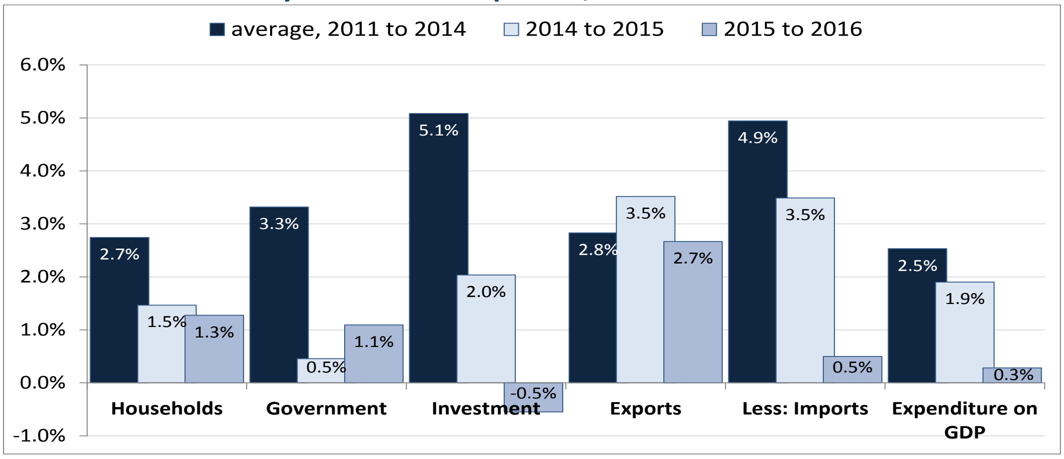
Behind the trends

Exports were the main driver of the surge in growth in the GDP in the second quarter of 2016, largely thanks to the auto industry. Critical for export growth was the persistence of relatively competitive exchange rates as well as some recovery in the US and Europe in the past year. While welcome, these developments emerged in the context of fairly gloomy prospects for growth in the medium term.

The main driver of growth in the past quarter was the recovery in the balance of trade on the back of a rapid increase in exports and a slowdown in imports. In contrast, investment declined and government spending remained virtually unchanged. These developments reflected the trends over the past two years, as Graph 14 shows.

Graph 14: Change in components of expenditure on the GDP, year to second quarter, 2011 to 2016

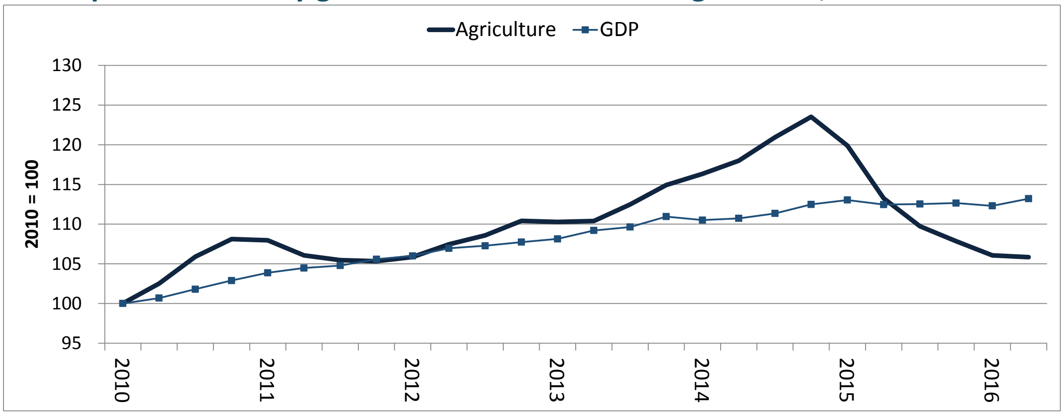


Source: Calculated from Statistics South Africa. GDP P0441 - Q2 2016. Worksheet QRU. Excel spreadsheet. Downloaded from www.statssa.gov.za in September 2016

Despite the relatively strong growth in the rest of the economy in the second quarter, agriculture posted its sixth consecutive quarter of economic decline. Statistics South Africa reported that in seasonally adjusted terms agriculture contracted by almost 15% from R78 billion in the fourth quarter of 2014 to R66 billion in the second quarter of 2016 (Graph 15).

A more detailed assessment of the impact of the drought and strategies to address it can be found in the additional briefing note.

Graph 15: Quarterly growth in total GDP and in agriculture, 2014 to 2016

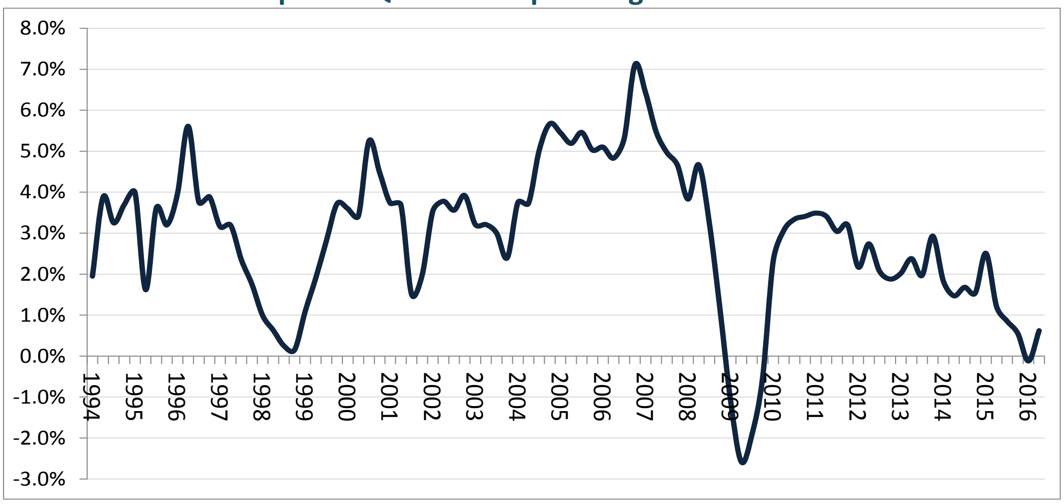


Source: Calculated from Statistics South Africa. Gross Domestic Product (Quarterly)(2016Q2). Excel spreadsheet downloaded in September 2016.

Despite the second quarter's growth, South Africa now finds itself in the most prolonged slowdown since 1994, as Graph 16 shows.

The sharp fall in growth since around 2013 mirrors international trends, especially in the upper-middle-income economies. From this standpoint, the question is whether the current uptick reflects a stabilisation in the slowdown, as producers adapt to the new realities with the end of the commodity boom, or a short-term improvement that does not herald a sustained recovery.

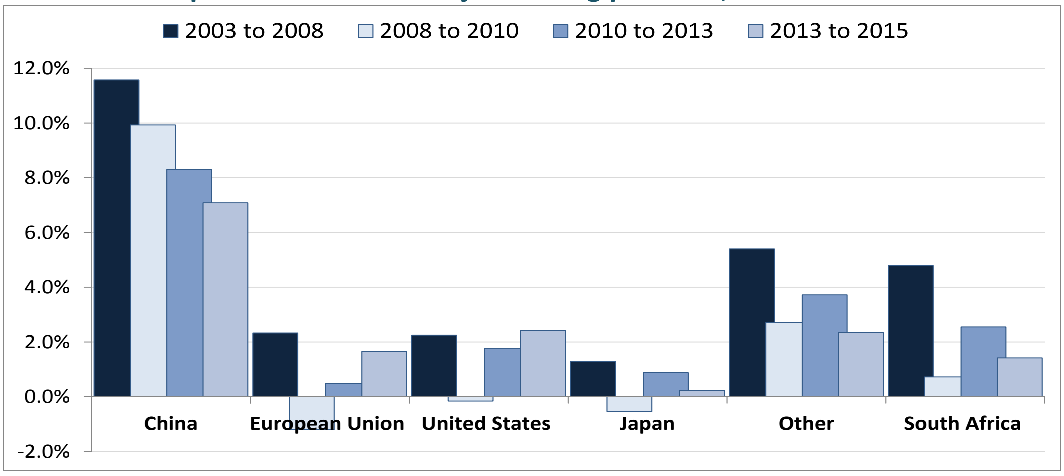
Graph 16: Quarter-to-quarter growth in GDP



Source: Statistics South Africa. Electronic database. Series on GDP growth. Downloaded from www.statssa.gov.za in September 2016.

South Africa's growth has mainly followed global trends, with a sharp slowdown in China from 2011 on top of sluggish growth in the global North since the 2008/2009 financial crisis. In Graph 17, the figures for China likely overstate the level of growth, but the trends are generally considered reliable.

Graph 17: Growth in major trading partners, 2003 to 2015



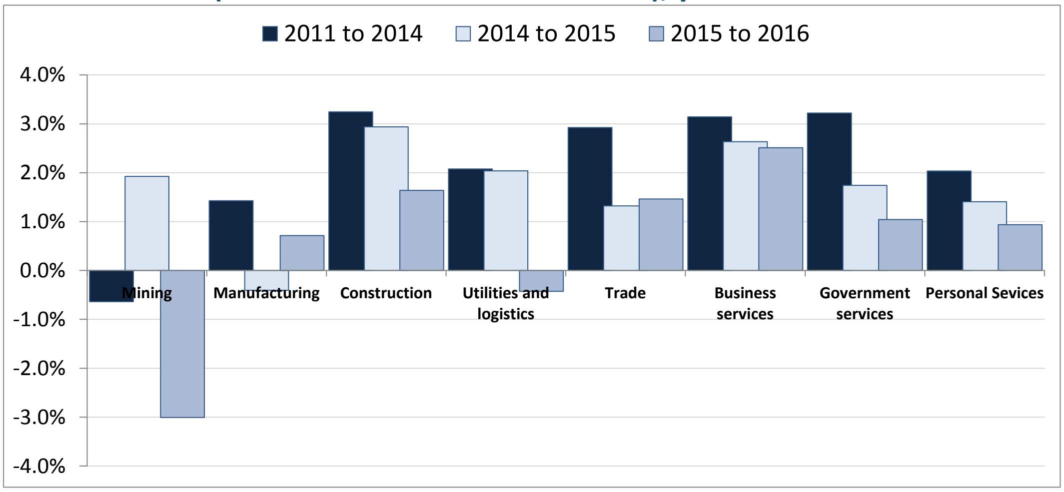
Source: Calculated from World Bank. World Development Indicators. Electronic database. Series on GDP growth. Downloaded from www.worldbank.org in August 2016.

In broad terms, the impact of the global and national slowdown can be summarised as follows:

- The mining value chain is most sharply affected. Besides the mines, which have seen falling employment and investment, this affects the makers of iron and steel and the ferro alloys and aluminium refineries as well as producers of capital equipment. These industries also depend heavily on electricity, so from 2008 they suffered more than the rest of the economy from the rapid increase in the electricity price combined with its rationing.
- Construction and government services expanded relatively rapidly from 2010, reflecting in large part efforts to sustain public spending, especially on infrastructure, after the global financial crisis. If the slowdown in public investment in the past year persists, construction growth will likely decline, while government services have already seen a slowdown.
- Within manufacturing, auto sales grew relatively rapidly, thanks in part to tax subsidies that attracted substantial new investments as well as the effects of the currency depreciation. Consumer goods and services excluding clothing also saw relatively robust growth. The chemicals value chain expanded too, presumably in part thanks to the fall in petroleum and coal prices.

Graph 18 shows growth by sector outside of agriculture in the year to June. Every sector has seen slower growth in the past two years, although manufacturing output improved in the year to June compared to the previous year. In contrast, mining and logistics shrank. Growth in government services slowed sharply as fiscal policy became more restrictive.

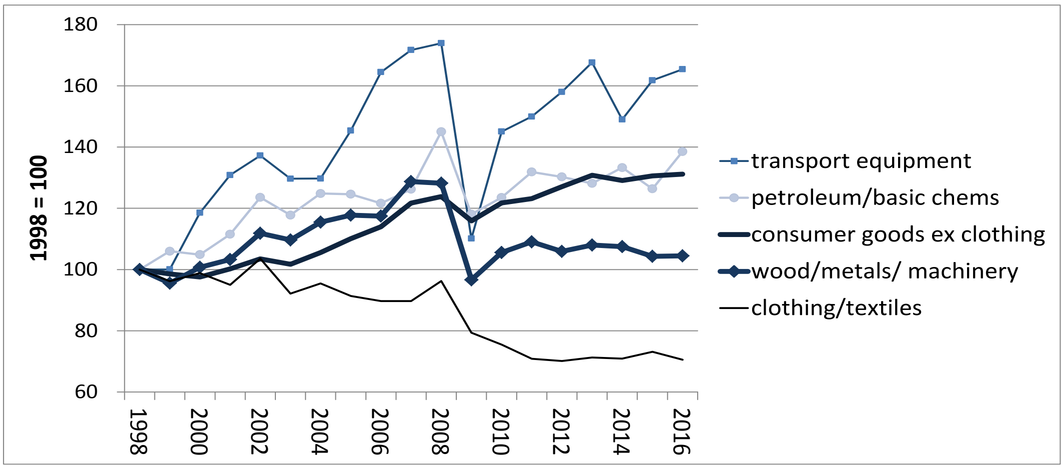
Graph 18: Growth by sector, 2011 to 2016 (share of GDP in 2016 in brackets), year to June



Source: Calculated from, Statistics South Africa. Gross Domestic Product (Quarterly)(2016Q2). Series on GDP in constant rand. Downloaded from www.statssa.gov.za in September 2016.

Within manufacturing, growth rates diverged for capital and consumer goods (Graph 19).

Graph 19: Growth in volume of production in manufacturing, 1998 to 2016 (1998=2016)



Note: Growth rates calculated using average change in volume of production from March to May for each year. Indices for volume of production for industries within groupings weighted by share in sales of the grouping in the relevant year. Source: Calculated from Statistics South Africa. Manufacturing production and sales from 1998. Excel spreadsheet. Series on actual sales and volume of production. Downloaded from www.statssa.gov.za in August 2016.

The relative resilience of the consumer goods and services industries can be attributed to a variety of factors.

- First, these industries generally see net benefits from currency depreciation since they use more local inputs rather than imports. As a result, the decline in the value of the rand would make them more competitive on both domestic and foreign markets.

- Second, government spending has tended to favour lower income households, in turn increasing their consumption over time. This group is more likely to buy local if the exchange rate is competitive. In contrast, the richest decile of households, which accounts for around half of domestic consumption, is more likely to acquire imported luxuries for which there are no local substitutes, including cars, electronics and luxury brands.
- Third, although growth in the region has slowed compared to the period before 2008/2009, it remains stronger than in much of the world. Southern Africa accounts for over half of South Africa's exports of consumer goods, but only a small share of commodity exports.