momentum investments

in the moment



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Production still prickly in June 2019 but enough for a growth rebound in the second quarter of 2019

Highlights

- Manufacturing production for June 2019 slumped by negative 3.2%, however growth in the second quarter rebounded to 0.6%.
- Only four out of the ten manufacturing divisions grew in the second quarter of 2019.
- Year-to-date growth in June reached a meagre 0.5%. More robust growth will be required in the second half of 2019 to surpass the annual growth number for manufacturing in 2018.
- The only division that contributed positively in June 2019, was food and beverages, adding 1.0%. Growth in this division slowed to 3.7% y/y from 6.3% y/y in May 2019.
- Growth in mining production for June 2019 decreased by 4.2% y/y, but growth for the second quarter of 2019 rebounded to 3.5%.
- The largest detractors from growth in mining production were gold (subtracting 2.1%), diamonds (subtracting 1.7%) and platinum group metals (subtracting 1.6%).
- Gold production subtracted 0.5% from the second quarter number of 3.5%. In month-on-month (m/m) terms, production continued to pick up, recovering from strike action between the end of 2018 and the first quarter of 2019.
- Although growth in manufacturing and mining production should improve in the second half of 2019, the production sector is likely to remain subdued on weak global and local sentiment.

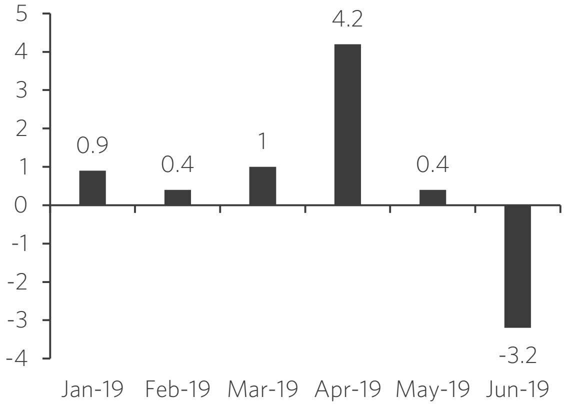
Manufacturing contracts more than anticipated in June 2019, but positive for the quarter

Statistics South Africa (Stats SA) released manufacturing production for June 2019. Growth in manufacturing slumped to negative 3.2% in year-on-year (y/y) terms after growing by 0.4% y/y in May 2019 (see chart 1). Y/y growth in nine of the ten manufacturing divisions was in negative territory in June 2019.

This was the first negative number for growth in overall manufacturing in y/y terms for 2019, however growth for the second quarter rebounded to 0.6% from a 2.4% contraction in the first quarter. The petroleum and chemical products division was the largest growth detractor in the second quarter of 2019, subtracting 0.3%. Meanwhile, food and beverages added 0.4% to the second quarter growth number of 0.6%. Only four out of the ten manufacturing divisions grew in the second quarter of 2019.

Year-to-date growth in June registered at a meagre 0.5%. This indicates that more robust growth will be required in the second half of 2019 to surpass annual growth in manufacturing for 2018.

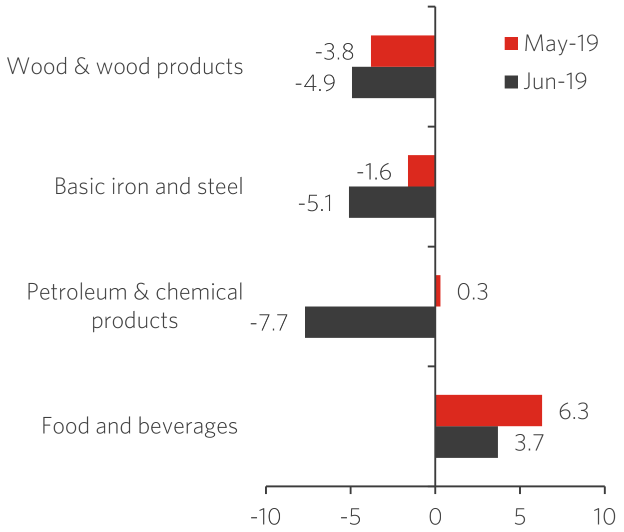
Chart 1: Manufacturing growth (% y/y)



Source: Stats SA, Momentum Investments

Detractors from the June 2019 y/y number emanated from petroleum and chemical products (subtracting 1.7% and contracting by 7.7% y/y), basic iron and steel (subtracting 1.0% and contracting by 5.1% y/y) and wood and wood products (subtracting 0.5% and contracting 4.9% y/y). The food and beverages division was the only division to contribute positively in June 2019, adding 1.0%, but production here grew slower at 3.7% y/y from 6.3% y/y in May 2019.

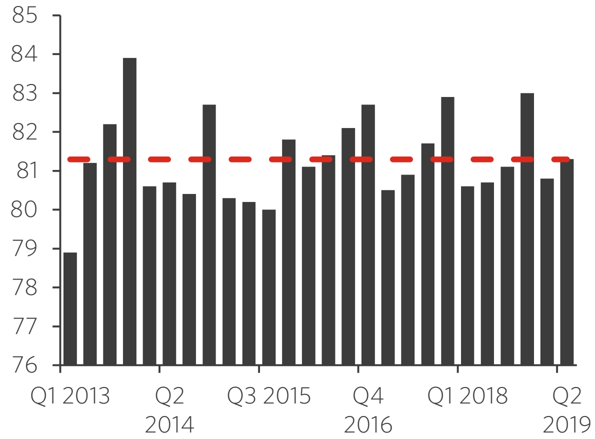
Chart 2: Growth in major contributors (%y/y)



Source: Stats SA, Momentum Investments

Capacity utilisation for the second quarter of 2019 aligned to the average of 81.3%, calculated from 2013, up from 80.8% in the first quarter of 2019 (see chart 3). This can largely be explained by a marginal improvement in demand.

Chart 3: Capacity utilisation (%)



Source: Stats SA, Momentum Investments

The purchasing managers' index (PMI) was below the 50 neutral mark in June 2019 and the Bureau of Economic Research's (BER) manufacturing survey was also lower at 22 index points for the second quarter of 2019.
These forward-looking indicators strongly signalled weakness in the manufacturing sector, which manifested in the second quarter of 2019 and suggests a robust recovery in production in the near term, to be unlikely.

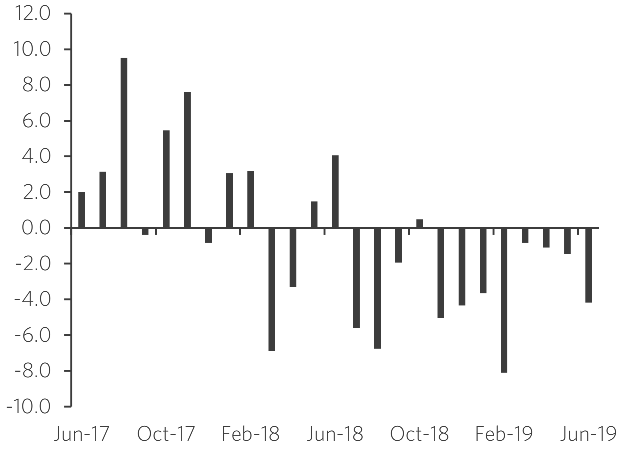
Growth in manufacturing could edge higher in July, in line with an uptick in the July PMI, which edged back into expansion (above the 50 neutral mark).
Global manufacturing PMIs are however still deteriorating, reflecting the weak global outlook.

Mining production contracted in June 2019, but firmed up for the second quarter reading

Mining production for June 2019 released by Stats SA decreased by 4.2% y/y after contracting 1.5% in May 2019 (see chart 4). The largest detractors were gold (subtracting 2.1%), diamonds (subtracting 1.7%) and platinum group metals (subtracting 1.6%). Mining production did improve to 3.3% m/m from 3.1% m/m in May 2019. This contributed to the 3.5% rebound in the second quarter of 2019, which previously contracted 3.0% in the previous quarter. Iron ore added 1.4% to the second quarter print, followed by positive additions of 1.0% and 0.9% from manganese ore and coal, respectively.

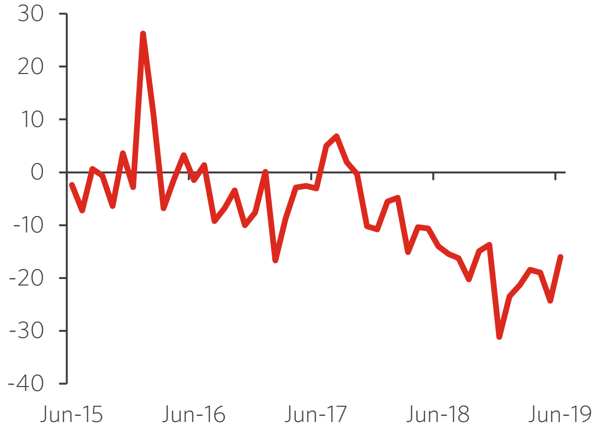
Growth in manganese ore remained robust in June at 24.6% y/y, although slower from 36.6% y/y in May 2019. Iron ore contracted by 1.9% in June 2019, from a deeper decline of 4.7% y/y in May 2019. This is the 9th consecutive decline since October 2018. Copper production contracted significantly by 40.6% y/y in June 2019, following on from positive growth of 38.3% y/y in May 2019. This was the first contraction in growth in copper production since December 2019. Diamonds declined for the second consecutive month in June 2019 by 33.2% y/y from negative 31.4% y/y in May 2019.

Chart 4: Mining growth (% y/y)



Source: Stats SA, Momentum Investments

Chart 5: Growth in gold mining production (% y/y)



Source: Stats SA, Momentum Investments

Gold production subtracted 0.5% from a 3.5% growth in the second quarter of 2019. Although gold production contracted for the 20th consecutive month, the decline to 16% y/y in June 2019 was softer relative to the 24% y/y contraction reported in May 2019 (see chart 5). The sector is still rebounding from the strike action that occurred between the end of 2018 and the first quarter of 2019. Cost pressures have also remained a detractor to growth in the industry.

Production in the mining sector declined for the 8th consecutive month in June 2019 in y/y terms, but the momentum in growth has improved, with growth in the sector recording in positive territory for the second quarter of 2019. Nevertheless, business conditions in the mining industry are likely to remain under pressure in the near term.

Waning employment growth in the production sector amid weak business conditions

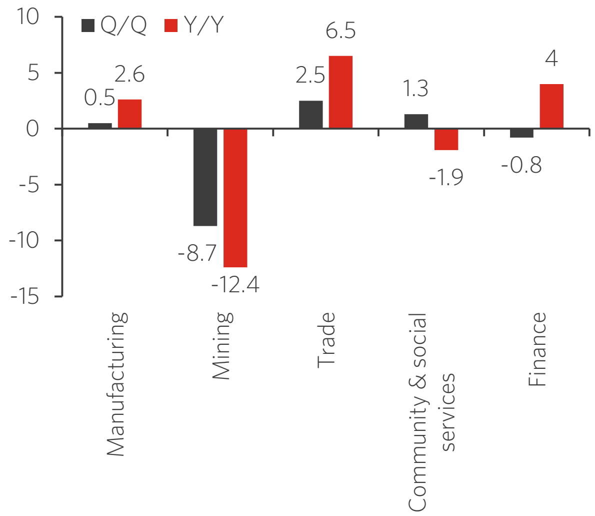
The rate of unemployment jumped again in the second quarter of 2019 to 29%. The production sector represents close to 13% of total employment. The mining sector only represented 2.3% of the share of total employment (direct contribution), but the decline in employment has been concerning. Employment in the sector has been on a declining trend since the peak experienced in the first quarter of 2016 (see chart 6). Manufacturing employment has shifted lower and moved sideways in the last few quarters (see chart 6). This matches the growth underperformance of the sector relative to overall growth in the economy.

Chart 6: Employment (index: Q1 2008 = 100)

Source: Stats SA, Momentum Investments

The production sector experienced limited to no growth in employment relative to the services sector in the second quarter of 2019 on a quarter-on-quarter and y/y basis (see chart 7). The production sector remains a vital driver of employment and therefore growth contributor because of the low-skills conundrum SA faces.

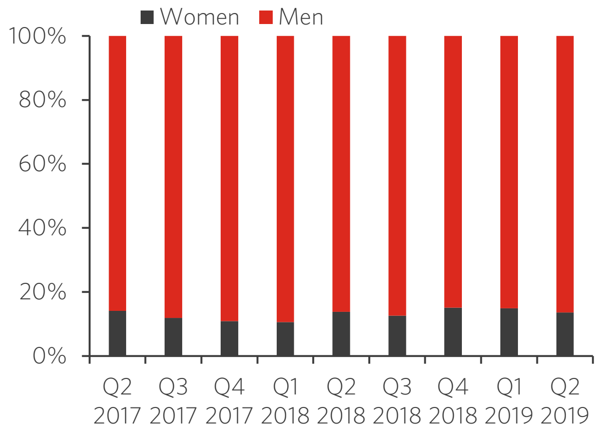
Chart 7: Unemployment (%)



Source: Stats SA, Momentum Investments

The mining sector reported only 14% of female employees in their total employee count in the second quarter of 2019, from 15% previously in the first quarter of 2019 (see chart 8). The sector has displayed a very protracted gender transformation from 10% in the first quarter of 2008, at the start of the quarterly labour force survey (QLFS). This sector has the second-lowest employment gender equality ratio, only preceded by the construction industry.

Chart 8: Mining employment split by gender (% share)



Source: Stats SA, Momentum Investments

However, initiatives like the GirlEng workshops, provided by De Beers with the objective of spreading knowledge on career opportunities in the mining sector through transferring science, technology, engineering and mathematics (Stem) skills, are expected to transform the industry at the margin. Although this is at a secondary and tertiary school level, it does set the tone for career knowledge and opportunities for females in the sector going forward.

Chart 9: Weaker business conditions (index level)

Source: Sacci, Momentum Investments

Confidence in the business sector waned again in July 2019 to 92 index points from 93.3 index points as shown by the SA Chamber of Commerce and Industry (Sacci). Although the downward trend that started in 2010 has slowed, this has accordingly been replaced with a more sideways trend which explains the current stagnant business environment (see chart 9).

Chart 10: Financial conditions

Source: Iress, Momentum Investments

Although financial conditions retreated to below the long-term average of 94 index points to 91.6 in May 2019 from 92.2 index points in June 2019 (see chart 10), businesses remain under pressure and continue to face subdued demand.

Although growth in manufacturing and mining production should improve in the second half of 2019, the production sector is likely to remain subdued on weak global and local sentiment.