ECONOMIC COMMENTARY - By Dr. Francois Stofberg

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ECONOMIC ACTIVITY AND THE FED'S PENDING DECISION

Last week's economic activity data reinforced our feeling that gross domestic product (GDP) growth in South Africa (SA) will remain subdued, and that we are still some distance away from pre-pandemic levels. Recently, the retail and manufacturing sectors took a hard blow owing to violent unrests and tighter COVID-19 restrictions. In July, retail sales plummeted 11.2% month-on-month (MoM). Even the year-on-year (YoY) figure fell by 0.8% and was, consequently, much lower than what analysts expected it to be, that is, 3.3%. Similarly, manufacturing contracted by 8% MoM. Luckily, the mining sector was insulated from these protests and restrictions; it expanded by 4.1% MoM in July. The net effect of these disruptions is that our economy will, most likely, see either very little growth in the third quarter of 2021, or contract ever so slightly.

In a similar vein, albeit with a better outlook, industrial production in the United States (US) lifted above its pre-pandemic level in August, and increased, once again, in September, albeit at a slower pace of 0.4% MoM. It seems that consensus has now, indeed, shifted to favour a persistent slowdown in the recoveries of most of the large economies around the globe. The Delta variant of the coronavirus continues to cause disruptions in global supply chains, particularly in Asia. Other than the severe semiconductor shortages, this was one of the main reasons Ford and General Motors (GM) announced expanded plant shutdowns for September. In the US specifically Hurricane Ida weighed on oil production in the Gulf of Mexico.

Over the past year, shipping costs have surged dramatically. One estimate, the cost of hiring a forty-foot container, increased eight-fold from its pre-pandemic average. Others, such as the cost paid by container companies to operate vessels from shipowners, are up six-fold. Mostly, high shipping costs are a result of supply constraints, having too few ships and containers, amid a surging demand for traded goods, after the bubble of pent-up demand burst. These shortages were compounded by staff shortages and social distancing measures at ports, hauliers, and warehouses, as well as by freak weather events, such as the typhoons in China in August. Some expert global consultancies believe that higher shipping costs might cause global consumer prices to rise by as much as 2%. However, this, of course, depends on how much of the costs can be passed on to the consumer; we think this is more of a worst-case scenario. Some imports can even be delayed until costs have normalised but, given the view that this might take until the end of 2021, they might have to wait a while.

During this week, the US Federal Reserve (Fed) will, once again, meet to decide about monetary policy in the world's largest economy. Our view is that they will signal, but not formally announce, tapering, that is, a decline in the pace of quantitative easing. We still believe that the Fed will, most likely, start their tapering at a very slow rate by the end of 2021. However, the incoming economic activity data that is persistently weaker will allow them to keep interest rates unchanged for a long time, possibly until 2023.

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