Economics Weekly

The key data in review

Date	Country	Release/Event	Period	Act	Prev
June 1	SA	Naamsa vehicle sales (% y/y)	May	2.4	4.1
	US	Nonfarm payrolls (000's)	May	223	159
	US	ISM manufacturing PMI	May	58.7	57.3
	Eurozone	Markit manufacturing PMI	May	55.5	56.2
	UK	Markit / CIPS manufacturing PMI	May	54.4	53.9
June 5	SA	GDP annualized (%)	1Q18	-2.2	3.1
June 7	SA	Manufacturing production (% y/y)	Apr	1.1	-1.6

Financial market indicators

	Close	1 W	1 M	1 Y
All Share	58 391.64	4.0%	0.9%	12.0%
USD/ZAR	12.98	2.2%	3.5%	1.1%
EUR/ZAR	15.33	3.2%	2.6%	6.1%
GBP/ZAR	17.46	3.4%	2.7%	4.9%
Platinum US$/oz	899.69	-0.8%	-1.3%	-4.8%
Gold US$/oz	1 297.18	-0.1%	-1.3%	0.8%
Brent US$/oz	77.32	-0.3%	1.5%	60.9%
SA 10 year bond yield	8.80	2.7%	5.8%	3.9%

Source: Bloomberg

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Highlights

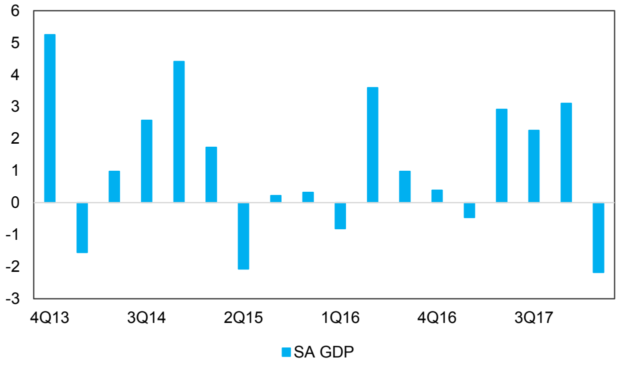
- **SA:** 1Q18 GDP growth disappointed sharply, even against our bearish forecast of -1% q/q. Growth contracted -2.2% q/q and expanded just 0.8% y/y. It was not a great start to the second quarter for the manufacturing sector with April output ring just 1.1% y/y, and down -1.6% y/y on a seasonally adjusted basis.
- **SSA:** Zambia headline inflation accelerated for the third consecutive month printing at 7.8% y/y in May from 7.4% and 7.1% in the two preceding months.
- **Global:** US nonfarm payroll employment rose at a faster 223,000 in May compared to 159,000 the month before. The US ISM manufacturing PMI jumped to 58.7 in May compared to 57.3 the month before. The Eurozone IHS Markit manufacturing PMI slowed to 55.5 in May from 56.2 in April. The UK IHS Markit / CIPS manufacturing PMI climbed to 54.5 in May from 53.9 the previous month.

South African Economy

1Q18 GDP growth disappointed sharply, even against our bearish forecast of -1% q/q. Growth contracted -2.2% q/q and expanded just 0.8% y/y. As expected, the headline number was dragged lower by the mining and manufacturing sectors, which contracted by -9.9% q/q and -6.4% respectively. A -24.2% q/q fall in agriculture output lopped 0.7 percentage points (pps) from growth, while a -3.1% contraction in the trade sector subtracted a further -0.4 pps. The utilities and construction sectors rounded off the misery, contracting -0.5% q/q and -1.9% respectively. While the weakness from the primary and secondary sectors were largely anticipated, the real disappointment came from the trade, catering and accommodation industry, suggesting that household consumption momentum is yet to take hold. Nevertheless, while household consumption expenditure moderated from 3.6% q/q in 4Q17 to 1.5% in 1Q18, the year-on-year momentum remains positive, accelerating to 3.1%. Fixed investment contracted by -3.2% q/q with private sector fixed investment falling by -2.7% q/q, which likely speaks to uncertainty hanging over policy implementation, the mining charter and land expropriation in particular. While the print is certainly disappointing and suggests that full year growth may have to be downwardly revised, we are reluctant to do so for now, for two primary reasons. Firstly, South Africa is not unfamiliar with a poor first quarter GDP number, and has indeed bounced back in the past. Secondly, there were no revisions to the historical data which suggests that this number could well be revised higher in future releases, and GDP revisions have typically been biased to the upside.

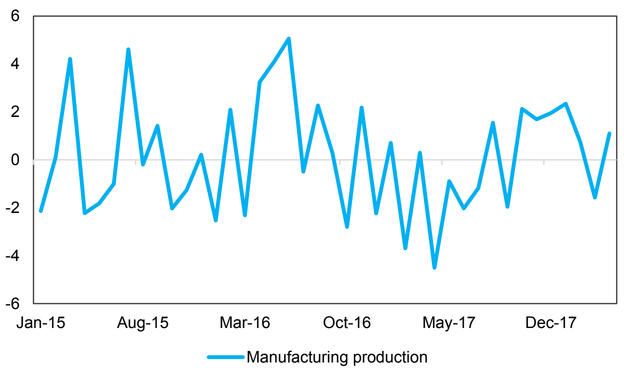
It was not a great start to the second quarter for the **manufacturing** sector with April output rising just 1.1% y/y, and down -1.6% y/y on a seasonally adjusted basis. To some extent, the disappointing number can be attributed to the reweighting of the manufacturing basket, but the sub-par growth trend shows no sign of being reversed. A 4% y/y increase in petroleum, chemical, plastic and rubber production in the month was responsible for a full 1 pps of the headline number, while a 2.6% y/y lift in food and beverage manufacturing accounted for an additional 0.7 pps. This growth was largely offset by a -5.1% y/y decline in wood, paper and pulp output, and a near 20% y/y fall in communication equipment manufacturing. Overall, the weakness was broad-based with few bright spots. Of particular concern was the -1.2% y/y decline in vehicle manufacturing. The situation for this sector could deteriorate further should the luxury vehicle import tariffs mooted by the Trump administration be signed into law. The domestic manufacturing and export sectors have failed to capitalise on relatively strong global growth, and a steady decline in “expected business conditions” in the Absa manufacturing PMI leads us to believe that the manufacturing sector will provide little in the way of growth through 2018.

Figure 1: SA GDP



Sources: Reuters, FNB Economics

Figure 2: Manufacturing production

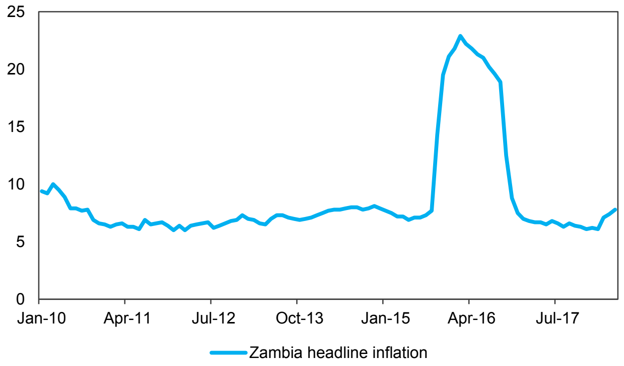


Sources: Reuters, FNB Economics

Sub-Saharan Africa

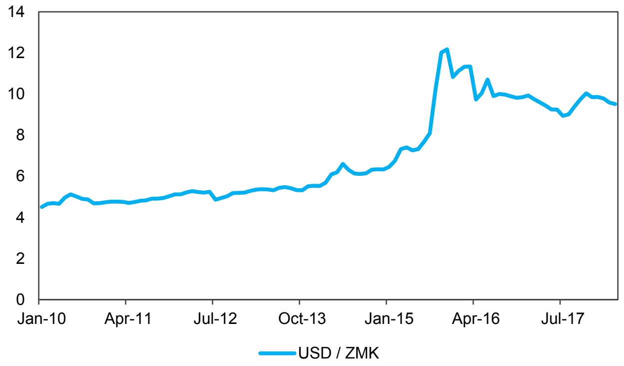
Zambia headline inflation accelerated for the third consecutive month printing at 7.8% y/y in May from 7.4% and 7.1% in the two preceding months. The sudden upturn in the inflation profile since the beginning of the year can largely be ascribed to the resurgence of food inflation amid mild drought conditions and an armyworm outbreak. Accordingly, we believe that this is the end of the bank’s cutting cycle as inflation nears the upper end of the 6-8% inflation target. While the inflation trajectory has lifted in recent months, we do not anticipate that recent adverse agricultural conditions will be enough to destabilise the overall inflation trajectory in the coming year. While risks are certainly tilted to the upside, particularly with higher than expected oil prices, it is reassuring that the Bank of Zambia also expects price pressures to be contained in the foreseeable future. As such, we believe that the Central bank will opt to keep the policy rate on hold for the remainder of the year.

Figure 3: Zambia headline inflation



Sources: Reuters, FNB Economics

Figure 4: USD/ZMK

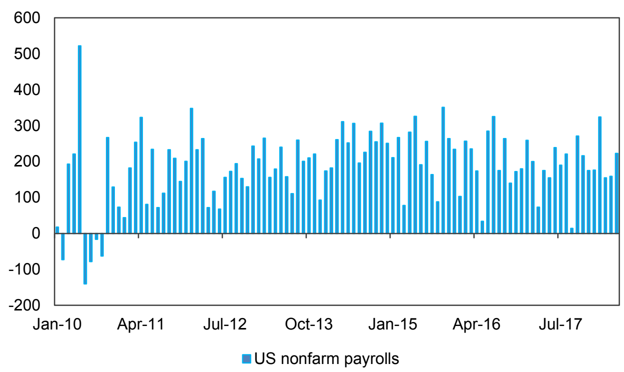


Sources: Reuters, FNB Economics

Global Snapshot

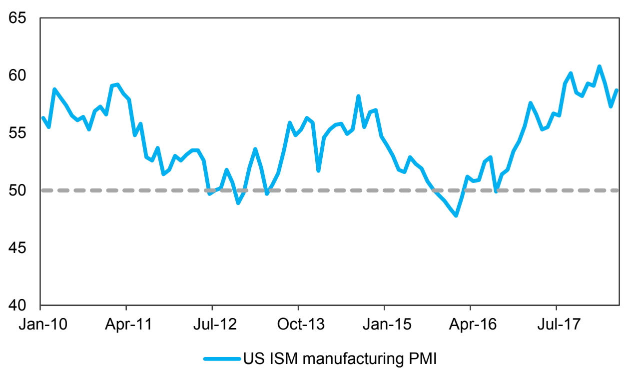
US nonfarm payroll employment rose at a faster 223,000 in May compared to 159,000 the month before and above Bloomberg consensus expectations of 190,000. The education and health services (+39,000), retail trade (+31,100) and construction (+25,000) sectors posted the largest job gains in the month and average hourly earnings remained relatively robust rising 2.7% y/y from 2.6% in April. While the unemployment rate edged down 0.1 percentage point to 3.8%, a near two decade low, so too did the labour force participation rate to 62.7%. Overall, the US continues to display an unwavering level of resilience in the labour market which should embolden the Fed to continue on their path of monetary policy normalisation.

Figure 5: US nonfarm payrolls



Sources: Reuters, FNB Economics

Figure 6: US ISM manufacturing PMI



Sources: Reuters, FNB Economics

The **US ISM manufacturing PMI** jumped to 58.7 in May compared to 57.3 the month before as all subcomponents, barring inventory, climbed even higher. 16 out of the 18 manufacturing industries reported growth in the month with survey respondents remaining relatively upbeat over production prospects. The lingering concern over President Trump's 25% tariff on steel imports, however, has resulted in superfluous price increases in the industry. We reiterate that we do not foresee proposed tariff measures as destabilising to the sectoral outlook as the proportional impact of such actions are relatively small at this stage.

The **Eurozone IHS Markit manufacturing PMI** slowed to 55.5 in May from 56.2 in April as new orders, output, employment and work backlogs lost steam. This registers as the lowest reading in over year providing further evidence of a slowdown in the Eurozone. Among member countries, Italy and Germany recorded 18 and 15 month low readings of 52.7 and 56.9 respectively. As pointed out in the survey, and in line with our expectations, capacity constraints and a relatively strong Euro have diminished export competitiveness and continues to hamper growth in the sector. Worryingly, manufacturing optimism plunged to the lowest level seen in nearly two years raising concerns that our initial expectations of a temporary soft patch in overall economic activity may persist longer than we initially anticipated.

The **UK IHS Markit / CIPS manufacturing PMI** climbed to 54.5 in May from 53.9 the previous month largely on the back of the highest accumulation of inventories in the Markit survey history. This indicates that manufacturers potentially overestimated order expectations providing further evidence of a slowdown in economic activity persisting in 2Q18. We maintain that domestic households will likely opt to replenish severely depleted savings levels which should subdue domestic demand. Accordingly, manufacturing production levels are unlikely to lift meaningfully in the coming months.

The Week Ahead

Retail, business confidence, mining and perhaps Fitch

April retail trade sales and mining production, due out on Wednesday and Thursday respectively, will provide a sense of how each sector started the second quarter of the year. The RMB/BER business confidence index is scheduled for release midweek, while wholesale and motor trade sales, also for April, are due out on Thursday. With Fitch having recently visited the country, there could possibly be a rating review from the agency, although they are not bound by any particular publication date.

Retail trade sales have been pretty robust in the first quarter of the year, but it wasn't enough to avoid a disappointing first quarter GDP contraction. The April print is an important one, not only because it represents the first month of the second quarter, but because it will be the first month to reflect the impact of VAT and fuel price increases on consumers' pockets. We think that these two additional drags on consumption will blunt the momentum in the sector and expect a moderation in March's growth number.

Mining output ended the first quarter on an atrocious note, contracting –8.4% y/y. While we hope that the April number will show a recovery, relatively subdued commodity prices and the impact of US tariffs on Chinese steel imports (and consequently Chinese demand for domestic iron-ore) may well see another monthly contraction. A very low April 2017 base may provide some reprieve.

The RMB/BER business confidence index jumped 11 points to 45 in 1Q18 on the back of a positive market response to the ANC elective conference and a stay of execution from Moody's. Nevertheless, some shine has been taken off the optimism as the reality of undoing a decade of near stagnation sinks in. We think there will be a moderation in business confidence in the 2Q18 reading, but that it will remain above its ten year average of 40.

Finally, Fitch analysts have held various meetings with private and public sector role players in recent weeks, and may well release their mid-year rating review next week, although there is no set publication date. As we did with S&P, we expect no rating change apart from an acknowledgement that the outlook, post the ANC elective conference, has improved.

Data to watch out for this week

Date	County	Release/Event	PPeriod	Survey	Prev
June 12	US	CPI (% y/y)	May	2.7	2.5
June 13	SA	Retail sales (% y/y)	Apr	-	4.8
	SA	RMB / BER business confidence	2Q18	-	45
	US	FOMC rate announcement (%)	June	2	1.75
	Eurozone	Industrial output (% m/m)	Apr	-	0.5
	UK	CPI (% y/y)	May	-	2.4
June 14	SA	Mining production (% y/y)	Apr	-	-8.4
	Eurozone	Refinancing rate (%)	June	0	0

Source: Bloomberg ("Survey" is the consensus forecast)

FNB SA Economic Forecasts

Economic Indicator	2015	2016	2017	2018f	2019f	2020f
Household consumption expenditure %y/y	1.8	0.7	2.2	2.1	2.0	2.1
Government consumption expenditure %y/y	-0.3	1.9	0.6	0.3	0.4	1.1
Gross fixed capital formation %y/y	3.4	-4.1	0.4	0.3	1.1	1.8
Real GDP %y/y	1.3	0.6	1.3	1.9	1.9	1.5
Total exports %y/y	2.8	1	-0.1	2.1	3.0	3.0
Total Imports %y/y	5.4	-3.8	1.9	0.7	2.4	2.5
Current account (% of GDP)	-4.4	-3.3	-2.5	-2.2	-2.5	-2.7
CPI (average) %y/y	4.6	6.3	5.3	4.9	5.1	5.2
CPI (year end) %y/y	5.3	6.7	4.7	5	5.3	5.1
Repo rate (year end) %p.a.	6.25	7.00	6.75	6.5	6.75	7.25
Prime (year end) %p.a.	9.75	10.5	10.25	10	10.25	10.75
USD/ZAR (average)	12.8	14.7	13.3	12.2	12.6	13.2

Source: FNB