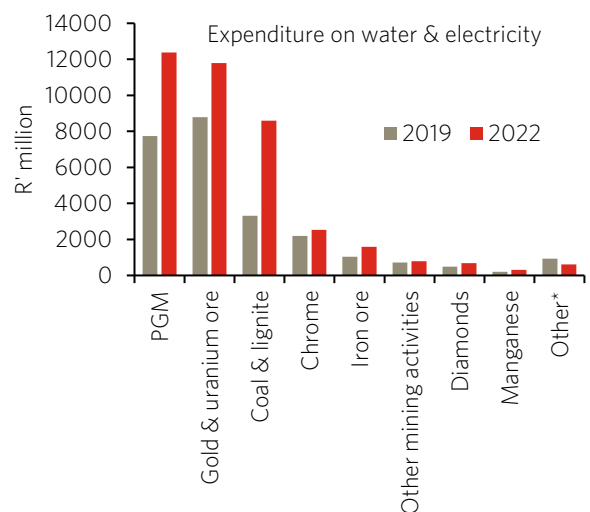
mining sector were employed in the PGM industry in 2022 (see chart 5). While the PGM industry employs the bulk of mine workers, it shed the most jobs between 2012 and 2022. At the beginning of this year, the Minerals Council announced potential job losses of between 4 000 and 7 000 in the PGM industry due to falling commodity prices and rising costs.

Chart 5: PGM industry absorbs the bulk of mining employees



Source: Stats SA, Momentum Investments
 * Other includes the same minerals detailed in chart 5's footnote

Chart 6: PGM miners spent the most on water and electricity in 2022



Source: Stats SA, Momentum Investments
 * Other includes limestone and limeworks, dimension stone, extraction and evaporation of salt, other stone quarrying, other chemical and fertiliser minerals, other minerals and materials not elsewhere classified

Water and electricity accounted for 5.9% of total expenditure in the mining sector. In 2019, gold and uranium ore miners spent the most on water but by 2022 it was the PGM industry that recorded the highest

expenditure on water and electricity (see chart .6). This suggests that PGM mining would be most affected by electricity and water shortages in the mining sector.

Manufacturers are less pessimistic about the general political climate

Manufacturing production experienced a better quarter in the second quarter, growing by 1.1% q/q compared to the contraction of 1.4% q/q in the first quarter of 2024. Six of the 10 industries expanded in the second quarter and the top three positive contributors were motor vehicles, parts, accessories and other transport equipment; food and beverages as well as basic iron and steel, non-ferrous metal products, metal products and machinery.

In the third quarter BCI survey results, RMB indicated that fewer manufacturers were concerned about the general political climate posing a constraint to investment. This means that the GNU has brought about some level of stability. This is expected to filter through positively to fixed investment decisions in the coming quarters.

Agribusiness confidence dropped to global financial crisis (GFC) lows

The agriculture sector contracted by 2.1% q/q in the second quarter of 2024 and thus detracted from economic growth in the second quarter. Poor performance in the sector corresponds with depressed sentiment by agribusinesses.

challenges with animal diseases, logistics inefficiencies and heightened geopolitical tensions. Furthermore, the survey was conducted before there was certainty about the new government structure following the general elections.

The Agbiz/IDC Agribusiness Confidence Index decreased to 38 in the second quarter from 40 in the first quarter. At 38, the index was at its lowest level since the third quarter of 2009. Agbiz attributed downbeat sentiment mostly to the negative effects of El Niño on summer crops. This was in addition to existing concerns in the sector including inadequate road infrastructure, inadequate municipal services,

Given some improvements in the logistics sector, more certainty since the formation of the GNU, Operation Vulindlela's expanded mandate on municipalities in its second term and the fading impact of El Niño, we may see some improvement in confidence among agribusinesses in the coming quarters. However, volatile weather patterns are likely to continue driving inconsistent activity in the agricultural sector.

Structural reform progress has the potential to boost business confidence and fixed investment

After years of slow progress in structural reform at an immense cost to the economy, the tide is turning and we are witnessing faster implementation. On 27 August 2024, The Presidency announced that the NWRIA Bill had been signed into law. This is an important milestone in addressing the water crisis because the bill "establishes a new agency that will be responsible for developing and managing national water infrastructure", similar to SANRAL in the transport sector. Furthermore, the NWRIA will be able to raise funds to increase investment in water infrastructure.

In the energy sector, the NTCSA was corporatised and commenced operations on 1 July 2024. The successful separation of transmission marks progress in the Eskom unbundling process and transition to a competitive electricity market.

Structural reform efforts are yielding tangible results in logistics and energy. In the energy sector, we have experienced a five-month break in loadshedding by the end of August 2024, with Eskom projecting a loadshedding-free summer (i.e. no loadshedding until 31

March 2025). In the logistics sector, the preliminary data shows that Transnet moved 151.7 million tonnes in 2023/24 (slightly above last year's volumes). While this is below the 170 million tonnes initially projected in the Recovery Plan, stable volumes provide tentative signs that the sharp decline in volumes may have been arrested (see chart 7). There is optimism for further improvement in volumes following the R5 billion loan agreement between the New Development Bank and Transnet and the R18.85 loan from the African Development Bank during the second quarter.

IOL reported that The Office of the Presidency indicated that the prospect of Operation Vulindlela's focus on municipalities in its second term has resulted in more Just Energy Transition (JET) pledges.

Continued improvements in logistics and energy will enhance the operating environment and allow

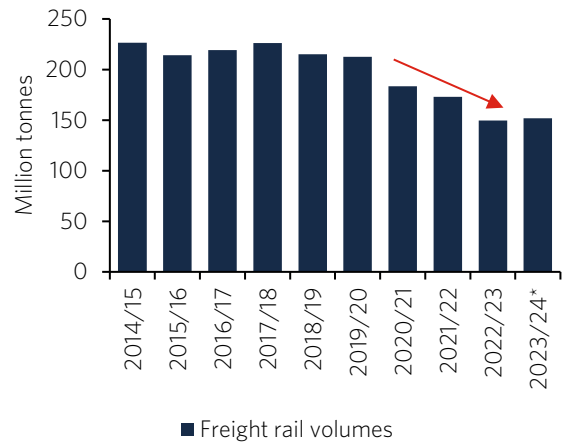
Business confidence is expected to trend upward and support economic growth

On the back of progress in the structural reform agenda and tangible results thereof, a more stable political environment since the formation of the GNU, the expectation of lower interest rates and reduced inflationary pressure, we anticipate that business sentiment will trend upward in the coming quarters.

Apart from pre-2008, the BCI only temporarily touched or breached the neutral mark (50%) and has languished at depressed levels over the past couple of years. With

businesses to invest in growing operations as opposed to investing to remain operational.

Chart 7: Tentative sign that a sharp decline in freight volumes has been arrested



Source: Transnet Recovery Plan, Statista, Momentum Investments
* Preliminary volumes

business sentiment having some ground to cover from the current level of 38 to reach 50, a lot will depend on whether or not the GNU can effectively further its reform agenda.

Our base case is for economic growth to improve from 1.1% in 2024 (previously 1%) to 1.8% in 2025 (previously 1.7%). The expected improvement in business sentiment supports this view.

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