

SA's economic growth could bring positive surprise in 2010



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Although likely to remain subdued in the opening months of the year, there is a good chance that following the FIFA World Cup, economic growth could be surprisingly solid and South Africa could end 2010 with annual GDP growth of over 3% year-on-year (y/y). This is notably above consensus forecasts.

We are expecting both consumer spending and private sector investment to remain weak for another quarter or so – these are the main drags on economic growth right now – but growth momentum should accelerate from the second quarter onwards as private demand recovers. The combination of a recovery in consumer demand, ongoing robust public sector spending, an end to the cycle of destocking, moderate export gains and the Soccer World Cup, could all combine to generate a surprisingly robust acceleration in growth during the middle quarters of 2010. We could even see another interest rate cut from the Reserve Bank adding to the positive conditions, should inflation surprise on the downside and the rand remain strong.

With the global recovery solidly underway, I believe the risks of a “W”-shaped downturn is relatively small. This means South Africa will benefit from revivals in both the developed and emerging markets, particularly China. This will help underpin our export volumes and prices of our commodity exports. Not only will this help the trade deficit, which should stay steady at around 4.5% of GDP this year, but the country should also continue to attract foreign capital inflows so that the rand depreciates only moderately against the US dollar over the year.

Other good news is that inflation should stay under control for the year. Barring any unforeseen shocks in the prices of oil or food, or the exchange rate, it should remain at the upper end of the Reserve Bank's 3%-6%

CPI target range. Our forecast is for CPI of 5.6% y/y at the end of 2010, not much changed from 5.8% y/y in November 2009 (the latest data). This has been driven by the stronger rand, lower food prices and weak consumer demand. However, there are still medium-term risks for inflation, as these trends will begin to reverse, combined with pressures from rising electricity and other administered prices, as well as lagged effects from the implementation of substantial wage hikes over the past year. Eskom will prove to be a thorn in the side of the economy for many years, probably throughout most of new decade.

With tame inflation, a rate cut seems unlikely

With inflation relatively tame for now, the most likely scenario is for interest rates to remain unchanged (with prime at 10.5%) for all of 2010. However, the Reserve Bank could surprise with a 50-basis point rate cut – possibly in the first quarter – should consumer spending prove particularly sluggish or inflation especially benign. However, in 2011 a more robust growth environment and gathering inflationary pressures could see rates starting to rise again, although the timing and speed of the next tightening cycle are hard to predict with any accuracy at this stage.

So after the year of big macroeconomic surprises that was 2009, on first examination our forecasts for 2010 paint a much quieter scenario – with relatively steady inflation, interest rates, currency and economic growth ahead. This should be welcomed by most South Africans. However, experience tells us that there are always unexpected shocks from some source, and this year will probably be no different.