ECONOMIC COMMENTARY - By Dr. Francois Stofberg

1 June 2020

ECONOMICS – THE MASQUERADE IN MAY

During May we were bombarded by a plethora of estimates on the likely impact of COVID-19 on the South African economy. The key lesson, however, was that there is still too much uncertainty to accurately forecast the likely impact. PWC estimated that the contraction can be as much as -19.2% if it was not for the R800 bn support offered by fiscal policy (R500 bn) and monetary policy (R300 bn). Considering the extensive support offered by the government, they reckon a -12.8% contraction is likely, with seven million jobs lost. What is important to note is that there are only about 14 million people employed in South Africa. As the weeks continued, these estimates luckily seemed a bit extreme.

Some interesting data, released by Redefine Properties, showed that consumers were shopping according to normal trends; those who have recently visited a mall, or a shop, would most likely agree. Additionally, we previously reported that only about 10% of consumers applied for payment relief, equating to roughly R30 bn. Far less than the R250 bn support offered by the government. Statistics South Africa (StatsSA) then solidified our view that the economic impact might not be as severe when they used survey data to show that only half of the industries were closed for the five weeks of level 5 lockdown. Interestingly, 10% of industries continued business as usual and 40% were impacted in some way or another. This is much better than the worst-case scenario our markets were pricing in and is also why we reduced our forecast to -7% for 2020. Another bit of motivation was the research on "survivalist entrepreneurs" that emerge during these black swan recessions. Out of desperation, these entrepreneurs use what little they have to enter industries with low education requirements and small start-up costs. In the United States, at least seven of the billionaire families started their entrepreneurial ventures during the great depression; the closest comparable recession to the one we are currently experiencing.

During the final week of May, the South African Reserve Bank (SARB) decided to reduce interest rates by another 0.50%, to add even more support to an indebted South Africa. Based on our estimate that inflation will most likely hover around 3% for 2020, there is room enough to cut the repurchase rate (currently at 3.75%) even more. In times of crises, real interest rates do not need to be positive. Monetary policy is probably more effective during a crisis, not in its ability to impact inflation, but in its ability to support consumption. Because incomes are threatened, the reduction in the cost of debt aids consumption. But some caution is advised, cutting interest rates too much can also trigger some nasties in upcoming years. Luckily though the SARB has proven their worth over the many decades. If not for them, inflation, and by implication the rand, would have been under a lot more pressure. They have been very successful in creating an environment of price stability over the long-term, which has set the platform for a thriving economy. Unfortunately, government finances have not been managed in a similar manner, or else this economy would have been booming.

And as May was ending, news headlines reported some concerning global events. China was encroaching on its 50-year agreement of autonomy with Hong Kong when they passed new security legislation that would make it a crime to undermine Beijing's authority. The agreement was set in 1984 between China and the United Kingdom and allowed Hong Kong certain freedoms that were not allowed on the Mainland. As a result, United States President Donald Trump revoked the special status Hong Kong had with the United States. Until now Hong Kong was treated separately from China, concerning customs and travel and for one, was not subject to trade tariffs. Donald Trump also terminated the United States' relations with the World Health Organisation (WHO). WHO will no longer receive any support from the United States. The termination was as a result of the allegations Trump's presidency made against WHO and China concerning gross misconduct during the COVID-19 pandemic.

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