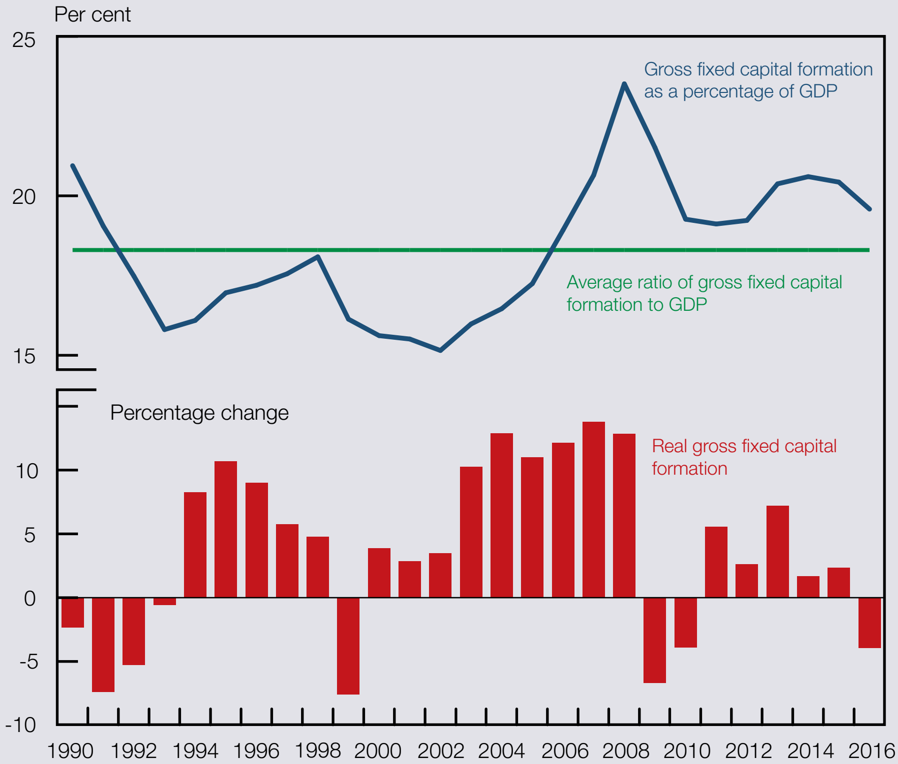
Box 2 The evolution of gross fixed capital formation

Gross fixed capital formation by private business enterprises and public corporations is an important determinant of long term economic growth. The evolution of gross fixed capital formation in South Africa can be analysed from three major perspectives. Firstly, real gross fixed capital formation expanded at a much slower pace in the period following the 2008/09 global financial crisis than in the preceding six years. Secondly, regardless of slower growth in gross fixed capital formation, expressed as a ratio of gross domestic product (GDP), it remained above its long-run average of 18.3% (from 1990 to 2016) since 2006. This ratio was held up by annual growth in investment frequently exceeding that in GDP. Lastly, the structure of capital investment by type of organisation, as reflected by both the kind of economic activity and the type of assets, changed markedly after the global financial crisis.

Real gross fixed capital formation



Sources: Stats SA and SARB

Growth in aggregate real gross fixed capital formation in South Africa averaged 9.2% per annum during the pre-crisis period from 2000 to 2008. Following the financial crisis, growth decelerated to a mere 0.6% per year. Gross fixed capital formation as a ratio of nominal GDP has also fallen from a recent peak of 23.5% in 2008 to 19.6% in 2016. This decline in the ratio occurred alongside the unwinding of boom conditions in global commodity prices from around mid-2008.

Weak global economic growth in recent years supressed the export demand for South African manufactured goods. Persistently low consumer and business confidence in the domestic economy have also resulted in the postponement of a number of key domestic private sector expansion projects. The negative impact of lacklustre growth in the world economy was also experienced by some other emerging market economies. This is evidenced by a similar though stronger decline in capital expenditure in India and to a lesser extent than South Africa in Brazil and Russia. As from 2008, the ratios of gross fixed capital formation to GDP in South Africa, Brazil and Russia averaged around 20%.

Gross fixed capital formation in selected emerging economies

Percentage of gross domestic product

Country	2008	2009	2010	2011	2012	2013	2014	2015	2016
China............................	40.1	44.9	45.0	44.9	45.3	45.5	45.0	43.8	43.3*
India	35.0	33.2	33.1	34.1	32.9	32.2	30.5	29.9	27.1
Russia	21.9	19.4	18.8	19.1	20.3	20.2	20.9	20.5	20.8
Brazil	19.3	19.1	20.5	20.6	20.7	20.9	19.9	18.1	16.4
South Africa.................	**23.5**	**21.5**	**19.3**	**19.1**	**19.2**	**20.4**	**20.6**	**20.4**	**19.6**

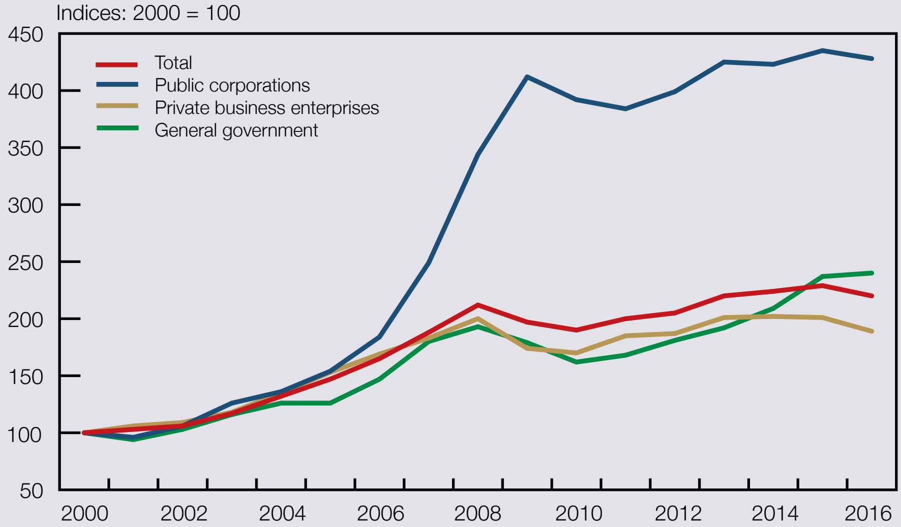
* International Monetary Fund (IMF) projection of gross capital formation

Sources: IMF, Haver Analytics and SARB

The structure of capital investment has changed in terms of the type of organisation driving investment. Weak growth in real fixed capital expenditure since 2009 largely reflected the slower pace of investment by both private business enterprises and public corporations. Real investment by private business enterprises during the period 2009 to 2016 contracted at an average annual rate of 0.5% after having increased by as much as 9.0% during the period 2000 to 2008. Over the same periods, average annual growth in real capital outlays by public corporations also slowed substantially to 2.8% from 11.9%.

Real gross fixed capital formation

Indices: 2000 = 100

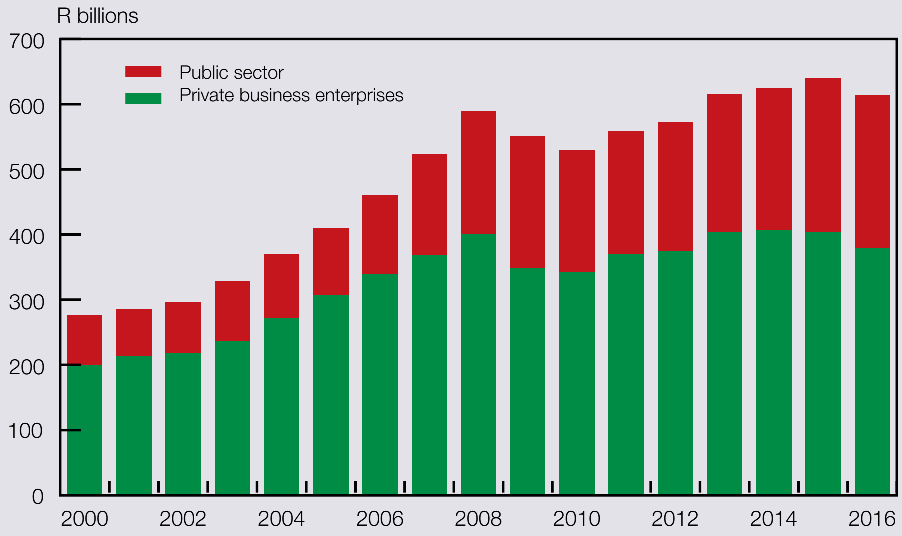


Sources: Stats SA and SARB

The period preceding the global financial crisis was characterised by a strong surge in gross fixed capital formation. The contribution of private business enterprises to total gross fixed capital formation amounted to 72.5% during the period 2000 to 2008, while public corporations contributed 11.5%. Subsequently, the contribution by private business enterprises declined to 61.1% in 2016, while that of public corporations increased to 20.2%.

The structure of capital investment also changed in terms of the kind of economic activity that attracted new investments. The decline in the contribution by private business enterprises to total fixed investment since 2009 was fairly broad-based. Only electricity generation experienced robust growth in gross fixed capital formation, supported especially by the surge in independent renewable energy projects being implemented. Capital investment in mining and exploration activities was, however, to a large extent delayed by a number of high-profile labour strikes as well as policy uncertainty in general, having contributed to the deferment of fixed capital investment. Weak output growth in mining and construction furthermore contributed to a contraction in gross fixed capital formation in manufacturing. Manufacturing was also negatively affected by rapidly rising electricity prices, sporadic labour unrest and loss of international competitiveness.

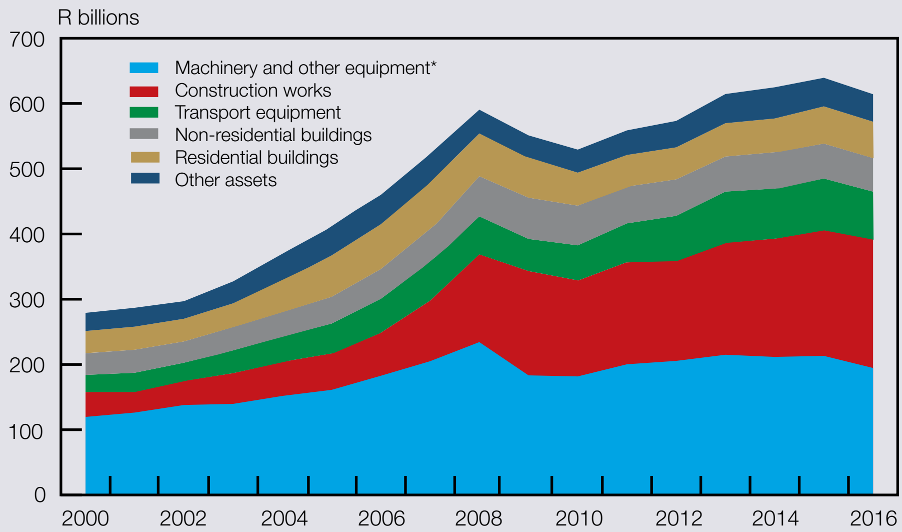
Real gross fixed capital formation



Sources: Stats SA and SARB

The increase in gross fixed capital formation by the public sector since 2009 was largely driven by a robust expansion of capital investment by public corporations, with capital outlays by general government increasing at a more moderate pace. Investment by public corporations occurred primarily in the transport and electricity generation sectors. Consistent with the National Development Plan, economic infrastructure investment relative to total public sector investment increased significantly from an average of 62.9% during the period 2000 to 2008 to 79.4% in 2016.

Real gross fixed capital formation by type of asset



* Including information, computer and telecommunications equipment

Sources: Stats SA and SARB

The structure of gross fixed capital formation also changed in terms of the type of assets being invested in. Since 2009, the contribution of investment in construction works to total capital investment increased meaningfully, largely reflecting capital investment by the public sector. Capital spending on construction works as a share of total fixed investment averaged 14.6% during the period 2000 to 2008, and doubled thereafter to 29.2% during the period 2009 to 2016. By contrast, the share of investment spending on machinery and other equipment declined as investment by private business enterprises waned.