WEEKLY ECONOMIC INSIGHTS

Together, Moving Gauteng City Region Forward

GAUTENG PROVINCE
ECONOMIC DEVELOPMENT
REPUBLIC OF SOUTH AFRICA

WEEKLY ECONOMIC INSIGHTS

18 – 22 NOVEMBER 2019

HIGHLIGHTS

- *S&P REVISES SA'S RATING OUTLOOK AMID WORSENING FISCAL & DEBT TRAJECTORY*
- **GLOBAL VALUE CHAINS KEY TO GLOBAL GROWTH & DEVELOPMENT**
- **MPC KEEPS RATES UNCHANGED**
- **FOOD & BEVERAGES INCOME LOW BUT STEADY IN SEPTEMBER**
- **CONSUMER INFLATION DECELERATES TO LOWEST RATE SINCE 2011**

S&P REVISES SA'S RATING OUTLOOK AMID WORSENING FISCAL & DEBT TRAJECTORY

On Friday 22 November 2019, Standard & Poor (S&P) Global Ratings revised SA's outlook from 'stable' to 'negative'. The ratings agency affirmed the country's long-term foreign currency rating at BB (negative) and the country's long-term local currency rating at BB+ (negative). In addition, South Africa's national scale ratings was affirmed at AAA/A-1 for the long and short-term.

Sighting low economic growth, worsening fiscal and deteriorating debt positions as the key reasons for the revision, S&P has warned that it could lower the country's rating, should the fiscal situation deteriorate any further (with a close eye being kept on SA's contingent liabilities particularly in relation to state-owned enterprises such as Eskom). Unfortunately, SA's weak macroeconomic performance has caused a material deterioration in the fiscal outlook and hit tax revenue generation. The ratings agency expects SA's economy to grow by 0.6% this year, down from the earlier forecast of 1% growth for 2019 - released in May. Key to note is that that per-capita growth will remain constrained and well below most emerging market economies.

GAUTENG PROVINCE
ECONOMIC DEVELOPMENT
REPUBLIC OF SOUTH AFRICA

[1] **Produced by Economic Planning Branch (Enquiries: Rebaone.Mokgotla@gauteng.gov.za)**

HIGHLIGHTS

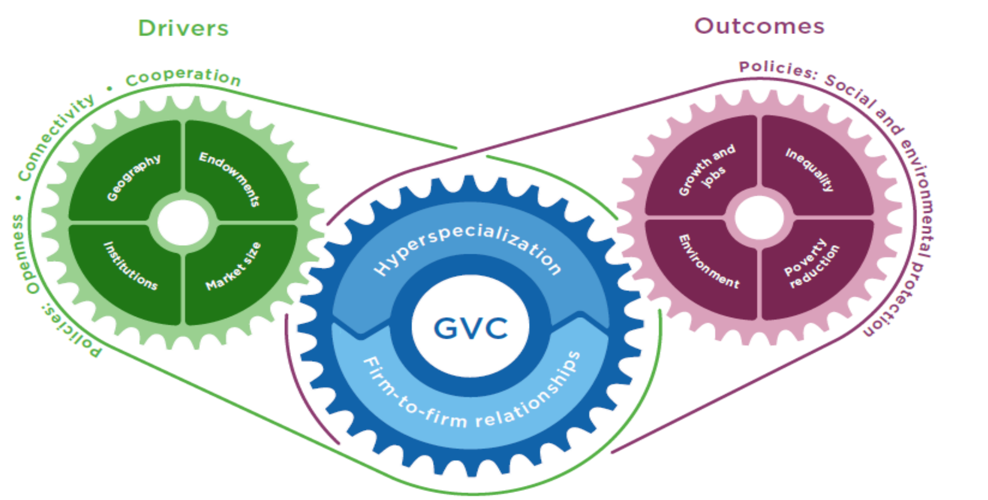
- *S&P REVISES SA'S RATING OUTLOOK AMID WORSENING FISCAL & DEBT TRAJECTORY*
- *GLOBAL VALUE CHAINS KEY TO GLOBAL GROWTH & DEVELOPMENT*
- **MPC KEEPS RATES UNCHANGED**
- **FOOD & BEVERAGES INCOME LOW BUT STEADY IN SEPTEMBER**
- **CONSUMER INFLATION DECELERATES TO LOWEST RATE SINCE 2011**

Government's efforts to overcome the challenges have centred on cutting costs across government spheres and several structural reforms. Eskom's financial and operations issues continue to weigh on government finances. And the additional R69 billion allocated to the power utility over the next three years (in addition to the R23 billion announced in the February budget), highlights the severity of the situation. Together, these allocations amount to an average 0.9% of GDP in each of the next three years, and will have a notable impact on government's fiscal metrics.

Nonetheless, the country's rating is supported by its monetary flexibility, well-capitalised and regulated financial sector, and deep capital markets. SA also has moderate external debt levels, with only about 8% of debt being denominated in foreign currency. The ratings agency noted that any further weakening in local economy or deepening of external funding pressures could support lowering the country's rating in coming months.

GLOBAL VALUE CHAINS KEY TO GROWTH & DEVELOPMENT

In a flagship report published recently by the World Bank titled *"Trading for Development in The Age of Global Value Chains"*, the role and significance of global value chains in promoting growth, creating jobs and reducing poverty is discussed, emphasising the need for industrial reform in developing countries and open and predictable policies in developed industrialised economies.

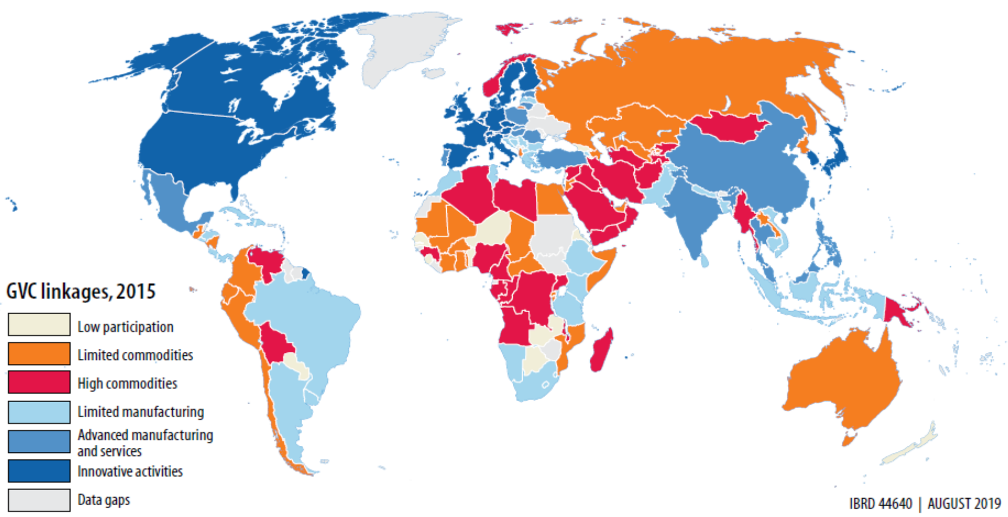


Global Value Chains (GVCs) break up the production processes across several geographical locations with firms each specialising in a specific input/task or component of the final product. The interactions between firms typically involves strong relationships between firms which consider their geography, special endowments, market size and institutional characteristics.

HIGHLIGHTS

- **S&P REVISES SA'S RATING OUTLOOK AMID WORSENING FISCAL & DEBT TRAJECTORY**
- ***GLOBAL VALUE CHAINS KEY TO GLOBAL GROWTH & DEVELOPMENT***
- **MPC KEEPS RATES UNCHANGED**
- **FOOD & BEVERAGES INCOME LOW BUT STEADY IN SEPTEMBER**
- **CONSUMER INFLATION DECELERATES TO LOWEST RATE SINCE 2011**

Supported by the rise of GVCs, international trade expanded rapidly after 1990, which greatly enabled global economic convergence as poor countries increased economic output and began to catch-up with wealthier, more developed economies. Specifically, productivity and incomes rose in countries such as China, Bangladesh and Vietnam, that effectively managed to integrate their operations into GVCs. However, trade growth has been sluggish since the 2008/9 financial crisis and this has been further complicated by the recent emergence of protectionist trade reforms in US-China trade war as well as uncertainties stemming from Brexit.



Prior to the financial crisis, GVCs grew steadily as technological advances in transport, information and communications as well as lower trade barriers prompted manufacturers to extend production processes beyond national borders. However, weaker levels of investment and reversal of trade reforms have contributed to the slowing pace of GVCs. As illustrated on the map above, South Africa's GVC linkages are limited to some manufacturing activities with countries such as Mauritius, Angola and Zambia being heavily reliant on commodities for their GVC linkages. In fact, not a single African country is categorised as being integrated into advanced manufacturing and services or innovative GVC. According to the World Bank, any future deepening or expansion of GVCs could stall, unless policy predictability is restored.

In addition, the World Bank highlights the following:

GVCs boost incomes, create better jobs and reduce poverty – in Ethiopia for example, firms that participate in GVCs are more than twice as productive as similar firms that participate in standard trade. In addition, a 1% increase

HIGHLIGHTS

- S&P REVISES SA'S RATING OUTLOOK AMID WORSENING FISCAL & DEBT TRAJECTORY
- *GLOBAL VALUE CHAINS KEY TO GLOBAL GROWTH & DEVELOPMENT*
- MPC KEEPS RATES UNCHANGED
- FOOD & BEVERAGES INCOME LOW BUT STEADY IN SEPTEMBER
- CONSUMER INFLATION DECELERATES TO LOWEST RATE SINCE 2011

in GVC participation is estimated to boost per capita income by more than 1% with the largest growth coming when countries transition from exporting commodities to exporting basic manufactured products. GVCs can also deliver better jobs as they draw workers out of less productive activities and into more productive manufacturing and services activities.

The rise of 4IR and new technologies promote trade and GVCs – evidence suggest that on balance, technological advancements are enhancing trade and GVC linkages. Innovation has led to the emergence of new traded goods and services, thus contributing to faster trade growth – for example in 2017, an estimated 65% of trade was in sectors that did not exist in 1992. Interestingly, shifts towards 3D printing and automation have contributed to higher productivity and larger scale production. This has in turn increased demand for input imports, particularly in automotive, rubber and plastics, metal and electronics and machinery sub-sectors in developing countries.

National policies can/should boost GVC participation – policies to attract foreign direct investment can aid in financing the capital, technology and management skills needed to fund product specialisation and key components for GVCs. More importantly, the World Bank emphasises the importance of ensuring that national policies are tailored to the specific circumstances (market size, endowments, geography and institutions) of a country and to very specific forms of participation in GVCs.

Global cooperation supports beneficial GVC participation – at the centre of GVCs is the international trade system and the rules, regulations and corresponding agreements. Because the costs of protection are magnified when goods and services cross borders multiple times, the gains from coordinated reduction of barriers to trade are further magnified for GVCs. The recently signed Africa Continental Free Trade Area Agreement is an ideal opportunity for deepening intra-Africa value chain linkages which could then be incorporated into GVCs.

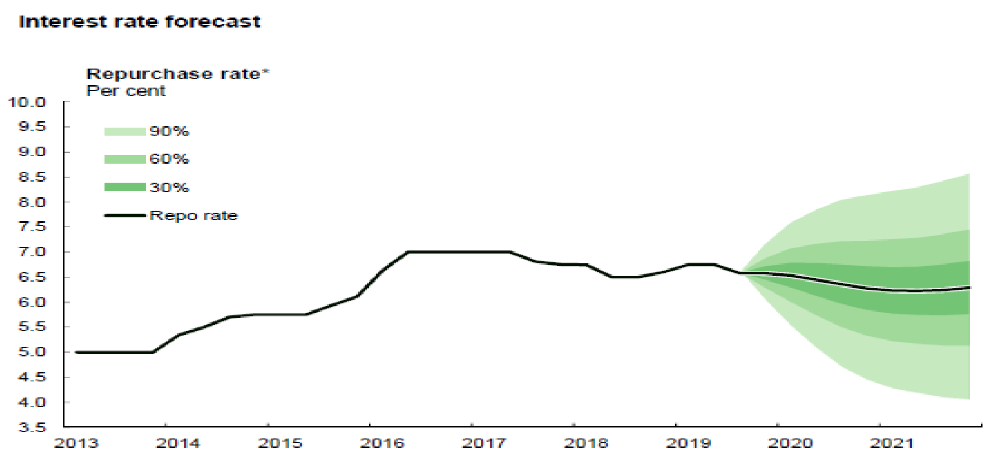
GVCs present opportunities to advance local industries; ensuring that they actively participate in global trade. Notwithstanding the geography and natural endowments, South Africa and Gauteng will need to ensure that sound policies are at the centre of trade and investment plans to ensure that the right industries are supported in the right way so they can be integrated into GVC to aid in growing the domestic economy.

HIGHLIGHTS

- S&P REVISES SA'S RATING OUTLOOK AMID WORSENING FISCAL & DEBT TRAJECTORY
- GLOBAL VALUE CHAINS KEY TO GLOBAL GROWTH & DEVELOPMENT
- *MPC KEEPS RATES UNCHANGED*
- FOOD & BEVERAGES INCOME LOW BUT STEADY IN SEPTEMBER
- CONSUMER INFLATION DECELERATES TO LOWEST RATE SINCE 2011

MONETARY POLICY COMMITTEE KEEPS RATES UNCHANGED

On the 21st of November 2019, the expectation of some financial relief for consumers was squashed, following the announcement of the decision by the Reserve Bank (SARB) Monetary Policy Committee (MPC) to keep the repo rate unchanged at 6.5%. Whilst the inflation reading for October moderated further as demand remains subdued, the rate was held steady to avert any further price increases, following an already negative inflation outlook for 2020. In the first quarter of 2020, inflation is expected to peak at 5.3% with the yearly average expected to measure at 5.1%. The forecasted uptick in inflation is underpinned by the outlook for wage growth, fuel, electricity and water prices which are forecast to rise steadily, as well as concerns about drought, which is expected to threaten the currently steady food prices. Thereafter, in 2021, inflation is expected to moderate slightly. Consequently, the interest rate is forecasts to average 6.3% both in 2020 and 2021.



Data source: South African Reserve Bank

In addition, the SARB has forecast lower economic activity for the rest of the year, with a downward revision of the GDP growth forecast for 2019 to 0.5%, from 0.6% in the previous MPC statement (with the output gap of 1.8%). For the next two years, gross domestic output is expected to record some recovery but will continue to perform below potential, with GDP growth for 2020 expected to reach 1.4% (from 1.5% in the previous statement) and that of 2021 measuring at 1.7% (from 1.8% in the previous statement).

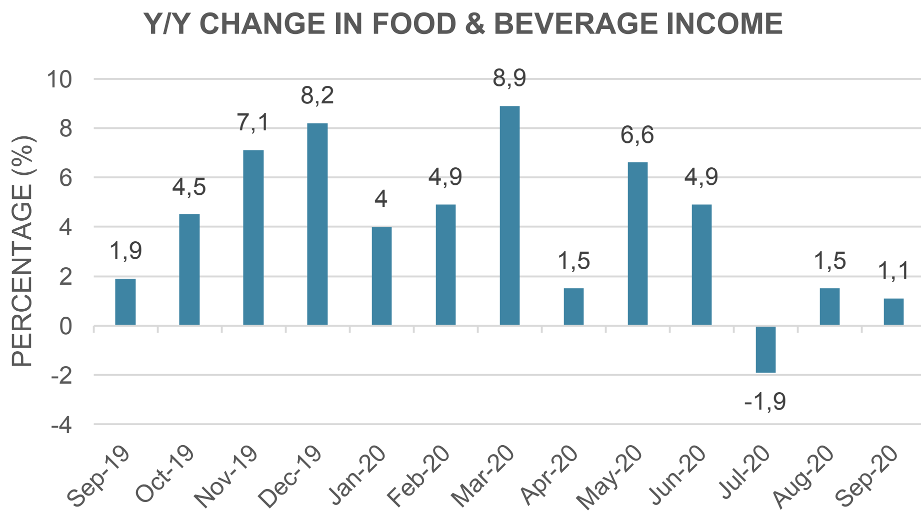
With the declining levels of consumer demand, the unchanged repo rate has robbed consumers of the reprieve from softer instalment repayment which could have boosted spending in the last quarter of the year.

HIGHLIGHTS

- S&P REVISES SA'S RATING OUTLOOK AMID WORSENING FISCAL & DEBT TRAJECTORY
- GLOBAL VALUE CHAINS KEY TO GLOBAL GROWTH & DEVELOPMENT
- MPC KEEPS RATES UNCHANGED
- *FOOD & BEVERAGES INCOME LOW BUT STEADY IN SEPTEMBER*
- CONSUMER INFLATION DECELERATES TO LOWEST RATE SINCE 2011

FOOD & BEVERAGES INCOME LOW BUT STEADY IN SEPTEMBER

On 18 November 2019, Statistics South released the latest Food and Beverages income figures. The publication revealed that income earned by the food and beverages industry increased by 1.1% year-on-year in September 2019, following an increase of 1.5% in August and -1.9% contraction in July.



Data source: Statistics South Africa

The increase in income generated by the industry was driven by improvements in bar sales (2.7%) and food sales (1.5%). On the other hand, a sizable contraction (-17.1%) was recorded for 'other income' during the period.

The figures per enterprise type revealed that income earned by restaurants and coffee shops increased by 1.8% in September, underpinned by the improvements in food and beverage sales. On the other hand, takeaway and fast-food outlets and catering services registered marginal increases of 0.4% and 0.2%, respectively.

For the quarter ending September 2019 (Q3:2019), income earned by the sector increased slightly by 0.3% compared to the same quarter last year. Ironically, the subdued quarterly performance was due to lackluster income for restaurants and coffee shops, which generated 1.2% less revenue than that of the third quarter of 2018.

Going forward, income levels in the industry is likely to gain traction in the last quarter of 2019, due to the seasonal increase in expenditure during the festive season. However, performance will begin to taper in the beginning of 2020 as consumption patterns lean towards preparation for the academic year.

HIGHLIGHTS

- **S&P REVISES SA'S RATING OUTLOOK AMID WORSENING FISCAL & DEBT TRAJECTORY**
- **GLOBAL VALUE CHAINS KEY TO GLOBAL GROWTH & DEVELOPMENT**
- **MPC KEEPS RATES UNCHANGED**
- **FOOD & BEVERAGES INCOME LOW BUT STEADY IN SEPTEMBER**
- *CONSUMER INFLATION DECELERATES TO LOWEST RATE SINCE 2011*

CONSUMER PRICE INFLATION DECELERATES TO LOWEST RATE SINCE 2011

On 20 November 2019, data released by Statistics South Africa showed that the consumer price index (CPI) registered at 3.7% for October, its lowest level in eight years and much lower than the 3.9% number expected by the market. This figure is down from September's figure which was 4.1%, suggesting that the prices of goods and services are rising at a much slower rate.

Factors that contributed to the lower CPI include fuel prices which decreased by 4,9% in October 2019 compared with the same month last year. On the other hand, food and non-alcoholic beverages annual inflation increased by 3.6%, whilst housing and utilities and miscellaneous goods and services increased by 4.8% and 5.7%, respectively in October.

The lower consumer and producer inflation rates in recent months have been touted as key indicators of a possible interest rate cut by the Monetary Policy Committee (MPC). Furthermore, analysts have cautioned that the lower CPI is also a result of a weak economy, as retailers and manufactures are not able to increase prices, as they try to retain sales to the already constrained household consumer sector. Notwithstanding, the much lower than expected CPI reading could come as a welcomed relief to cash-strapped consumers with Black Friday and Christmas around the corner.

INDICATORS: Week 18 - 22 Nov 2019

CONSUMER PRICE INDEX

3.7% y/y
Oct'19

FOOD & BEV

1.1% y/y
Sep'19

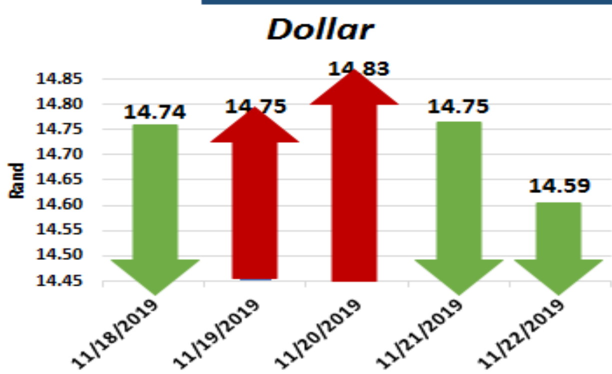
Source: Statistics South Africa, 2019

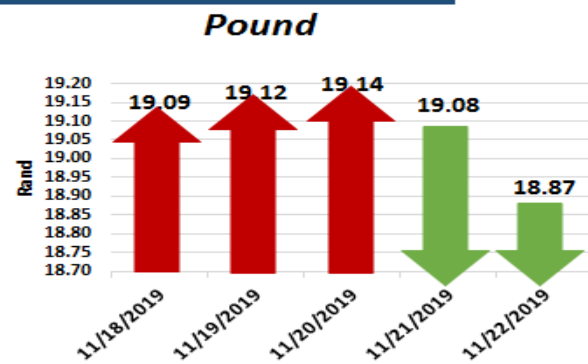
REPO RATE

6.5% y/y
Sep'19

Source: South African Reserve Bank, 2019

RAND/DOLLAR/POUND EXCHANGE RATE





Source: SARB, 15:00, 22 Nov '19

COMMODITIES

BRENT CRUDE OIL PER BARREL	GOLD PER OUNCE	PLATINUM PER OUNCE
$63.85 22 Nov'19	$1 468.30 22 Nov'19	$908.74 22 Nov'19
$61.91 15 Nov'19	**$1 467.45 15 Nov'19**	**$880.89 15 Nov'19**

Source: Trading Economics, 15:00, 22 Nov'19

Chief Content Editor: Motlatjo Moholwa

Content Editor: Bokang Vumbukani-Lepolesa

Contributors:

Motshidisi Mokoena, Mmalehlohonolo Sekoaila,
Makhanana Malungane, Khanya Fakude, Rendani Siwada