

SOUTH AFRICAN CHAMBER OF COMMERCE AND INDUSTRY

Business Confidence Index

October 2016



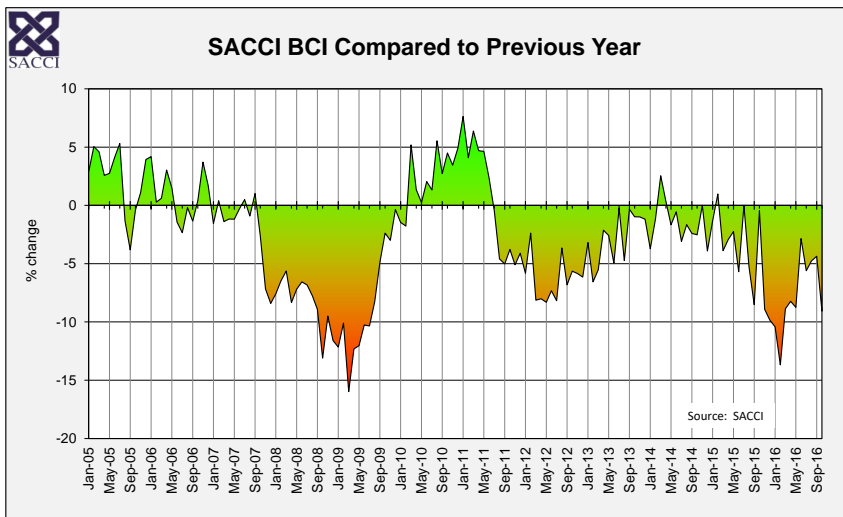
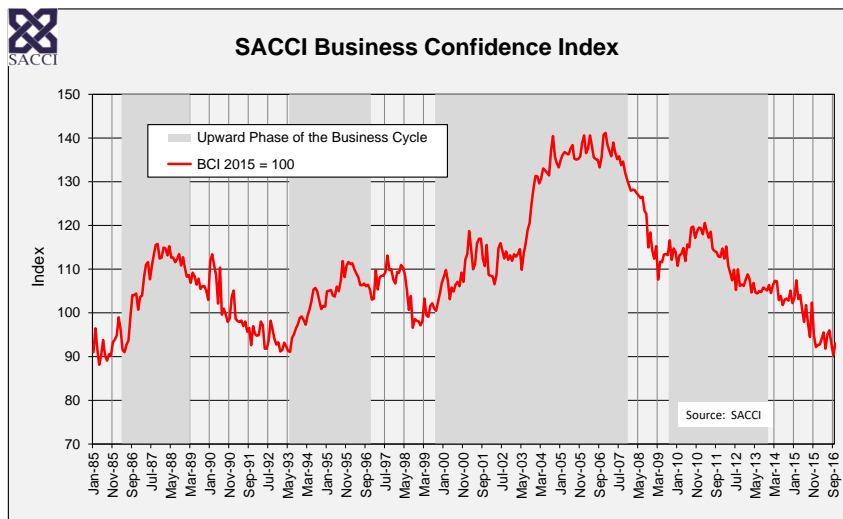
Content:

- **The SACCI Business Confidence Index (BCI)**
- **This Month's BCI Results**
- **Impact of Sub-indices on the SACCI BCI**
- **Economic Commentary**
- **General Economic Indicators**

Because of information lags and changes in expectations, the dynamics of the business mood, at times, may 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	2009	2010	2011	2012	2013	2014	2015	2016
January	112.4	110.8	119.4	112.4	108.8	104.5	103.4	92.6
February	115.3	113.2	118.0	115.2	107.7	106.4	107.4	92.7
March	107.6	113.5	120.6	110.8	104.7	107.3	103.2	94.0
April	111.7	114.8	118.7	109.2	106.9	107.2	104.1	95.5
May	111.6	111.8	117.2	107.4	104.7	102.9	100.6	91.8
June	113.3	115.7	118.5	109.9	104.4	103.8	97.9	95.1
July	113.5	115.0	114.6	105.2	105.0	101.8	101.8	96.0
August	113.2	119.5	114.2	110.0	104.8	103.0	97.6	92.9
September	116.6	119.8	113.9	106.2	105.8	103.3	94.5	90.3
October	112.1	117.2	112.9	106.5	105.5	102.8	102.3	93.0
November	114.7	118.7	112.8	106.2	105.1	105.1	95.1	
December	113.9	119.5	114.7	107.7	106.4	102.2	92.2	
Average	113.0	115.8	116.3	108.9	105.8	104.2	100.0	



This Month's BCI Results

The Business Confidence Index (BCI) of SACCI increased by 2.7 index points in October 2016 to register 93.0 compared to 90.3 in September 2016. This BCI number is 9.3 points below the October 2015, but the October 2015 was an upward outlier from the general downward trend of the BCI in 2015. Since December 2015, the BCI moved sideways but became more unpredictable.

After recovering relatively well up to July 2016 (when the BCI reached 96.0), the BCI contracted to 90.3 in September 2016. The recovery in the BCI in October 2016 was against the odds of slow domestic and global economic performance and local socio-political distractions that adversely influenced the business climate. The volatility in the business climate had a notable negative effect since the end of 2015. The consequence was that the BCI averaged 93.3 since December 2015 to October 2016 compared to 101.3 over the eleven months to October 2015 – down by 8.0 index points.

The more transparent and enlightened atmosphere that followed the local government elections in the beginning of August 2016 was followed by allegations early October 2016 against the Minister of Finance. This created renewed uncertainty in the business environment with adverse market and business reaction. Although this had a bearing on the business mood, business showed resolve and remained resilient.

Overall, the BCI sub-indices were more positive in October 2016 than in September 2016. Three more sub-indices made a positive contribution in October 2016 than in September 2016. Seven sub-indices contributed positively month-on-month (m/m) to the BCI in October 2016 and one remained unchanged. Positive monthly contributions to the BCI mainly came from merchandise export volumes, the rand exchange rate, merchandise import volumes and real retail trade. The largest negative impact on the BCI came from the dollar price of gold and platinum, energy supply and share prices on the JSE.

The real business environment performed slightly better in October 2016 if compared to September 2016. In October, four of the seven of the real business sub-indices improved and one remained unchanged. The m/m financial climate improved as three of the six financial sub-indices improved on the September levels while during September none of the six financial sub-indices improved on their August 2016 readings.

The annual BCI sub-index comparison between October 2016 and October 2015 still reflect no change of the tight business climate as the majority of the sub-indices (10 of 13) recorded below last year's October levels - (see box on page 4). No real activity sub-index was positive year-on-year (y/y) in October 2016. However, two of the six financial sub-indices made positive y/y impacts on the BCI in October 2016 and one remained unchanged.

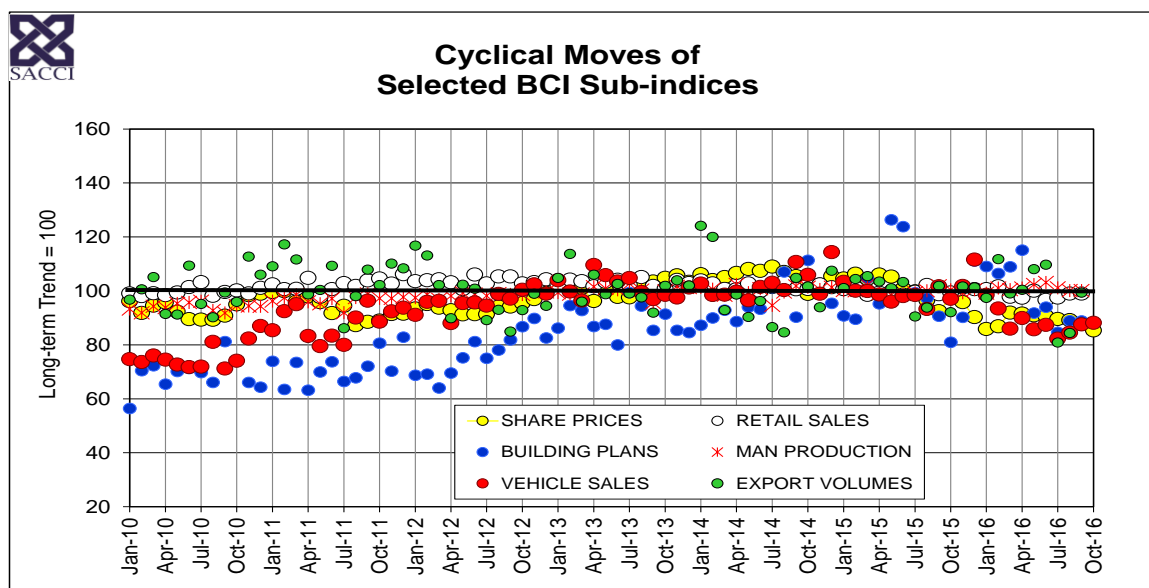
The largest negative y/y contributions to the BCI in October 2016 came from lower merchandise import volumes, lower share prices, lower merchandise export volumes and more expensive energy supply. The real business environment was under more pressure than a year ago. Financial conditions were less restrictive on the business climate than a year ago; with positive y/y impacts on the business climate came from the US dollar price of gold and platinum, and the rand exchange rate.

Impact of the 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	-	-	-	+
Exports	+	+	-	-
Imports	+	+	-	-
Vehicle sales	0	+	-	-
Retail sales	+	+	-	-
Construction - buildings	+	-	-	-
Inflation ¹	+	0	-	-
Share prices	-	-	-	-
Real private sector borrowing	+	-	0	-
Real financing cost	-	0	-	-
Precious metal prices	-	-	+	+
Rand exchange rate	+	-	+	-

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

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



Economic Commentary

Resilient Businesses in Adverse Circumstances

The stabilisation and reinvigoration of the South African economy calls for an active phased process that has been initiated by the Minister of Finance. Apart from subdued economic global growth, the South African economy has virtually stalled. As a first step in the recuperating process, the Medium Term Budget Policy Statement (MTBPS) provided a framework for the tough road ahead for the South African economy. The Minister of Finance, in his speech delivered in Parliament on the 26th of October 2016, held up a solemn picture of South Africa's economy over the medium-term. Apart from lower growth of 0.5% for 2016, the Minister indicated that there are serious impediments holding back the economy.

Notwithstanding political differences between and within certain political formations, the lack of business and investor confidence is amongst the most contemporary matters to deal with. The lack of political direction, economic policy uncertainty and some serious public sector malpractices must be dealt with speedily.

The MTBPS indicated that real engagements would have to be taken, to get the economy back on track. Economic growth does not only depend on a single event like the MTBPS, but there is logical other policy steps that must complement and enhance the economy and entices private sector activity of a lasting nature. Such steps must provide the economy with the momentum to grow, create wealth, provide returns on capital and create employment. The absence of these technical economic necessities is impeding the economy.

Need for Politically Stable Business Environment

Political stability is a prerequisite for economic progress. The economy and South Africa in general are confronted by many challenges and uncertainties. There must be a notable interaction and reiteration process between participants within the economy. The MTBPS provides a framework for the public sector to weigh priorities and give an indication to what extent the state could adhere and afford collective needs.

A major role of the MTBPS is to become aware of the confines the economy provides to reach goals and create economic growth and job opportunities. It is imperative that the iterative process of politics and the economy must take place where the latest MTBPS succeeded in bringing home current limitations of government and prepare the economy, as a first step, for future economic performance and job creation.

Preparing for the Rating Agencies

One of the most prominent criteria for South Africa is to improve economic growth on a sustainable basis in order to address the fiscal dilemma and balance of payments matters that affect South Africa's credit rating. An investment downgrade to junk status could make the process of economic recovery more cumbersome and costly.

In June 2016, Standard & Poor's downgraded South Africa's sovereign foreign currency rating to BBB minus with a stable outlook - one level above the non-investment grade. Fitch Ratings dropped its ratings outlook to negative and retained its BBB rating. In July 2016, Moody's warned that its Baa1 rating for South Africa was at risk of a downgrade.

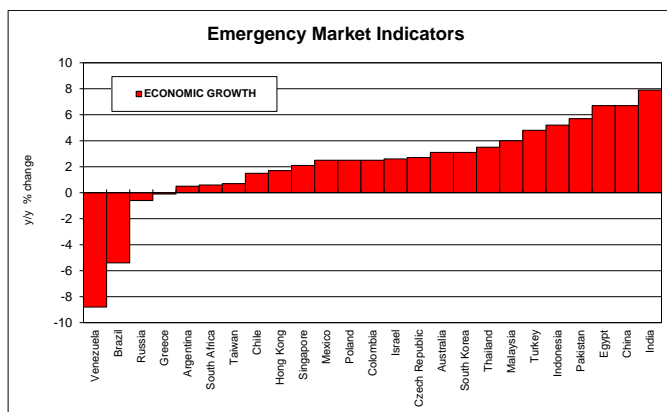
The downgrades were driven mainly by slowing GDP growth, which makes South Africa more vulnerable to capital outflows, rand depreciation, and rising budget and current account deficits. Junk status could sharply increase foreign borrowing costs for the government and private sector, discourage investment, force large bond sales by foreign investors given stringent investment criteria for fund managers. It is not clear to what degree financial markets have factored in rating probabilities

A Case for the South African Economy

Prior to delivering the MTBPS, the Treasury and a business contingent visited foreign investors putting forward the proposition that South Africa will attend to the matters referred to by the rating agencies. The MTBPS was the confirmation by the government that fiscal discipline and public sector financial management enjoy the necessary attention. This indicates at least that an unexpected weakening in conditions would be necessary before being downgraded to non-investment (junk) status.

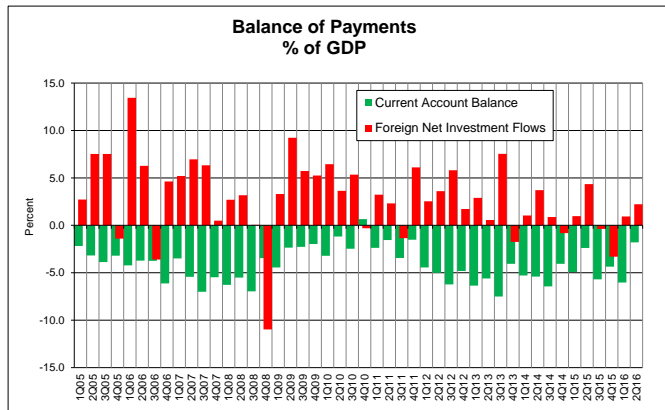
However, investors do not only rely on the scrutiny of only one rating agency. Investors may differ but usually two of the three major agencies need to give a non-investment rating before the borrower would be regarded to have “junk” status.

The three main reasons for an increasingly negative assessment of South Africa are prolonged weak economic growth, rising cost of serving growing government debt, and protracted current account deficits.



GDP growth - This is South Africa’s weakest and most crucial performance indicator. It is one of the slowest growth rates among emerging markets. This implies lower government revenue, higher fiscal deficits, infirm investment spending and infrastructure creation, causing rising social and political tensions that again cause feeble economic growth. At present South Africa finds itself in such a destructive causal relationship. This is a noticeable reason why the business and investment climate worsened. The ability of the current administration to implement the necessary labour or other economic reforms is seen as a downside risk.

Government debt: Relative little of South Africa’s government debt (approximately 11%) is in foreign currency. However, pressures are mounting on the government’s budget deficit targets (as tax receipts were likely to fall and spending pressures to mount), while total government debt had been rising. The MTBPS is a sincere effort to change direction of the debt servicing risk.



Current account balance: South Africa’s current account deficit of the balance of payments (BoP) appears to be chronic despite improving lately. If the deficit is to remain at 4% to 5.5% of GDP, it could be a substantial risk element. However, the deficit declined to 1.8% of GDP in the 2nd quarter of 2016 and might have improved even further in the 3rd quarter of 2016 due to weak growth and low fixed investment spending. The cumulative trade account deficit (merchandise trade) of the BoP improved from R115 billion in the first nine months of 2015 to R89 billion in the first nine months of 2016.

Inflation contained: Although inflation is anticipated to exceed the upper limit of the inflation target range over the medium term, the Reserve Bank’s timely action on interest rate policy contained the inflationary process. The current inflation is largely fuelled by exogenous factors. The restricted inflation lowers the risk for a downgrade.

Conclusion

Much hinges on economic growth over the next two to three years. Should the GDP growth outlook remain weak, South Africa could be downgraded by the ratings agencies for a lengthy period. The effort by the Minister of Finance to prevent a downgrade in December 2016 should be commended. The imperative to lift economic growth is also a precursor for business confidence to translate into investor confidence.

South Africa may not be on the edge of a sudden drop to junk status. The MTBPS, if fittingly implemented, is the first shield to prevent a further downgrade.

General Economic Indicators

Indicator	Period	Direction	Latest	Previous	2015	2010
Consumer inflation headline urban (%)	Sep-16	▲	6.1	5.9	4.6	4.3
Consumer inflation urban - excl. food, bev. & fuel (%)	Sep-16	▼	5.7	5.8	5.7	4.6
Money supply M3 eop (% Δ Y-o-Y)	Sep-16	▲	5.6	5.5	10.5	6.9
Private sector credit eop (% Δ Y-o-Y)	Sep-16	▲	7.2	6.2	10.2	5.5
Real prime overdraft rate eop (%)*	Sep-16	▲	4.5	4.4	3.8	4.2
Liquidations number sa	Sep-16	▼	159	171	1962	3992
Bond yield 5-10y govt eop (%)	Oct-16	▲	8.40	8.31	8.82	7.41
R / US\$ average	Oct-16	▼	13.91	14.06	13.02	7.32
R / Euro average	Oct-16	▼	15.33	15.80	14.14	9.71
Prime overdraft rate eop (%)	Oct-16	▶	10.50	10.50	9.75	9.00
Indicator	Date	Direction	Latest	Previous	2015	2010
Income & wealth tax / GDP (%) saar	q2-16	▲	16.7	15.3	15.1	14.2
Total tax / GDP (%) saar	q2-16	▲	29.7	28.9	28.1	25.4
Public sector borrowing requirement / GDP (%)	q2-16	▲	4.8	3.1	5.0	5.0
Public sector expenditure / GDP (%)	q2-16	▼	28.3	28.7	28.3	27.1
Budget Balance / GDP (%)	q2-16	▼	-2.8	-3.2	-4.5	-4.6
Imports / GDE (%)	q2-16	▲	31.2	31.0	31.4	27.7
Exports / GDP (%)	q2-16	▲	31.7	30.2	30.7	28.6
Net foreign investment flows / GDP (%)	q2-16	▲	2.2	0.5	0.4	3.8
Current account balance / GDP (%)	q2-16	▼	-1.8	-5.8	-4.3	-1.5
Gross domestic saving / GDP (%) saar	q2-16	▲	16.5	14.9	16.4	18.0
Gross capital formation / GDP (%) saar	q2-16	▼	19.7	20.2	20.7	19.5
Net fixed capital formation / GDP (%)	q2-16	▲	-	-	6.6	6.1
GDP growth (% Δ Y-o-Y)	q2-16	▲	0.6	-0.1	1.3	3.0

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