

The health of the economy

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Recent economic publications have provided an indication of the health of the South African economy. While showing an improvement there are concerns as to whether we can sustain our current economic growth.

GDP and manufacturing growth slow but healthy

StatsSA released GDP figures that showed a robust acceleration in economic growth from a healthy 4.5% in Q4 2010 to 4.8% in Q1 of 2011. Surprisingly, manufacturing was the biggest contributor to growth despite the relatively strong rand. It looks like domestic economic recovery is gaining traction although there are challenges going forward.

The Purchasing Managers Index, which is a good leading indicator of manufacturing activity, has been declining, although it remains above 50 index points which indicates expansion. Also the Reserve Bank's leading indicator, while still pointing towards future economic expansion, has been slowing down which means that in the second half of the year quarterly growth might not be sustained at these levels. Although the International Monetary Fund (IMF) did not cut South Africa's growth forecast for this year it is important to remember that sustained growth for our manufactured exports rely on the strong growth of the economies of our global trading partners.

Consumers continue to spend

The Reserve Bank's quarterly bulletin provided a fairly optimistic picture of the state of consumer fortunes. For a second consecutive quarter, consumer spending increased from 4.8% in Q4 of 2010 to 5.2% in Q1 of 2011.

Not surprisingly, the durable goods component increased strongly in line with the good performance of car sales in the first months of 2011. The tide seems to have turned in subsequent months so it will be interesting to see how this affects growth in overall expenditure in the second quarter of the year.

An increase in disposable income, which happened despite the increase in unemployment over the same period, continues to highlight the point that those consumers with jobs are still able to increase expenditure. Part of the increase in income can be explained by a reasonably strong performance of the equity market. It has been mentioned before in this newsletter, but it bears repeating, with economic growth we need to see an increase in the economy's ability to create jobs; the size of the current labour force and consumers who can independently provide for themselves is too small. Despite the robust growth in consumer spending, its contribution to GDP has declined from 62.7% before the crisis in 2008, to 58.2% in Q1 2011.

Clearly this is an important part of the economy and it will only grow sustainably as job creation improves. The good news is that the latest consumer confidence index indicates that consumers are confident about the future state of the economy and their finances which bodes well for spending.

Debt remains stubbornly high

While consumers have been quite hesitant in acquiring new debt, both as a result of tighter bank lending conditions and their own prudence, the rate at which current debt levels are coming down is not very encouraging. At the prevailing low interest rates, the cost of servicing debt is at historical lows, but the ratio of household debt to disposable income has barely moved from the recent peak of 82% in Q2 of 2008 to 76.8% in Q1 of 2011. This poses a concern about affordability going forward; given the upward trend in inflation, the Reserve Bank might need to increase interest rates in the last quarter of this year or early 2012. This will put further pressure on consumers' debt levels.

Savings takes a knock

It is a matter of concern when South Africans do not save enough. Not only does it disadvantage the individual who does not save, but it has an impact on the wider economy. Part of the money that is needed to pay for machinery, equipment, roads, etc (items that add to South Africa's productive capabilities) comes from the country's saving pool. In case this is not sufficient, money for this "capital expenditure" is obtained through foreigner's investment money that comes into the country. South Africa doesn't want to become dependent on these foreign monies because a change in foreign investors' attitude and perceptions towards South Africa might reverse the trend, cutting off a source of money that we have become dependent on. We would much rather local savings are used to build our economy.

Corporate South Africa remains the core of national saving although the corporate saving rate was marginally down from Q4 2010. This will continue to decrease as companies draw on their savings to expand their businesses.

Disappointingly, household saving as percentage of GDP continued at a low 1.5%. With debt levels remaining high, it's important to reduce these levels because the cost of servicing debt might rise faster than the return on savings in the short run. We need to develop a saving culture rather than a reliance on debt to finance consumption expenditure.

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