Capacity utilisation: stifled economic activity, on the Covid-19 economic lockdown is increasingly seeing the risk of business failures rise sharply

Tuesday 12 May 2020

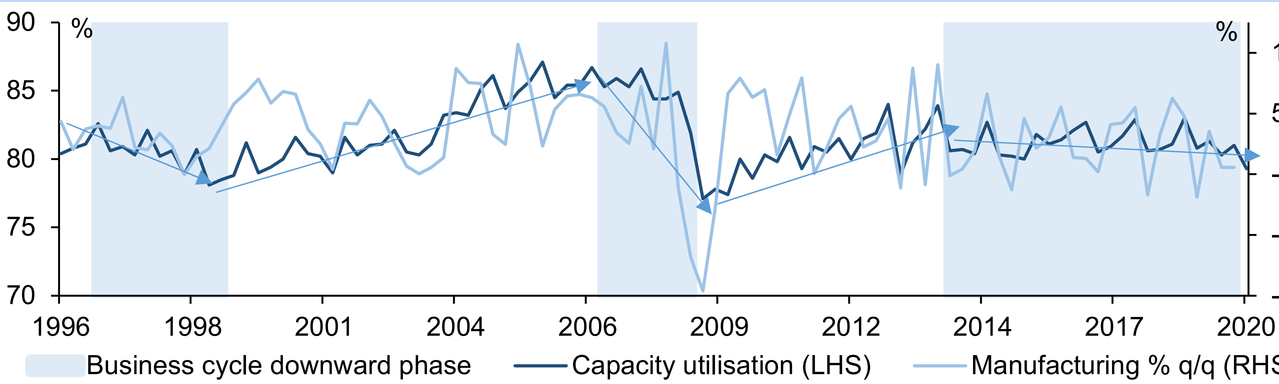
Figure 1: Manufacturing capacity utilisation and underutilization of production (%) - breakdown

	2018			2019				2020
	May	Aug	Nov	Feb	May	Aug	Nov	Feb
Utilisation of production capacity	**80.7**	**81.1**	**83.0**	**80.8**	**81.3**	**80.3**	**80.9**	**79.3**
Underutilisation of productive capacity	19.3	18.9	17.0	19.2	18.7	19.7	19.1	20.7
Shortage of raw materials	2.1	2.0	1.6	1.9	2.2	2.5	2.6	3.1
Shortage of skilled labour	1.0	1.0	0.9	1.0	1.0	1.0	1.1	1.1
Shortage of semi-unskilled labour	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Insufficient demand	11.5	11.7	10.8	12.1	11.7	12.4	11.6	12.7
Other	4.5	4.0	3.5	4.0	3.6	3.6	3.6	3.6

Source: Stats SA

- In February 2020, the manufacturing sector's utilisation of its capacity (data collected every three months) fell to 79.3% of total capacity, from 80.9% in November 2019 in the seasonal run down post the festive period. This does not include the impact of the lockdown, which will be extremely severe.
- The next reading will be for May 2020 (but released in August this year), and will incorporate the brunt of the economic lockdown's impact on the utilisation of manufacturing capacity, with many producers still not operational under level 4, or not yet fully operational in the fight against the spread of Covid-19.
- 54% Of businesses surveyed by Statistics SA in the first two weeks of April already said they will cease to exist before mid-July if the lockdown is not eased substantially further (to a level where they can generate sufficient turnover to avoid closing). Most businesses will have lost incomes needed to pay staff and other costs, resulting in retrenchments rising substantially and firms shutting down permanently.
- The situation is even more dire, as the economic effect of a lengthy lockdown will be geometric, not linear – that is it will cause an increase of cascading negative effects as households and corporates run out of savings and run up debt. The collapse will become bigger as it feeds off itself. The negative impact on the economy will not be as straight forward as simply looking at the impact of one month's worth of lockdown and then multiplying it by five for five months for example. The longer the severe lockdown persists, the quicker the number of business failures will escalate. This applies to unemployment too.
- The longer the severe lockdown lasts, the more rapidly unemployment will escalate, eventually towards 50%, and the less likely it is that jobs will be there when it has ended due to firm closures. Already up to 31% of businesses surveyed may have ceased to exist, as this is the percentage that was surveyed in early April that said they cannot last for more than a month without sufficient turnover.

Figure 2: Capacity utilization in manufacturing production vs growth in manufacturing production



Source: Stats SA

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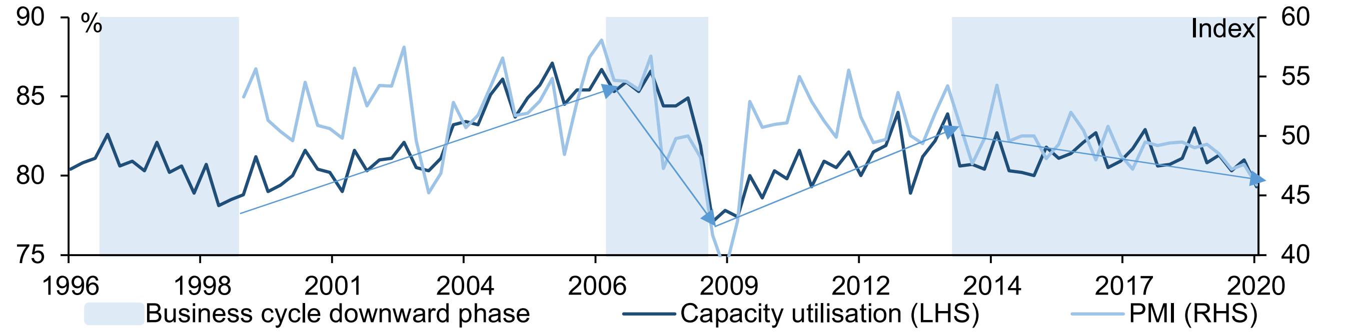
Figure 3: Capacity utilization in manufacturing production vs PMI



Source: Stats SA

- The extreme lockdown we have seen on the South African economy will drive a deep and severe recession in South Africa. We estimate that will now be well in excess of around the -5.0% y/y we estimated in April on the basis, at that time, that SA would move more quickly through its levels of lockdown. A GDP contraction of above 10% y/y for 2020 is instead now quite possible on a lengthy, severe lockdown (one at the high levels of 4 or 5 for most of Q2.20), as many corporates not only temporarily cease activity, but do so permanently. This would clearly also suppress the anticipated recovery in the economy in Q3.20 due to these corporate failures.
- We originally estimated that the contraction in GDP would be -37.1% qqsaa in Q2.20. However, this looks now more likely to be closer to -65% qqsaa in Q2.20 (GDP growth would then be closer to -14.0% for 2020), if not worse, without a quicker opening up as the economy is only at level 4 lockdown and we are approaching the halfway mark of the second quarter, i.e. mid May.
- The very slow, gradual approach South Africa has taken to opening up the economy has already seen a number of key employers go into business rescue. Support has mainly been aimed at SMMEs, but a number of larger corporates (employers) are needing it too. Both the health risks and the economic risks to lives (and livelihoods) are vitally important, and both are likely to be long lasting.

Figure 4: Utilisation of production capacity in the manufacturing industry by division

Manufacturing divisions	Weight	Contribution	% ch y/y
Food and beverages	26.64	80.2	-1.2
Textiles, clothing, leather and footwear	3.12	70.9	-1.2
Wood and wood products, paper, publishing and printing	11.45	80.7	-1.6
Petroleum, chemical products, rubber and plastic products	23.07	82.6	-1.8
Glass and non-metallic mineral products	3.19	77.8	-0.3
Basic iron and steel, non-ferrous metal products, metal products and machinery	18.69	73.5	-3.1
Electrical machinery	1.64	77.7	-1.0
Radio, television and communication apparatus and professional equipment	1.54	79.9	-1.3
Motor vehicles, parts and accessories and other transport equipment	7.57	81.8	-1.2
Furniture and other manufacturing	3.11	80.0	1.6
Total manufacturing	**100**	**79.3**	**-1.5**

Source: Stats SA

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Figure 5: Weights according to manufacturing major groups

	2017-2019 (based on value added for 2015-2017)
Food and beverages	**26.64**
Meat, fish, fruit, etc.	6.69
Dairy products	2.15
Grain mill products	3.37
Other food products	8.14
Beverages	6.29
Textiles, clothing, leather and footwear	**3.12**
Textiles	0.78
Other textile products	0.40
Knitted, crocheted articles	0.09
Wearing apparel	1.04
Leather and leather products	0.46
Footwear	0.35
Wood and wood products, paper, publishing and printing	**11.45**
Sawmilling and planing of wood	1.73
Products of wood	2.57
Paper and paper products	4.14
Publishing	1.43
Printing recorded media	1.58
Petroleum, chemical products, rubber and plastic products	**23.07**
Coke, petroleum products and nuclear fuel	8.67
Basic chemicals	4.29
Other chemical products	6.19
Rubber products	1.24
Plastic products	2.68
Glass and non-metallic mineral products	**3.18**
Glass and glass products	0.66
Non-metallic mineral products	2.52
Basic iron and steel, non-ferrous metal products, metal products and machinery	**18.69**
Basic iron and steel products	3.57
Non-ferrous metal products (including precious metals)	2.58
Structural metal products	1.99
Other fabricated metal products	3.79
General purpose machinery	2.58
Special purpose machinery	3.41
Household appliances	0.77
Electrical machinery	**1.64**
Radio, television and communication apparatus and professional equipment	**1.54**
Radio, television and communication apparatus	0.90
Professional equipment	0.64
Motor vehicles, parts and accessories and other transport equipment	**7.56**
Motor vehicles	2.82
Bodies for motor vehicles, trailers and semi-trailers	0.47
Parts and accessories	3.04
Other transport equipment	1.23
Furniture and other manufacturing	**3.11**
Furniture	1.07
Other manufacturing groups	2.04
Total	**100**

Source: Stats SA

- The survey from which the capacity utilisation data is drawn covers utilisation of production capacity by large manufacturing enterprises, i.e. those with VAT turnover greater than R100 million per annum, on a three monthly basis from approximately 980 large enterprises, a subset of approximately 45 130 manufacturing enterprises.
- These enterprises conduct activities in the processing, making, packing and manufacturing of products and the slaughtering of animals, including poultry. It also covers the installation, assembly, completion, repair and related work.
- The percentage utilisation of production capacity in the manufacturing industry is a measure of the use of manpower, plant and machinery in manufacturing. Other reasons include downtime due to maintenance, changes in productivity and seasonal factors.

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