



Herman van Papendorp

Head of Investment Research & Asset Allocation



Sanisha Packirisamy

Economist



Roberta Noise

Economic Analyst

Business confidence slumps to its lowest level in 20 years

Highlights

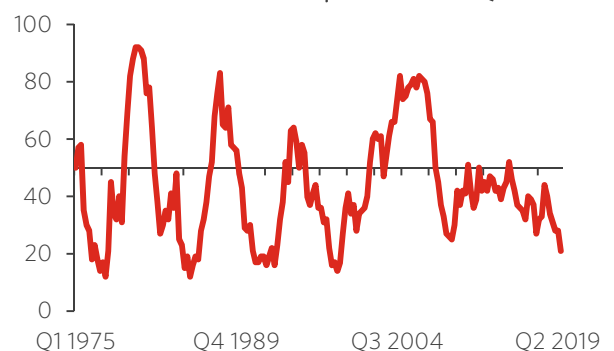
- The Business Confidence Index (BCI) for the third quarter of 2019 plummeted to a 20-year low of 21 index points from 28 index points in the second quarter of 2019.
- There was a deterioration in four of the five sub-indices, whereas three of the sub-indices had improved in the second quarter of 2019. All the sub-indices remained significantly below their historic median in the third quarter of 2019.
- The new vehicle dealers' sub-index was the only sub-index that improved by 5 index points to 22 index points in the third quarter of 2019, but sentiment in this sector remains depressed.
- The manufacturing sector sub-index also nosedived to 16 index points, which are levels last seen in the second quarter of 1999. The latest print was only two index points shy from the lowest level reported in the third quarter in 1985. Eleven index points was shaved off the retail sector sub-index in the third quarter of 2019, from 28 index points in the second quarter of 2019.
- The 25 basis point repo rate cut in July 2019 failed to invigorate optimism in the business environment, suggesting elevated political uncertainty and demand concerns are weighing more negatively on corporates.
- Weak business confidence is unlikely to turn the corner soon, unless significant reforms are implemented.

Further collapse in business confidence

The Bureau of Economic Research (BER) released the BCI for the third quarter of 2019. The index plummeted to a 20-year low of 21 index points (see chart 1). The BCI remained unchanged between the first and second quarter of 2019, before weakening in the third quarter. The BCI has trailed below the 50 neutral mark (a value above 50 signals optimism and pessimism is indicated when the value dips below 50) for the 19th consecutive quarter.

There was a deterioration in four of the five sub-indices, whereas three of the sub-indices had improved in the second quarter of 2019. All the sub-indices remained below their historic median in the third quarter of 2019 (see chart 2).

Chart 1: Business confidence plummets in Q3 2019

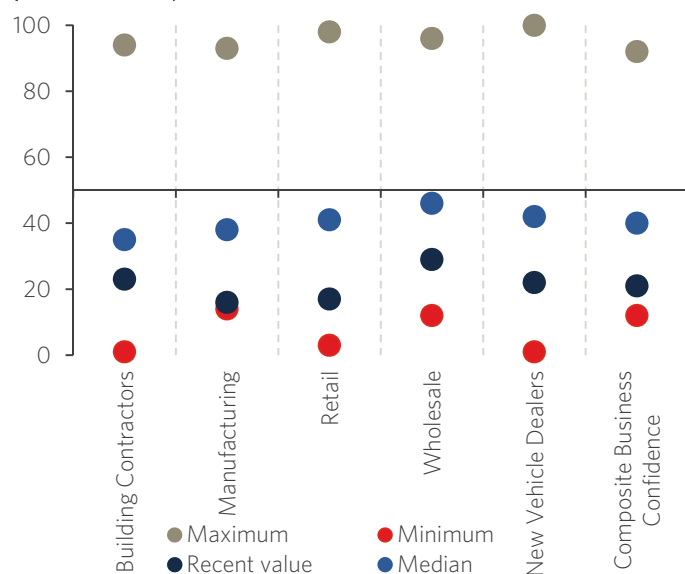


Source: BER, Momentum Investments, data up to Q3 2019

The new vehicle dealers' sub-index was the only sub-index that improved by 5 index points to 22 index points in the

third quarter of 2019. However, it remains meaningfully below the 50 neutral mark. The manufacturing sector sub-index also nosedived to 16 index points, which were levels last seen in the second quarter of 1999. The latest print was only two index points shy from the lowest level reported in the third quarter in 1985. Eleven index points were shaved off the retail sub-index in the third quarter of 2019, from 28 index points in the second quarter of 2019. The building contractors' sub-index lost the seven index points it gained in the second quarter, in the third quarter of 2019. Although wholesalers have the highest sentiment levels relative to the other sub-indices at 29 index points (although below the 50 neutral mark) in the third quarter of 2019, the sub-index lost 13 index points from 42 in the second quarter of 2019.

Chart 2: Business confidence sub-indices (1975 to 2019)



Source: BER, Momentum Investments

Despite the manufacturing sector having added 0.3% (previously negative 1.1%) and the trade sector having contributed 0.5% (previously negative 0.5%) to growth in gross domestic product (GDP) in the second quarter of 2019, it is likely these positive additions were boosted by the low base in the first quarter of 2019, as a result of load shedding. The poor BCI figure confirms the uptick was thus largely unrelated to an increase in demand in the third quarter of 2019.

The BCI surveyed 1800 people between 14 August 2019 and 2 September 2019, which was before the escalation in

xenophobic attacks in the local economy. The attacks would likely have knocked the confidence print and could still show up in the fourth quarter print. Data released by Statistics South Africa (Stats SA) in July 2019, just before the business confidence survey was conducted, showed that insolvencies rose 4.6% in year-on-year (y/y) terms and 15.2% in the first five months of 2019. Liquidations also rose by 5.8% y/y and 11.9% in the first six months of 2019, highlighting difficult operating conditions.

Although the South African Reserve Bank's (Sarb) Monetary Policy Committee (MPC) cut the repo rate by 25 basis points in July 2019 to help boost growth, easier monetary conditions failed to invigorate optimism in the business environment. The weakness in the third quarter business confidence reading will likely translate into a continuation of weak demand, intensified by high policy uncertainty.

An economic policy paper was released by National Treasury towards the end of August 2019. Although it was well received by the market, the discussion paper is likely months away from seeing some of these reforms being implemented, given the fractious political environment. The constraining political environment fails to spark much confidence in the likelihood of the more politically challenging reforms materialising, while progress on the easier-to-implement reforms has also disappointed.

The influx of retrenchment news justifies weak business conditions and significant pressure felt by households and businesses. High-frequency data for new vehicle sales in July and August remained negative and continued to highlight consumers' preferences for entry-level or pre-owned vehicles, indicating weakness in consumer purchasing power. Manufacturing production for July 2019 was negative and the BER's Purchasing Managers' Index (PMI) failed to remain above the 50 neutral mark and reported broad-based deterioration across the sub-indices. This confirms the business environment remains challenging.

Weak business confidence is unlikely to turn the corner soon, unless significant reforms are implemented.

