SOUTH AFRICAN CHAMBER OF COMMERCE AND INDUSTRY

Business Confidence Index

February 2019

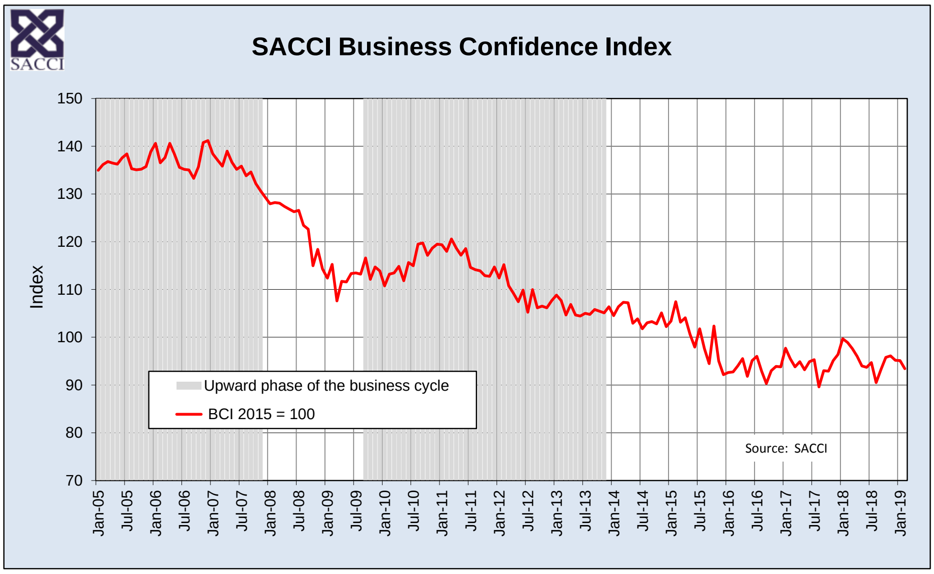
SACCI

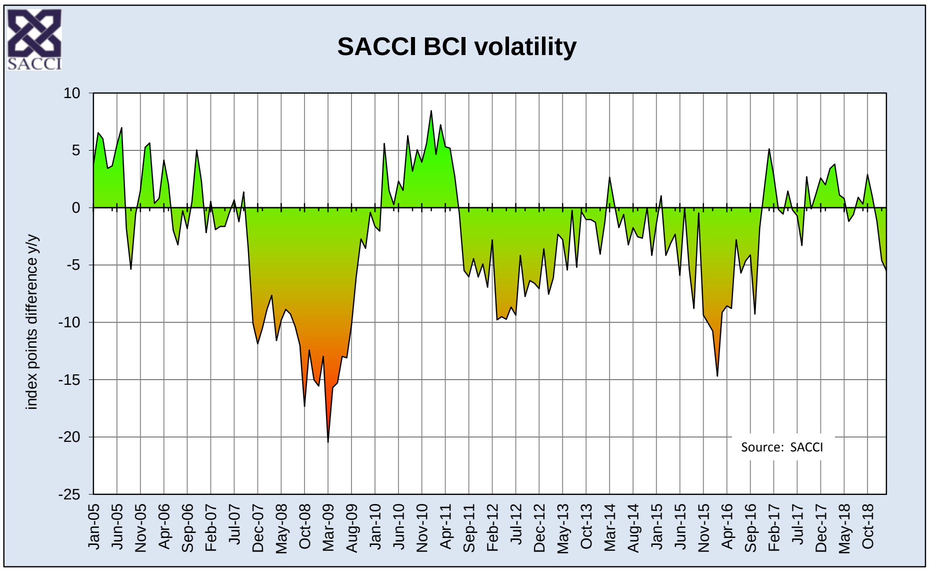
Content:

Because of information lags and changes in expectations, the dynamics of the business mood, may, at times, be at variance with the economic environment. As a result, always read the BCI with other economic data and the accompanying economic commentary. For notes on the BCI, see the SACCI website at www.sacci.org.za.

The SACCI Business Confidence Index
2015=100

Month	2012	2013	2014	2015	2016	2017	2018	2019
January	112.4	108.8	104.5	103.4	92.6	97.7	99.7	95.1
February	115.2	107.7	106.4	107.4	92.7	95.5	98.9	**93.4**
March	110.8	104.7	107.3	103.2	94.0	93.8	97.6	
April	109.2	106.9	107.2	104.1	95.5	94.9	96.0	
May	107.4	104.7	102.9	100.6	91.8	93.2	94.0	
June	109.9	104.4	103.8	97.9	95.1	94.9	93.7	
July	105.2	105.0	101.8	101.8	96.0	95.3	94.7	
August	110.0	104.8	103.0	97.6	92.9	89.6	90.5	
September	106.2	105.8	103.3	94.5	90.3	93.0	93.3	
October	106.5	105.5	102.8	102.3	93.0	92.9	95.8	
November	106.2	105.1	105.1	95.1	93.9	95.1	96.1	
December	107.7	106.4	102.2	92.2	93.8	96.4	95.2	
Average	**108.9**	**105.8**	**104.2**	**100.0**	**93.5**	**94.4**	**95.5**	





This month's BCI results

SACCI's Business Confidence Index (BCI) declined in February 2019 to 93.4. This is 1.7 index points lower than in January 2019 and 5.5 points below the February 2018 BCI level of 98.9. The level of the BCI during the first few months of 2018 was to a large extent driven by expectations of an improved business climate. Business confidence however deteriorated throughout 2018 as the economy and the business climate came to terms with and realised that the structural challenges in the economy lie beyond short-term remedies.

Although action has been taken against some corrupt practices and maladministration, the current preparations by political role-players for the upcoming elections may lead to additional economic policy uncertainty resulting in a tentative business climate in the weeks ahead. This situation will cause the business mode to remain cautionary over the short-term.

Five of the thirteen sub-indices of the **SACCI** BCI improved on their January 2019 readings, five declined and three were unchanged. The main positive month-on-month (m/m) effects on the BCI were increased merchandise export volumes, higher share prices on the JSE, and more real credit extended to the private sector. The rand on average remained stable in February 2019 against the three major trading and investment currencies. Less merchandise import volumes, a dip in real retail sales, uncertain energy supply and less real value of building plans passed, made notable negative contributions to the BCI in February 2019.

In February 2019 the year-on-year (y/y) decline of 5.5 points in the BCI exceeded the 4.6 points decline of January 2019. This negative trend might gather momentum if present strategic economic challenges are not addressed notwithstanding the upcoming election. The y/y dip in the BCI in February 2019 was mainly caused by less merchandise import volumes, a weaker weighted rand, higher core[1] inflation, and lower all-share prices on the JSE. Marginally higher merchandise export volumes and less real financing cost (by default due to higher core inflation), made minor positive y/y contributions to the BCI.

Two of the seven real-activity indices made positive y/y impacts on the BCI in February 2019, while only the real cost of finance (by default) had a positive y/y effect on the business climate compared to a year ago. Four of the six financial sub-indices had negative y/y impacts on the business climate with real private sector credit unchanged on a year ago.

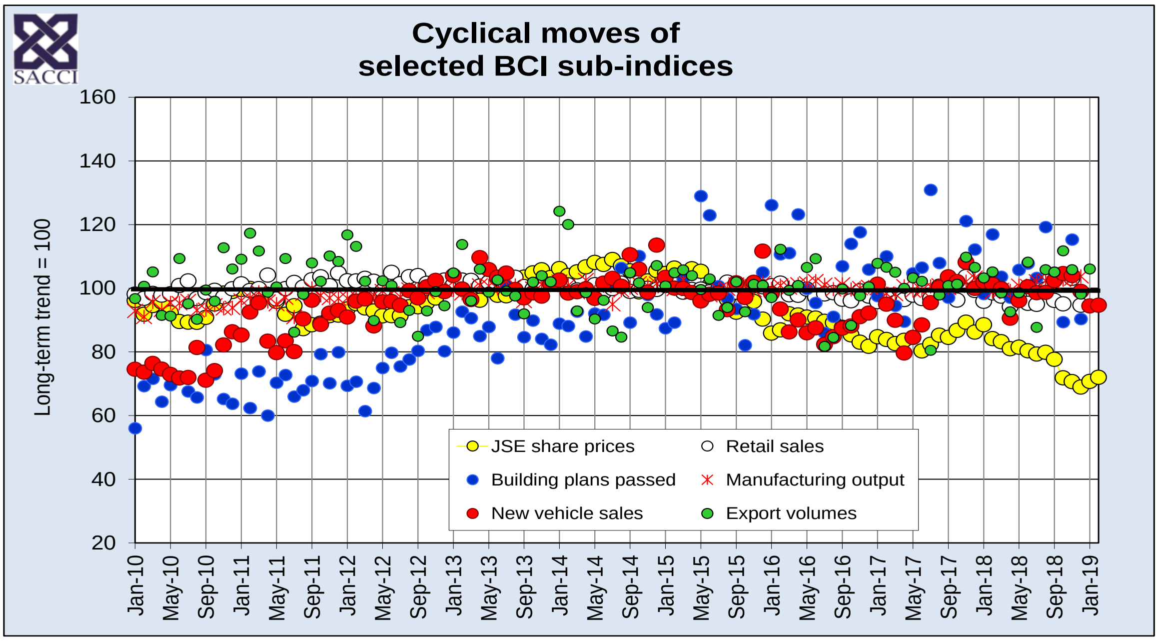
[1] Consumer inflation excluding petrol, food and non-alcoholic beverages.

Impact of BCI sub-indices on the BCI

Business climate indicators *	m/m changes		y/y changes	
	This month	Previous month	This month	Previous month
Energy supply	-	+	-	+
Manufacturing	+	o	+	+
Exports	+	-	+	-
Imports	-	-	-	-
Vehicle sales	o	-	-	-
Retail sales	-	+	-	o
Construction - buildings	-	+	-	-
Inflation[1]	-	-	-	-
Share prices	+	+	-	-
Real private sector borrowing	+	-	o	-
Real financing cost	o	o	+	+
Precious metal prices	+	o	-	-
Rand exchange rate	o	+	-	-

** See notes on BCI on www.sacci.org.za*

1. Excludes petrol, food and non-alcoholic beverages.



Economic commentary

Sensitive Economic Environment

A number of economic uncertainties still mark the global economic scene. Apart from risks due to lower world growth, an unresolved Brexit and its implications for Europe and Britain (among the 10 largest world economies), the trade war impact, capital flows, volatile exchange rates and tighter financial conditions in advanced economies; these are all factors prevailing on the global economic stage and contribute to global economic sensitivity. Geo-political tensions are contributing to the nervousness in the current climate.

Domestically, the South African economy faces serious challenges. These challenges are now deeply entrenched and need to be handled with urgency and care. The upcoming elections do not only serve as an opportunity to establish credible representation, but also provide a platform to come to a rational and sustainable economic policy framework that carries the support of the business community.

Forging Ahead – SONA and Budget 2019/20

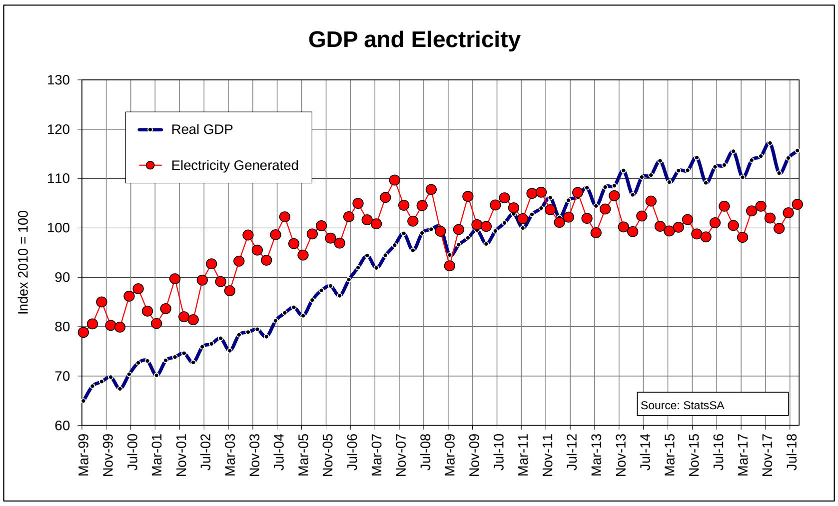
During the State of the Nation Address (SONA), the President provided an indication of the road ahead. A number of matters loomed large and included:

- A desperate financially and technically struggling Eskom
- The National Prosecuting Authority (NPA) to pay attention to serious corruption and related crimes
- Preparing for the Fourth Industrial Revolution
- Building of homes and urbanisation
- Converting public schools into technical high schools
- Promoting and accelerating tourism, and
- Securing more fixed investment.

Budget 2019/20 may ward off a credit rating downgrade from Moody's, but South Africa is still at risk of the agency lowering South Africa’s outlook from stable to negative. The Budget reflects a daunting fiscal environment with revenue projections being lower than in the 2018 MTBPS and, with expenditure higher in 2019/20, the fiscal deficit widens to 4.5% of GDP for 2019/20.

Treasury reduced its GDP growth forecast for calendar year 2019 to 1.5% from 1.7% as anticipated in the MTBPS of October 2018. This caused the deficit to widen with projections of South Africa’s government debt levels to rise to above 60% in 2023/24, compared to the MTBPS expectation of less than 60% of GDP.

Minister Mboweni stated that government will not take on Eskom’s debt and Eskom ultimately remains responsible for settlement. Treasury, however, set aside R23bn a year to financially support Eskom during its reconfiguration. The allocations to Eskom will service Eskom’s debt and allow for redemption requirements as well as funding urgent operational improvements. Figure 1 indicates how the mismatch between electricity supply and economic activity developed over time and partly reflects Eskom's predicament.



It appears that Moody's credit rating agency, while noting the continuing fiscal risks, may keep South Africa's rating for the short-term unchanged with a probable negative outlook. The election results and economic policy reaction (pertaining to certainty and direction), may prevent further credit downgrades. However, a negative outlook can suggest a rating downgrade over the medium term if the future policy direction implies increased fiscal risks.

South Africa's debt servicing costs will rise to R247bn by 2021/22 - the fastest growing item in the budget. The remuneration of the employee's bill may be contained due to cuts in personnel as well as the estimated effects of interventions such as early retirement. However, reductions in expenditure are offset by the allocations for Eskom, the new infrastructure fund and the 2021 Census. The expenditure ceiling is thus revised upwards by R14 billion in 2019/20.

Government's tax proposals amount to R15 billion in 2019/20 and R10 billion in 2020/21. Direct taxes remained unchanged accompanied by improvements at SARS that are expected to address declining tax assessments - not all of which can be attributed to lower economic growth.

Specific tax proposals include:

- No changes to personal income tax brackets, while the tax free threshold increases. It is expected raise R12.8 billion.
- Carbon tax will be implemented on 1 June 2019.
- Increasing the fuel levy by 29c/litre, consisting of a 15c/litre increase in the general fuel levy, a 5c/litre increase in the Road Accident Fund (RAF) levy and the introduction of a carbon tax on fuel of 9c/litre. Increases in fuel taxes together with the carbon tax on fuel will raise R1.3 billion.
- Increases in alcohol and tobacco excise duties will raise revenue of R1 billion.
- White bread flour, cake flour and sanitary pads will be zero-rated for VAT purposes from 1 April 2019.
- The eligible income bands for the employment tax incentive will be increased

from 1 March 2019.

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Revenue collection continues to fall short due to slow economic growth and tax administration concerns. The revised tax revenue estimate for 2018/19 is R15.4 billion lower than the 2018 MTBPS estimate. Problems with tax administration, as highlighted in the findings of the SARS Commission, partly explain poor revenue-collection performance.

The Commission of Inquiry into Tax Administration and Governance by the South African Revenue Service (the SARS Commission), has recommended steps to improve governance. SARS is strengthening its operations by re-establishing the Large Business Centre, a move generally welcomed by business, and setting up a dedicated unit to tackle syndicated tax evasion.

Budget expenditure over the Medium-term Expenditure Framework (MTEF) period is expected to be R5.9 trillion with the bulk of the spending allocated to education and culture, social development, health and community development. The expenditure ceiling is increased by R16 billion over the next three years mainly due to provisional allocations for reconfiguring Eskom, which amount to R69 billion.

Compensation of employees remains the largest category of spending, accounting for an average of 34.4% of consolidated expenditure over the MTEF period. Government expenditure is set to increase on average by 7.8% over the MTEF period, from R1.67 trillion in 2018/19 to R2.09 trillion in 2021/22. Expenditure continues to grow above inflation, with real expenditure growth averaging 2.4%.

Conclusion

Public sector activities and events like SONA and the Budgets are important for setting the mood in the economy on a course for growth, whilst creating a conducive business climate, and promoting a positive investor outlook. The economy is emerging from a difficult period that affected business confidence, in a climate of policy uncertainty and hesitant economic performance. It led to a substantial increase in unemployment levels as a consequence.

It is against this background, that the present economic performance, the SONA, the Budget, and business confidence should be appraised. Business confidence will remain under pressure and success will hinge on implementing, building and improving on these baselines.

General economic indicators

Indicator	Period	Direction	Latest	Previous	2018	2013
Consumer inflation headline urban (%)	Jan-19	▼	4.0	4.5	4.6	5.8
Consumer inflation urban - excl. food, bev. & fuel (%)	Jan-19	▲	4.6	4.5	4.3	5.4
Money supply M3 eop (% Δ Y-o-Y)	Jan-19	▼	5.1	5.6	5.6	5.8
Private sector credit eop (% Δ Y-o-Y)	Jan-19	▲	6.5	5.0	5.6	6.3
Real prime overdraft rate eop (%)*	Jan-19	▼	5.4	5.5	5.5	2.9
Prime overdraft rate eop (%)	Feb-19	►	10.25	10.25	10.25	8.50
Liquidations number sa	Jan-19	▼	155	159	1845	2374
Bond yield 5-10y govt eop (%)	Feb-19	▼	8.62	8.73	8.91	7.73
R / US$ average	Feb-19	►	13.83	13.82	13.24	9.65
R / Euro average	Feb-19	▼	15.68	15.78	15.62	12.82

Indicator	Date	Direction	Latest	Previous	2017	2012
Income & wealth tax / GDP (%) saar	q3-18	▼	14.0	16.6	15.4	14.2
Total tax / GDP (%) saar	q3-18	▼	27.6	30.2	28.0	26.3
Public sector borrowing requirement / GDP (%)	q3-18	▲	4.2	3.9	4.6	6.0
Public sector expenditure / GDP (%)	q3-18	▼	27.5	27.7	27.5	27.2
Budget balance / GDP (%)	q3-18	▲	-7.9	-2.2	-4.4	-5.2
Imports / GDE (%)	q3-18	▲	30.1	27.8	28.7	30.7
Exports / GDP (%)	q3-18	▲	30.1	28.3	29.8	29.7
Net foreign investment flows / GDP (%)	q3-18	▼	2.1	5.6	2.7	6.4
Current account balance / GDP (%)	q3-18	▼	-4.5	-2.0	-2.4	-5.1
Gross domestic saving / GDP (%) saar	q3-18	▲	14.6	14.4	16.2	14.8
Gross capital formation / GDP (%) saar	q3-18	▲	18.0	17.7	18.6	20.0
Net fixed capital formation / GDP (%)	q3-18	▼	-	-	5.2	6.1
GDP growth (% Δ Y-o-Y)	q3-18	▲	1.1	0.4	1.3	2.2

Δ=change; eop=end of period; Y-o-Y=year-on-year; q=quarter; sa = seasonally adjusted;
saar=seasonal adjusted annual rate; GDP=Gross Domestic Product;
GDE=Gross Domestic Expenditure. *Deflated by inflation excl.food, bev. & fuel.