NWU Business School Policy Uncertainty Index (PUI) 3Q 2023

EMBARGOED UNTIL MONDAY 2 OCTOBER 2023

EXECUTIVE SUMMARY

- Although remaining well in negative territory, the NWU Business School PUI for 3Q 2023 declined to 71.8 from 76.2 in 2Q 2023 (baseline 50). While several contrary factors kept the PUI elevated, there were apparently enough positive ones to bring the PUI slightly lower over the past three months.
- Globally, there is a continued overall slowdown in the world economy. World economic growth is now estimated by the IMF to be about 3% in 2023, and global commodity prices are lower. New uncertainties have arisen around the Chinese economy, with growth there now being forecast to be only about 4% in 2024.
- Global inflation in 2023 is expected to fall from 8.7% to 6.8%, but underlying (core) inflation is projected to decline more slowly. The US Fed decided on September 20 to again keep interest rates unchanged but warned that further rises were still possible. The US economy still appears to be the strongest 'locomotive' in the world economy.
- A positive development in SA was the better-than-expected GDP growth of 0.6% in 2Q 2023. This was allied with stronger high-frequency data for the manufacturing sector in 3Q 2023, encouraging gains in certain confidence indices, and firm evidence of increased private investment in renewable energy.
- Inflation is now within the SARB's 3%-6% target range. At its meeting on September 21, the SARB's Monetary Policy Committee (MPC) decided by a 3-2 vote on a 'hawkish pause' to again keep interest rates unchanged for now.
- Another source of potentially positive news was the closer collaboration between business leaders and government to tackle urgent challenges in the crucial spheres of energy, logistics and crime. The successful BRICS summit in August also had a useful business spinoff.
- Nonetheless, there is still a high degree of volatility and uncertainty in SA's current growth dynamics, especially as heavy load-shedding resumed for most of September. Household finances also remain under strain. Another negative factor was the renewed sharp deterioration in SA's public finances and uncertainty as to how this will be managed in the Medium-Term Budget Policy Statement (MTBPS) on November 1.
- Fixed capital formation trends are now looking better, but consumer spending is still under great pressure. The MPC, presently, sees the risks to the growth outlook as 'balanced'. GDP growth in 2023 will be positive but is still only likely to be about 0.6%. The economy struggles to gain momentum in the face of global and domestic headwinds yet remains surprisingly resilient.
- Negative trends like policy uncertainty are reversible and remediable. Stronger economic growth now requires multi-tiered good news on the implementation front, especially on the energy outlook. SA must, therefore, urgently implement the remedies, reforms and growth positives available to promote a stronger economic turnaround in the months ahead.

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"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 policymakers 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 between the policy uncertainty index and 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 each year in January, April, July, and October. 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 3Q 2023 – 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.

Unpacking the three elements constituting the latest PUI shows converging trends as follows:

i. *media data* reflects a decline in references to policy uncertainty
ii. the *survey of economists* gauges that the level of uncertainty remains broadly unchanged
iii. The University of Stellenbosch's Bureau for Economic Research *survey of manufacturers* experiencing policy/political uncertainty is slightly lower at 84, compared to 86 previously

3. NARRATIVE ON FACTORS INFLUENCING ECONOMIC/POLICY UNCERTAINTY

3.1 Global Economic Outlook

According to the International Monetary Fund (IMF), global economic recovery is still slowing, but across widely divergent sectors and regions. Global growth is projected to fall from a previously estimated 3.5% to 3.0% in both 2023 and 2024. While the forecast for 2023 is modestly higher than predicted earlier in the year, it remains weak by historical standards. The SARB's latest forecast for 2023 global economic growth is 2.6%. In a September report, the OECD described the global economy as more resilient than expected this year but sees the 2024 growth outlook as weak.

Global inflation in 2023 is expected to fall from 8.7% to 6.8%, but underlying (core) inflation is projected to decline more slowly in several economies. US headline inflation rose to 3.7% in August amidst a sharp hike in energy prices. US core inflation then also accelerated for the first time in six months. International commodity prices continue to be volatile. Commodity price trends, especially in the energy and food spheres, partly reflect the geopolitical uncertainties which continue to permeate global economic prospects.

A BUSA cargo report (8/9/2023) says that Oxford Economics sees global trade declining by 1.5% in 2023, as compared with the World Trade Organization's (WTO's) 1.7%. Risks to the WTO forecast are said to be on the downside, thus highlighting the prevailing uncertainty about the outlook for the global economy. There have been negative developments in the Chinese economy that create uncertainty. A few months ago, the large Chinese economy was rebounding in a highly positive way, but it has recently dissipated into weak growth and deflation.

Commodity exporters are especially vulnerable to China's slowdown. The Chinese economy absorbs about a fifth of the world's oil, half of its copper, nickel and zinc, and three-fifths of its iron ore. China's setback comes at a time when most of the rest of the world, especially the US economy, remains on balance a positive 'locomotive' for the global economy. Fortunately, Chinese industrial output and retail sales have lately shown encouraging signs of stabilising, as a worst-case scenario of a 'hard landing' for China's economy would be bad news for the global economy.

There also remain concerns about the outlook for the eurozone economy, which has shown a mixed economic performance. There have again been both 'leaders' and 'laggards' in the euro-zone. Higher interest rates have begun to affect the European economy, as intended by the European Central Bank's (ECB's) tough stance on wanting to reduce inflation. The impact of tougher monetary policy is expected to peak in the eurozone towards the end of 2023, although unemployment has remained low for now. On September 14, the ECB again increased interest rates to a record level as the Bank decided to put curbing inflation as its highest priority.

On the other hand, strong US economic growth this year continued to defy forecasters. Despite widespread predictions of a slowdown, recent better-than-expected data suggests American economic growth may exceed 2% in 2023 as a whole. On the inflation front, it seems the US Fed will keep interest rates higher for longer. At its meeting on September 20, the Fed again held borrowing costs unchanged for now but warned of possible interest rate increases later if inflation worsens. Expert opinion remains divided on the prospects of a 'soft landing' for the US economy.

Amidst the global slowdown, the IMF expects GDP growth in sub-Saharan Africa (SSA) to decline to 3.6% in 2023. Although the IMF again emphasised that the reduced SSA growth masks significant variations across the region, painful austerity and economic adjustments continued to assail many economies as they grappled with rapidly rising public debt and social tensions. For the African continent as a whole, a positive development was the acceptance of the African Union (AU) as a permanent member of the G-20 group of countries on September 7.

3.2 South African Economic Outlook

Although remaining well in negative territory, the 3Q 2023 PUI showed a welcome easing to 71.8 from its historical high of 76.2 reached in 2Q 2023. While negative factors shaping the PUI were still strong enough to keep the PUI highly elevated, there were enough positive factors to outweigh the negative ones sufficiently to reduce the PUI to its present level. The persistence of high policy uncertainty – both globally and domestically – nonetheless remains a significant factor in the economic outlook.

On the positive side, in SA, the better-than-expected GDP growth of 0.6% in the second quarter of 2023 was again good news. This was mainly the outcome of more moderate Eskom blackouts in June compared with April and May, together with other encouraging trends that helped generate positive growth figures. Economic growth forecasts for 2023 as a whole are now converging on about 0.6% - 0.7%. The SARB's composite leading business cycle indicator increased by 0.1% in July 2023, reflecting a measure of resilience in the economy. However, there remains a high degree of volatility in SA's growth dynamics.

Inflation indices continued to reflect a declining tendency for some months. However, with both headline inflation and producer inflation rising again in August, it suggests that inflation may be 'sticky' for the time being. At its meeting on September 21, the Monetary Policy Committee (MPC), in another 'hawkish pause' again kept borrowing costs unchanged for now. The period of stability in borrowing costs since May has been a positive factor in business and consumer confidence in current economic circumstances.

In addition, the outlook in the agriculture sector is broadly positive. And fixed capital formation generally also appears to now be showing a more positive trend. The MPC revised its GDP growth forecast for 2023 as a whole upward from 0.4% to O.7% while leaving its 2024 growth expectation unchanged at 1%. At present, the SARB assessed the risks to the medium-term growth outlook to be 'balanced'.

The successful BRICS summit held in Johannesburg in August had a valuable spinoff through the active participation by business. The BRICS summit was a valuable enabler and facilitator of new trade and investment opportunities in a changing BRICS landscape. SA will nonetheless now need to strategise afresh to help turn the bigger decisions taken at the BRICS summit into reality, while also ensuring that they indeed become the vehicle for progressive economic gains for the country as a whole.

Another source of potentially better news has been the current closer collaboration between senior business leaders and government to unblock three immediate policy priority areas of energy insecurity, logistical challenges at Transnet, and crime levels. If successful, the outcomes could help to enhance predictability and reduce uncertainty as to what government may do next in key performance areas that are essential to underpin stronger economic growth.

On the negative side, however, the economic outlook for the rest of the year was recently described by a Nedbank survey as 'bleak'. Consumer spending is under great pressure. High-frequency economic data, such as retail sales and credit demand, have weakened as a result of higher borrowing costs and inflation, which have squeezed disposable income. Monetary policy remains restrictive. There is also the unfolding scenario of 'a tale of two deficits' for SA in the period ahead – in both the balance of payments and public finance spheres.

And although the manufacturing sector has improved in recent months, its future momentum could be constrained by negative developments as a result of persistent load-shedding, logistical challenges and vulnerable consumer demand. Consumer and business confidence are not yet high enough to strongly support economic activity. There remain serious delivery challenges at different levels. Unless ameliorated, these negative factors may impart a brittleness to the economic outlook as 2023 draws to a close.

A key source of additional uncertainty has been the serious deterioration in SA's public finances as tax revenues have fallen and government spending has remained high. The fiscal outlook is now much worse than projected in the February Budget. Weak corporate taxes and the higher public sector wage bill are the primary culprits. In its recent MPC statement, the SARB also warned that if serious fiscal sustainability concerns raise SA's risk premium, this leads to elevated interest rates.

The Treasury is now wanting an overall 'freeze' on public sector spending at various levels – but the full impact on the economy remains uncertain until the fiscal picture becomes clearer. The key Medium Term Budget Policy Statement (MTBPS) on November 1, therefore, needs to provide certainty as to how heightened fiscal risks will now be managed. With national elections pending in 2024, MTBPS fiscal decisions are likely to be a 'tug-of-war' as to the right, but tough, policy trade-offs needed.

Social unrest in SA may have a negative impact on the economy ahead of next year's national elections. RMB Chief Economist and Head of Research Isaah Mhlanga, commenting in the latest RMB/BER Business Confidence Index, says: "It will become increasingly important to also consider the impact of unrest, such as recently seen in the Western Cape, on South Africa's economic fortunes in the run-up to the national elections next year."

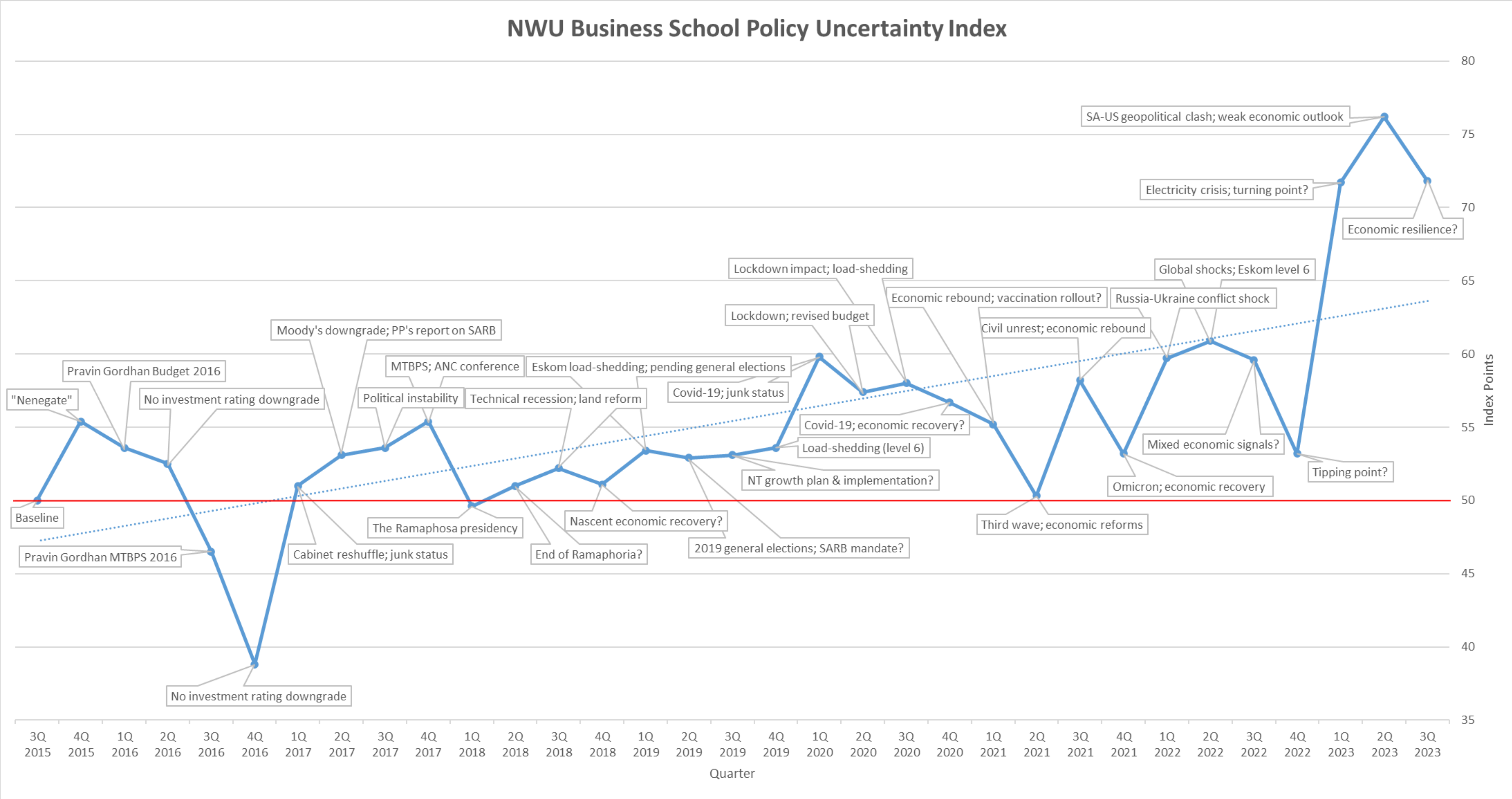
3.3 Summary and Conclusion

Although lower, in 3Q 2023, the PUI remains well in negative territory for now. The Ten-Year Review of the National Development Plan (NDP) recently released by the National Planning Commission (NPC) urges that, *inter alia,* "in the immediate term SA needs to deal with policy uncertainty, and significantly enhance policy coordination and coherence." The NPC further pleads for "consistency in government policy and engagement with stakeholders." (Ten-Year Review of the NDP 2012-2022, p. 52).

Unless ameliorated, negative factors could inject brittleness into SA's economic resilience. SA's weak economic performance thus again emphasises the urgent need for growth-friendly policies. Economic growth now requires multi-tiered good news regarding the implementation of policies and projects, especially to provide energy security. Negative trends like policy uncertainty are reversible and remediable if the right steps are taken in a timely fashion.

Delivery requires sustained prioritisation. SA must, therefore, urgently build on the remedies, reforms and growth positives that are available. As SA moves ahead, the domestic challenge remains to expedite the implementation of half-forged policies and projects that can reduce policy uncertainty, strengthen investor confidence, and facilitate a policy environment that is solid, coherent and consistent.

North-West University Business School
2 October 2023


NWU Business School Policy Uncertainty Index
Index Points
Quarter
80
75
70
65
60
55
50
45
40
35
3Q 2015
4Q 2015
1Q 2016
2Q 2016
3Q 2016
4Q 2016
1Q 2017
2Q 2017
3Q 2017
4Q 2017
1Q 2018
2Q 2018
3Q 2018
4Q 2018
1Q 2019
2Q 2019
3Q 2019
4Q 2019
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2Q 2020
3Q 2020
4Q 2020
1Q 2021
2Q 2021
3Q 2021
4Q 2021
1Q 2022
2Q 2022
3Q 2022
4Q 2022
1Q 2023
2Q 2023
3Q 2023
Baseline
"Nenegate"
Pravin Gordhan Budget 2016
No investment rating downgrade
Pravin Gordhan MTBPS 2016
No investment rating downgrade
Cabinet reshuffle; junk status
Moody's downgrade; PP's report on SARB
Political instability
MTBPS; ANC conference
The Ramaphosa presidency
Technical recession; land reform
End of Ramaphoria?
Eskom load-shedding; pending general elections
Nascent economic recovery?
2019 general elections; SARB mandate?
Covid-19; junk status
NT growth plan & implementation?
Load-shedding (level 6)
Lockdown; revised budget
Lockdown impact; load-shedding
Covid-19; economic recovery?
Economic rebound; vaccination rollout?
Civil unrest; economic rebound
Third wave; economic reforms
Omicron; economic recovery
Russia-Ukraine conflict shock
Global shocks; Eskom level 6
Mixed economic signals?
Tipping point?
Electricity crisis; turning point?
SA-US geopolitical clash; weak economic outlook
Economic resilience?