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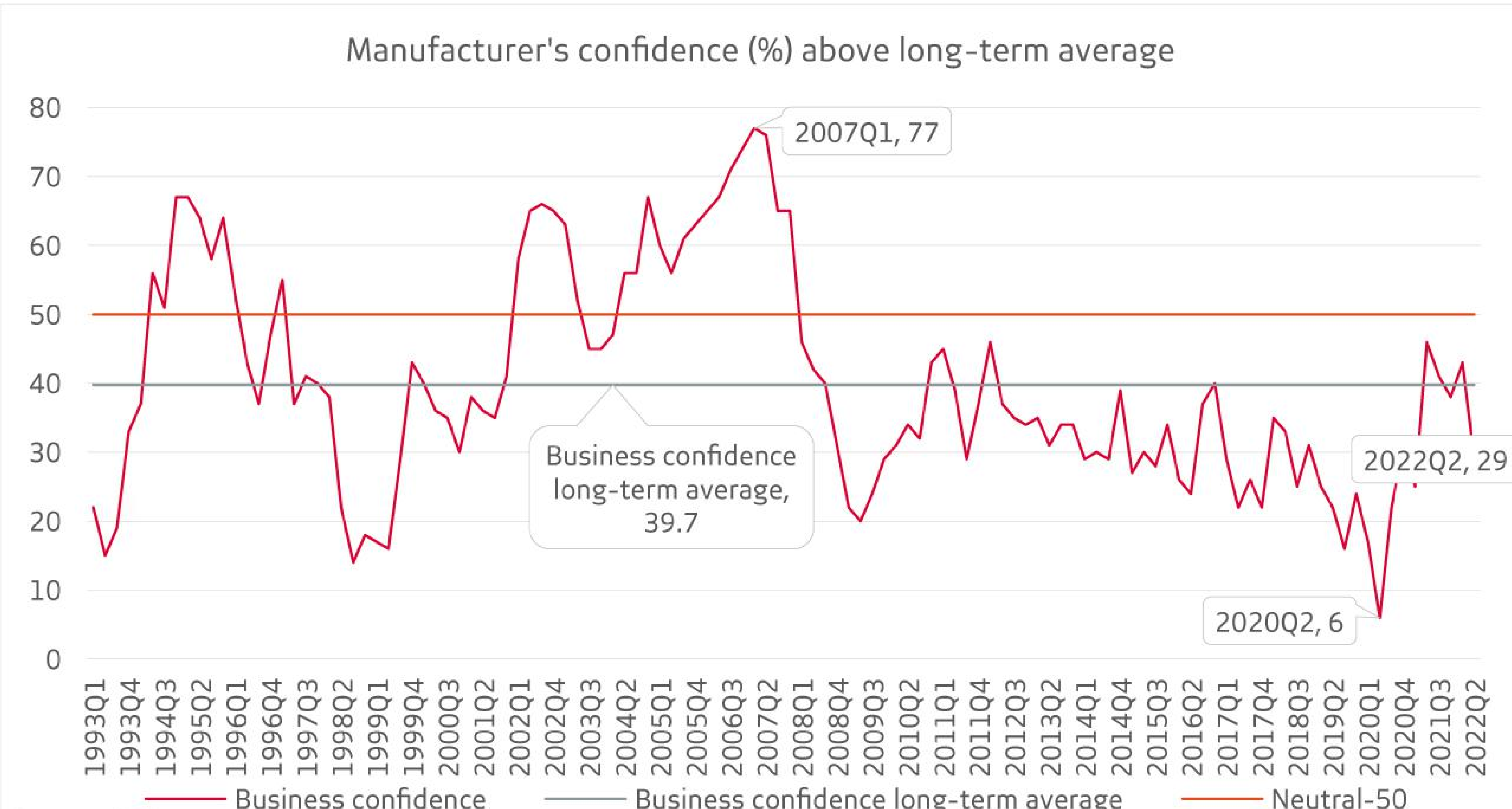
Manufacturers remain resilient while facing multiple constraints, which need to be overcome to reignite growth in the sector

As the South African economy continues its recovery from the initial shocks of COVID-19 at a much faster pace than initially anticipated, manufacturing remains a key sector to the country's recovery plan and to achieve our future growth by creating jobs and lessening our reliance on imported products.

Although manufacturers are once again proving their resilience with a general trend of improving confidence and activity levels, the road to recovery has been a bumpy one and we cannot ignore that the sector has been through a tumultuous time over the past two years. Global lockdowns, COVID-19, strikes, riots and Russia's invasion of Ukraine have led to notable constraints on the supply chain.

Most recently, the KwaZulu-Natal floods resulted in reduced activity levels during April, with some lingering effects in May, as seen in the Absa Purchasing Managers Index (PMI), and an overall knock to manufacturers' confidence levels, visible in the Q2 Absa Manufacturing Survey conducted by the Bureau for Economic Research (BER).



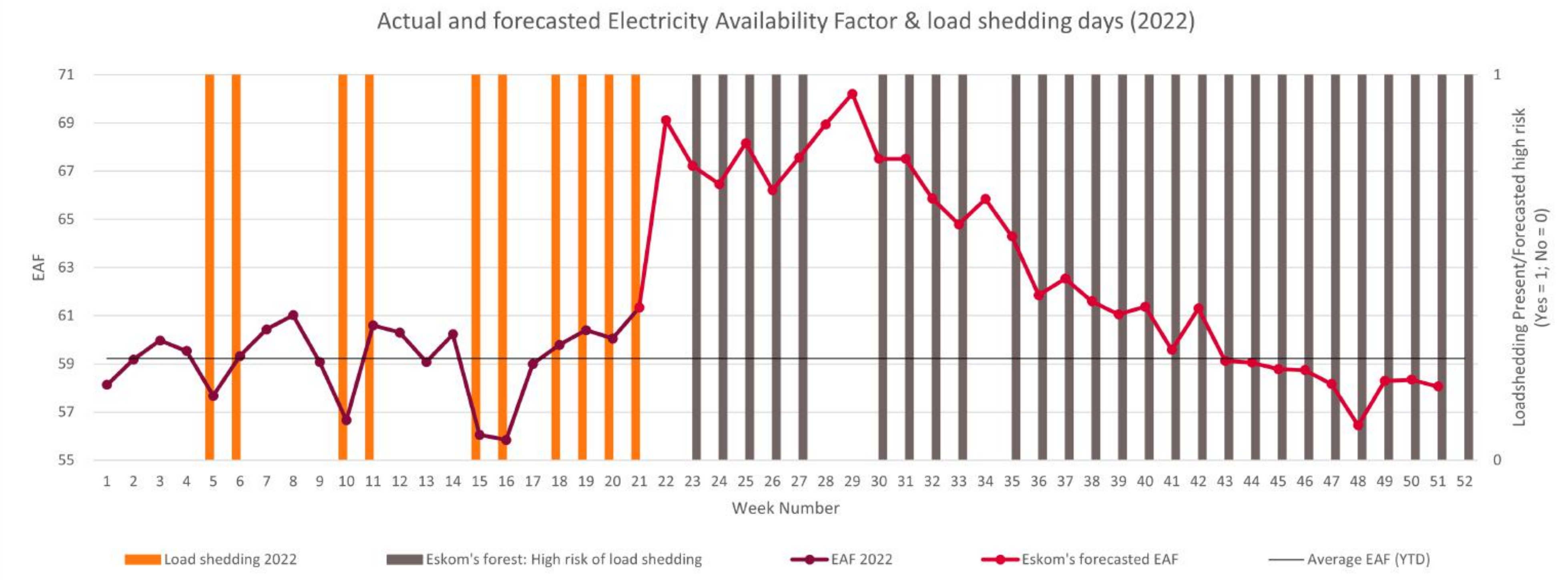
Source: BER

According to Statistics South Africa, manufacturing sales value and production levels have shown a strong recovery in Q1 of this year, with January, February and March 2022 sales (not seasonally adjusted) 13%, 17% and 22% higher respectively than in the corresponding month of 2019 (pre-COVID-19). The seasonal dip in the April sales figures were exacerbated due to the KZN floods and intensified bouts of load shedding, however, they are positively 12% higher than those seen in April 2019.

Management of working capital has become more vital than ever as manufacturers continue to face raw material shortages and long lead times for deliveries. To counter these effects, many manufacturers are stocking up on inventory to ensure that they would not lose sales and can win new business. Rising input costs such as oil, plastic and steel materials, compounded by the effects of rising electricity tariffs and elevated transport costs, are squeezing manufacturers' margins. With the longer inventory days, increased cost of production and transport delays, cashflows have seen pressure and funding of working capital cycles is a key consideration.

Load shedding continues to be exacerbated by operational problems at even Eskom's most reliable plants, and unplanned outages caused by a lack of maintenance remains the leading cause. With an electricity availability factor (EAF) – how much energy is available relative to total installed capacity – target of 80% as noted in the Integrated Resource Plan (IRP), Eskom is struggling to maintain a level above 60%.

Eskom forecast a medium to high risk of load shedding every week for the remainder of the year. Over the winter period alone, the expectation regarding load shedding is 100 days. While in previous years we did not experience more than 80 days of loading shedding in the entire year, 2022 is set to be the worst year of load shedding yet.



Eskom forecast a medium risk of load shedding in weeks 22, 25, 27-29, 31 & 34 (Eskom does not forecast a low risk of laod shedding for the remainder of the year)

Although below the expected double-digit increase, tariff increases for 2022 were, once again, above headline CPI. While this puts pressure on manufacturers' margin, further down the value chain, consumers are also facing a reduction in their spending power, which, along with rising fuel and food costs, should negatively impact demand.

Without affordable and reliable energy, productive sectors will struggle to hit their potential. Positively, we have seen enabling regulatory changes in the energy sector. Manufacturers are taking their energy journey into their own hands with the installation of renewable energy solutions to hedge against tariff increases and unreliable energy supply, including batteries in their installation to future-proof their business.

Manufacturers are not only investing in their energy journey, but are also reinvesting into their production processes. As manufacturers continue to find ways to reduce costs, this investment tends to go into new machinery and equipment that is more efficient, cost-effective and productive.

As the recovery continues and we return to an environment of easing raw material shortage and some respite to the supply chain issues, manufacturers will hopefully see reduced costs and a more efficient working capital cycle. Structural changes remain a key consideration for South Africa to not only recover, but to grow in the future. It is therefore vital for all stakeholders in this sector to engage and share insights.

As electricity prices continue to soar, Renewable Energy is increasingly becoming a viable option. If you're considering ways of integrating it into your business, Absa's Green Asset Finance is the answer you are looking for.

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