STATE OF THE **SA BUSINESS CYCLE**

3rd Quarter 2023 15 October 2023

NAVIGATE THE BUSINESS CYCLE WITH CONFIDENCE

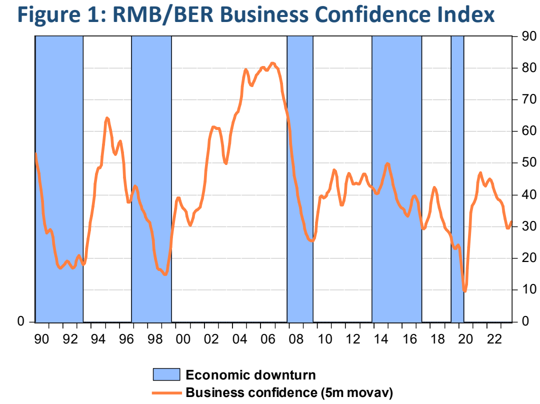
With a solid understanding of the country's economic history and by applying the appropriate econometric techniques, Business Cycle Analytics is a provider of reliable real time and forward-looking information on the domestic business cycle

REPRIEVE IN LOADSHEDDING ASSISTS SUPPLY SIDE OF ECONOMY, 23Q2

On the supply-side, SA economic growth is constrained owing to infrastructure constraints and socio-political pressures, particularly in the run-up the next year's national elections. **Real GDP growth surprised on the positive side during 23Q2**; compared to the weak first quarter, real growth of 0.6% was registered. Growth was driven by a rebound in the tradable goods sectors, with agriculture (up 4.2%), manufacturing (2.2%) and mining (1.3%) registering strong growth.

The easing in electricity supply aided these sectors, more exposed to loadshedding. Water- and electricity production contracted by only 0.8%, but year-on-year, the sector is still down 6.3%. Another growth factor, **is the investment in renewable energy**, assisting a sustained bottoming-out in the construction sector, also being evident in private fixed investment. Combined with public sector investment, **real gross domestic fixed investment grew by 3.9%**.

Figure 1: RMB/BER Business Confidence Index



Source: BCA

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The demand side of the economy is on a weakening trajectory, **albeit that a measure of resilience remains**. Retail, wholesale, and accommodation real value add contracted by 0.4% and is down 0.8% (year-on-year). The pressure on the consumer sector is also reflected in the modest growth of the services sectors. Financial & business services sector and personal services value add were both up 0.7%, with only modest growth year-on-year.

Government real value add was also up 0.6% and 0.7% (year-on-year). Government consumption jumped by 1.7% and is up 2.8% (year-on-year). This spending provides countervailing growth and adds to resilience in domestic expenditure. **Household budgets are under severe pressure owing to high interest rates, a serious lack of job creation and high uncertainty**.

While the broadest measure of demand, real domestic expenditure, registered strong growth of 1.4% (and 2.6% year-on-year), most of this spending was imported. Real imports jumped by 3.3% and were up 7.6% (year-on-year). Despite the more competitive rand exchange rate, real exports remained under pressure, expanding by a modest 0.9%.

Third quarter economic indicators confirm that the consumer-facing sectors remain under pressure. Public spending and the easing of inflation are sources of sustained resilience, despite the moderate weakening trajectory. Retail and wholesale volumes continued to weaken into July.

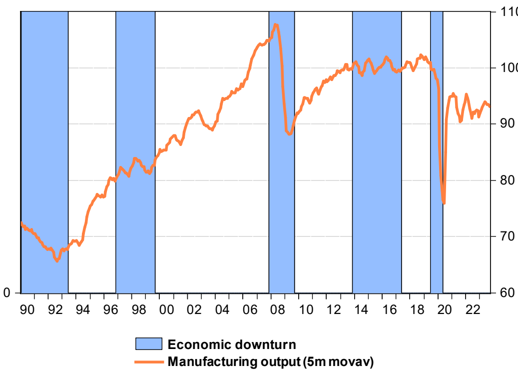
While business confidence did recover in these sectors, this was mainly owing to improved profitability being driven by the easing of purchasing prices. Durable goods and new vehicle dealers, and in the wholesale sector, consumer goods firms continue to struggle.

The business cycle[1]

World economic forecasts are being scaled down. The EU and UK economies appear to be heading for recession and as noted, possibly the US. China's trend growth is slowing to a more sustainable pace. On the positive side, it appears that the Japanese economy has been successfully reflated, with real growth recovering. Developing countries are under pressure from the tight financial environment as well as the strong US dollar, **weighing on fx-denominated debt**.

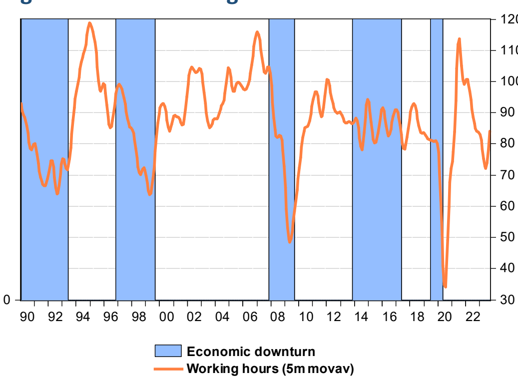
Global industrial production as reflected in composite PMI indicators is in negative territory. Sticky inflation in the leading industrial countries causes interest rates to stay higher for longer. Consumers are therefore under pressure, reflected in falling sentiment levels, which also contains an element of uncertainty. **US dollar strength is likely to persist until a pivot in US interest rates is signalled**. Depending on how contained such a development will be the economic outcome will be determined.

Figure 2: MNF production volume



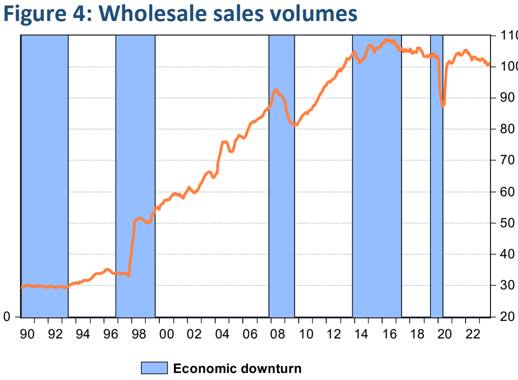
Source: BCA

Figure 3: MNF working hours



Source: BCA

Figure 4: Wholesale sales volumes



Source: BCA

[1] BCA hereby wishes to acknowledge that the recession-dating algorithm was designed and developed at the BER, Stellenbosch University.

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Overall business confidence rebounded by six index points, with the RMB/BER Business Confidence Index jumping to a level of 33. Export growth improved as the agriculture, mining and manufacturing sectors benefited from the ease in load shedding during 23Q3 and the depreciation of the rand exchange rate **improved international competitiveness.**

A two-thirds net majority of business survey respondents remain unsatisfied with general business conditions. The problems in Western Cape and KZN transport also affected economic activity.

The BER's recession-dating algorithm confirms the weakening, yet resilient, tendency on the demand side of the economy. Some components indicate a tentative peak in economic activity shaping during the second half of 2021/ early-2022.

The outlook is for a sustained easing in core inflation and hopefully interest rates have peaked. **The outlook remains challenging and highly uncertain**.

THE US ECONOMY MAY ALSO BE HEADING FOR RECESSION

Viewed from a **purely cyclical perspective**, the US economy may be heading for a recession, despite the headline news of sustained strong growth. Second quarter now-casts for 23Q3 growth are strong, but key economic indicators and macro forces **suggest the underlying momentum is weakening**.

The yield curve is in deep inverted territory (and has predicted each recession from the early-1980s); the cyclical momentum of GDP turned sharply downward, 23Q2; real manufacturing volumes are flat; retail sales volumes are down (chart), in line with the decline in consumer confidence; real M2 money supply growth is in negative territory; housing price increases have come to a standstill; while lower inflation has boosted real personal disposable income, this key indicator of the US economy has merely bottomed-out.

High real interest rates, contracting real banking credit and the burden of **high fiscal deficits and rising debt are all driving the weakening momentum.** Non-farm payroll employment growth is still positive and continues to underpin the economy. Year-on-year growth has receded though, and it must be pointed out that employment is always a lagging indicator.

Lower inflation ahead should ease the pressure in interest rates. The US economy is resilient and financial markets benefit from investment in the AI sector. **A recession may be on the cards but may prove to be brief/ mild.** This is absenting from the geo-political developments.

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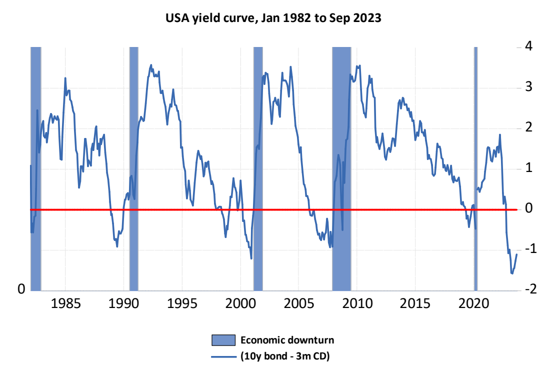
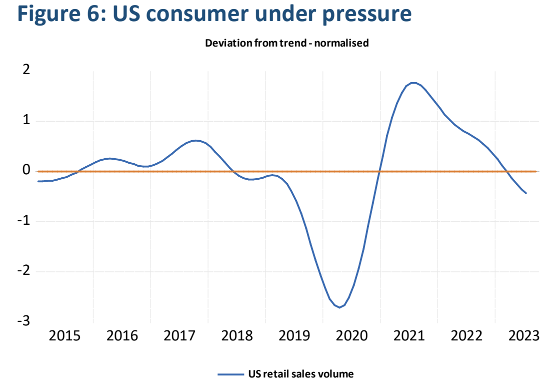
Figure 5: Deeply inverted US yield curve



Source: FRED database

Figure 6: US consumer under pressure



Source: FRED Database

"When you adopt a cyclical worldview, your outlook will be in the minority whenever the chance of an economic turning point is high".

Achuthan & Banerji

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