

Economic Factors (2016-2023) - Javier

Economic growth

South Africa's economic growth has been sluggish, with annual GDP growth averaging below 1%. The country faces significant structural challenges, including high unemployment rates, especially within Black and Asian communities. Political instability, worsened by corruption scandals, such as the ANC scandal in 2018 and the trial of former President Jacob Zuma, has contributed to a lack of investor confidence and hindered economic growth ([Coface, n.d.](#)). A significant challenge is South Africa's energy crisis, with the national power grid, managed by Eskom, suffering from years of mismanagement and corruption. This has led to frequent power outages, disrupting economic activity and investor confidence. As of 2023, these issues have persisted, affecting industries, including IKEA, which faces operational challenges in energy-dependent retail sectors. The retail giant has had to address logistical hurdles due to power outages impacting store operations ([DBSA, n.d.](#)). The COVID-19 pandemic further strained the economy, shrinking it by 7% in 2020 ([Gov.za, n.d.](#)). While some recovery occurred in 2021 and 2022, growth has remained minimal. South Africa's reliance on commodity exports, particularly mining, exposes it to external shocks. The mining sector, a critical part of the economy, has seen volatility. For retailers like IKEA, the fluctuations in the global economy and commodity prices directly impact operational costs and demand for particular product lines.

Income Levels and Purchasing Power

Income inequality remains one of South Africa's most pressing challenges, with the country holding one of the highest Gini coefficients globally. Over 50% of the population lives below the poverty line ([Gov.za, n.d.](#)). Unemployment surpassed 32% in 2023, with Black and Asian communities being disproportionately affected. This inequality and the rising cost of living have eroded the purchasing power of South African consumers, a trend also visible in the retail sector, where customers are spending less due to inflationary pressures. IKEA, which caters to higher-income and budget-conscious customers, faces unique challenges in a market where the income gap is pronounced. The company's pricing strategies, mainly focusing on affordable home goods, have been adapted to address these disparities. However, the demand for products at lower prices has been growing, forcing IKEA to reconsider its local supply chains and product offerings to make its goods accessible to a broader range of consumers. Despite these challenges, IKEA's sustainability initiatives, including affordable furniture for low-income households and support for local manufacturing, help it navigate the country's income disparities ([Coface, n.d.](#)). **inflation and Interest Rates**

Next due: 18 July 2024

CURRENT INFLATION RATE

3.8%

INFLATION TARGET

3-6%

Inflation has been a critical concern in South Africa, driven by global supply chain disruptions and rising energy costs. The South African Reserve Bank (SARB) has traditionally kept inflation within a 3-6% target range. Still, inflationary pressures have surged, particularly in the energy and food sectors ([South African Reserve Bank, n.d.](#)). These challenges have directly affected retailers like IKEA, whose cost structure is influenced by energy prices and the price of raw materials. During the COVID-19 pandemic, the SARB slashed interest rates to a record low of 3.5% to stimulate economic growth. However, by mid-2023, the SARB had raised the repo rate to 8.25% to combat rising inflation. For companies like IKEA, interest rates impact consumer spending on big-ticket items, including home furniture. With high inflation and increasing interest rates, the overall demand for home goods has become more price-sensitive. To counteract these challenges, IKEA has maintained its focus on cost-efficient operations, including local sourcing and adjusting its supply chains, to offer more competitive pricing in a market where inflation erodes purchasing power.



Foreign Direct Investment (FDI) Inflows

South Africa's FDI inflows have needed to be more consistent due to political uncertainty, labour strikes, and policy challenges surrounding land reforms and state-owned enterprises. The period between 2016 and 2019 saw a significant decline in FDI, though recovery began in 2021 with investments in critical infrastructure and renewable energy ([DBSA, n.d.](#)). IKEA has been an active player in South Africa's retail market since 2016, contributing to the country's FDI inflows. The company invested in retail expansion and

local manufacturing, establishing stores in major cities like Johannesburg and Cape Town. IKEA's investments focus on increasing its footprint in the market and supporting South Africa's energy transition by sourcing products locally and adopting renewable energy solutions for its stores and warehouses ([DBSA, n.d.](#)). However, political challenges, such as uncertainty around land expropriation, continue to threaten long-term investment stability. Nonetheless, IKEA's emphasis on sustainability and local production positions it well in a market that increasingly prioritizes these values.

Key Industries and Economic Sectors

- **Mining:** South Africa remains a global leader in platinum, gold, and chromium production. However, the mining sector faces challenges from declining commodity prices, labor disputes, and environmental regulations ([Coface, n.d.](#)). For retailers like IKEA, the mining sector's volatility affects raw material costs and supply chain stability, which can trickle down to the price of home goods.
- **Manufacturing:** South Africa's manufacturing sector has faced headwinds from power shortages and high labor costs, with the automotive and chemicals industries being major contributors to exports. The government is working on reindustrialization policies to localize production, but challenges remain. IKEA's approach to local manufacturing has strategically reduced dependence on imported goods and mitigated supply chain disruptions. IKEA has set up manufacturing partnerships with local suppliers for products such as flat-pack furniture, ensuring its continued presence in the market despite challenges ([DBSA, n.d.](#)).
- **Agriculture:** Agriculture contributes around 2.5% to GDP and is critical to employment and export. South Africa is a major exporter of citrus, wine, and maize. However, climate change and droughts have negatively impacted production. IKEA's sustainable sourcing strategies focus on procuring raw materials such as wood and textiles from local, responsibly managed agricultural sources, helping to support the agricultural sector amidst environmental challenges ([Gov.za, n.d.](#)).
- **Energy:** South Africa is transitioning from coal to renewable energy sources to address the ongoing energy crisis. The government has prioritized renewable energy projects to alleviate the country's power shortages ([DBSA, n.d.](#)). IKEA has strongly advocated renewable energy in its store operations and product sourcing. The company has committed to powering all South African stores with renewable energy, aligning its operations with the country's energy transformation goals.
- **Financial Services:** South Africa has a sophisticated financial services sector that contributes significantly to the economy. However, political instability has limited its growth potential. A stable financial system is essential for IKEA to secure financing for its expansion plans. The country's economic infrastructure supports IKEA's investment in the South African market despite challenges in other sectors ([Coface, n.d.](#)).