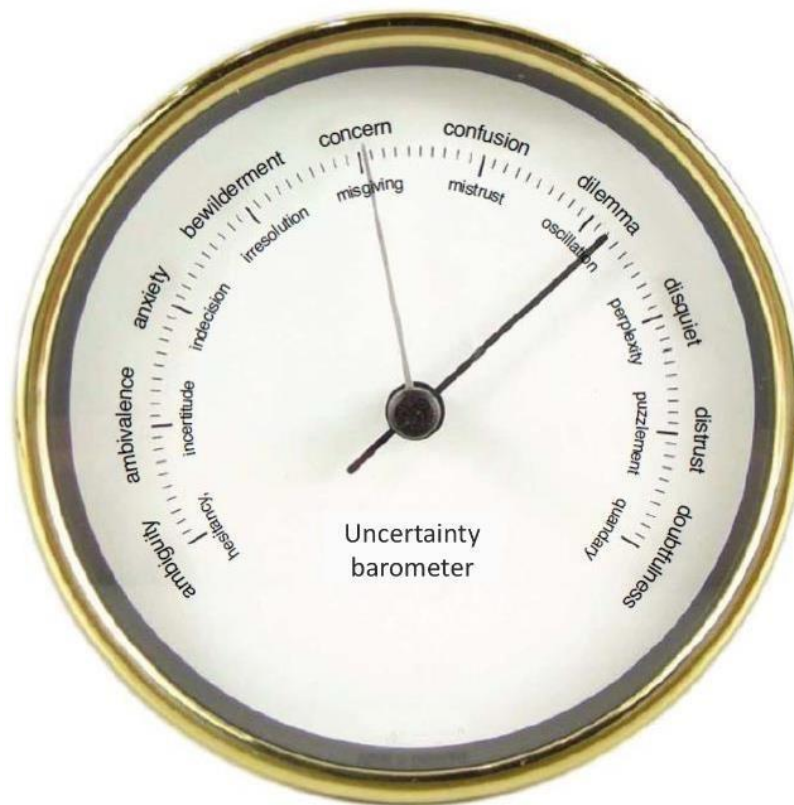




NWU Business School Policy Uncertainty Index (PUI) 4Q 2022



**EMBARGOED UNTIL
MONDAY
9 JANUARY 2023**



EXECUTIVE SUMMARY

- The NWU Business School 4Q 2022 PUI eased to 53.2 from 59.6 in 3Q 2022 (baseline 50). Although still in negative territory, the positive factors in the past three months outweighed the negatives ones to significantly reduce the 4Q 2022 PUI. The record elevation of the PUI in recent years owed much to a formidable combination of negative global and domestic factors that persisted for a while. But the calibration of the 4Q 2022 PUI suggests that some of these negative factors have either ameliorated, or are now being largely 'priced in' by the markets.
- Globally, the Russia-Ukraine war, inflation, recession fears and widespread uncertainty have nonetheless continued to shape world economic prospects. The International Monetary Fund (IMF) recently cut its 2023 global growth forecast from 2.9% to 2.7%. The IMF believes that more than a third of economies world-wide will have contracted by the end of 2022, or will do so during 2023.
- On inflation the good news is the mounting evidence that global inflation may have peaked, or is close to that point. Although future interest rate hikes in several key economies may be less aggressive, there is unlikely to be an early return to softer monetary policies. Several key markets appear to have adjusted to that scenario.
- While SA will not entirely escape unfavourable global developments positive trends in SA in recent months have included the much-better-than-expected GDP growth figures in 3Q 2022, a slight easing in the rate of inflation, lower fuel prices, improved employment figures, and a well-accepted Medium Term Budget Policy Statement in October. The re-election of President Cyril Ramaphosa as ANC President appears to have had a particularly favourable impact on the 4Q 2022 PUI.
- Negative factors that influenced the 4Q 2022 PUI included the shock resignation of Eskom CEO André de Ruyter, intensified load-shedding, the twin impact of high inflation and higher interest rates on disposable income of households, continued low business and consumer confidence levels, and residual uncertainties arising from the ANC's elective conference in December 2022. The SA economy is struggling to gain momentum in the face of various socioeconomic challenges. There are no grounds for complacency.
- A reduction in policy uncertainty nonetheless creates a useful platform on which to encourage new investment and job-rich growth. President Ramaphosa has a strong political mandate to tackle the domestic constraints on SA's economic performance, such as on the energy front. The big challenge in 2023 remains the rapid and successful implementation of key economic reforms that further reduce policy uncertainty and ignite confidence.

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NWU BUSINESS SCHOOL POLICY UNCERTAINTY INDEX (PUI) IN 4Q 2022 EASED TO 53.2 COMPARED TO 59.6 IN 3Q 2022 (baseline 50), BUT REMAINS IN NEGATIVE TERRITORY

“Among the FUNDAMENTAL structural reform items is POLICY CERTAINTY. Simple but fundamental to the investor community. Remember that you cannot force people to invest, but you can create an environment which makes it easier to invest, create jobs and, hey presto, develop the country” (former Finance Minister Tito Mboweni, 16/12/2021)

1. INTRODUCTION

As outlined when the PUI was launched in early 2016, the role of policy uncertainty has loomed large in much of the recent economic debate in SA. It is seen to have important implications for business confidence and the investment climate in the country. Hardly any recent economic assessment or media release from international or local financial institutions, business lobbies, economic analysts, financial journalists, or credit rating agencies appears without the inclusion of the words 'policy uncertainty' occurring in them.

The design of a policy uncertainty index for SA has nonetheless been spurred not only by economic circumstances in the country, but also by the increasing academic and policy interest globally around the cause, effect, measurement, and definition of policy uncertainty. There is now a 'World Uncertainty Index' (WUI) created recently by the IMF and Stanford University to calibrate rising levels of policy uncertainty in the global economy.

There have been many manifestations of policy uncertainty in SA over the years. The institutional setting and policy making environment clearly influence the extent to which negative shocks and developments lead to bad outcomes and tough policy challenges. It seemed that the time had arrived to craft a more accurate measurement of this recurrent factor in SA's economic outlook. A deeper understanding of how uncertainty 'shocks' affect the SA economy helps policy makers to assess how future shocks will impact markets and business. The outcome of this research will now be made regularly available on a quarterly basis to hopefully fill a gap in our monitoring of the economic environment.

Interesting correlations have been found of the policy uncertainty index with economic outcomes. Empirically it shows that when economic policy uncertainty is strongly present in the environment, it indeed lowers investment, employment, and output. High levels of such policy uncertainty inhibit meaningful investment and consumption. Elevated policy uncertainty in many countries contributes to sluggish growth. Economic policy uncertainty then has actual consequences for the economy.

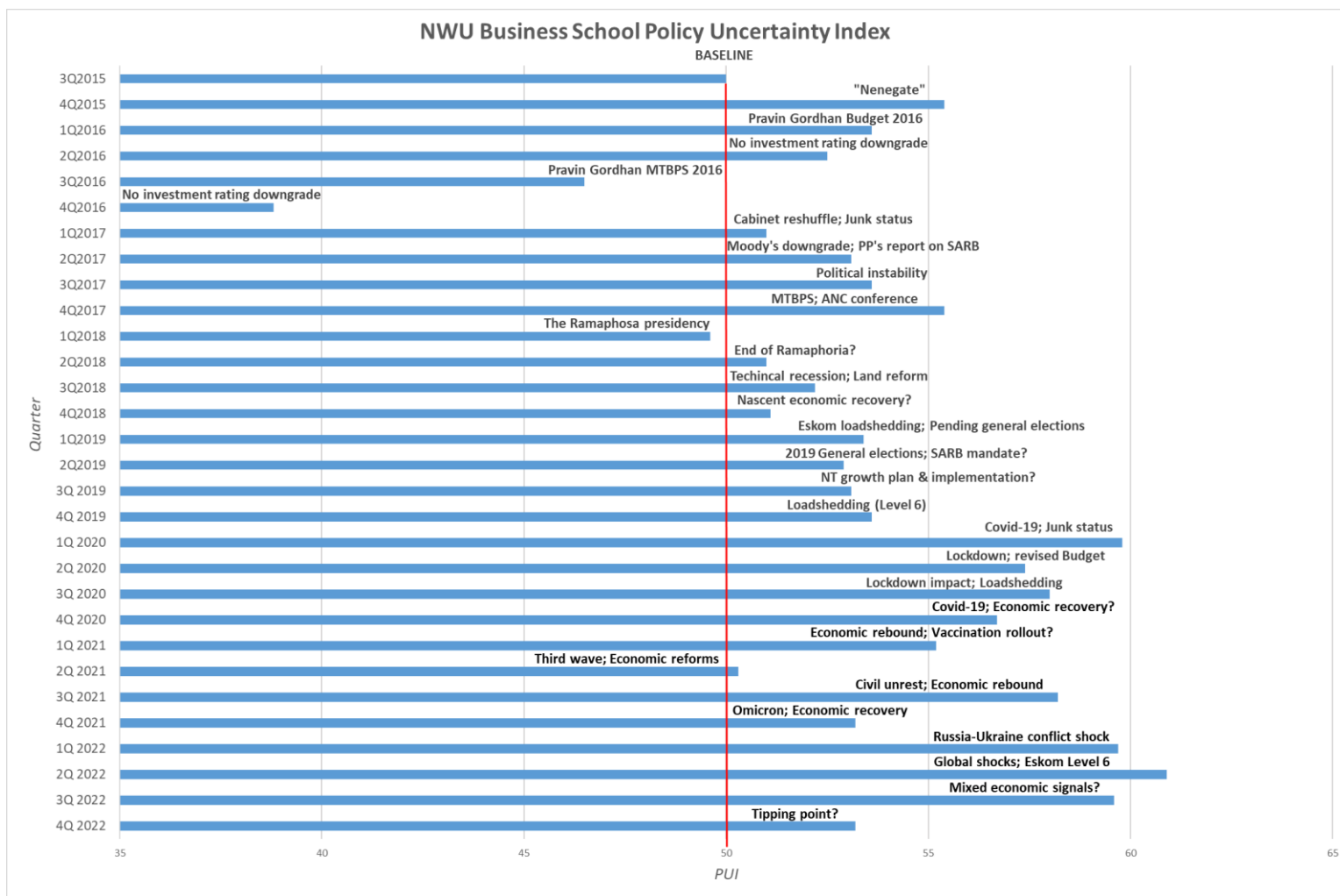
The PUI is published in January, April, July, and October of each year. An increase beyond 50 reflects heightened policy uncertainty; a decline in the PUI means reduced uncertainty. The value of the PUI as a proxy for policy uncertainty will lie in tracking changes in policy uncertainty over time.

2. PUI RESULTS FOR 4Q 2022 - WHAT DO THEY SAY?

The PUI is the *net* outcome of *positive* and *negative* factors influencing the calibration of policy uncertainty over the relevant period. The results show that the 4Q 2022 PUI at 53.2 eased considerably from the 3Q 2022 PUI at 59.6, but remains in negative territory (baseline 50)

Unpacking the three elements constituting the latest index shows the following:

- i. *media data* reflected a decrease in references to economic/policy uncertainty
- ii. the *survey of economists* indicated that policy uncertainty had declined
- iii. University of Stellenbosch's Bureau for Economic Research *survey of manufacturers* experiencing policy/political uncertainty increased from 76 to 83



3. NARRATIVE ON FACTORS INFLUENCING ECONOMIC/POLICY UNCERTAINTY

3.1 Global Economic Outlook

On the international scene the Russia-Ukraine war, inflation and recession fears have continued to strongly shape the economic prospects of many economies as the year had unfolded. The three major 'locomotives' driving the world economy – the US, Europe, and China – are all to a greater or lesser extent slowing down. They will continue to do so into 2023. China in particular is now expected to show its weakest economic growth in several decades.

In a recent survey the International Monetary Fund (IMF) forecast that more than a third of economies world-wide will have contracted by the end of 2022, or will do so during 2023. The World Bank (WB) therefore believes that, in these more vulnerable circumstances, even a small shock could knock the global economy off course and precipitate a wider recession. It would seem that economic growth and interest rates are now the two main variables to watch globally in 2023.

The IMF has cut its overall 2023 global growth forecast from 2.9% to 2.7%. Growth predictions from the private sector have been more bearish. The IMF believes there is a one-in-four chance that global growth will fall below 2% in 2023 and a probability of 10%-15% that it will drop below 1%. The IMF again stressed that the general global outlook 'remains fraught with uncertainty'.

On the positive side it may be that the basic resilience of the US economy means only a mild recession or a 'soft landing' there, despite much higher interest rates. 'In short', says The Economist (10/9/2022), 'the dollar is the go-to currency because America has proved a reliable source of economic growth.' What, of course, is needed to weaken the dollar is that the global growth 'gap' must narrow and for growth prospects outside the US to improve.

On the inflation front there is mounting evidence that global inflation may have peaked, or is close to that point. Central banks, however, remain cautious. And although future interest rate hikes in several economies may be less aggressive as we move into 2023, there is unlikely to be an early return to softer monetary policies. Central banks, including the US Fed, will want to see more definitive evidence of declining inflation – and even in some cases likely rising unemployment – before cutting interest rates. Several markets are gradually adjusting to that scenario.

Regarding Sub-Saharan Africa the IMF expects the region's GDP growth to have slowed sharply by more than 1% to 3.6% in 2022 and to remain at about that level in 2023. This is the inevitable outcome of the above-mentioned slowdown in advanced economies and emerging markets, tightening global financial conditions and volatile commodity prices. In a region already wearied by ongoing shocks (such as Covid-19) rising food and energy prices are severely impacting on the vulnerable. The IMF says that public debt and inflation in Sub-Saharan Africa are at levels not seen in decades.

These deteriorating economic conditions are also creating serious socio-political tensions. Earlier this year The Economist (25/6/2022) built a statistical model demonstrating that rises in food and fuel

prices were, under certain conditions, a strong portent of political instability. The risks for economic growth in Sub-Saharan Africa are presently on the upside, the extent depending on what steps are taken to offset or mitigate the escalating pressures. And the SA economy?

3.2 The South African Economy

3.2.1 Balance between positive and negative factors influencing the 4Q 2022 PUI

As 2022 drew to a close the NWU Business School PUI eased significantly from 59.6 in 3Q 2022 to 53.2 in 4Q 2022. Exceptional circumstances have combined in recent times to strongly elevate the PUI, ranging from Covid-19 to geopolitical developments, civil unrest, and record Eskom load-shedding (see PUI chart). But the calibration of the 4Q 2022 PUI suggests that some negative factors have either ameliorated, or are now being largely 'priced in' by markets

Externally, the immediate global implications for the SA economy have registered in five broad uncertain ways: the continued Russia-Ukraine war; the accelerated slowdown in the world economy, including for Sub-Saharan Africa; weaker international commodity prices; the outlook for energy and food prices; and a world that has moved into a cycle of 'dearer money'.

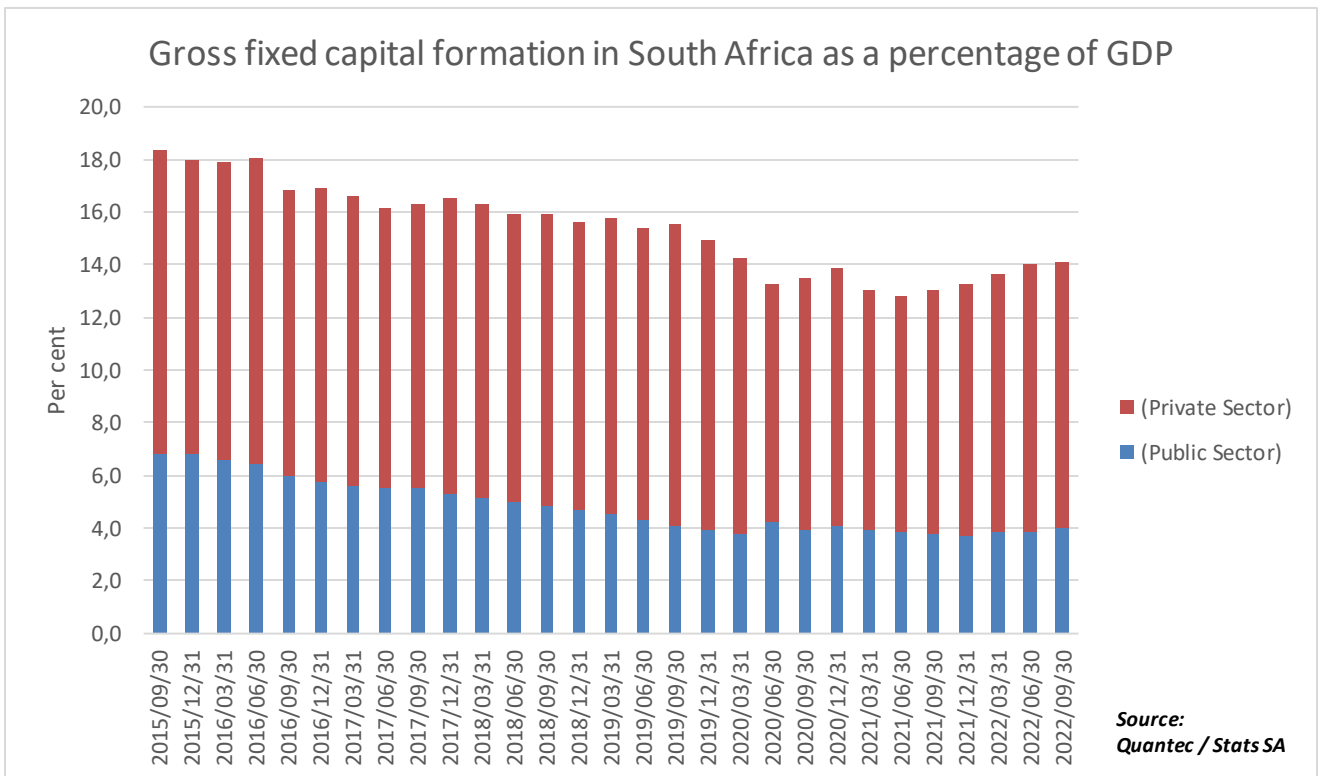
But positive trends in SA in recent months included the much better-than-expected GDP growth in 3Q 2022 (after negative growth in the second quarter), a slight easing in the rate of inflation, lower fuel costs, better employment figures, additional anti-corruption steps, a well-accepted Medium Term Budget Policy Statement (MTBPS) in October and the leadership outcome of the ANC 55th elective conference in December. The credit rating agencies have also maintained a stable outlook for SA, although the 'junk' investment rating itself remains unchanged for now.

In particular, SA's real GDP in 3Q 2022 rose by 1.6%, which was well ahead of consensus forecasts of only 0.4%. While there may also have been technical reasons for this outcome, the upshot is that growth forecasts have had to be revised upward. For 2022 as a whole growth is now likely to be about 2.3% (instead of the consensus view of 1.8%) and for 2023 GDP growth may be about 1.4% (instead of the consensus view of 1.2%). This surprise GDP growth was largely driven by agriculture with its bumper crop yield, together with support from most other sectors of the economy.

Political developments may also have played an important role. The re-election of President Cyril Ramaphosa as ANC President at the recent ANC elective conference appears to have had a particularly favourable impact on the 4Q 2022 PUI. President Cyril Ramaphosa emerged from the conference with a strong mandate and majority support in the hierarchy of the governing ANC. Business and the markets perceived the new ANC leadership as committed to expediting economic reform and implementing pro-growth policies and projects in 2023.

On the other hand, the factors keeping the 4Q 2022 PUI in negative territory included:

- the shock resignation of Eskom CEO André de Ruyter in mid-December put a big question mark over the future role and functioning of Eskom. Although the further intensified Eskom blackouts during 4Q 2022 took their toll on economic and business activity, business and markets saw De Ruyter as a stable factor broadly moving Eskom in the right direction in its future financing and restructuring.
- the continued weakening in household spending as high inflation and higher interest rates increasingly had a negative impact on disposable income (SARB Quarterly Bulletin, December 2022). Food inflation continued to erode household budgets, especially of poor and working-class families. Interest rates in SA will rise further in 2023, though probably at a slower pace. Business and consumer confidence have persistently remained at low levels.
- higher fixed capital formation has remained modest and as yet is an insufficient pillar for the job-rich growth that SA needs (see chart) Over the next decade the percentage of total fixed investment to GDP needs to almost double, from its present 14% to about 25%, if SA is to attain and sustain inclusive economic growth rates well beyond 2%.



- as 2022 drew to a close it remained uncertain as to, firstly, how soon the stronger political mandate would indeed translate into rapid and tangible implementation of urgent economic reforms, such as around Eskom and, secondly, what resolutions affecting the economy would have been decided at the postponed ANC ‘hybrid’ conference on January 5. How these factors unfold and interact at the policy level will play a big role in the prospects of shifting the PUI into positive territory in 2023.

3.2.2 Summary and Conclusion

The SA economy is struggling to gain momentum at a time of serious socioeconomic challenges. But a lower level of policy uncertainty creates an opportunity to strengthen SA's economic prospects. President Cyril Ramaphosa now has a strong political mandate that must be visibly translated into tangible implementation of a positive reform agenda that has urgency and momentum in 2023. The ball therefore remains largely in SA's court.

Stronger economic growth in SA now requires multi-tiered good news on the implementation front in 2023, especially on energy matters. Absent that, it is hard to see the economy attaining the levels of investment and job creation that it needs. There is no room for complacency. The big challenge in unlocking SA's true economic potential remains the rapid and successful implementation of key domestic reforms that further reduce policy uncertainty and ignite confidence.

North-West University Business School

9 January 2023