Community Growth Funds

Economic Report

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2023

Q2 Report 2023

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Quarterly Report Contents

Quaterly Economic Commentary

Global Economy:

The second quarter marked a psychological turning point for the global economy in terms of growth, inflation and monetary policy settings.

While growth continued to surprise to the upside during April and May, softer growth signals emerged during June. Headline inflation slowed more decisively during the past few months, compared to still high inflation in the first few months of 2023. Unfortunately core inflation eased far less. Investors initially liked this mix of still decent growth and lower inflation, but the still-too-strong growth presented headaches for most central banks.

Global growth has been surprisingly strong despite substantial interest rate hikes over the past 18 months. While manufacturing activity has downshifted, service industries have maintained robust growth. Easing supply chain constraints, the spillover effects from the Chinese reopening and lower gas prices in Europe, combined with resilient private sector activity (including relatively robust private consumption expenditure) have provided significant support.

US growth was lifted by robust employment, supporting consumer spending. Labour market strength finally seems to have peaked – and while further weakness is expected in coming months, the economy will likely still achieve the Fed Chairman Jerome Powell's oft-repeated 'soft landing'.

The Federal Open Market Committee paused the rate hiking cycle in June to allow for a gauging of the impact of past rate hikes on the economy and inflation. But they warned that more rate hikes could be needed. Since the 'pause' meetiWng the data was somewhat conflicting with employment stronger than expected, while inflation surprised to the downside.

Chinese growth strength in the first quarter was displaced by a sudden slowing in the second quarter. As a result, the Chinese authorities have employed incremental policy easing measures to support the economy. These included rate cuts and other monetary and fiscal easing measures. Growth in 2023 is still expected to be stronger than in 2022 – around 5.5% vs 3%.

Restrictive policies in the developed world, easing policies in China and elsewhere in the emerging world, will aid better growth in Emerging Economies. Combined with the soon-to-bepriced expectations by markets of US rate cuts will further aid a risk-on trade, away from developed economies towards emerging economies. South Africa, despite her many homegrown problems should benefit from that. This includes prospects for the rand exchange rate to recover against a weakening dollar, which will likely be the result of such a risk-on trade.

Quaterly Economic Commentary

SA Economy:

Conflicting forces impacted the SA economy during the second quarter of 2023. Growth surprised sharply to the upside relative to much weaker performance expectations.

Growth surprised sharply to the upside relative to much weaker performance expectations. On the flipside,ambiguity around the Government's 'neutral' stance on Russia's war against Ukraine led to significant concerns.

Relative to widely held fears that the economy would slip into recession in the first few months of the year, gross domestic product (GDP) rebounded strongly in the first quarter. After the negative growth performance in the last quarter of 2022, the view was that the severe loadshedding in 2023 would result in another negative growth quarter in the first three months of 2023.

With the data release in early June, it became clear that the economy has become far more insulated against loadshedding. First quarter GDP showed growth of +0.4% (on a quarteron-quarter percentage change basis) or +1.4% on an annualised basis. While this is a very weakgrowth performance relative to what this country needs, the unexpected positive growth was a welcome windfall.

Of all the production sectors, only utilities and agriculture experienced negative growth. Unexpected positive growth in mining and manufacturing production showed the private sector's resilience in the face of loadshedding.

Spending also performed better than feared. Real -household consumption expenditure recorded +1.6% annualised growth in the first quarter of 2023 and wholesale, retail and car sales all printed further positive growth numbers in April. New car sales were up almost 10% in the second quarter compared to sales in quarter one.

The message is clear; while the electricity crisis is a big detriment to sentiment, the underlying position is not quite as dire as feared. The economy has become more resilient and better equipped to run on less Eskom-generated power. While growth has been dismal and will undoubtedly be weak for the rest of the year, it is not the all-fall-down scenario envisioned at the start of 2023. We expect real GDP growth of 1.2% in 2023.

Despite this better-than-feared growth performance overall sentiment took a severe beating when the 'Lady R' situation exposed SA's Russia stance. This has exposed the SA economy to even more risk around potential sanctions and expulsion from AGOA. The risk around this has since been defused somewhat. While USA sanction against SA would be devastating,the probability of sanctions is currently very low.

Inflation remained relatively 'sticky' during quarter one, averaging 7% due to continued high food inflation. However, pipeline prices, from farm to factory suggested food and other price pressures were easing, which should soon reflect in consumer prices. By May, partly thanks to food inflation dropping from 14.3% in April to 12% in May, headline CPI inflation eased to 6.3%.June food inflation will likely ease further to around 11% and headline inflation could drop to below 6%.

Quaterly Economic Commentary

SA Economy:

While the Reserve Bank has been rightly concerned about continued high inflation expectations, the decline in actual inflation will also drive expectations lower.

It is now time for it to pause and gauge the economic impact of past rate increases. While their risk-averse stance has served the economy well, there is no need for further rate hikes given the recent easing in headline and food inflation.

Current SA economic growth is still very weak but has proven relatively resilient in the face of many challenges. As argued before we expect policy changes to lift medium-term economic growth to better levels than the dismal growth of the recent past. Inflation is easing back to intarget performance and interest rates are close to a peak.

The rand exchange rate will benefit from US rates peaking, a softer dollar and a risk-on trade globally. The rand is substantially weaker than fundamentals suggest – likely pricing in more risk than needed. As such, the rand could recover markedly from present levels.