The economic outlook may look bleak – but it is not all bad news

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It is tempting to panic when markets are uncertain, but knee-jerk reactions and deviating from your investment plan are not the best ways to navigate the turbulence. In a recent Glacier webinar, Patrick Mathabeni, Research and Investment Analyst at Glacier Research, unpacked the current challenges that consumers feel at a global and local economic outlook level and that are profoundly impacting investments and wallets, but it's not all bad news.

Where has my money gone?

An increase in inflation feels like your money is being 'eaten'. In practical terms, the items in your shopping basket that cost you R100 last year, may be costing you upwards of R120 now. Or if you still only have R100 to spend, you will probably find yourself having to remove some items from your basket when you reach the till. Currently global consumer inflation is at historic highs, and this finds its roots in many factors – chief of which is the excessive monetary policy easing by central banks during COVID-19, coupled with global supply chain bottlenecks and the prevailing war between Russia and Ukraine.

The drivers of US inflation

Patrick lists a number of factors that have contributed to the current US inflation rate:

1. In the last 18 months, the energy crisis and rocketing housing and food prices have added to the woes.
2. The US has the lowest unemployment rate in many years, over 6 million people (+/-3.6%) were reported to be unemployed and around 12 million jobs are available on the job market. Interestingly, over 4 million Americans have quit their jobs voluntarily over the past 18 months or so[1]. And here's the conundrum:
    - The high inflation needs to be slowed.
    - There are too many jobs chasing too few people which means wages and salaries have

    to be increased to attract people back into the job market.
    - Raising wages increases inflation.
3. Slowing global growth – growth projections have been revised down significantly between 2021 and 2023.

How did we get here?

Here are some of the reasons for the current economic outlook and why we are feeling the crunch:

1. COVID – the shutdowns and economic - as well as social - lockdown, was a trigger event for a crisis in the markets. Recovery has been slow.
2. Overstimulation of the US economy. $1.9 trillion in a stimulus package was created – money given to people to sustain them through lockdown and to ensure that the economy would keep going.
3. Global supply chain pressure – the stop-start scenario of many economies during COVID and the shortage of labour meant that goods supplied were not meeting the demand, therefore pushing prices up.
4. The US Federal Reserve ignored inflation for a while, describing it as transitory. They continued the stimulus package for too long. Now the only solution to reduce inflation is to raise interest rates.
5. The war in Ukraine -Russia is a key producer of oil and other natural resources globally. The war and the consequent sanctions in Russia, in part, have contributed to supply disruptions and the increase in fuel and commodity prices. Ukraine, on the other hand, is a large global producer and exporter of wheat and maize, which also contributed to the rise in food prices.

On the home front in SA

In the local economy, unemployment remains one of the biggest challenges of our time. While 40 million South Africans could and should be employed, only 14.9 million have jobs. Our other challenges are well-known:

- Unsustainable debt levels which make up 70% of the national GDP, giving rise to significant debt servicing costs.
- Eskom remains another key challenge to the SA economic outlook. Firstly, from an economic growth point of view given the impact of power outages on all sectors. Secondly, the utility's debt levels are unsustainably high.
- South Africa's muted growth. Our economy is largely driven by consumption rather than production. We also have the lowest levels of fixed capital investment in manufacturing, mining and infrastructure – projects that could potentially employ hundreds of thousands of people.
- The likelihood of a further hike in the interest rate. A consumption-led economy like South

Africa depends on people spending to drive the economy. An increase in the interest rate means pressure on the consumer's spending power. This leads to a slowing economy and a negative impact on consumer confidence. Increasing the interest rate, though, may be the only way to contain inflation.

- The conundrum of the weak rand. From a market point of view, a weaker rand is good for rand-hedge stocks (which generate substantial revenue offshore). However, a weaker rand in the context of dollar-denominated debt, is not supportive. A weaker rand is also very challenging in the context of oil imports which are paid for in dollars. This will impact adversely on the fuel price for the consumer.

The silver lining

Here some of the positives that can take the edge off our collective anxiety:

1. We received mining revenue overruns, which were used to pay debt and pay social grants during COVID.
2. SA bond yields are attractive. They are also amongst the most attractive in the world on a real yield basis. Currently 10-year bond yields are in excess of 10%, while inflation is around 7.5%.
3. SA equities continue to offer compelling valuations, but one has to be selective in this environment and partner with an appropriate fund manager

Keep calm and do nothing – for now

Patrick suggests some ways to navigate the turbulence:

- Find ways to spend less and manage your personal budget.
- There are ways to save and invest, even in tough economic times and looming interest rate hikes.
- Remain invested in growth assets. They tend to do better than bonds in the long term as inflation can be passed onto consumers (in the case of companies with strong competitive positions).
- Diversified investment portfolios continue to be the best investment course to navigate this environment.
- Stick to your long-term investment plan. And consult your adviser before making any changes in your investment plan.

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[1] The Great Resignation in the US has been a result of a variety of factors, some of which are related to workplace dissatisfaction; wanting to continue with remote working but not being given the freedom to do so by their employers; burnout from long working hours during COVID (especially essential services workers); and the COVID stimulus package.

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