

COVID-19

The possible economic consequences of COVID-19 for South Africa

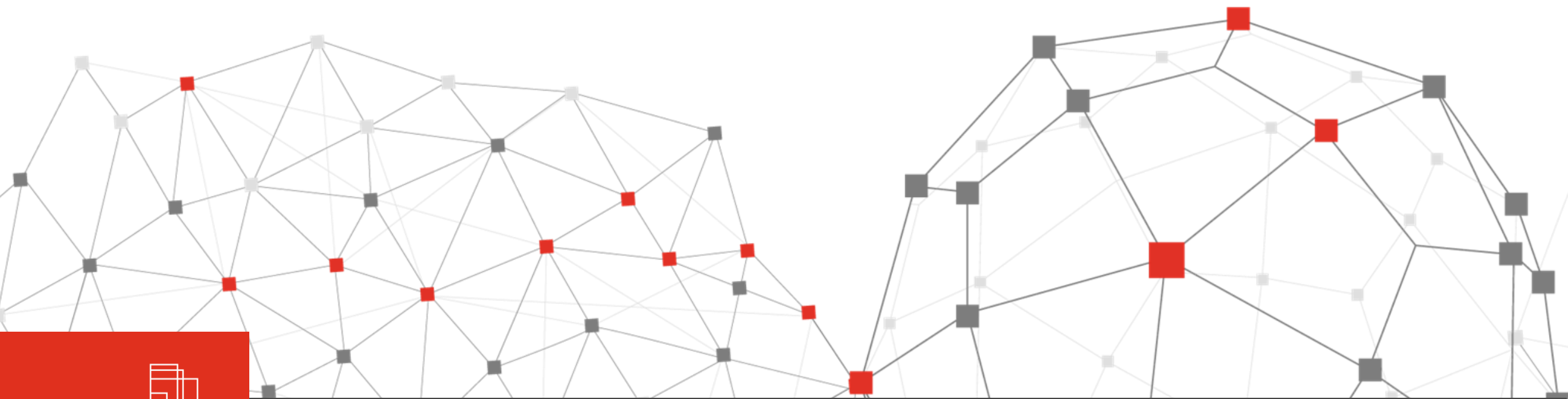


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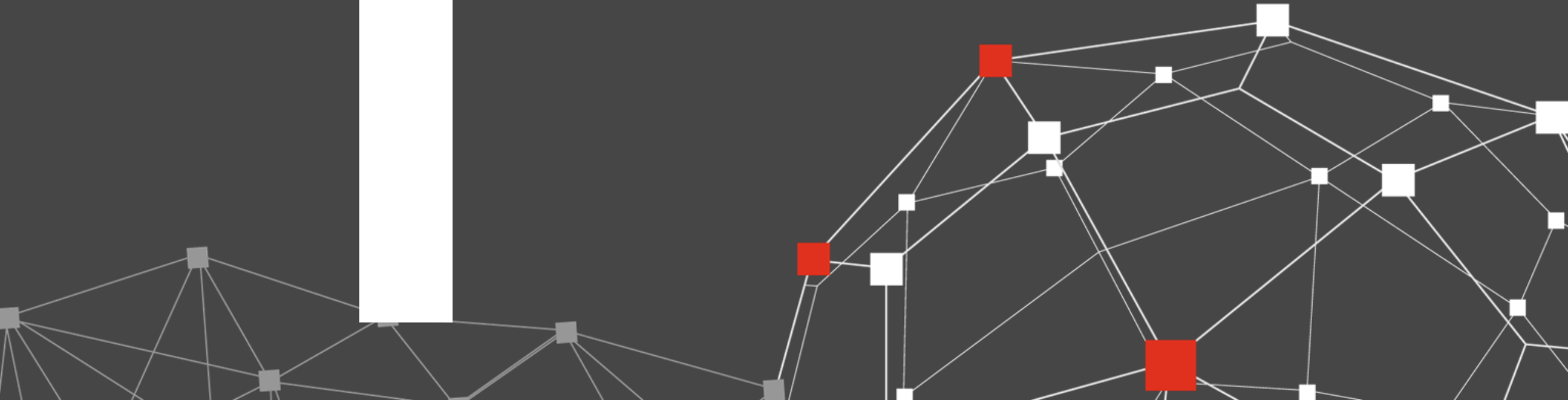
Principles for policy interventions: flattening the recession curve and healing the economic “scar tissue”

Important note about this publication

- The information in this presentation is reflective of our interpretation of the situation as on **17 April 2020**.
- It is not possible for PwC to assess with any certainty the implications of COVID-19 on the local and global economy, both generally in terms of how long the current crisis may last and more specifically in terms of its impact on specific organisations. From the supply side of the economy, businesses are likely to face significant operational challenges due to authorities implementing measures to contain and/or prevent the spread of COVID-19. From the demand side, purchasing activity of goods and services may be significantly impacted. To the extent that PwC has attempted to form a view of the economic situation and the potential impact of COVID-19 thereon, the potential variation between the current view and actual results are likely to be materially greater than it might historically have been.
- During this crisis that was caused by a “Black Swan” event, i.e. an event we have not seen before, time series forecasts based on historic business cycles will not be able to capture the full impact of COVID-19.
- PwC applied an Input/Output modelling approach, capturing the loss in GDP from the shock through the interdependencies of the different sectors of the economy.
- Our analysis is driven by a set of informed assumptions but uncertainty is very high and, as a result, these should not be taken as precise estimates. Rather they give broad indications of the order of magnitude of the potential impacts in different scenarios based on information available at the time of writing.
- This content is for general information purposes only, and should not be used as a substitute for consultation with professional advisors.



Framing the crisis:
first humanitarian,
then economic



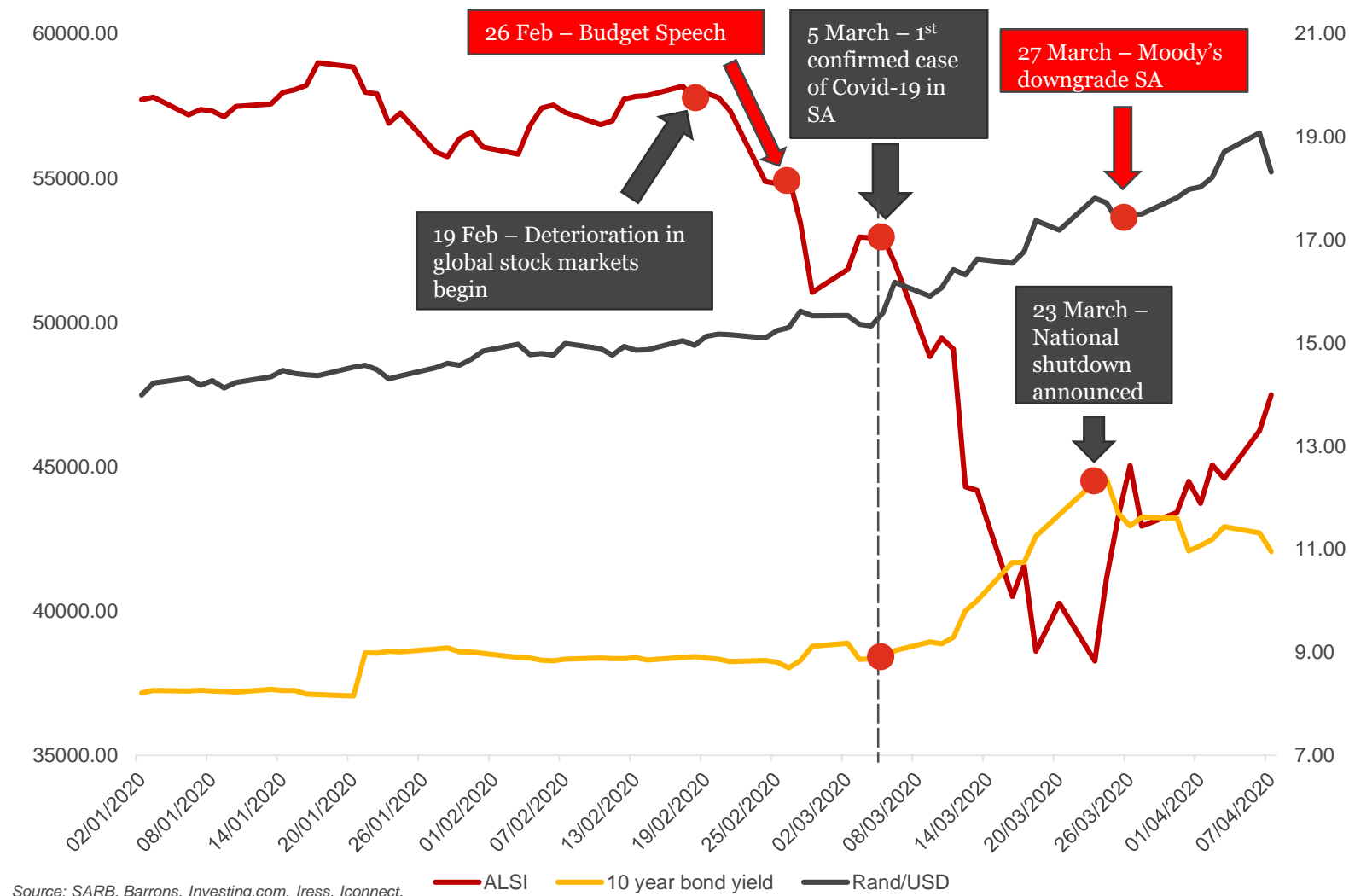
South Africa's economy was already weak at the start of 2020

South Africa started the year in a technical recession after a 0.8% q-o-q decline during 2019Q3 and a 1.4% q-o-q decline during 2019Q4. Budget 2020 presented an expected fiscal deficit of 6.8% and public debt ratio of 65.6%.



Source: National Treasury, StatsSA ■ Budget 2019 ■ MTBPS 2019 ■ Budget 2020

Market triggers: COVID-19 shocks vs local shocks

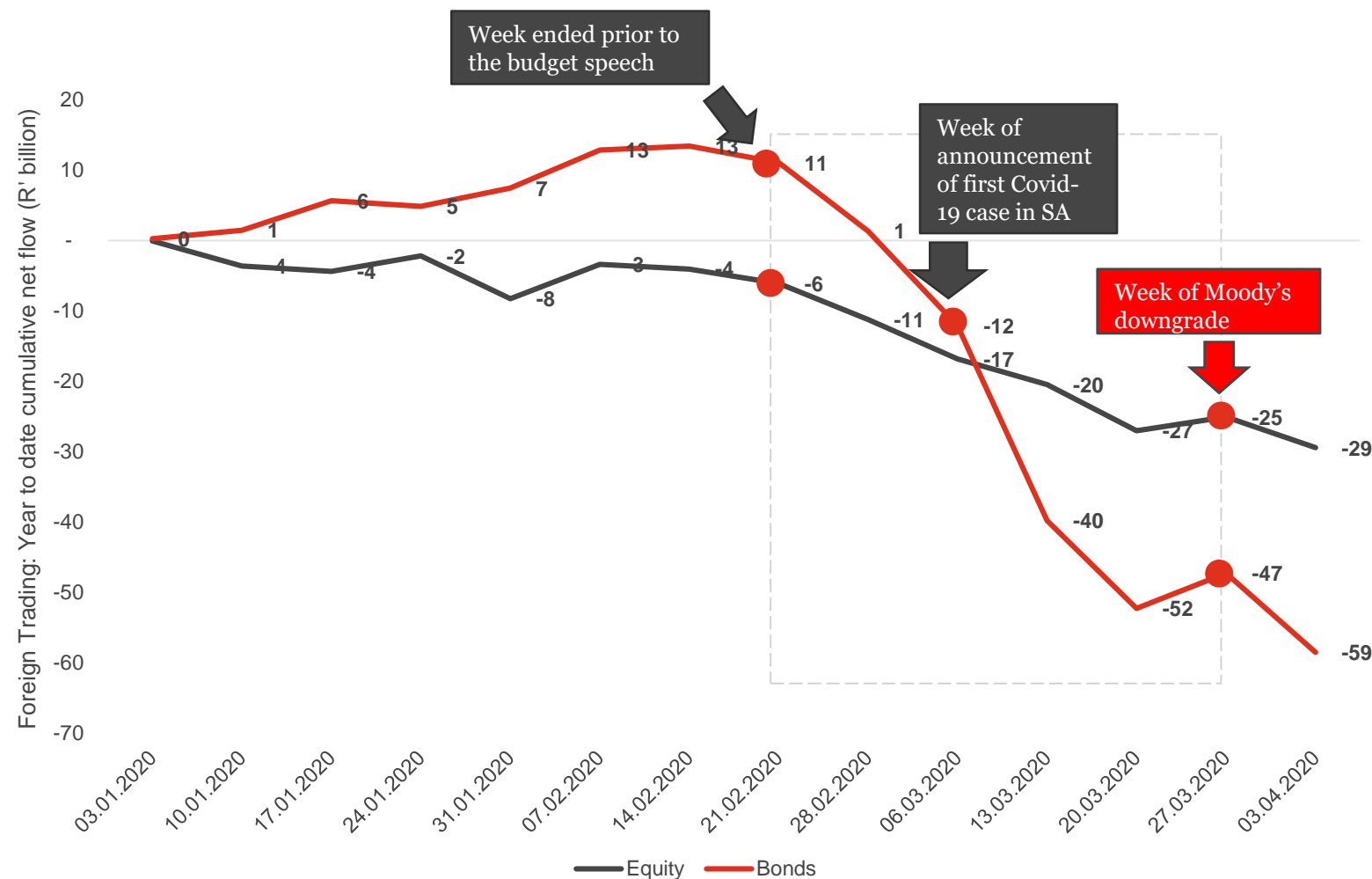


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- **Bond yields** peaked at **R12.36** on 24 March 2020, following the **announcement of nation wide lockdown** on 23 March 2020.
- From the announcement of the **first confirmed COVID - 19** case to this **peak**, bond yields **had risen 39%**.
- Since the start of the year, the **ZAR/USD exchange rate** was down **36%** at 4 April 2020.
- Following the **Moody's downgrade** announcement on 27 March 2020, the **rand depreciated** by approximately **9%** over the following week.

Net cumulative flows: foreign trading on bonds and equities

- From the **week prior to the budget speech** (week ended 21 February 2020) the **net cumulative flow of foreign trading on bonds** shifted from an **inflow of R11.1 billion** to an **outflow of R58.5 billion** (week ended 3 April 2020)
- The **net cumulative outflow of foreign trading on equities** increased from an **outflow of R6.1 billion** (week ended 21 February 2020) to an **outflow of R29.4 billion** (week ended 3 April 2020)
- The **outflow in foreign trading of bonds** increased further following the **announcement of the first COVID-19 case** in SA.



Source: Johannesburg Stock Exchange

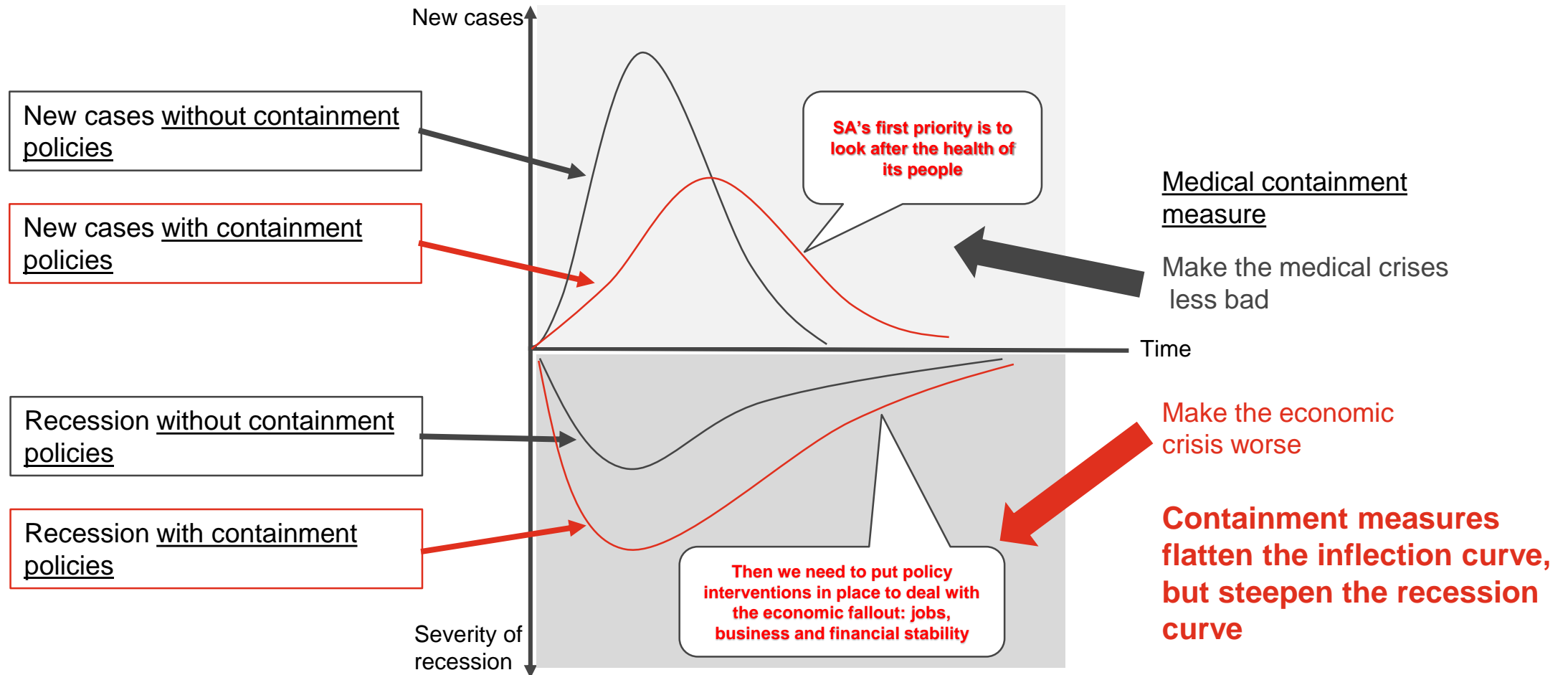
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Note: The data represents the net cumulative year to date flow (i.e difference between purchases and sales) for foreign trading on bonds and equities

South Africans' health and livelihoods are the first priorities

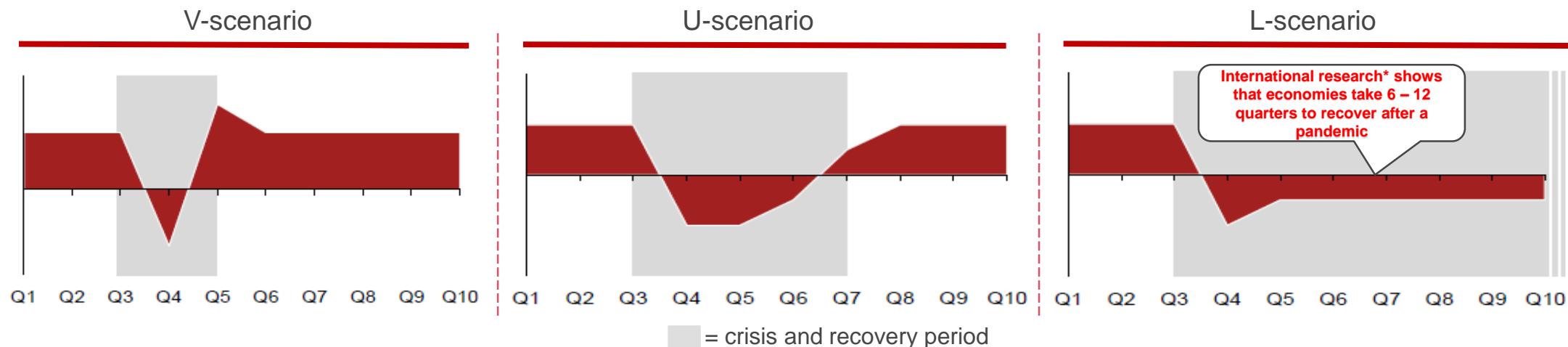
Policy options should be considered to reduce the economic fallout



Source: Adapted from Centre for Economic Policy Research (CEPR)

Policy interventions should be proportionate to the potential economic impacts

Depending on the length of the lockdown and the rate at which business and consumer confidence return, economic impacts could be less or more severe.



Shock impact on the economy as a whole, followed by **swift and complete recovery**

Reduction in full-year growth, but **limited to one year**

Postponement of investment and consumption **rather than cancellation**

Mild

Sustained recession, return to previous GDP level over several quarters

Performance and overall growth of **at least two full years affected**

Postponement and, in part, **sustained restriction of investment and consumption**

Medium

Drastic impact on economic performance and **prolonged recession**, threats to the monetary and financial system.

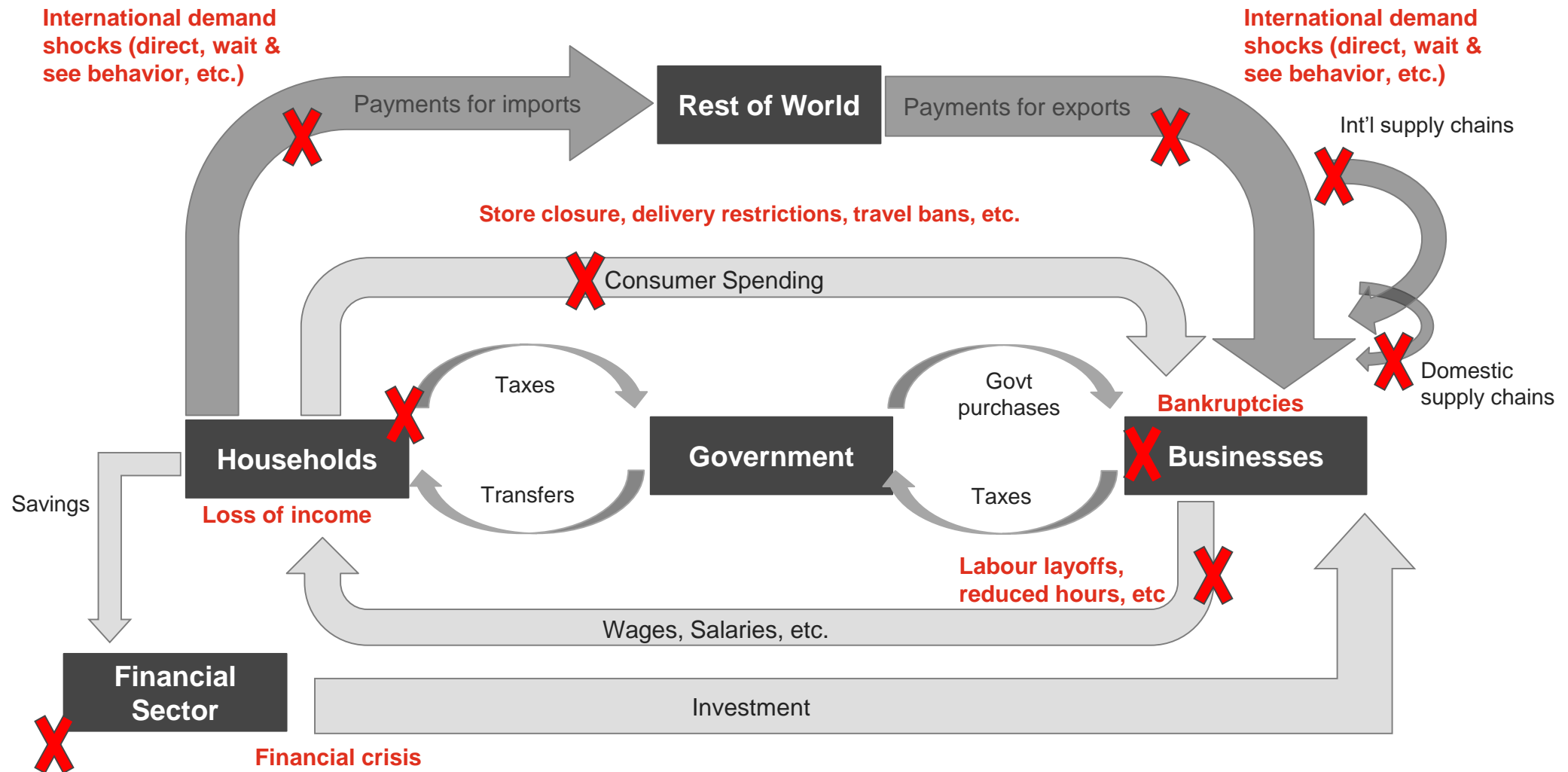
Return to the level of total output before COVID-19 **not foreseeable**

Deep restrictions on investment/consumption

Severe

* Available on request

COVID-19's multiple strikes in the circular flow of income diagram (X where interventions are required)



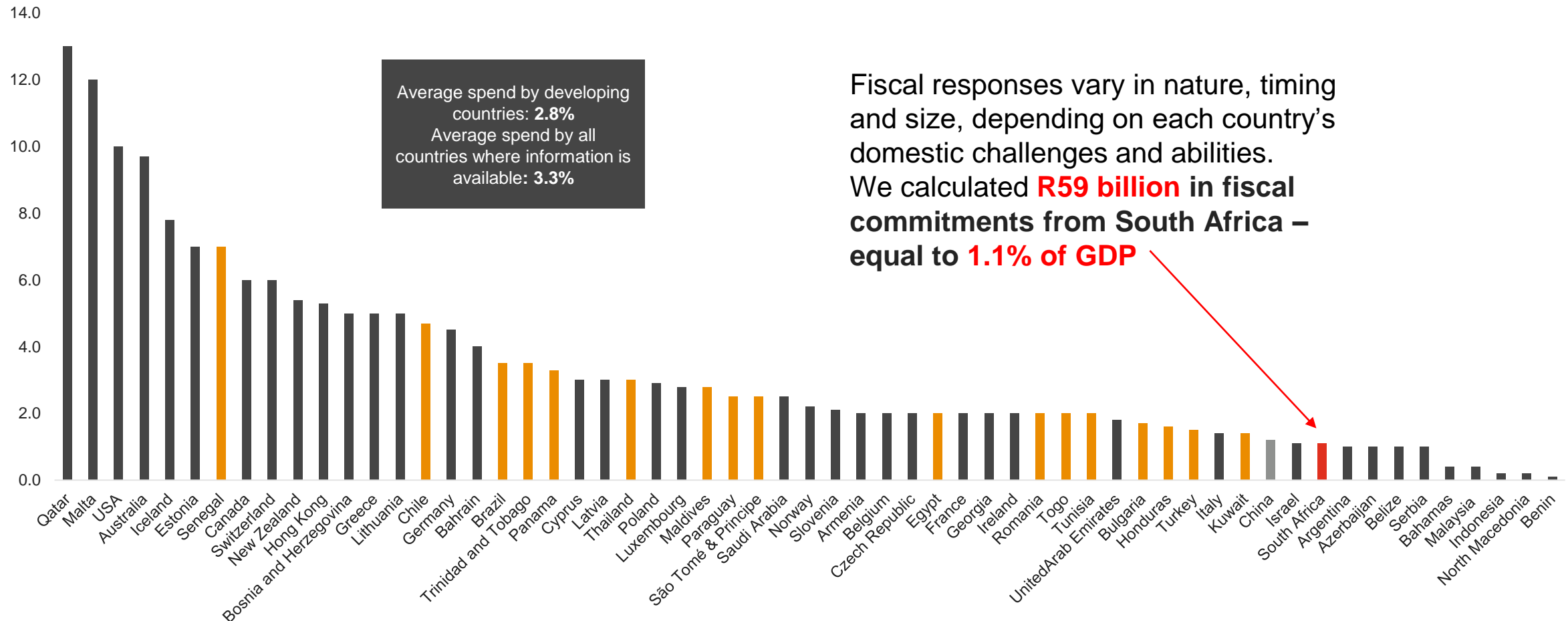
Source: Adapted from Centre for Economic Policy Research (CEPR)

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How does South Africa's fiscal injection compare?

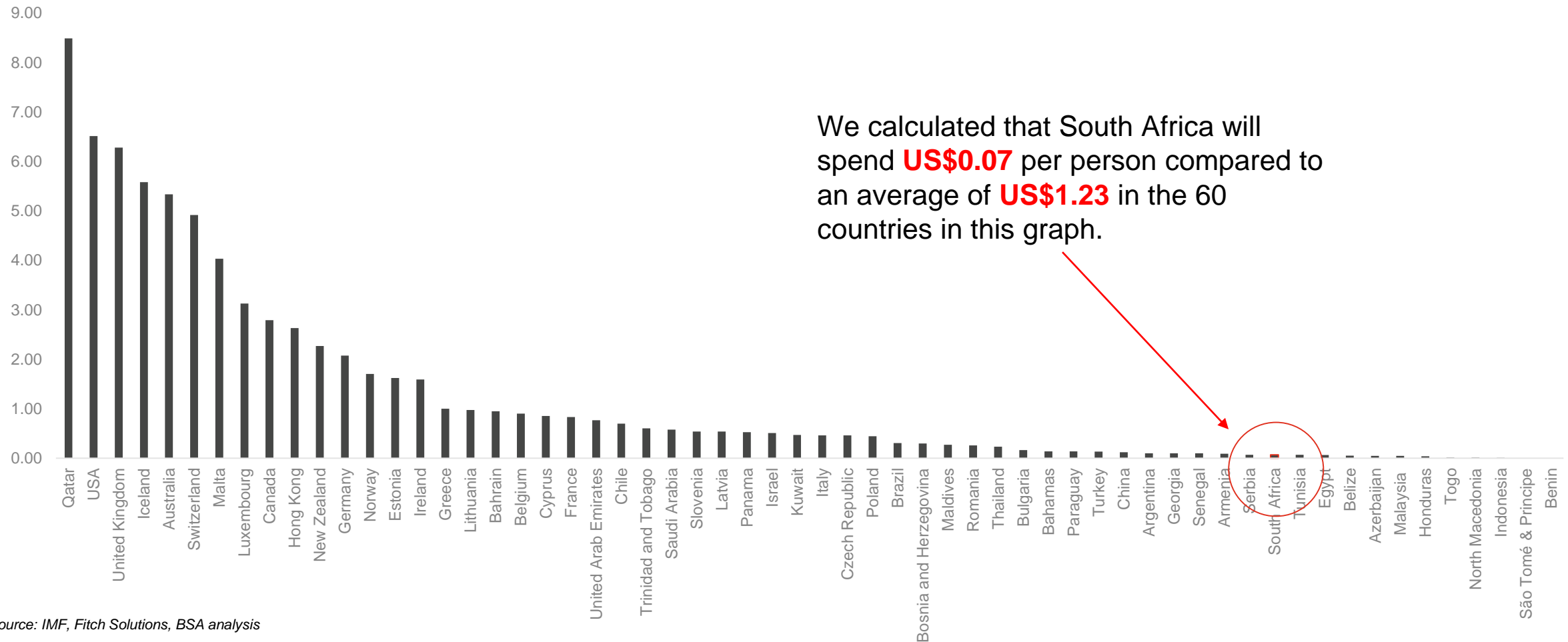
South Africa is on par with China, but most other countries are spending more (as % of GDP) on their COVID-19 stimulus responses.



Source: IMF, BSA analysis

How does South Africa's fiscal injection compare?

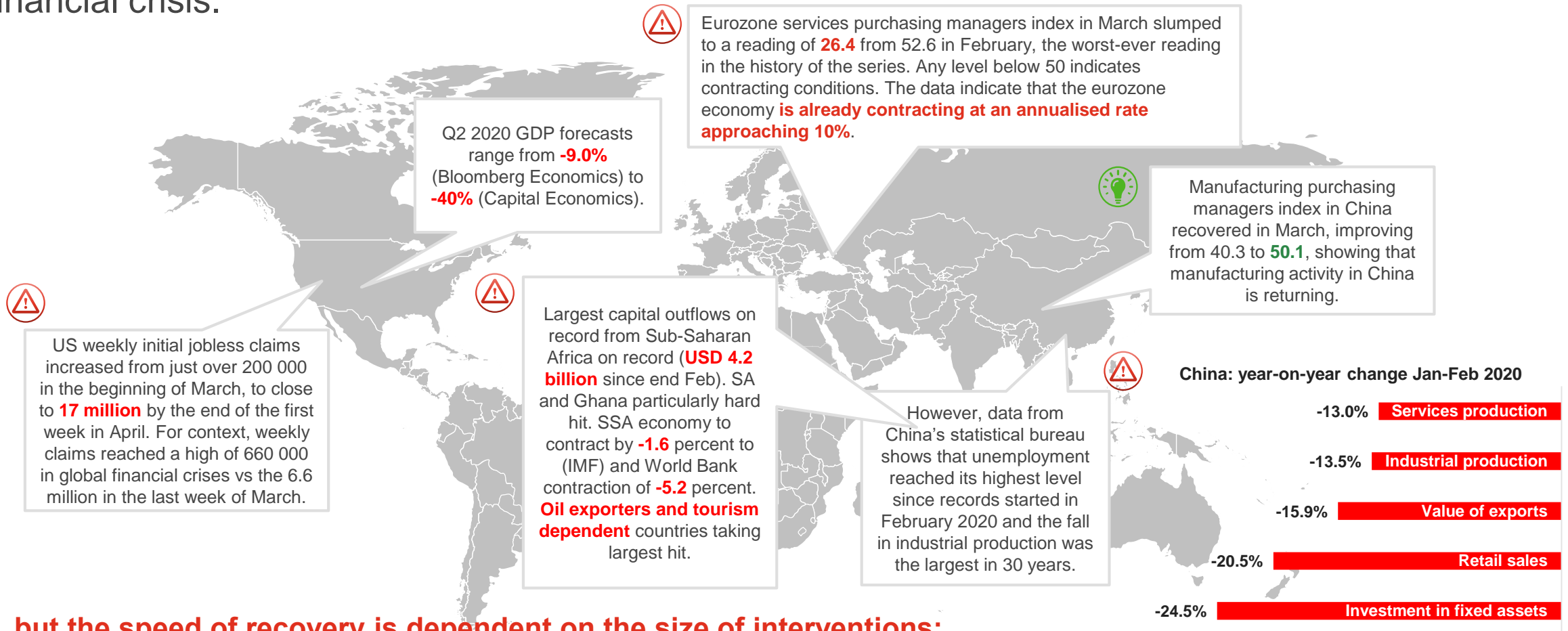
South Africa is behind most countries in US\$ stimulus spend per capita.



Source: IMF, Fitch Solutions, BSA analysis

Trends and developments in the global economy

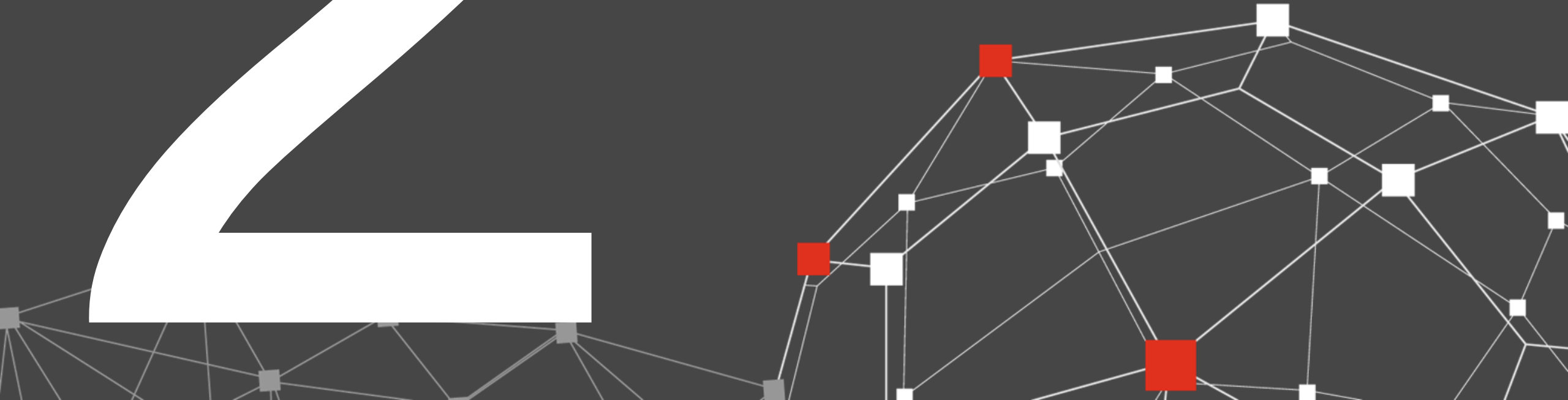
Data from around the globe shows that the impact of COVID-19 is set to be worse than the 2008 financial crisis.



...but the speed of recovery is dependent on the size of interventions; return of consumer and business confidence.

2

The impacts and
scenarios we
modelled



How this section is structured

1



Understanding the transmission channels of COVID-19 through the economy

2



Define different scenarios (length, extend, full partial) of lockdowns

3



Consider the impact of monetary policy and fiscal policy interventions on the economy

4



Consider options for a partial lockdown (which sectors can open up and how might demand look like)

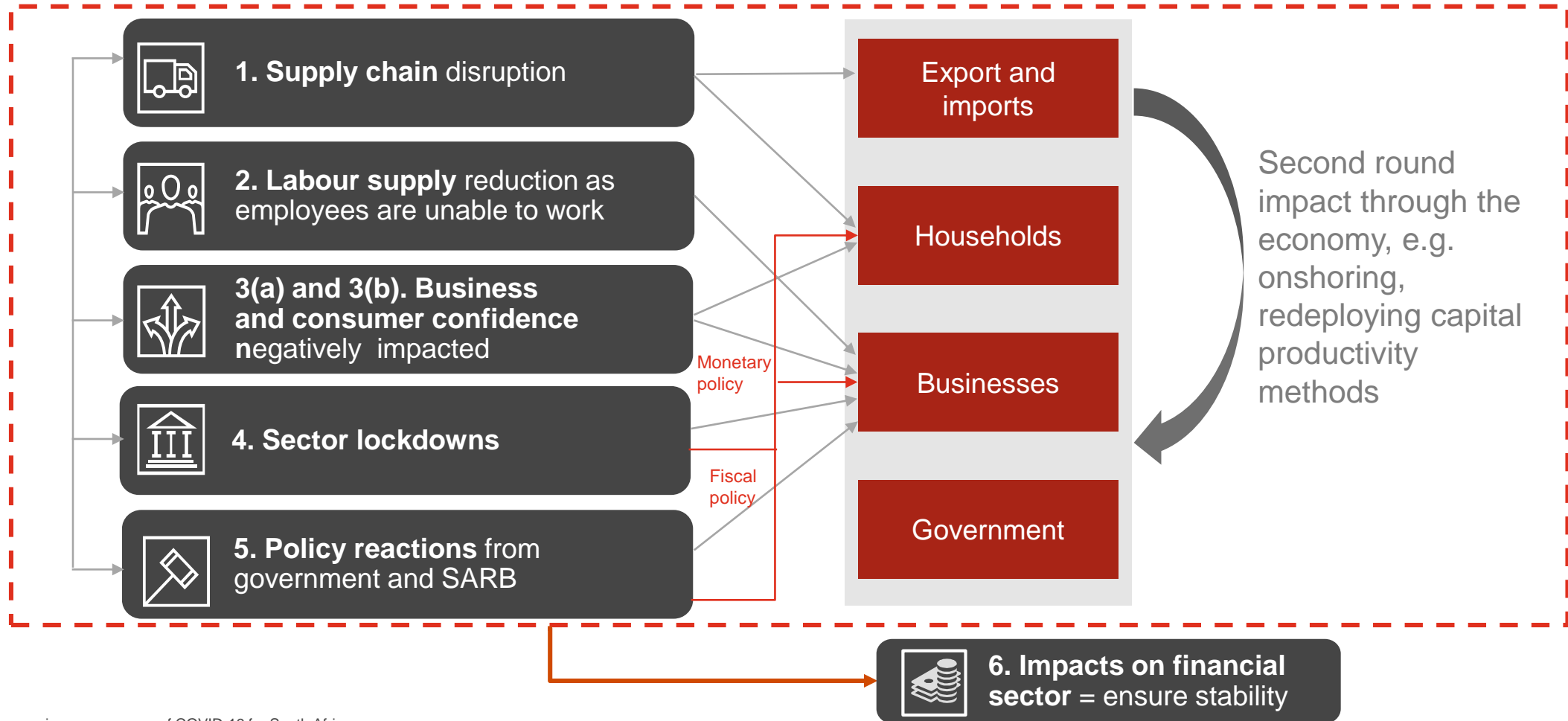
5



Consider any other positive impacts on sectors in the economy such as communication or local manufacturing of healthcare products

Modelling the economic impact

Although not exhaustive, we identified the following main transmission channels through which COVID-19 can impact the SA economy. Other reinforcing and mitigating impacts are likely.



Different scenarios and its impact on the economy

	Scenarios		
	Scenario 1: Mild	Scenario 2: Medium	Scenario 3: Severe
Narrative of scenario	A 3 week full lockdown and a 2 week partial lockdown with a 7-month gradual improvement in the economy. Not all sectors improve at the same rate.	An 3 week full lockdown and a 5 week partial lockdown with a 9-months gradual improvement in the economy. Not all sectors improve at the same rate.	A 3-month full lockdown with a 12-month gradual improvement in the economy, with the exception of the business confidence and supply chain components within the transmission channels that remain suppressed throughout the remainder of the calendar year (and beyond).
Supply chains	<ul style="list-style-type: none"> Significant reduction in imports and exports of around 14% for 2 months, gradually improving thereafter. 	<ul style="list-style-type: none"> Shock to imports and exports for 3 months, peaking at around 14%, gradually improving thereafter. 	<ul style="list-style-type: none"> Shock to imports and exports for 18 months plus, peaking at around 14%.
Labour supply	<ul style="list-style-type: none"> Lost workdays remain at historically high levels until at least Q2/Q3 of 2020 and then gradually start to revert to normal levels. 	<ul style="list-style-type: none"> Lost workdays remain at historically high levels until at least the end of the year and then gradually start to revert to normal levels 	<ul style="list-style-type: none"> Lost workdays remain at historically high levels for the next 18 months
Consumer confidence	<ul style="list-style-type: none"> Consumers defer major purchase decisions because of uncertainties for 6-12 months. Specific impacts on sectors impacted by lockdown. 100% shutdown of these sectors for a period of 1 month, with a gradual improvement thereafter. 	<ul style="list-style-type: none"> Consumers defer for 12-18 months and consumption focuses on essential items. Specific impacts on sectors impacted by lockdown. 100% shutdown of these sectors for a period of 3 months, with a gradual improvement thereafter. 	<ul style="list-style-type: none"> Consumers defer for 18 months plus and consumption focuses on essential items. Specific impacts on sectors impacted by lockdown. 100% shutdown of these sectors for a period of 3 months, with a slow improvement thereafter.
Business investment	<ul style="list-style-type: none"> 12% reduction in business investment for 2 months, gradual improvement thereafter. 	<ul style="list-style-type: none"> 12% reduction in business investment for 3 months, gradual improvement thereafter 	<ul style="list-style-type: none"> 12% reduction in business investment for period longer than 12 months.
Impact of lockdown	<ul style="list-style-type: none"> Airline, leisure and retail activities shut 25-100% of their operations (depending on sector) for 3 weeks. Certain parts of the economy starts to open up after 3 weeks (more detail on how that will look is later in this section of the presentation). 	<ul style="list-style-type: none"> Airline, leisure and retail activities shut 25-100% of their operations (depending on sector) for 3 weeks. Certain parts of the economy starts to open up after 3 weeks (more detail on how that will look is later in this section of the presentation). 	<ul style="list-style-type: none"> Airline, leisure and retail activities shut 25-100% of their operations (depending on sector) for 12 weeks.

Policy response

Fiscal response will be from increased expenditure in tackling the pandemic and providing financial support to otherwise viable businesses, but limited room. Interest rate reductions as well as quantitative easing option for SARB.

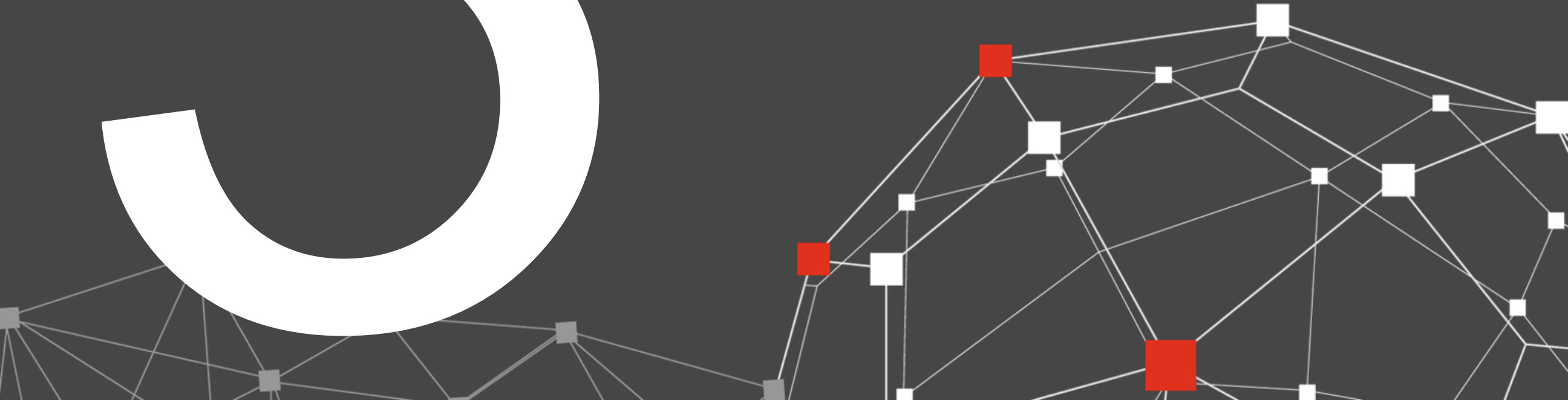
	Scenarios		
	Scenario 1: Mild	Scenario 2: Medium	Scenario 3: Severe
Nature of support	<ul style="list-style-type: none"> Based on current, known fiscal interventions, as well as monetary policy interventions already announced. 	<ul style="list-style-type: none"> Fiscal stimulus assumed to be equal to percentage share of GDP spend by other developing countries that has announced interventions, further expansionary monetary policy through a cut in the Repo rate. 	<ul style="list-style-type: none"> Fiscal stimulus assumed to be equal to percentage share of GDP spend by all other countries that has announced interventions, further expansionary monetary policy through a cut in the Repo rate.
Fiscal support	<ul style="list-style-type: none"> R59bn stimulus, equal to approximately 1.1% of GDP. 	<ul style="list-style-type: none"> R150bn stimulus, equal to approximately 2.8% of GDP. 	<ul style="list-style-type: none"> R177bn stimulus, equal to approximately 3.3% of GDP.
Monetary policy	<ul style="list-style-type: none"> The SARB engages in a precautionary cut to its Repo Rate equivalent to 2 percentage points. The SARB also provides commercial banks with incentives to offer help to bank customers in dealing with supply chain and workforce disruptions. 	<ul style="list-style-type: none"> The SARB cuts its Repo Rate by 2 percentage points. The SARB also provides commercial banks with incentives to offer help to bank customers in dealing with supply chain and workforce disruptions. SARB also intervenes through open market reactions, quantitative easing. 	<ul style="list-style-type: none"> The SARB cuts its Repo Rate by 2.75 percentage points. The SARB also provides commercial banks with incentives to offer help to bank customers in dealing with supply chain and workforce disruptions. SARB also intervenes through open market reactions, quantitative easing.

Potential impacts of partial lockdown: Scenario 1 and scenario 3: positive impacts

	Scenarios
	Scenario 1: Mild partial lockdown and Scenario 3: Medium partial lockdown
Mining exports to China	Restarting of mines and potential restart 50% of demand for mining products to China.
Automotive exports	Restarting 50% of automotive exports.
Agriculture citrus exports	Recovery of 80% of demand for citrus products (export season to start in the next 2 – 3 months).
Construction projects already on the go	Restart 50% of construction projects already on the go.
Online retail	Allowing online retail of all products. South Africa's typical online retail demand is 1.5% (World Wide Worx), but we assume that take-up will increase to 5% .
Vehicle sales	Allowing vehicle retailers to reopen. However, we assume that demand will only recover to 25% of pre-COVID-19 demand.
Hardware and paint	Allowing hardware and paint to be sold online. However, we assume that demand will only recover to 50% of pre-COVID-19 demand.
Communication sector boost from data consumption	Assuming increase in the demand for data. Around 16% of total revenue from telecommunication companies come from data. We assume that working from home increases the demand for data for the remainder of the year by 100%, keeping in mind the 1/3 reduction in data costs.
Restaurants: allowing take away activities	Allowing restaurants to provide take away through delivery services, we assumed 100% of the demand will recover.
Food manufacturing	Assuming that food sales will continue during lockdown we assumed that food sales will increase by 10% .
Transport impacts	The transport sector will benefit from the increased delivery activities. However, since this sector is linked to other sectors through the sector impacts already, so a separate impact shock was not included for this.
Professional and other related services	A shock for professional services sector was not included however it is good for business confidence of the country.
Localisation and local manufacturing	There is a portion of the production of medical devices, masks and other PPE items that can be localised and manufacturing locally, however, a very small portion of the current import market can be localised.

3

Results of the
economic impact
modelling



How this section is structured: how to read the graphs

1
The results of the economic impact assessment without interventions

•For each of the scenarios, we show the full impact on GDP, jobs and the budget deficit assuming no interventions and also ignoring the current fiscal and monetary policy interventions as well as future expected interventions. These are all **negative shocks**.

2
Taking into account the fiscal policy interventions

•Then we add the potential impact of fiscal policy interventions. This is a **positive shock** that reduces the extent of the economic contraction.

3
Taking into account the monetary policy interventions

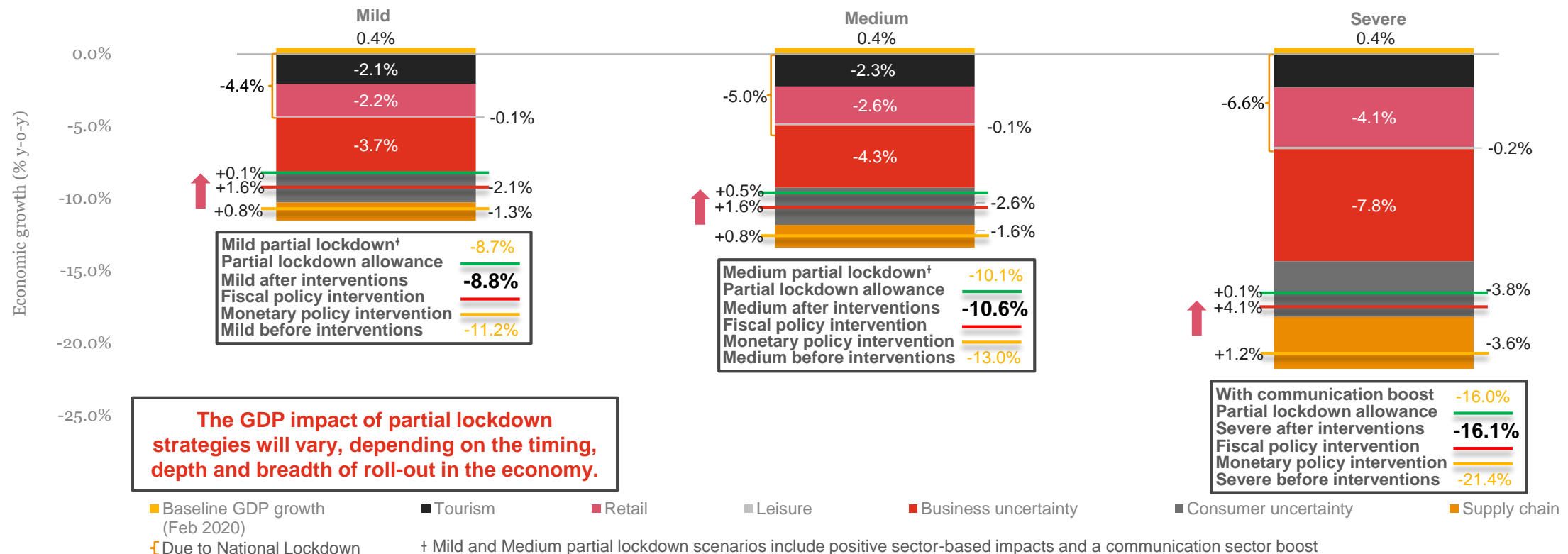
•Then we add the monetary policy interventions, including the interest rate reductions. This is a **positive shock** that reduces the extent of the economic contraction.

4
Taking into account the potential positive impacts of certain sectors opening up earlier or other potential positive impacts such as local manufacturing on communication demand

•Then we consider the potential impact on the economy of opening certain parts of the economy from lockdown earlier, as well as the potential positives from increased demand for data in the communication sector and some potential local manufacturing of PPE that replaces imports. These are all **positive shocks** that reduce the extent of the economic contraction.

Impact on real economic growth in 2020 (incl. interventions)*

After factoring in the effect of the current known monetary and fiscal policy interventions under full lockdown conditions, South Africa could experience a real annual GDP contraction of -8.8% in the mild, -10.6% in the medium and -16.1% in the severe scenarios, relative to the start of 2020. Partial lockdown conditions under our mild and medium scenarios would allow certain businesses to start operating and positively impact GDP.

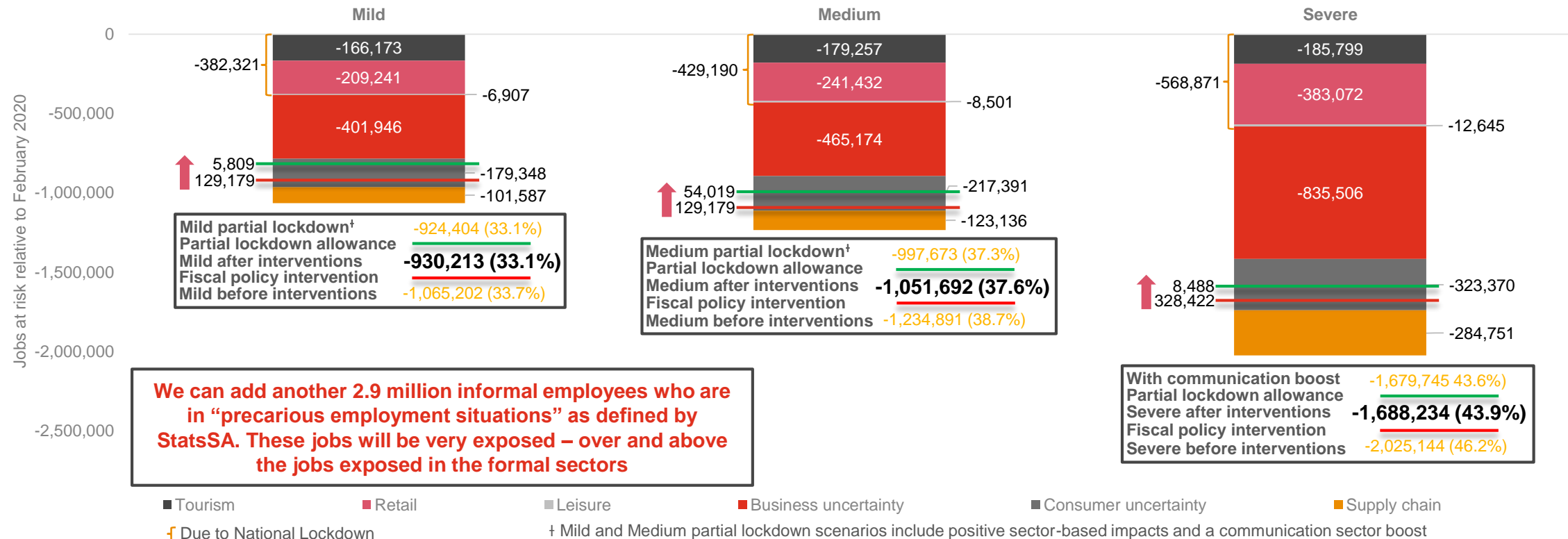


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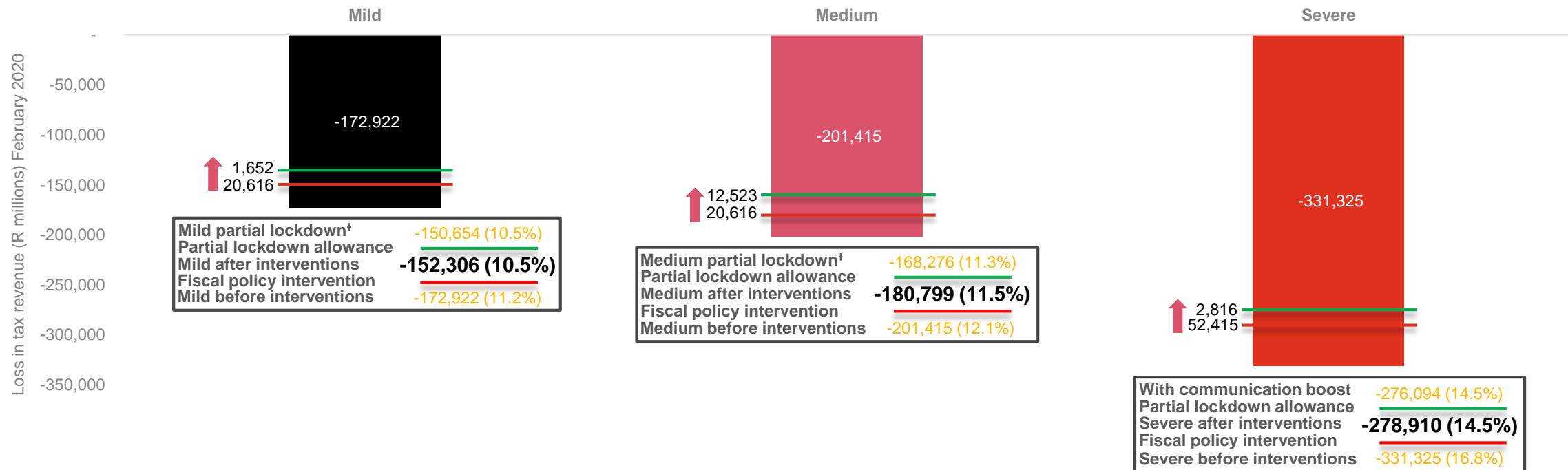
Impact on formal jobs at risk in 2020 (incl. interventions)*

Our model suggests that the current known policy could secure around 130,000 formal jobs at risk. Therefore, from South Africa's baseline unemployment rate of 29.1% in February 2020, this implies an increase to 33.1% in scenario 1 and 37.3% in scenario 2, and, 43.6% in scenario 3 respectively. Partial lockdown conditions under our mild and medium scenarios would allow certain businesses to start operating and secure some jobs.



Impact on fiscal deficit in 2020 (incl. interventions)*
















Our model suggests that the current known policy interventions could reduce the potential tax revenue loss by around R16 billion. This implies an increase in the fiscal deficit to -10.5% in scenario 1 and -11.3% in scenario 2 and -14.5% in scenario 3 respectively. Partial lockdown conditions under our mild and medium scenarios would allow certain businesses to start operating and contribute to tax revenue.



† Mild and Medium partial lockdown scenarios include positive sector-based impacts and a communication sector boost

Identifying critical sectors for interventions (excl. interventions)*

Depending on the linkages and exposure of different sectors to the scenarios modelled, the impacts below could be expected on GVA.

Industry (agriculture & mining)	Base case before COVID-19	Impact	2020 gross value added change			
			Mild	Medium	Severe	
 Citrus Fruit	0.1%	Slightly negative	-1.0%	-1.1%	-1.8%	
 Deciduous Fruit	0.1%	Slightly negative	-0.1%	-0.1%	-0.2%	
 Subtropical Fruit	0.1%	Slightly negative	0.1%	0.1%	0.1%	
 Vegetable	0.1%	Slightly negative	-0.2%	-0.3%	-0.5%	
 Livestock	0.1%	Slightly negative	-0.7%	-0.9%	-1.4%	
 Game	0.1%	Slightly negative	0.0%	0.0%	-0.1%	
 Dairy	0.1%	Slightly negative	-0.2%	-0.2%	-0.4%	
 Forestry	0.1%	Slightly negative	-1.4%	-1.6%	-2.5%	
 Fishing	0.1%	Slightly negative	-3.8%	-4.4%	-6.8%	
 Cereal and Crop	0.1%	Slightly negative	-2.3%	-2.6%	-4.1%	
 Poultry	0.1%	Slightly Negative	-1.7%	-1.9%	-3.0%	
 Other Agriculture	0.1%	Slightly negative	-4.2%	-4.8%	-7.5%	
 Gold	0.4%	Negative	-6.7%	-7.6%	-12.1%	
 Coal and lignite	0.4%	Negative	-7.6%	-8.7%	-13.6%	
 Other Mining	0.4%	Negative	-20.4%	-23.3%	-36.2%	












* **Interpretation of impact on communication sector** is based on current feedback from market players, as well as international trends suggesting an increase in demand as people work from home during lockdown or equivalent directives. This could change as the economy start to open up again.

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Identifying critical sectors for interventions (excl. interventions)*

Depending on the linkages and exposure of different sectors to the scenarios modelled, the impacts below could be expected on GVA.

Industry (manufacturing)	Base case before COVID-19	Impact	2020 gross value added change			
			Mild	Medium	Severe	
 Meat, fish, fruit, vegetables, oils and fat products	0.2%	Slightly negative	-3.8%	-4.4%	-6.9%	
 Dairy products	0.2%	Slightly negative	-3.2%	-3.6%	-5.7%	
 Grain mill, Bakery and Animal feed products	0.2%	Slightly negative	-1.5%	-1.8%	-2.8%	
 Other food products	0.2%	Slightly negative	-0.8%	-1.0%	-1.6%	
 Beverages and tobacco products	0.2%	Slightly negative	-1.4%	-1.6%	-2.6%	
 Textiles, clothing, leather products and footwear	0.2%	Very negative	-15.7%	-17.9%	-27.8%	
 Wood and wood products	0.2%	Very negative	-27.9%	-31.8%	-49.4%	
 Furniture	0.2%	Very negative	-21.7%	-24.8%	-38.5%	
 Paper and paper products	0.2%	Very negative	-24.9%	-28.4%	-44.1%	
 Publishing and printing	0.2%	Very negative	-17.8%	-20.3%	-31.5%	
 Chemicals and chemical products (incl. plastic products)	0.2%	Very negative	-31.4%	-35.8%	-55.5%	

















































Identifying critical sectors for interventions (excl. interventions)*

Depending on the linkages and exposure of different sectors to the scenarios modelled, the impacts below could be expected on GVA.

Industry (manufacturing)	Base case before COVID-19	Impact	2020 gross value added change			
			Mild	Medium	Severe	
 Rubber products	0.2%	Very negative	-32.7%	-37.3%	-57.8%	
 Non-metallic mineral products	0.2%	Very negative	-30.2%	-34.4%	-53.3%	
 Basic metal products	0.2%	Very negative	-26.2%	-29.9%	-46.4%	
 Structural metal products	0.2%	Very negative	-11.0%	-12.5%	-19.5%	
 Other fabricated metal products	0.2%	Very negative	-24.9%	-28.4%	-44.0%	
 Machinery & equipment	0.2%	Very negative	-37.4%	-42.6%	-66.0%	
 Electrical machinery & apparatus	0.2%	Very negative	-36.9%	-42.1%	-65.2%	
 Communication, medical and other electronic equipment	0.2%	Very negative	-23.0%	-26.2%	-40.6%	
 Manufacturing of transport equipment	0.2%	Very negative	-30.8%	-35.1%	-54.4%	
 Other manufacturing & recycling	0.2%	Negative	-6.4%	-7.3%	-11.4%	

Identifying critical sectors for interventions (excl. interventions)*

Depending on the linkages and exposure of different sectors to the scenarios modelled, the impacts below could be expected on GVA.

Industry	Base case before COVID-19	Impact	2020 gross value added change					
			Mild	Medium	Severe			
 Electricity	0.2%	Very negative	-15.7%	-17.9%	-27.7%			
 Water	0.2%	Very negative	-6.7%	-7.7%	-12.0%			
 Construction	0.1%	Very negative	-16.9%	-19.3%	-29.9%			
 Wholesale & retail trade	0.4%	Slightly negative	-2.7%	-3.2%	-5.1%			
 Catering & accommodation	0.4%	Very negative	-35.3%	-40.3%	-62.5%			
 Transport	0.2%	Very negative	-15.5%	-17.7%	-27.4%			
 Communication	0.2%	Very negative	-18.5%	-21.1%	-32.7%			
 Finance and insurance	0.8%	Very negative	-9.8%	-11.3%	-17.9%			
 Real estate	0.8%	Negative	-19.8%	-22.6%	-35.4%			
 Business services	0.8%	Negative	-6.7%	-7.8%	-12.5%			
 General government and personal services	0.4%	Slightly negative	-2.7%	-3.1%	-5.0%			
 Tourism	0.4%	Very negative	-10.4%	-11.9%	-18.7%			

Conclusions from economic modelling results

The following conclusions from the economic modelling results are important for consideration in the policy interventions.

1. Key countries where SA that will be exposed as a result of the reduction in export demand that will need support in some form or alternative markets: **China, Germany, US, UK, India**
2. Key sector where SA that will be exposed as a result of the reduction in export demand that will need support in some form or alternative markets: **Platinum, gold, diamonds, iron ore and manganese ore, coal, vehicle exports, machinery (laboratory equipment), steel, fruit**
3. Key sectors that will be impacted by the reduction in demand due to the lockdown that will need support: **Accommodation, transport, finance and insurance.** This is due to the size and number of linkages of these sectors to the most severely impacted areas of the economy.
4. The most lasting and damaging impact on the economy is likely to come from **the lack in business confidence and resulting reduction in business investment.** However, this is in response to reduced consumer demand
5. Between **business uncertainty and consumer uncertainty**, those two factors will be the **key drivers** leading to a so-called L-shaped recovery.
6. Potential for job loss in the formal sector is significant. However, around **2.9 million jobs** in **the informal sector** is also on the line.

4

Principles for policy interventions:
flattening the
recession curve and
healing the economic
“scar tissue”



A note on policy interventions

Both the economic consequences of and policy response to COVID-19, will lead to a significant increase in government debt levels, which will probably take longer to address than the MTBPS period.

Where possible, interventions should be...

Targeted at immediate pain points, timely	Impactful	Primarily supply-side interventions during lockdown, thereafter demand side	Easily implementable in the immediate short term	Be temporary and not deviate from overall long-term policy
<ul style="list-style-type: none">Aggressive, decisive and immediate action is imperative <ol style="list-style-type: none">First, support to healthcare sectorSupport workers, businesses; ensure financial stability:<ul style="list-style-type: none">Emergency assistance to workers, firms, and financial firms need to be put in place quicklyShort term: compensate negative effects on corporate liquidity and stability for banking system	<ul style="list-style-type: none">Prioritise interventions with highest returnsPrioritise sectors that are the most vulnerable to job losses and / or business failurePrioritise sectors and interventions that contribute most to job creation and growth	<ul style="list-style-type: none">Demand-side interventions will be less effective during lockdownAfter lockdown, however, demand side interventions will be needed to get the economy going again	<ul style="list-style-type: none">Easiest: interventions where no legislative change is required (or if so, these can be changed by way of a money bill)Make use of existing mechanismsBuild confidence through dialogue and certainty	<ul style="list-style-type: none">Ensure time limit to prevent measures that are difficult to reverse and will create long-term negative side-effects / costsSize of the response should be relative to the severity of the economic impact

Contact us



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Thank you

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