



First Quarter 2023 Report

Issued April 2023

Introduction

Knowledge of the future direction of economic variables and the ability to accurately forecast changes in economic activities have been an active pursuit of economics and business research. Researchers believe that the use of sentiment indices (such as the Business Confidence Index (BCI)) and expectations usually produce more predictive results and content for the performance of the economy. This is because these indices represent independent determinants of key macroeconomic variables and reflect the overall state of the economy.

The BCI helps to determine the current economic situation and future direction of commerce, monitors growth in output, and presents an advance warning of turning points in economic activity. The index is computed using data collected from the business community through methodical surveys.

This report presents the Durban BCI for the first quarter of 2023, which is the third BCI constructed using survey data collected from senior private sector managers in eThekweni Municipality. The index ranges from zero to 100, where 100 reflects extreme confidence, 50 stands for neutral views, and 0 indicates extreme lack of confidence. Thus, an index of less than 50 implies lack of confidence in the local economy or a negative business outlook, while an index greater than 50 denotes the reverse (i.e. confidence in the local economy

or a good/positive business outlook). A BCI of 50 represents a neutral stance.

The Durban BCI

The Durban business confidence index (DBCI) slipped from 44.04 in the fourth quarter of 2022 to 43.27 in the first quarter of 2023. This, however, masks substantial differences across industries. For instance, confidence in the manufacturing sector declined by 7.89 index points, from 38.69 in the fourth quarter of 2022 to 30.8 in the first quarter of 2023. This decline is slightly below albeit comparable to the decline of 9 index points in the sector at a national level, from 26 in the fourth quarter of 2022 to 17 in the first quarter of 2023. This is largely ascribed to the ongoing power outages in the country, which have acutely affected sales and production in the manufacturing sector. The uncertainty induced by calls for a 'national shutdown' that was scheduled for 20 March 2023 may have contributed to the plummeting of confidence in the manufacturing firms.

In the electricity sector, confidence unexpectedly rose by 24.91 index points to 30.21 between the fourth quarter of 2022 and the first quarter of 2023. The increase in the index may be explained by the initiatives put forward by the government to deal with the electricity crisis in the country. That is, the declaration of a state of national disaster and appointment of an electricity minister (in response to the severe load shedding in the



**DURBAN CHAMBER
OF COMMERCE AND
INDUSTRY NPC**

country). Although it has improved, the index in the sector, remains significantly below 50, which shows a lack of confidence in the economy by players in the sector. Other factors, such as the increase in electricity tariffs, are also likely to have had a detrimental effect on confidence in this sector.

In the wholesale and retail trade sector, consistent with the national level, confidence declined from 58.72 in the fourth quarter of 2022 to 26.37 in the first quarter of 2023. This reflects the impact of load-shedding which has led to a reduction in operating hours and steep costs of running electricity backup equipment, such as generators.

In addition, the general decline in business confidence in Durban is indicative of the rising cost of living (e.g. food prices) and interest rates coupled with relatively stagnant compensation growth. Confidence in the financial sector in Durban fell sharply from 49.97 in the fourth quarter of 2022 to 37.73 in the first quarter of 2023. It is conjectured that the decline in business confidence in this sector is largely due to tight financial conditions coupled with weak economic growth in the country and globally.

The transport, storage and communication sector, which is deemed as one of the pillars of the KwaZulu-Natal (KZN) province and the City of Durban, experienced an overwhelming rise in confidence between the fourth quarter of 2022 and the first quarter of 2023. It rose by 15.44 index points, from 51.44 in the fourth quarter of 2022 to 66.88 in the first quarter of 2023. Similarly, the construction sector, unlike the RMB/BER national index, witnessed an improvement in confidence. It rose from 33 in the fourth quarter of 2022 to 66.04 in the first quarter of 2023.

Service Delivery

There was no change in the perception of businesspersons on the efficiency of the

authorities on service delivery in the first quarter of 2023. Among the surveyed businesspersons, 78% (as was the case in the fourth quarter of 2022) reported that if they (or anyone else) reported a 'poor service delivery' complaint, it is very unlikely that the authorities would attend to it. This partly explains the marginal change in Durban's BCI (a decline of 0.77 percentage points) in the first quarter of 2023.

The survey respondents also reported that among the services provided by the government in Durban, electricity is the worst followed by environmental management (sewerage, solid waste and parks), roads and public safety (police, fire and ambulance services), in that order, as was the case in the fourth quarter of 2022.

Review of Selected Macroeconomic Indicators

While the economy of KZN is yet to recover completely from the July 2021 unrest and the April 2022 floods and mudslides, there is evidence of progress towards near-full recovery within the foreseeable future. Despite the poor national economic performance and unfavourable external economic conditions (e.g. rising interest rates in the United States of America, Euro bloc and the United Kingdom; a decline in global economic growth (estimated at 2.8% in 2023 from 3.4% in 2022 by the International Monetary Fund); and adverse effects of the war in Ukraine, among others) the KZN economy seems to show elements of resilience and indications that it has gone past an economic trough. Business confidence in the largest Metropolitan Municipality in the province, eThekweni, (Durban BCI) rose significantly from 35.47 in the third quarter of 2022 to 44.04 in the fourth quarter of 2022 before marginally declining to 43.27 in the first quarter of 2023.

While the national economy grew by 1.6% in the third quarter of 2022, the KZN economy



DURBAN CHAMBER
OF COMMERCE AND
INDUSTRY NPC

grew by 2.1% over the same period. The growth recorded in the KZN economy is reflected in the declining trend in the unemployment rate in eThekweni Municipality from 21.8% in the third quarter of 2022 to 17.6% in the fourth quarter of 2022, as reported by the StatsSA's Quarterly Labour Force Survey.

In spite of these positive economic developments in the local economy in KZN generally and eThekweni Municipality, specifically, high inflation and interest rates continue to adversely affect businesses and individuals in the province. Statistics South Africa reports that inflation rose to 7.0% in February 2023, from 6.9% in January 2023. The survey respondents are not optimistic that there will be an improvement in the second quarter of 2023. The survey found that 71.0% of the respondents expect inflation to rise in the second quarter of 2023. Not surprisingly, a large proportion of the respondents (77.4%) expect that interest rates will increase in the second quarter of 2023 as the South African Reserve Bank (SARB) attempts to contain the inflationary pressure.

The current inflation rate remains above the upper limit of the SARB's target range of 3% - 6%. The high inflation has largely been driven by commodity and electricity prices across the country, and constrained supply as a direct consequence of the severe load shedding, among others.

The SARB is forecasting that headline inflation will drop to 5.4% in 2023 from 7% in December 2022. Consistently, they anticipate that the Monetary Policy Committee (MPC) will raise interest rates to achieve the expected declining in the rate of inflation. This will, in turn, hurt most businesses, particularly small enterprises. Presently, about 42% of businesses in the Durban area consider their financial situation tight, and over 50% expect it to remain unchanged in the second quarter

of 2023. The tightness of financial conditions for most businesses, together with the ongoing and worsening power outages, hinder the expansion of most businesses and drive others out of business, consequently constraining the creation of job opportunities and threatening to reverse the gains made in terms of unemployment reduction in the City and the Province. According to Statistics South Africa, unemployment dropped by 4.2 percentage points to 17.6% in the fourth quarter of 2022 from 21.8% in the third quarter of the same year.

Over 30% of the businesses in Durban reported having experienced a decline in their production volumes while over 20% expect this decline to persist to the second quarter of 2023. The decline in production volumes is largely due to the effect that the load-shedding has had on businesses, and especially small businesses that can hardly afford to install backup energy systems. This underscores the need for the government to urgently deal with the ongoing energy crisis, or provide support to small businesses that will insulate or alleviate the impact of load-shedding on their operations.

Over 40% of businesses in the Durban area reported having experienced a decrease in their orders/or sales in the first quarter of 2023 and 23% expect that the orders will continue to decline in the second quarter of the year. The decline in sales is attributed to the rising cost of living in the country.

Following the persistently high inflation rates (see Figure 1), the SARB at its January 2023 MPC meeting raised its benchmark repo rate by 25 bps from 7% in December 2022, and kept the repo rate at 7.25% for the entire first quarter of 2023 (Figure 2). The tight monetary policy (high-interest rates) causes businesses to halt expansions and slows down job creation in the province. It further reduces consumer and business spending, hence, lowering the total value of a company's



DURBAN CHAMBER OF COMMERCE AND INDUSTRY NPC

stock. This in turn slows down the provincial economic growth due to low investment as a result of a high costs of borrowing, leading to an increase in unemployment rates.

Figure 3 presents the exchange rates of the South African rand vis-à-vis the United States dollar (ZAR/USD). The South African rand has weakened against the US dollar reaching R17.00 per US dollar at the beginning of January 2023 and R18.50 in March 2023. This volatility of the Rand reflects the uncertainty in the economy. The severe electricity supply disruptions and the heightened political tension resulting from the release of the Section 89 independent panel report has negatively impacted on the performance of the South African rand/ US dollar exchange rates since the beginning of December 2022. The weakened rand has pass-through effects on the Durban and KZN economy, especially on international trade and input costs of production, as investors are sceptical and worried about their expected rates of return on investments.

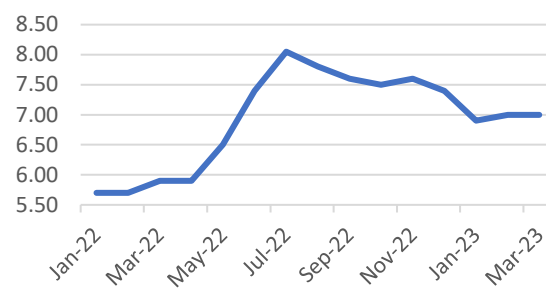
Post Script

The prolonged electricity shortages, water rationing and infrastructural deficit in the province of KwaZulu-Natal continues to be a major setback and have a severely suppressing effect on growth of the KZN economy as well as business mood of the province. The electricity shortage has increased the amount that businesses are paying each month to maintain standard operational levels – whether it be installing solar electricity generation equipment, uninterrupted power supply devices, or heavy-duty diesel generators.

The levels of load shedding increased from 75 days in 2021 to 207 days in 2022, and the figure is expected to increase more than two-fold in 2023 with the more prolonged hours of load shedding being experienced each day.

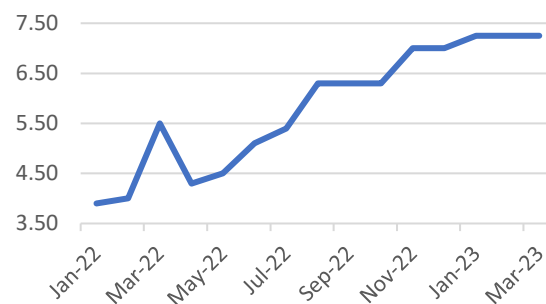
Businesses, both small and large, are spending large amounts of money every month to keep the lights on, consequently increasing their direct costs of production. In addition, inflationary pressures arising from high interest rates, weakening of the rand and high electricity tariffs or power generation costs are adversely affecting Durban’s economy through an increase in the cost of living and investment.

Figure 1: South Africa’s Inflation Rates



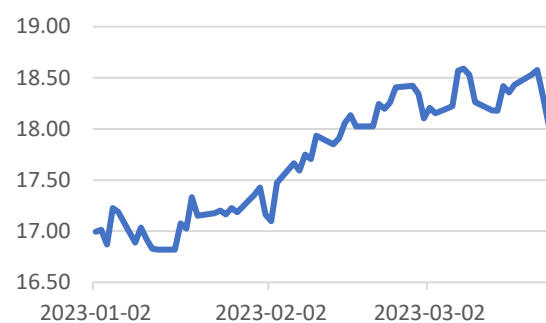
Data Source: Statistics South Africa

Figure 2: South Africa’s REPO rates



Data Source: South African Reserve Bank

Figure 3: ZAR/USD Exchange Rates



Data Source: South African Reserve Bank

Authors: Harold Ngalawa, Ntokozo Nzimande and Adebayo Kutu, Macroeconomics Research Unit, University of Kwa-Zulu-Natal



DURBAN CHAMBER OF COMMERCE AND INDUSTRY NPC