South Africa Viewpoint

It's all go in 2024: an election, rate cuts and new budget

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GEM Economics
EEMEA | South Africa

Tatonga Rusike
Sub-Saharan Africa Economist
MLI (UK)
+44 20 7996 8446
tatonga.rusike@bofa.com

EEMEA FI Strategy & Economics
MLI (UK)

See Team Page for List of Analysts

ANC likely to stay in power – with a little help.

South Africa faces a busy year in 2024. A general election is coming up, likely in May, where polling suggests the governing ANC could fail to win an outright majority and require a coalition to remain in power. The risk of the ruling party losing power – albeit small – makes election scenarios uncertain, turbulent, and noisy. According to political analysts the ANC is likely to stay in power, with some support from small partners – meaning the status quo is maintained on economic policy.

SARB interest rate cuts likely to start in July

A turbulent 2Q will make it challenging for the SARB to start cutting in May, as priced by the market. Rather, we think cuts are likely from July. We now think the Fed could start cutting in March and by 100bp in 2024, giving the SARB more room for cuts. We pencil in the SARB cutting 75bp, previously 50bp, as domestic inflation moderates, averaging 5% in 2024E, and the global environment becomes more dovish.

Weak fiscal with some marginal improvements

The fiscal outlook remains largely weak on expenditure containment pressures + Eskom support still part of the fiscal framework until 2025. The 2024 budget is coming up in February and is unlikely to contain much good news, beyond no new taxes. New allocations to Transnet are likely, while Social Relief Distress grant could be made permanent beyond 2025. Near term marginal improvements in revenue collection and moderating expenditure growth will keep fiscal less bad.

Abbreviations

SARB is South African Reserve Bank

ANC is African National Congress

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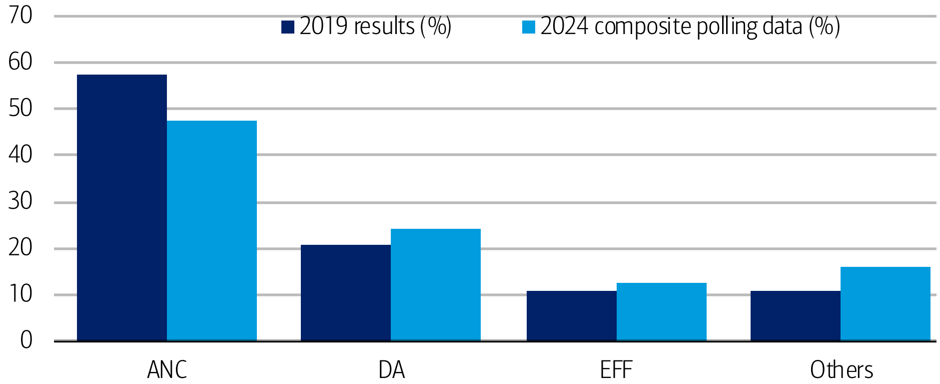
Elections: noisy but likely status quo

Exhibit 1: 2019 election results and polling data

The ANC could get <50% and form a coalition to govern - more likely with "others" than the two main opposition parties



Source: IEC, Combined polling data from Ipsos, CRA, and Brenthurst compiled by Frans Cronje

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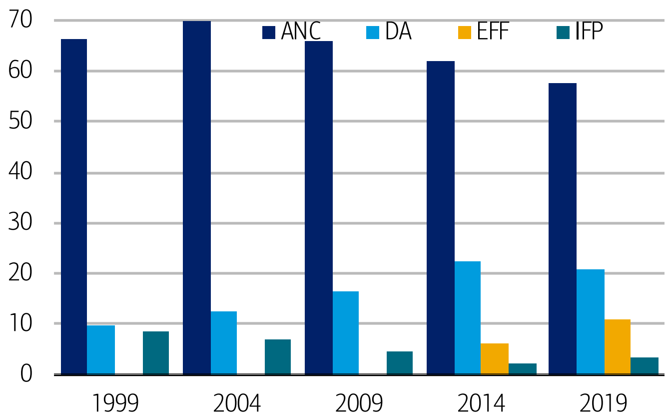
Exhibit 2: Historical national election results

Governing ANC support has been declining since 2009. However, opposition parties have a small share of votes relative to the ANC



Source: Independent Electoral Commission

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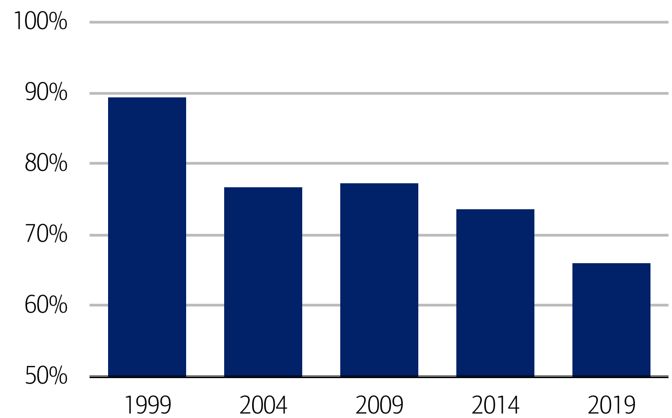
Exhibit 3: Voter turnout in past elections

Voter turnout has reduced over the years



Source: Independent Electoral Commission

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May for general election, although delays are possible.

Upcoming general elections tentatively in May 2024 are unlikely to produce an outright winner, per opinion polls. The constitution allows elections to be held between April and August, and they traditionally take place in April or May. However, this time there is growing consensus that the upcoming elections could be delayed, so the independent Electoral Commission can be better prepared and educate voters on changes since the last general elections in 2019. Since then, more parties and independent candidates have emerged, meaning the list of candidates might not fit onto one page, as is usually the case. Therefore, the election officials need to prepare and educate voters accordingly. No official date has yet been announced by the President. We assume that this could be made at the State of the Nation Address scheduled for 8 February.

Declining ANC support but no proper opposition to take its place

Political analysts seem to agree on the risk of the governing ANC getting <50% of the vote. Opinion polls show this in a range of 40-50%, while opposition polling results are fragmented, dividing the vote.

ANC support has been declining over the years (see Exhibit 2). The challenge is that there is no direct political competitor as in other major or regional peers. For example, Republicans vs Democrats in the US, Conservatives vs Labour in the UK or New Patriotic Party (NPP) vs National Democratic Congress (NDC) in Ghana. Of the main opposition parties, the Democratic Alliance (DA) is the largest with a share of just over 20%, followed by the Economic Freedom Fighters (EFF) at over 10%.

The EFF is left leaning with policies that include the expropriation of land, mines, banks, and other strategic sectors without compensation. The DA, on the other hand, is centre-right, more moderate and with a track record of governing Cape Town and the Western Cape province. However, the DA base is largely perceived to be dominated by white voters, and a touchy subject in a country where unemployment, poverty and inequality are divided along racial lines. Even so, attempts to woo middle-class voters have failed with multiple black leaders leaving the DA and forming their own small parties. Former DA leaders, Mmusi Maimane, and Herman Mashaba, now lead their own small parties- Build One South Africa, and ActionSA respectively. Other new parties include the Patriotic Alliance and Rise Mzansi while IFP, is long standing with a large base in KwaZulu-Natal (KZA). Former president Zuma has endorsed the new Umkhonto weSizwe (MK) party, which may eat into the ANC's voter base. There are also independent candidates competing for the first time.

Overall, the share of small parties and independent candidates could be around 15%. This fragmentation makes it easier for the ANC to enter into a coalition with a small party without worrying about the DA or the EFF. Our baseline view is the status quo is maintained: the ANC governing in coalition with a small party or outright majority. According to political expert Frans Cronje of Frans Cronje Private Clients, various polling results put the ANC support in a range of 40-50%. Ultimately, however, voter turnout will be key to the ANC outcome as it has a large loyal support base that goes out to vote. A low turnout could benefit the ANC, while a higher turnout could be driven by protest votes. Historically, turnout has declined at every election despite a new generation of voters at each one, see Exhibit 3.

Status quo means no change in economic policy…

The status quo is not necessarily bad as it is known and means a slow pace of economic reforms. Eskom and Transnet remain the key focus of reforms. With unemployment over 30%, the current government is not keen on labour market reforms that could mean job cuts in public sector institutions. Ultimately, it is looking like lacklustre growth over the medium term: barely positive growth in per capita terms.

Foreign policy: US relations had thawed but…

South Africa wants everyone to coexist happily in a multi-polar world. At least that's what the authorities said after the strain on US/SA relations over Russia in May 2023. In response to US allegations of arming/supporting Russia. The President of South Africa launched a judicial enquiry into the Lady R, the Russian ship that docked in Cape Town in early December 2022. The judicial enquiry concluded there was no evidence of sending arms and the US did not pursue the matter further. South Africa remained under the AGOA, a free trade initiative offered to African countries to export into the US market. Domestic and international lobbying also ensured that the Russian President did not attend in a person a BRICS summit in August 2023 hosted by South Africa. The International Criminal Court (ICC) issued a warrant for Putin's arrest, which would have forced South Africa as a signatory member of the ICC to comply with the warrant.

… now under new strain with the Israel case

In 2024, South Africa is taking Israel to the International Court of Justice (ICJ) on allegations of genocide in Palestine during the current conflict with Hamas, a grouping that governs Gaza in the state of Palestine. The South African state has no strong economic or political ties with Israel, although there is a significant wealthy Jewish Israeli population in South Africa. Israel has strong ties with US and the EU, which have supported Israel. The case is set to be heard in coming days/weeks in court. This action could further strain SA's relations with the US and, to some extent, the EU.

SARB cutting cycle starts in 2H 24E

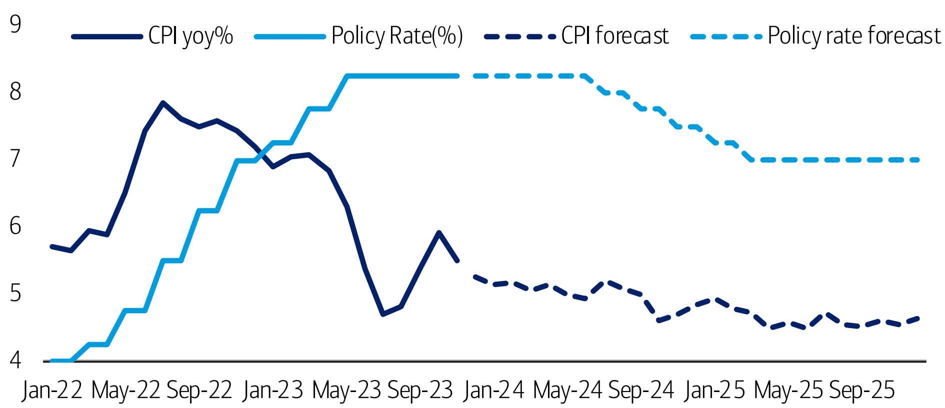
The first cut is the deepest: 75bp in 2024, 50bp in 2025.

What's changing? We are adding a 25bp cut to our 50bp baseline in 2024. We now forecast 75bp of cuts in 2024 then 50bp in 2025, resulting in a terminal rate of 7%. Why? The global environment is becoming more dovish, and our US economists have brought forward the timing of the Fed's first cut to March from June. An earlier move by the Fed would give the SARB more room for cuts up to 75bp. The market is pricing about 94bp of SARB cuts in 2024 as early as May, while cumulative cuts to 2025 amount to 112bp. We argue that there are domestic setbacks that could constrain earlier and more substantial cuts. We expect a total of 125bp cuts in the cutting cycle to a terminal rate of 7% in 2025, which is largely aligned with market expectations.

We believe July will mark the start of the SARB's cutting cycle. The bad news is that the cutting cycle is likely to be shallow – a cumulative 125bp over two years to 2025 compared with 475bp of hikes from November 2021 to May 2023. Be that as it may, the global environment appears more dovish. The Fed is likely to cut about 100bp in 2024 starting in March. In our view, this earlier move would give SARB room to cut 75bp in 2024, compared with our previous baseline of 50bp. Our view is supported by the fact that domestic inflation seems to be gradually moderating.

Exhibit 4: Inflation and Monetary Policy outlook

Headline CPI set to decelerate in December and January towards 5.3% and 5.1%, respectively, and likely to average 5% in 2024. We expect the SARB to cut 75bp in 2024 and 50bp in 2025



Source: BofA Global Research estimates

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Headline CPI on a moderately decelerating trend

After printing 5.5% year on year in November, we expect headline CPI to continue trending down moderately. That is, inflation at 5.3% in December and 5.1% in January 2024. Lower international oil prices translate into lower fuel prices, which is the main driver of easing inflation pressures. Domestic petrol prices declined by -2.7% in December and about -3.3% in January. This is likely keep inflation on a downward trend despite upside pressures from medical schemes in January.

Medical inflation is likely to spike in January 2024. Usually, medical insurers raise prices in February, but they have brought forward their annual price adjustments by a month, with firms having announced average increases of around 7% from January: 7.5% for Discovery Health, 6.9% for Bonitas and 6.9% for Momentum. The proposed increases are roughly in line with the regulator's guidance for price rises of 5% plus a utilisation estimate of 3.2-3.8%.

The impact of El Nino – delayed rains – is likely to be felt in harvests in the next two months, resulting in lower yields around March/April 2024 and thus higher food prices. The rainy season falls from around November to March. South Africa has been experiencing La Nina, the opposite phenomenon, over the past three years – in effect, above-average rainfall. So that can mitigate the El Nino phenomenon given some reserves are already in the system. The last El Nino event was in the 2015/16 rainy season and largely resulted in higher food prices and inflation exceeding the upper end of the 6% target, from around 5%.

All change: SARB MPC transitions in 2024

SARB Deputy Governor, Kuben Naidoo, resigned in October, nearly 18 months before his term in office was to end in January 2025. His departure date is yet to be confirmed by the appointing authority, the presidency. Naidoo was one of the frontrunners to succeed the current governor, Lesetja Kganyago, whose term ends in November 2024. The first terms of two other deputy governors, Fundi Tshazibana and Rashad Cassim, will expire in July 2024. They are likely to be reappointed for a second time in the coming months. Two new members look likely for 2024 – replacements for Kuben Naidoo and Governor Kganyago. However, Governor Kganyago is open to staying for a third term.

David Fowkes was appointed advisor to the Governors in December 2023. Fowkes has been a SARB senior economist since 2013 and has published various academic papers on topics including why South Africa could not implement quantitative easing during the Covid-19 pandemic. He strikes us as an orthodox economist and a likely hawk. Advisors have naturally transitioned to be voting members of the SARB MPC, so we think he is likely to get a seat as an MPC member. We believe the vacant deputy governor position could also still be filled, along with one additional member of the MPC, taking it to seven over the course of 2024.

Exhibit 5: South Africa Monetary Policy Committee Composition
Two members could leave the central bank in 2024

South Africa Monetary Policy Committee Members		
Governor	Lesetja Kganyago	Appointed Governor in November 2014, and reappointed for a second term on 9 November 2019. Will complete second term on 8 November 2024.
Deputy Governor	Kuben Naidoo	Appointed Deputy Governor on 1 April 2015, having served as advisor to the Governor since 2013. Resigned in October 2023 with term of office set to expire in March 2025.
Deputy Governor	Fundi Tshazibana	Previously served as special adviser to the Governor and was appointed as Deputy Governor on 10 July 2019. Likely to be reappointed for a second term in 2024.
Deputy Governor	Rashad Cassim	Previously head of Economic Research and statistics at SARB and appointed Deputy Governor on 10 July 2019. Likely to be reappointed for a second term in 2024.
Head of Research	Chris Loewald	Current head of Economic Research. Appointed to MPC on 1 June 2019.
Two vacancies		

Source: SARB, BofA Global research

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Monetary policy tailwinds

- The Fed cuts in March and more aggressively, which could lead to a weaker USD, stronger ZAR and lower pass-through to domestic inflation. The ZAR strengthens below 18 sooner and the SARB could consider cutting in 2Q 24.

Monetary policy headwinds

- Bad/noisy election outcomes with no real winners that weaken the ZAR above 20 and constrain the SARB from unwinding monetary policy tightening. Monetary policy remains restrictive for longer.

- A bad budget that widens baseline deficit projections beyond market expectations.

Weak fiscal with some marginal improvements

The fiscal outlook remains largely weak over the next two years while Eskom support is still part of the fiscal framework and new allocations to Transnet are likely, making the Social Relief of Distress grant permanent beyond 2025.

In the current fiscal year, revenue growth has picked up moderately while expenditure growth is starting to slow. We now see revenue R15 billion higher than the National Treasury's October 2023 baseline, largely from corporate income tax (over collection by R10 billion) and VAT (R5 billion) while PAYE is likely to meet the revised October 2023 target. Another near-term data point is upcoming December 2023 corporate tax revenues. However, we think that the December tax take is likely to mirror that of June, which means no real shift.

Reigning in spending growth is going to be challenging in the remaining months of the fiscal year. Typically, spending is highest in the last three months of the fiscal year. Since the mid-term budget policy statement, monthly spending growth has reduced to close to 5% compared with 10% in the first three months of the fiscal year. Our near-term fiscal forecasts remain weak, despite marginal improvements. That is, below 5% for the headline main budget deficit, excluding Eskom support in the current fiscal year, with similar levels in the 2024/25 fiscal year.

Budget 2024: still keeping an eye on the purse strings

Beyond no new taxes, Budget 2024 is unlikely to offer much good news. The budget framework has R15 billion in additional tax revenue in the baseline, likely thanks to bracket creep – less inflation adjustment on tax brackets. The National Treasury is targeting a headline main budget deficit of -4.3% of GDP (BofA -4.8%). Expenditure pressures remain on wage bill spending, social grant spending and higher transfers to weak state-owned enterprises. We think there will still be disappointments in the pace of expenditure containment, while we pencil in new allocations to Transnet in 2024.

Transnet default unlikely: like Eskom, it is too big to fail

On 30 November, the National Treasury announced a R47 billion guarantee facility to Transnet, representing over 0.6% of GDP. Direct government support is likely to be limited to servicing upcoming debt repayments and, to some extent, a turnaround plan to keep the entity well capitalised. The government does not want to Transnet to default: like Eskom, it is too big to fail. Direct budget financing looks inevitable, either below or above the line. We think that overall exposures to Transnet will not exceed 1% of GDP despite its total debt being about R130 billion or close to 2% of GDP.

The current two-year wage deal expires in March 2025. New agreements usually settle above budgeted baselines, presenting spending risks for the 2025 fiscal year. The temporary Social Relief of Distress (SRD) grant that cost up to 0.5% of GDP was extended for another year to make a decision after 2024 elections. We think that the SRD grant – introduced in 2020 at the onset of the COVID-19 pandemic to cover unemployed adults – is likely to become permanent and weaken fiscal. So, we keep the grant in our estimates throughout the forecast horizon. The mechanics of withdrawing it have proved difficult given structurally high unemployment and a looming election in May 2024. Discussions and technical work have focused on how to make the social grant permanent, under a basic income grant, although on a smaller scale than the current set-up.

To cover short-term funding gaps the National Treasury has utilised sukuk issuance (R20 billion), switches and treasury bills. Treasury bills are already overfunded above the R48 billion in the budget and the Treasury plans to moderate their use as a financing instrument. Floating-rate notes can be used sparingly as demand is cyclical with rising inflation. On the external financing side, there are no plans for external market issuances over next two years. The Treasury is instead likely to rely on external concessional and leverage transition financing. Out of the required $2.4 billion repayments, $2.3 billion has already been raised from various concessional sources: $1 billion from the World Bank, €500 million from the Kreditanstalt für Wiederaufbau (KfW), $300 million from the Agence Française de Développement (AfD), and a $500 million New Development Bank loan.

Fiscal could finally turn the corner in 2026

We pencil in improvements in the fiscal path in 2026 – when our forecasts start to align with the Treasury's, **Eskom support falls off**, there is a strong primary surplus (over 1% of GDP) and debt to GDP could stabilise at just below 80% of GDP.

2026 is the year to become constructive on the fiscal outlook. Eskom's three-year financial support of R254 billion falls off in the year ending March 2026, and the deficit will likely be a true reflection of the government's actual net borrowings. Eskom support is currently being accounted for below the line or excluded as part of spending but included in borrowings. South Africa's debt stabilising primary balance is usually 0.5-1% of GDP. From 2026, primary surpluses will likely reflect the true fiscal stance as opposed to the current the case of below the line items.

Fiscal tailwinds

- Access to part of the Gold and Foreign Exchange Contingency Reserve Account (GFECRA) kept at the SARB on behalf of the government. Access to this source of funding could reduce borrowing levels and likely lead to lower related costs due to reduced supply. In our view, the likelihood of accessing this fund in the February budget is low, less than 20%. If anything, it's likely that a new set of rules and procedures on accessing central bank profits could be introduced post the ongoing study.

- No new allocations to Transnet or new expenditure priorities to stay in check with spending targets. Modest upward revisions to revenue forecasts. Fiscal comes in line with Treasury targets. The probability here is at least 30%.

- Higher GDP growth – fewer power cuts, continued strong investment spending, and a rate-cutting cycle could help push GDP growth somewhat above estimates. While unlikely, closer to 2% growth could be a welcome tailwind and change the fiscal outlook earlier than our 2026 baseline.

Fiscal headwinds

- New expenditure allocations are introduced in the 2024 budget without corresponding cuts; Transnet allocations exceed our baseline.

- Very low GDP growth of 0-1% in real terms would drag down fiscal forecasts. Driven either by intensive power cuts, a protracted election cycle/inconclusive outcomes or coalition agreements that slow policymaking and weaken the business environment.

Exhibit 6: South Africa Key Macroeconomic indicators
Growth pick-up in 2024 from very weak levels in 2023

	2019	2020	2021	2022	2023e	2024f	2025f
Real GDP growth (%yoy)	0.3	-6.0	4.7	1.9	0.5	1.5	1.7
CPI average (%yoy)	4.1	3.3	4.6	6.9	5.9	5.0	4.6
Policy rate (%,end of period)	6.5	3.5	3.8	7.0	8.3	7.5	7.0
Fiscal Bal (% of GDP)	-6.1	-9.8	-5.1	-4.7	-5.9	-5.7	-5.9
Primary Bal (% of GDP)	-2.5	-5.7	-0.9	0.0	-0.9	-0.5	-0.5
Debt (% of GDP)	57.2	70.2	68.0	71.1	75.0	75.7	78.1
Current Account Deficit % of GDP	-2.6	1.9	3.7	-0.5	-1.5	-2.5	-2.5
Exchange rate (USD/ZAR end period)	14.0	14.7	15.9	17.0	19.0	17.8	18.4
Exchange rate (USD/ZAR avg)	14.5	16.5	15.0	16.5	18.6	18.2	18.1

Source: Haver, BofA Global Research

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Underperform	N/A	≥ 20%

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