TAX YEAR-END SAVINGS

Economic update

Reviving South Africa's economic growth – we need fiscal credibility, economic reforms and an investment drive.

Global outlook – slightly more positive

Global economic growth has stabilised but remains weak. The slowdown in the United States and China is however expected to be more than offset by improvement in some large emerging markets, the euro area and the United Kingdom. Inflation expectations remain stable, at or below targets in advanced economies and trending lower in emerging markets. Consequently, interest rates in many advanced economies are expected to remain low, which will support global growth.

The direction of the US dollar has a disproportionate impact on the global economy as global trade is priced in US dollars to a large extent. The US dollar is expected to weaken against major currencies, which implies little exchange-rate related inflation in emerging markets. This will help emerging market economies and global economic growth.

The biggest four global risks that dominated financial markets in 2019 have been reduced:

- US–China phase one trade deal
- Boris Johnson's decisive victory in the UK elections
- De-escalation of the US–Iran tensions
- US recession risks.

Domestic outlook – lifting economic growth

With a marginally positive global outlook, we would have expected South Africa's economic growth to pick up as well. However domestic constraints, including electricity shortages, a weak consumer demand, and a constrained fiscus all contribute to a weak economic growth outlook of about 1.0% this year and 1.5% in 2021.

To improve this growth outlook, three things are needed:

1. **Re-establish confidence in the management of the country's finances**
   This requires National Treasury to achieve the budget targets they set.
2. **Implement economic reforms**
   The required reforms have been discussed at length – what remains is faster implementation, which has marginally improved so far.
3. **Attract fixed investment**
   The success of implementing economic reforms will attract fixed investment, which will ultimately lift economic growth.

Inflation remains low

Inflation has been lower than expected for most of 2019 and the outlook remains benign. The SARB has cut interest rates by 0.25% to 6.25% to boost consumer demand; however, the impact of this rate cut on economic growth is negligible.

There is still room for more cuts but the risk of a downgrade in the country's credit rating from Moody's keeps the SARB cautious. The credit rating downgrade is largely expected by financial markets so the impact on asset prices will likely be limited. However, the impact on the economy, following a downgrade, is usually painful and lasts for a very long time depending on the speed and extent of the action taken by Government.

Financial market performance and outlook

Global markets have performed relatively well in 2019 compared to 2018. Developed market equities, driven by US equities, outperformed emerging markets and local equities. Global bonds underperformed other global asset classes, which is a reversal of 2018 market dynamics where bonds performed better than equities.

The Johannesburg Stock Exchange performed in line with emerging markets but domestic economic issues limited the investment returns. Resources shares, largely the gold and platinum sector, performed well, while financials had poor returns.

The longer-term trend has been towards lower investment returns, which we have highlighted over the past few years. However, for 2020, emerging markets equities appear cheap and with stronger fundamentals. In similar fashion, domestic equities also appear cheap, which should benefit investors who have added holdings of local equities in their portfolios. Local bonds also continue to offer attractive interest rates, particularly in an environment where global bonds offer negative or close to zero interest rates.