A note on developments in the retail-trade sector

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Introduction

South Africa's services-providing industries have increased their share in the total economy significantly over the past fifty years or so. This reflects the increasing sophistication of the South African economy, but other factors, such as the end to economic isolation and the repeal of sanctions in the early 1990s, trade liberalisation, globalisation and the associated technological progress, also contributed to the growing importance of the services industries.

1 The views expressed are those of the author and do not necessarily reflect the views of the South African Reserve Bank.

All the subsectors of the tertiary sector are not benefiting equally from these structural changes. The share in total gross domestic product of the transport, storage and communication subsector, and the financial services subsector increased during the 1990s. By contrast, the contribution of the total trade subsector initially remained broadly unchanged but declined later in that decade.

The aim of this note is to briefly review some developments in the retail-trade sector since the beginning of the 1990s. Firstly, changes in the contribution of the retail-trade sector to total gross value added are reviewed. In the section thereafter the growth in real value added by the retail-trade sector is described. This is followed by a short overview of changes in the sector's gross fixed capital formation, saving and net lending. The subsequent section analyses the composition of factor income in the retail-trade sector. This is followed by a discussion of employment changes, while concluding remarks are made in the final section.

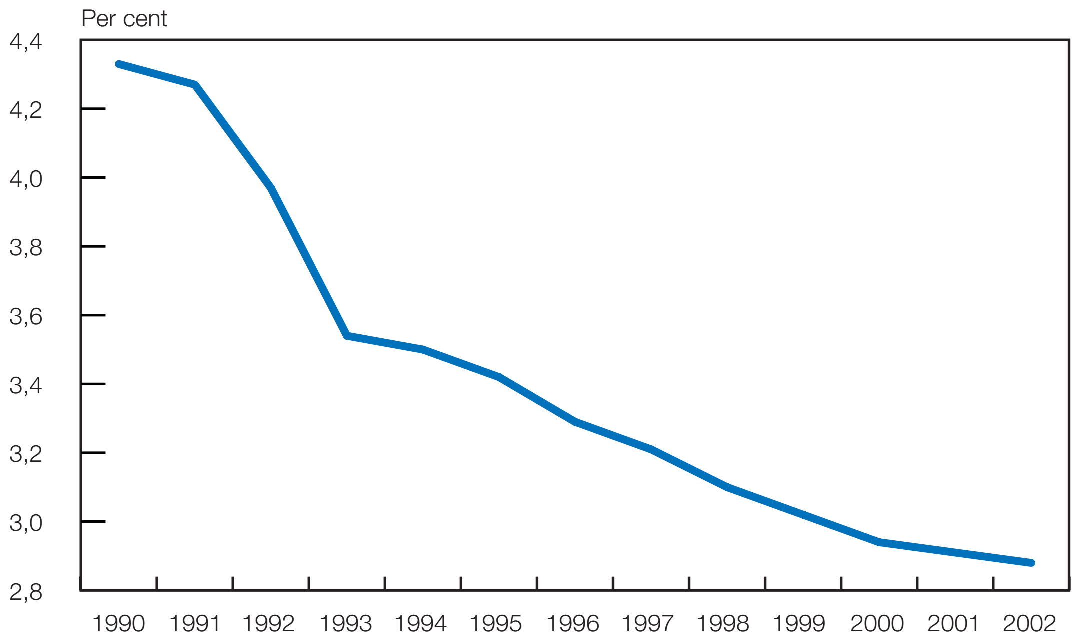
Contribution to total gross value added

The services-providing industries of South Africa increased their share in the national economy from 49½ per cent in the 1950s to 64 per cent in 2002. This can mainly be attributed to the faster growth in real value added by services-providing industries relative to the goods-producing industries and was particularly evident in the transport, storage and communication sector and the financial intermediation, insurance, real-estate and business-services sector.

The growing importance over the past decade of the transport, storage and communications sector can mainly be attributed to the expansion of the fixed-line telephone infrastructure to previously under-serviced areas and the introduction of cellular-telephone networks. Financial intermediation, insurance, real estate and business services benefited, among other things, from the liberalisation of financial markets and the growing demand for financial services brought about by globalisation. In addition, government increased its share in overall gross value added in order to improve service delivery in the years after 1994.

After the contribution of the *retail-trade* sector to the total economy had remained constant at a level of about 4 per cent from the 1950s to the 1980s, this contribution declined to 3 per cent in 1998 and remained at around that level until 2002. The share of the *overall commerce sector* (i.e. the wholesale, retail and motor-trade, and catering and accommodation sectors) in the total economy declined somewhat from the 1950s to the 1980s, before increasing during the 1990s. The increased contribution in the 1990s can partly be attributed to the increase in real value added by the motor-trade and the catering and accommodation subsector.

Contribution of gross value added by retail trade to total gross value added



The declining share of the traditional retail-trade sector relative to total gross value added reflects a change in consumers' buying behaviour in the second half of the 1990s. Among other things, this is evident in a shift away from traditional retail goods to new products and services. Also, a growing portion of final consumption expenditure by households was directed to wholesalers (establishments of which sales to final consumers constitute less than half of their turnover) and this reduced the gross value added by the retail-trade sector.

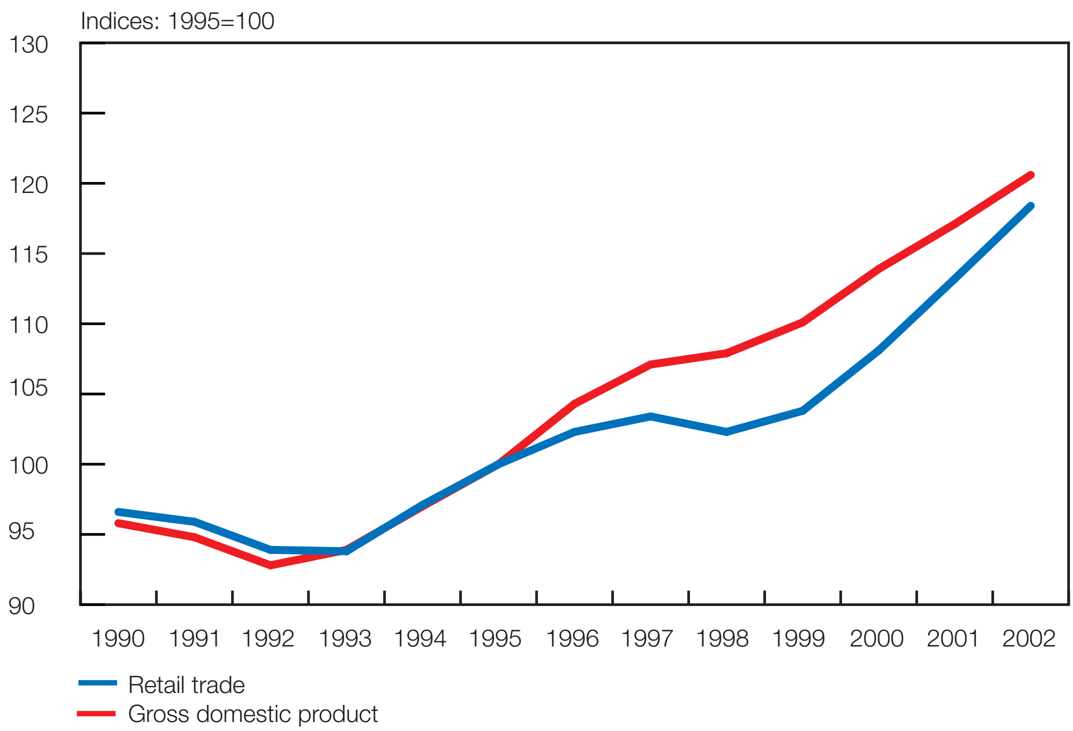
Table 1: Sectoral contributions to total gross value added

Period	Goods-producing industries	Services-providing industires	Commerce		Transport, storage and communi-cation	Financial interme-diation, insurance, real-estate and business services	Other services-providing indus-tries
			Total	Retail trade			
Decade averages							
1950s	50½	49½	14½	4	9½	9½	15½
1960s	48½	51½	14	4	9½	11½	16
1970s	47½	52½	13	4	9½	13½	16½
1980s	49	51	12	4	8½	12½	17½
1990s	39	61	14	3½	9	16½	21½
Years							
1993	39½	60½	14½	3½	8½	16	21
1994	39½	60½	14	3½	8½	16	21½
1995	38½	61½	14½	3½	9	16½	21½
1996	37½	62½	14	3½	9	16½	22½
1997	36½	63½	13½	3½	9	17½	23
1998	36	64	13½	3	9½	18½	23
1999	34½	65½	13	3	9½	19½	23
2000	34½	65½	13½	3	10	20	22½
2001	35	65	13½	3	10	20	22
2002	36	64	13½	3	10	19½	22

Growth in real value added

The growth in real value added by the retail-trade sector since the beginning of the 1990s has followed roughly the same pattern as the growth in real value added by the broad commerce sector and the economy as a whole. Following the long and severe downward phase of economic activity from 1989 to 1993, the real value added by the retail-trade sector increased at an average annualised rate of about 3 per cent from the first quarter of 1993 to the second quarter of 1997. This was lower than the annualised 3½ per cent growth recorded in the total gross domestic product over the same period.

Real gross value added of retail trade and gross domestic product



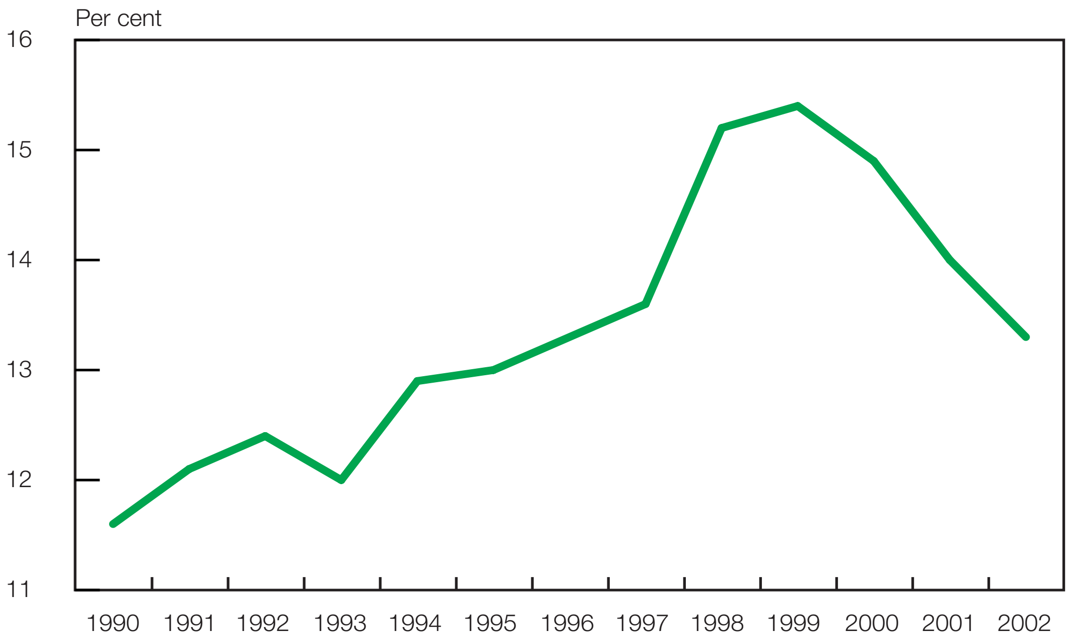
Around the middle of the 1990s the South African economy benefited materially from the repeal of trade and financial sanctions and from progress made in combating inflation. As the recovery in economic activity from June 1993 to November 1996 became more broadly based, consumers became more optimistic. Real final consumption expenditure by households increased strongly, boosting growth in the real value added by the retail-trade sector. This stronger demand for consumer goods occurred in all main spending subcategories, but expenditure on durable and semi-durable goods increased more briskly than the spending on other categories of goods and services.

An increase in the disposable income of households and a rise in the debt-financing of consumption expenditure underpinned the demand for durable goods during most of the 1990s. Households apparently made full use of the easy accessibility of debt financing facilities offered by the banking sector and by retailers themselves. In addition, the redistribution of income to households with a high propensity to consume, lifted expenditure on essential goods and services after 1993.

The real value added by the retail-trade sector *contracted* at an average annualised rate of 4 per cent from the second quarter of 1997 to the fourth quarter of 1998. Global economic conditions, particularly the financial turbulence in south-east Asia in 1997 and 1998, adversely affected South Africa and other emerging-market economies. The domestic financial securities markets experienced severe downward pressure in May 1998. The domestic monetary policy stance was tightened and the prime lending rate of banks rose from 18,25 per cent in May 1998 to 25,5 per cent in August 1998. Business and consumer confidence deteriorated quite severely in 1998.

As the slack in the economy became more pronounced, households' disposable income was adversely affected by declining employment, high debt-to-income ratios and high debt-servicing costs. There was also a sharp increase in the tax burden of households from about 11½ per cent of current income in 1990 to more than 15½ per cent in 1999. Wealth effects following the decline in equity values in the second half of 1998 also weighed on households' willingness to spend. All these factors contributed to slower growth in consumer demand, curbing the growth in the real value added by the retail-trade sector.

Income tax paid as percentage of current household income



The South African economy recovered robustly from the setbacks suffered during the financial crises of 1997 and 1998. From the beginning of 1999 to 2002 the real value added by the retail-trade sector increased at an average annualised rate of 4½ per cent, faster than the increase of 3½ per cent in the broad commerce sector and the 3 per cent in the economy as a whole. Activity in the retail-trade sector benefited from solid consumer demand, following strong growth in the real disposable income of households.

The real disposable income of households from 1999 to 2002 was boosted by, among other things,

- the consistent lowering of the tax burden of households from 15½ per cent of current income in 1999 to 13½ per cent in 2002;

- an increase in the net property income of households as the declining interest rates lowered debt-servicing costs; and
- increases in nominal labour compensation in excess of increases in the prices of consumer goods and services.

An analysis of the composition of final consumption expenditure shows a distinct shift in expenditure patterns away from those goods and services traditionally supplied by retailers. Expenditure on these goods and services (essentially consumer goods) increased at an average annualised rate of 2½ per cent during the period 1999 to 2002, compared with an increase of 3 per cent in total household consumption expenditure.

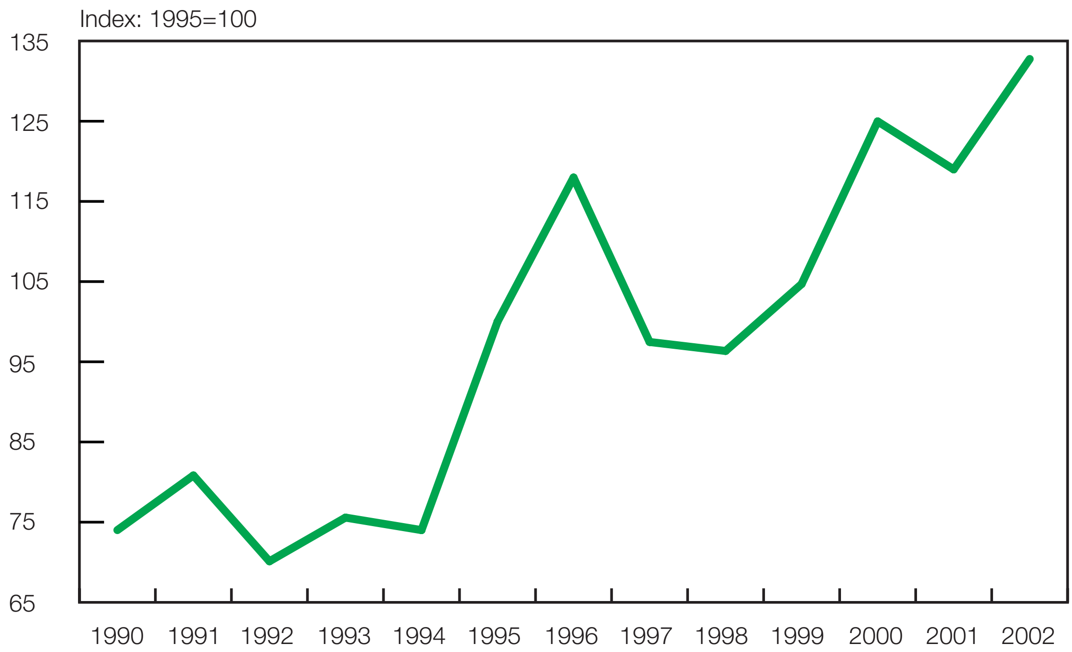
In part, this was a reflection of the faster pace of price increases in spending categories that are considered essential by households. It is estimated that increases in the prices of petrol, medical products and services, transport services, household fuel and power and educational services diverted spending of some R17 billion away from traditional retail goods in the period 1999 to 2002. The popularity of cellular telephones and Internet services, together with a strong rise in outlays by households to secure property and living conditions, contributed further to this apparent structural shift in spending habits.

Gross fixed capital formation

Gross fixed capital formation by the retail-trade sector increased rather poorly in the early part of the 1990s, but picked up in the second half of the decade, lifting the average annual growth rate of real fixed capital formation by the retail-trade sector to about 4 per cent for the decade as a whole.

The peaceful conclusion of the political transition in 1994 was followed in 1995 and 1996 by a rapid expansion of retail-trade facilities. This expansion was temporarily interrupted during the financially turbulent years of 1997 and 1998, but a fairly robust

Real gross fixed capital formation by the retail-trade sector

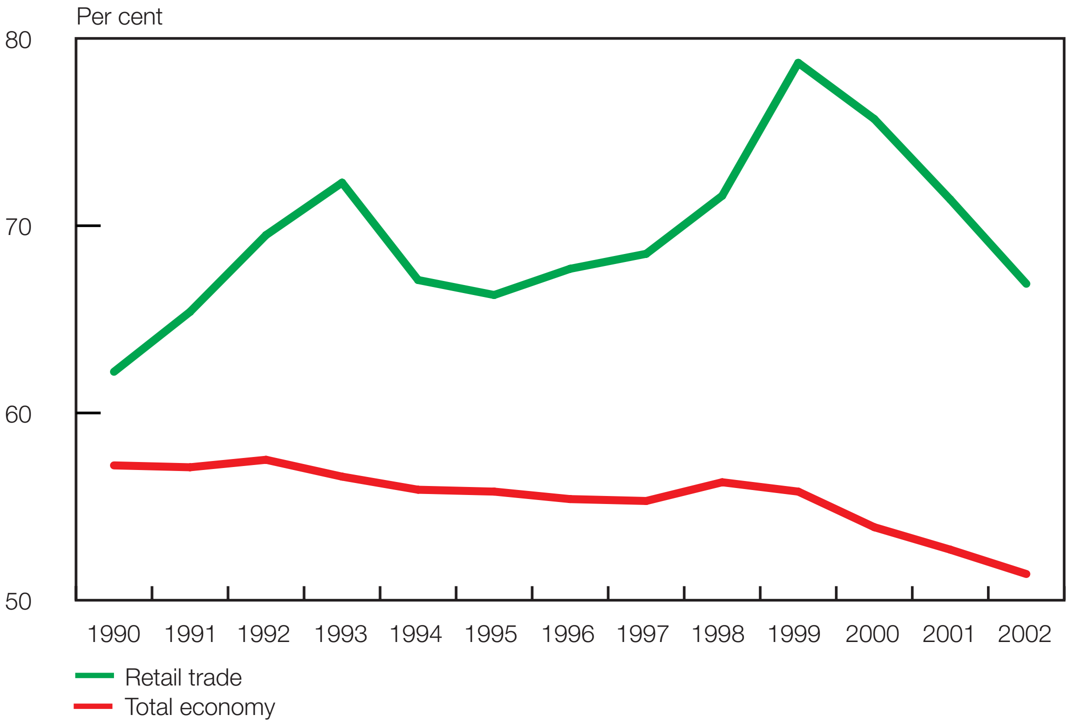


and prolonged recovery got under way in 1999. Several large shopping malls were developed during these years, and new investment in transport and other capital equipment such as barcode scanning devices was also stepped up substantially. In addition, strong growth in the demand for franchising facilities contributed to the expansion of capacity in the retail-trade sector.

Factor income

An analysis of developments in the components of factor income in the retail-trade sector shows that, on average, almost 71 per cent of total factor income was allocated to employees over the past four decades. The economy-wide ratio was 56½ per cent. During the 1990s, labour's share in the total value of output originating in the retail-trade sector drifted higher, on balance, from 62 per cent in 1990 to about 78½ per cent in 1999, before falling back to 66½ per cent in 2002. By contrast, employees' share in economy-wide factor income declined almost uninterruptedly from 57 per cent in 1990 to 51½ per cent in 2002.

Compensation of employees as percentage of total factor income in the retail-trade sector and in the total economy

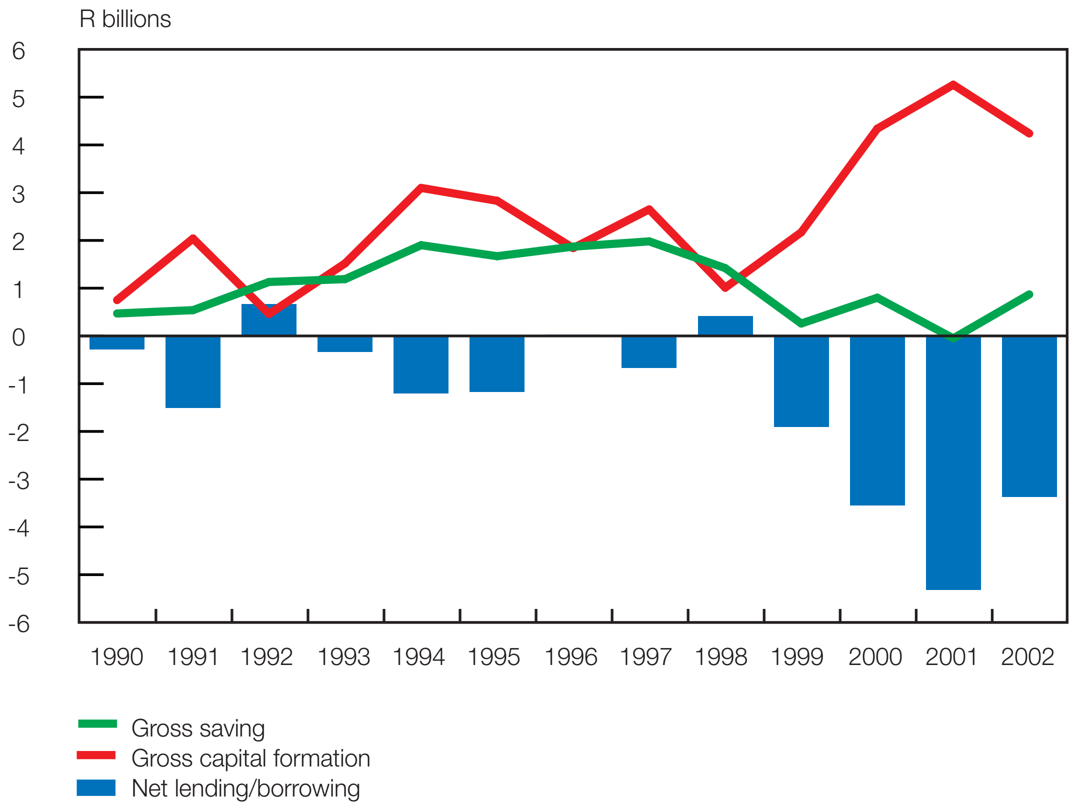


The expansion of employees' share in total factor income in the retail-trade sector from 1990 to 1999 coincided with two downward phases of the business cycle. Rising employee rewards relative to overall factor income are not uncommon in periods of economic contraction. Operating surpluses and profits in the retail-trade sector are far more severely compressed than employee compensation during times of economic slack. In fact, the number of employees in the retail-trade sector increased from 1997 to 1999 despite the slowdown in the economy. As activity picked up during 2000, retail businesses were able to restore their operating margins and spread their overhead costs over larger sales volumes, increasing the share of operating surpluses in total factor rewards and lowering the share of employee compensation.

Saving and net lending

The gross operating surpluses of the retail-trade sector grew at a comparatively modest average annual rate of 6 per cent during the 1990s. Rising dividend and tax payments caught up with the slow growth in operating surpluses, causing gross saving in the retail-trade sector to reach a peak in 1997 and to generally decline in the ensuing years. As fixed capital formation grew quite strongly in the second half of the 1990s and inventories were accumulated, gross capital formation by the retail-trade sector tended to exceed gross saving. The retail-trade sector accordingly became increasingly dependent on external sources for meeting its investment requirements. In 2001 the saving shortfall of R5,3 billion was equal to 20 per cent of the value of output originating in the retail-trade sector.

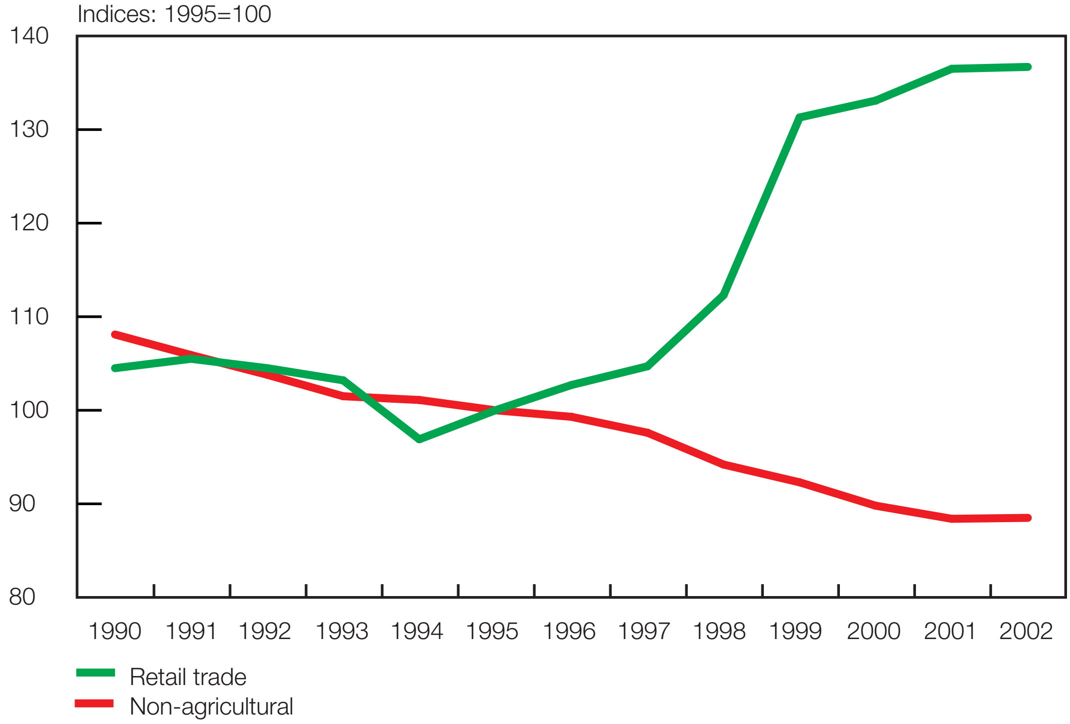
Excess of gross capital formation over gross saving in the retail-trade sector



Employment trends

Contrasting the dismal performance of employment creation in the manufacturing sector and in the total formal non-agricultural sectors of the economy, employment in the retail-trade sector has increased substantially since the middle of the 1990s. Employment in the retail-trade sector grew at an average annualised rate of 4½ per cent from 1995 to 2002. The increase in employment in the retail-trade sector can also be attributed to the expansion of retail space in a number of large shopping centres in major metropolitan areas and heightened franchise activities in the retail-trade sector over the past number of years.

Formal employment in the retail-trade and total non-agricultural sectors*



* Based on quarterly surveyed data in selected industries

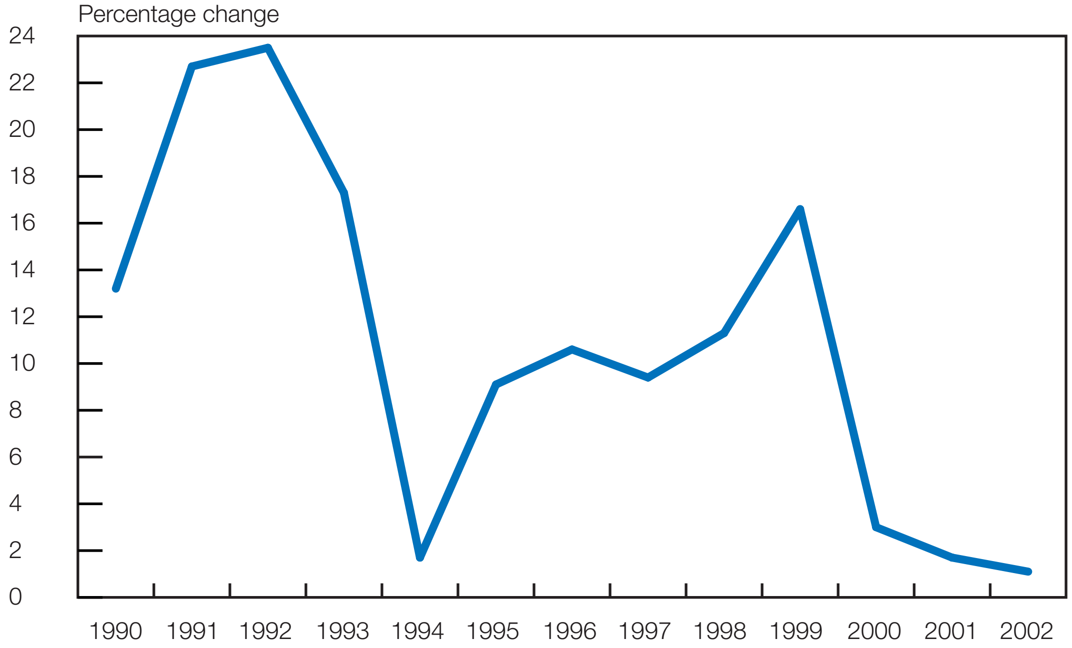
The increase in employment levels in the retail-trade sector, at an average annualised rate of 7½ per cent from 1994 to 1999, was significantly faster than the increase of 1½ per cent in real value added by this sector. Consequently, real output per employee in the retail-trade sector fell during this period and the share of employee compensation in total factor income increased. Although employment numbers increased further at an average annualised rate of 2½ per cent from 1999 to 2002, real value added increased at a rate of 4 per cent, causing real output per employee to rise. This was partly due to technological advances such as integrated barcode scanning and impovements in pricing, payment and inventory control systems. The growth in labour productivity in the retail-trade sector since 2000 compressed the growth in nominal unit labour cost to modest levels, thereby contributing to the containment of inflation in the economy.

Summary

Despite the increase in the share of the services-providing industries in the domestic economy, the share of the retail-trade sector has remained more or less unchanged since the 1950s. This followed from the fact that the growth in real value added by the retail-trade sector followed broadly a similar pattern as the growth in economy-wide real value added. Still, the real value added by the retail-trade sector was directly influenced by changes in consumer demand. This was particularly evident during 1998 and 1999 when tight monetary conditions curbed the growth in consumer spending.

An analysis of the composition of final consumption expenditure shows a distinct structural shift in expenditure away from goods traditionally sold by retailers, mainly in response to sharp price increases in some goods categories considered essential by households. The popularity of new products such as cellular telephones and other electronic devices and services also contributed to this structural shift.

Nominal unit labour cost in the retail-trade sector



A distinct characteristic of the retail-trade sector is the relatively high share of factor income allocated to employee compensation, averaging about 71 per cent in the period 1950 to 2002. Although job creation in the overall economy was very poor, the retail-trade sector has consistently increased employment opportunities since 1995. In recent years the internally generated saving of the retail-trade sector fell increasingly short of fixed capital formation in the sector, making the retail-trade sector more and more dependent on external resources to finance capital expenditure.

Despite the prominent share of labour in total factor income, the growth in nominal unit labour cost in the retail-trade sector generally slowed down during the 1990s, thereby contributing to the containment of inflation in the economy.