COMMENTARY

ECONOMICS COMMENTARY: ECONOMIC IMPACT OF COVID19

17 March 2020, Tuesday, Durban.

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MKI Economics Commentary is a brief note intended to provide MKI's interpretation of key economic events such as the Budget, MTBPS, Monetary Policy (Interest Rates), Employment data releases and other topical economic events.

THE ECONOMIC IMPACT OF COVID19

Moses Kotane Institute supports the broad measures announced by His Excellency, Honourable President Cyril Ramaphosa on COVID 19 in his Nation address on Sunday, 14 March 2020. The measures would have been with full awareness of the economic impact against a backdrop of the Republic already in its second recession in 2 years with 2020 growth already revised downward to just 0.4% as recently as in the February budget.

WORST FINANCIAL MARKETS PERFOMANCE IN HISTORY, PENSIONERS TO PAY DEARLY

Monday, 16 March 2020 is officially the worst Johannesburg Securities Exchange share plunge ever recorded in history, falling by 12% taking its total losses in the past seven days to 17%. Pensioners and savers have therefore seen their holding plummeting. Losses have not been limited to share prices only, the yield on the government bonds reached 10.75% as at 17 Mar 2020 5:15 GMT, significantly raising government borrowing costs. This will likely result in larger budget deficit as more interest costs will be borne by government. Figures 1 & 2 below depicts the financial market turmoil as a result of COVID19.

Figure 1: JSE/FTSE ALL Share Price Index Performance Source: Investing Economics

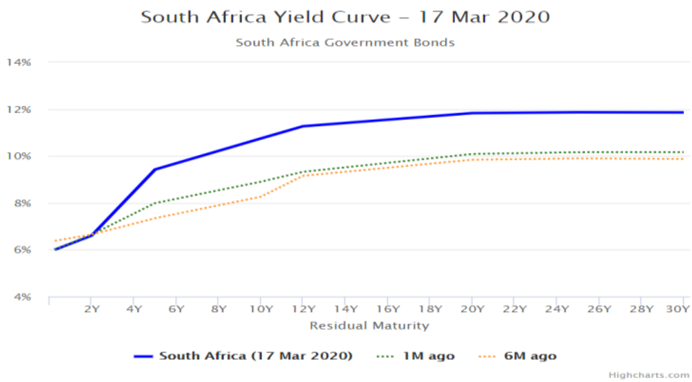

Figure 2: SA Bond Yield. Source: Highcharts.com

TOURISM, FINANCE, TRADE AND MANUFACTURING MOST AFFECTED ECONOMIC SECTORS

The impact of COVID19 is felt across the entire economy, however, the tourism, finance, trade (maritime) and manufacturing are the most affected economic sectors. Compounding the matters is the fact that these sectors account for large percentage of South Africa's GDP. Tourism has a multiplier effect of eight in terms of job creation. The entire value chain is being destroyed from airline, transportation, accommodation and related services. The important Meetings, Incentives, Conferences and Meetings subsector has grounded to a halt, with huge implications for the entire value chain. KZN in particular is very strong on Tourism, Trade (with two hugely important harbours), a strong manufacturing (including automobiles). South Africa relies on foreign portfolio investments (shares and bonds) to finance its huge trade account deficit. This has seen the rand reaching R16.52 as at 17 March 2020, 5h37 GMT. In all, the economy is taking a battering from the COVID19.

LOWER OIL PRICE AND INFLATION

The oil has been tumbling in the markets – consolation for the long-suffering South African consumer, reaching $31.41 as at 17 March 2020. This will result in a significant drop in local fuel prices. This will have positive effects on the general price levels. This will anchor inflation expectations to a range of between 4.2 to 4.5 percent in the short-term, supporting Moses Kotane Institute's view that the South African Reserve Bank (SARB) cuts interest rates to 5.75% from 6.25% at the conclusion of the Monetary Policy Committee meeting on Thursday, 19 March 2020. A full percentage point to 5.25% is possible given large moves by the US Federal Reserve Bank which cut interest rates to near zero percent, however, the SARB has tended to move interest rates by 25 basis points at each meeting.

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LIKELIHOOD OF RECESSION HEIGHTENED & LIMITED SCOPE FOR FISCAL AND MONETARY STIMULUS

Having already revised growth estimated to just 0.4% as recently as February 2020, there is an increased risk of growth curtailed to 0.2% at best and most likely a full year recession. In the absence of any fiscal stimulus, and if the COVID19 not stabilising by June 2020, recession is almost certain. Moses Kotane Institute is of the considered view that tools available to Treasury are very limited and are unlikely to stimulate the economy, the major constrains being a likely larger than anticipated revenue shortfall. Since there are major disruptions to large economic sectors such as tourism, retail and trade, industry profitability suffers significant drops which in turn will result revenue shortfall.

Moses Kotane Institute
INNOVATION. THE FUTURE

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RESEARCH INNOVATION MARITIME

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SOVERIEGN CREDIT RATINGS LIKELY REVISED FURTHER INTO JUNK STATUS

The markets have fully discounted the likelihood of credit ratings agencies moving the sovereign credit rating into junk status by Moodys and moving further deep into junk status by Fitch and S&P, especially if the pandemic does not stabilise by end of June 2020. The expected revenue shortfall, deterioration in debt metrics as a result of anticipated zero economic growth at best and recession as our economic estimates prediction.

INNOVATION, THE FUTURE

Organisations that have invested sufficiently in innovation, such as innovation in remote working, digital customer services will to an extent offer business continuity. An example is in higher education. Many institutions have activated plans to offer academic problems online. Organisations can do well to make digitisation of their services a core competitive strategy. Capabilities around telemedicine, for example, can prepare the country to better cope with disruption as a result of pandemic, such is the case in the present moment.

CONCLUDING REMARKS

There is no doubt whatsoever that the comprehensive response to the COVID19 is most welcome. The South African economy is taking a huge blows in all economic metrics as a result of the COVD1 pandemic. Losses are not only limited to the financial markets and sectors such as tourism, trade and manufacturing, the losses cut across the entire economy. Pensioners' savings are plummeting, industry profitability is being wiped off resulting in larger than planned revenue shortfall which will result in further deterioration in budget deficit and debt metrics. There is hardly any room to fiscal stimulation and the likely interest rate reductions will take time to work through the economy. In the current environment and in the absence of COVID19 stabilising before end June, recession is almost certain.