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Manufacturing and mining production still in the doldrums in October 2019

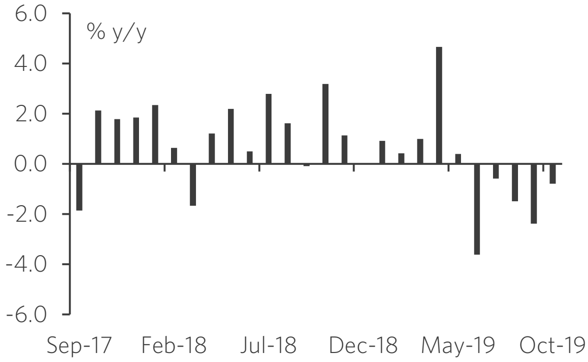
Highlights

- Manufacturing production volumes contracted by 0.8% in October 2019, less than the 2.4% contraction reported in September 2019. Growth in manufacturing production has been in contraction since June 2019.
- Seven of the ten manufacturing divisions reported negative rates in October 2019.
- Food and beverage was the only manufacturing division which added significantly to growth in October 2019.
- The manufacturing sector is feeling the pain of rising protectionism globally.
- An intensification of load shedding will likely cause further political uncertainty and dent any renewed investment prospects.
- Mining volumes contracted by 2.9% in October 2019 after decreasing by 0.6% in September 2019. Four out of the twelve mining divisions reported growth in October 2019.
- Copper, diamonds and manganese ore volumes reported double-digit contractions in October 2019.
- In our view, domestic constraints and weak global demand will likely prevent a significant improvement in manufacturing and mining production.

Fifth consecutive month of contracting manufacturing volumes

Statistics South Africa (Stats SA) released October 2019 manufacturing production volumes, which contracted by 0.8% in year-on-year (y/y) terms, less than the 2.4% y/y contraction reported in September 2019 (see chart 1). Manufacturing production has been in contraction since June 2019. The Iress consensus, however, expected a more significant contraction of 2.5%. There was however, a rebound in seasonally-adjusted manufacturing production, which reported an improvement of 2.7% in month-on-month (m/m) terms, up from a 2.7% m/m contraction.

Chart 1: Manufacturing production contracted less

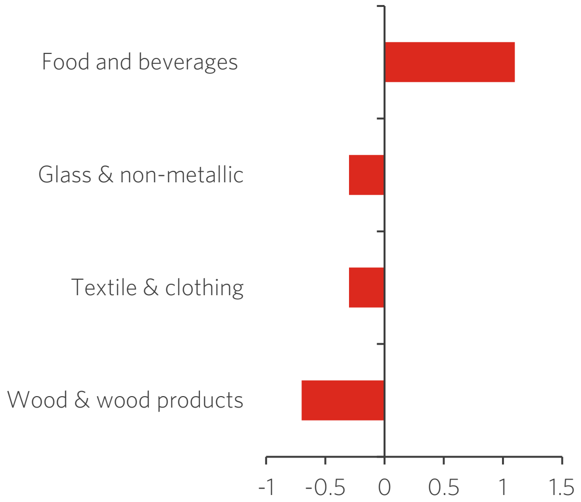


Source: Stats SA, Momentum Investments

Seven of the ten manufacturing divisions reported negative rates in October 2019.

Wood and wood products reported the largest subtraction of 0.7% from the October 2019 number followed by basic iron and steel, which removed 0.4%. The textiles, clothing, leather and footwear division alongside the glass and non-metallic mineral products manufacturing divisions removed 0.3% respectively from manufacturing growth for October 2019. The food and beverage division was the only manufacturing division which added significantly to growth in October 2019 (see chart 2).

Chart 2: Manufacturing division contribution in October 2019 (%)

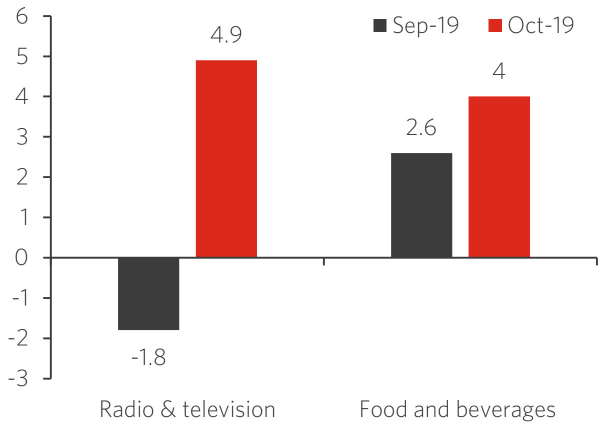


Source: Stats SA, Momentum Investments

Glass and non-metallic mineral product manufacturing volumes fell by 10.7% y/y in October. This was a steeper collapse relative to the 6.9% y/y contraction reported in September 2019. Textiles, clothing, leather and footwear manufacturers also reported a more significant decline in growth in volumes in October 2019 relative to September 2019. Volumes in this division contracted by 9.6% y/y after declining by 6.1% in the previous month.

Volume growth by radio, television and communication manufacturers finally broke out of negative territory and grew by 4.9% y/y in October 2019, previously contracting by 1.8% y/y. Food and beverage volumes grew by 4.0% y/y, up from 2.6% y/y in September 2019 (see chart 3).

Chart 3: Manufacturing division growth (% y/y)



Source: Stats SA, Momentum Investments

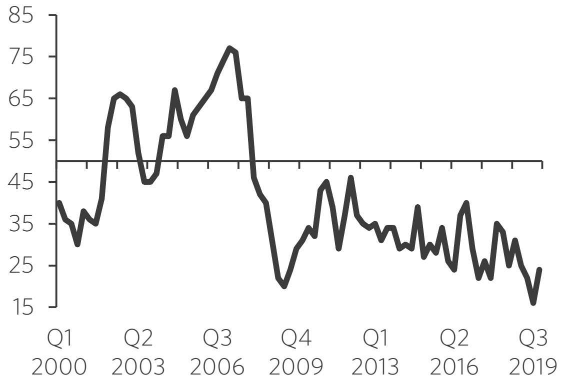
Growth in manufacturing production remains subdued underpinned by low confidence and muted demand in the local economy, while slowing global growth has negatively affected external demand for SA's manufacturing exports.

Sentiment continues to keep manufacturing production weak

Business confidence among manufacturers has been depressed for some time now with interim, short-lived increases but never enough to breach the 50 neutral mark (see chart 4). Manufacturers' sentiment improved to 24 index points in the fourth quarter of 2019 from a low of 16 index points in the third quarter of 2019.

Contributors to the sustained low business confidence among manufacturers include the continuous instability of electricity supply and increasing water supply disruptions.

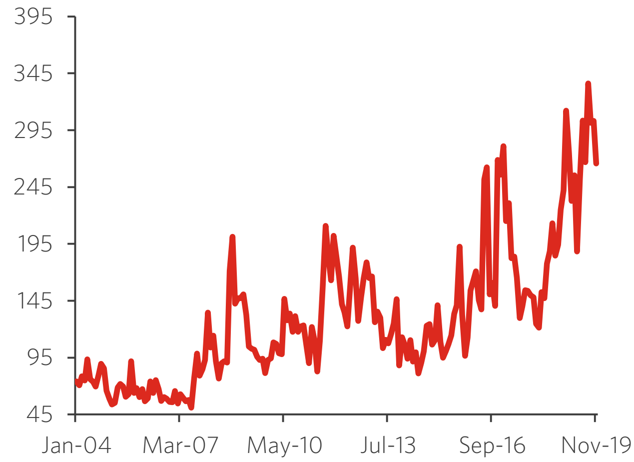
Chart 4: Manufacturing business confidence (Index)



Source: BER, Momentum Investments, data up to Q4 2019

The SA manufacturing cycle is feeling the pain of rising global protectionism. The ongoing trade war has contributed to the rise in global economic policy uncertainty, which peaked in August 2019 but softened marginally after that (see chart 5).

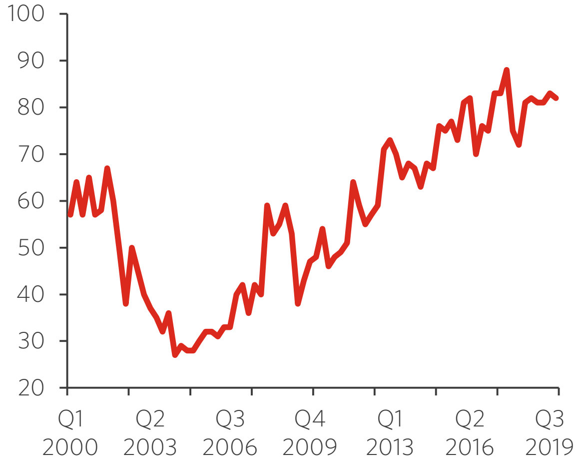
Chart 5: Global political uncertainty (Index)



Source: Politicaluncertainty.com, Momentum Investments

The share of manufacturers rating domestic political uncertainty as a critical constraint to investment continued to rise above 80% in the fourth quarter of 2019 (see chart 6). Uncertainty around various policies has also resulted in the delay of the long awaited investment cycle. The recent intensification of load shedding will likely cause further political uncertainty and dent any renewed investment prospects.

Chart 6: % of Manufacturers rating domestic political uncertainty as a constraint to investment



Source: BER, Momentum Investments, data up to Q4 2019

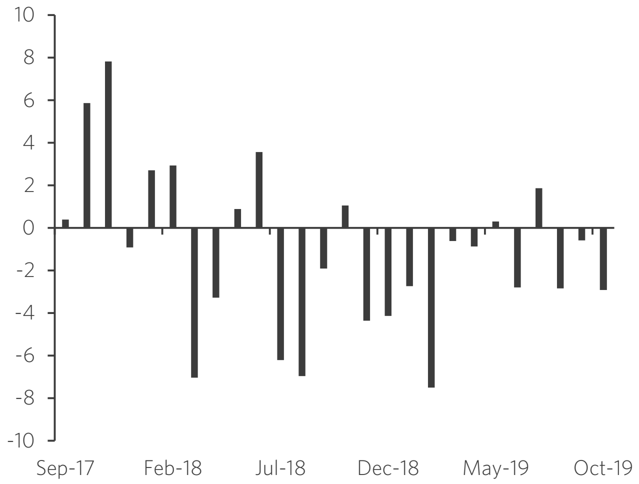
In addition, the manufacturing purchasing managers' index has remained below the 50 neutral mark for the majority of 2019. Forward-looking indices (New sales orders and purchasing commitments) are also in contractionary territory signalling that the status quo in manufacturing production growth will likely remain the same in the near term.

Mining production volumes experience deeper contraction in October 2019

Stats SA mining volumes decreased by 2.9% y/y in October 2019 following a 0.6% decrease in September 2019 (see chart 7). The October reading undershot the Iress expectation for a 2.7% y/y contraction. This marked the third consecutive decline in growth in mining production. Seasonally-adjusted growth in mining production volumes maintained its 1.0% m/m growth rate from September 2019 in October 2019. Four out of the twelve mining divisions reported growth in October 2019.

Domestic and global variables contributed to the slowdown in mining production including electricity supply constraints, water supply shortages and a slowdown in demand.

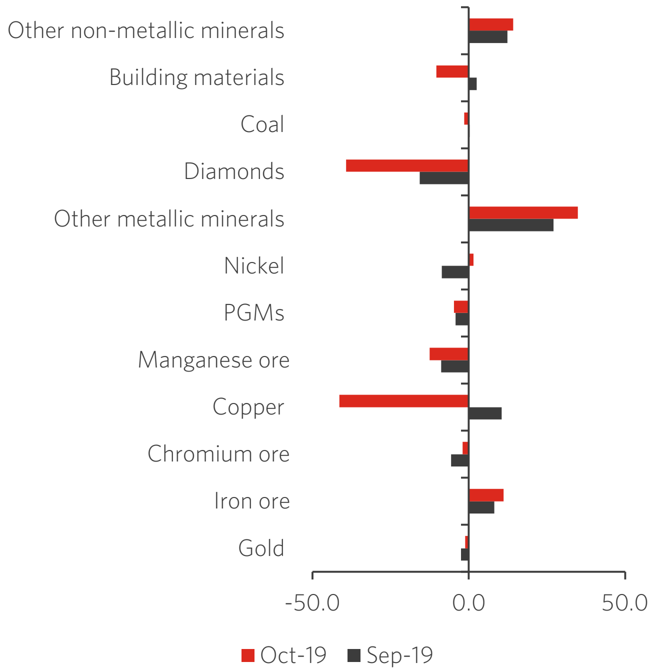
Chart 7: Mining production contracted further (% y/y)



Source: Stats SA, Momentum Investments

There were several double-digit contractions reported in the October 2019 mining production report (see chart 8). Copper production contracted by a significant 41.4% y/y in October 2019, down from 10.5% y/y in September 2019. Diamond volumes plunged 39.3% y/y from a softer 15.8% y/y drop in September 2019. The October growth contraction in diamond volumes was the sixth in a row. Manganese ore volumes contracted for the second consecutive month by 12.5% y/y from 8.9% y/y in September 2019.

Chart 8: Growth in mining production by division (% y/y)



Source: Stats SA, Momentum Investments

Other metallic mineral volumes rose by 34.9% y/y, up from 27.1% y/y in September 2019. Other non-metallic mineral volumes grew by 14.2% y/y in October 2019, up from 12.4% y/y, equating to three consecutive double-digit increases in volumes. Iron ore volumes improved by 11.1% y/y from 8.2% y/y in September 2019, while nickel volumes grew by 1.5% y/y previously contracting by 8.7% y/y.

Several reports indicate that a few mining companies were forced to stop operations due to electricity shortages when load shedding increased to stage 6. Increased load shedding will impact the fourth quarter mining production number. In our view, domestic constraints and weak global demand will likely prevent a significant improvement in manufacturing and mining production.