Potential Economic Impacts of COVID-19 on South Africa

Introduction

After a brief period of surveillance and assessment, South Africa adopted two main responses to the novel coronavirus (COVID-19):

- First, it encouraged self-isolation and social distancing. All schools were required to close on 18 March 2020.
- It then implemented a tighter lockdown on 27 March 2020, initially lasting twenty-one days. Most industries were legally required to cease production unless work could be done remotely from places of residence.

The government then extended the lockdown to the end of April, a total of thirty-four days. It made no adjustments to the regulations affecting the movement of people or business activities.

On 21 April 2020 the government announced a large economic stimulus plan to ameliorate the economic impacts of the lockdown.[1] Valued at approximately R500bn (USD $26bn), it equates to roughly 10 percent of GDP (2019, nominal)[2] and approximately 25 percent of the 2020–2021 national budget, announced in late February.[3] It is also larger than the latest official central bank forecast for 2020 GDP growth, which stands at –6.1 percent (but does not account for the new stimulus package).[4] Over 20 percent of it will come from reallocations of the existing budget, meaning that other government spending priorities will lose out.

Compared to most Western counties, South Africa implemented lockdown early, only a few days after it became clear that the number of positive cases had begun to increase exponentially. A government assessment published on 13 April 2020 suggests that this early surge in new infections was almost entirely made up of South Africans returning from overseas and passing the virus to family, friends and co-workers.[5] Local transmission has remained limited to date. The trend in total positive cases flattened from exponential to linear as soon as the lockdown began, suggesting that pre-lockdown measures had helped.

The government appears to be of the view that the lockdown itself has also helped to prevent a return to exponential growth in new infections. The risk of this happening is one reason given for extending the lockdown. Another is that South Africa is entering winter, which normally brings seasonal colds and flu. The third is that the healthcare system requires more time to prepare for projected peak demand for beds, ventilators, protective equipment for medical staff and so on—now estimated to arrive in September 2020.

1 Naido, Prinesha, Cohen, Michael, and Mbatha, Amogelang, "South Africa Sets $26 Billion Plan to Save Virus-Hit Economy", Bloomberg (21 April 2020), available at https://www.bloomberg.com/news/articles/2020-04-21/south-africa-unveils-26-billion-plan-to-help-virus-hit-economy

2 South African Reserve Bank, Full Quarterly Bulletin, No. 295 (March 2020), available at https://www.resbank.co.za/Publications/Detail-Item-View/Pages/Publications.aspx?sarbweb=3b6aa07d-92ab-441f-b7bf-bb7dfb1bedb4&sarblist=21b5222e-7125-4e55-bb65-56fd3333371e&sarbitem=9797

3 Republic of South Africa, National Treasury, Budget Review 2020 (26 February 2020), available at http://www.treasury.gov.za/documents/National%20Budget/2020/review/FullBR.pdf.

4 White, Ray, "Reserve bank cuts repo rate to 4.25%", EWN (14 April 2020), available at: https://ewn.co.za/2020/04/14/reserve-bank-cuts-repo-rate-to-4-25

5 Ministerial Advisory Group on COVID-19, SA's COVID-19 epidemic: Trends & Next steps, Department of Health, Republic of South Africa (13 April 2020), available at: https://sacoronavirus.co.za/2020/04/13/sas-covid-19-epidemic-trends-next-steps/

Economic impacts

Pre-lockdown initiatives caused adverse economic consequences such as cancelled conferences and holidays, reduced retail activity, and reduced productivity under remote working conditions. These were significant for some businesses, Edcon being among the more prominent examples.[6]

The lockdown is expected to generate far larger negative impacts. These will follow import and export disruptions already caused by the earlier lockdowns in China and other East Asian countries. China is South Africa's largest trading partner (for imports and exports).

Lockdowns generate supply shocks, as all types of business facilities are forced to close or cease operations (manufacturing plants, retail centres, offices, construction sites, transport services, etc.). These closures will harm employment and cause some businesses to fail. The negative demand shock associated with it will also inhibit economic recovery. Similar patterns have played out, or are playing out, in all of South Africa's major trading partners—the main sources of demand for both South African exports and inward foreign direct investment.

Knock-on impacts on credit markets and banks may arise as borrowers default on loans and credit lines and government deficits widen. Other negative impacts, for example on the exchange rate, the stock market, and the credit rating of government debt,[7] have already been realized in South Africa. All have been pronounced and significant.

How long will it take for supply and demand conditions to normalise in South Africa and in its trading partners? Will banks need support? What is the outlook for inflation, employment and growth? How will impacts on government debt feed back into the economy in future?

Quantifying the impact on the real economy is nearly impossible. A simplistic view might assume very limited economic activity for the period of the lockdown and remove that from forecasted GDP for 2020. But the reality is likely to be much more complicated.

Had this virus been contained, as with SARS,[8] we would likely be assessing the impacts on South African growth of a relatively short-lived slowdown confined, mainly, to China. COVID-19 has not only caused that initial slowdown but also will cause a synchronised and dramatic (albeit temporary) shutdown of economic activity in many countries—with much bigger impacts on demand for South African goods and supply of inputs to make those goods. It is difficult to think of historical parallels for such an event. The fact that no one seems to know how long it may take to return to normal conditions—or what the 'new normal' might entail—complicates matters further.

The fact that no one seems to know how long it may take to return to normal conditions—or what the 'new normal' might entail—complicates matters further.

Nevertheless, we can identify various channels through which impacts will materialise. We can also look to Asian countries for evidence of GDP impacts, since the epidemics in these countries are more advanced. We look at China, which implemented a strict lockdown, and Singapore, which avoided a lockdown but has still seen a significant contraction in economic activity.

6 Child, Katherine, "Edcon faces collapse as sales fall at least R1.2bn", Business Day (26 March 2020), available at: https://www.businesslive.co.za/bd/companies/retail-and-consumer/2020-03-26-edcon-faces-collapse-as-sales-fall-at-least-r12bn/

7 CNBC Africa, "Moody's downgrades SA to junk" (27 March 2020), available at: https://www.cnbcafrica.com/sa-downgrade/2020/03/27/moodys-downgrades-sa-to-junk/

8 Severe acute respiratory syndrome (SARS) is a respiratory virus which appeared in China in 2003 and spread to more than two dozen countries in Europe, North America, South America and Asia.

South Africa

The most immediate parallel to the current economic crisis is the global financial crisis (GFC) of 2007 and 2008, which had a huge economic impact around the world. However, it is possible that the impact of COVID-19 on South Africa will be worse than the impact of the GFC. South Africa's economy and public finances are in significantly worse shape now than they were in 2008, suggesting bigger implications for, at least, the budget deficit and public debt. Economic growth prior to the GFC was also significantly higher than it had been in the period leading up to this crisis, while unemployment was lower.

Economic impacts could materialise through several potential channels:

Real economy impacts:

Disrupted supply chains from China's earlier lockdown and those of other East Asian countries that may be important sources of imports for South Africa, including telecommunications. For example, China supplies 85 percent of South Africa's mobile phones.[9] Wuhan is the largest producer of optical fibre and cable in the world.[10]

The lockdown in South Africa: significant contraction in output with knock-on effects for business closures, employment losses, reduced domestic demand (and saving), credit markets turmoil, government deficits, the exchange rate, stock markets, etc. There is no guarantee of a rapid bounce-back, especially if businesses close and jobs are lost. It will take time to re-establish these businesses and jobs, because demand will remain depressed. Some services exports requiring international travel (e.g. tourism) may take a long time to recover.

External demand for South African exports will have already declined and will remain depressed as major export markets including China contract or slow down due to their own lockdowns. This includes exports of services such as tourism (which is a key forex generator and employment creator for South Africa), which will take much longer to recover than exports of, for example, the automotive industry (manufacturing sector). Global demand for iron ore, a significant South African export, has already suffered.[11] If it remains depressed after South Africa's lockdown finishes, then the problems facing iron ore miners will not be limited to the supply shock caused by the lockdown itself.

Delayed investment projects and lower FDI than expected.

Lower state revenue and higher spending, leading to wider deficits and a deteriorating debt position, which was already considered to be precarious.

Forecasted impact on GDP and government finances.

- Demand for electricity is an indication of the depth of the impact of the lockdown on economic activity in South Africa. By early April, demand had declined by roughly one-third.
- The April 2020 Monetary Policy Review of the South African Reserve Bank (SARB)[12] was released just before the lockdown extension was announced. It suggests that GDP will contract by between 2 percent and 4 percent in 2020, down from a January 2020 forecast of 1.2 percent growth.
- The extended lockdown will presumably cause an even greater contraction. The governor of the SARB was quoted on 14 April 2020 suggesting contraction of over 6 percent.[13] The 2009 contraction caused by the GFC was 1.5 percent.
- The SARB's April Monetary Policy review also suggested the possibility of a budget deficit of more than 10 percent in 2020–2021 (6.8 percent had been forecast in the February 2020 Budget[14]).

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9 Strategy&, *Impact of trade-disrupting COVID-19 on South African business* (20 February 2020), available at: https://www.pwc.co.za/en/assets/pdf/impact-of-trade-disrupting-covid-19-on-sa-business.pdf

10 Mackenzie, Janet, "Some of the potential impacts of Covid-19 on the TMT sector in Africa", Polity (16 March 2020), available at: https://www.polity.org.za/article/some-of-the-potential-impacts-of-covid-19-on-the-tmt-sector-in-africa-2020-03-16

11 van der Merwe, Morné, et al., "South Africa: The Impact of COVID-19 on Key African Sectors", Global Compliance News (26 March 2020), available at: https://globalcompliancenews.com/south-africa-the-impact-of-covid-19-on-key-africian-sectors/

12 South African Reserve Bank, *Monetary Policy Review* (April 2020), available at: https://www.resbank.co.za/Lists/News%20and%20Publications/Attachments/9839/Monetary%20Policy%20Review%20%E2%80%93%20April%202020.pdf

13 Cronje, Jan, and Magubane, Khulekani, "Reserve Bank again cuts repo rate by 1 percentage point; predicts 6.1% fall in GDP for 2020", fin24 (14 April 2020), available at: https://www.fin24.com/Economy/South-Africa/just-in-reserve-bank-again-cuts-repo-rate-by-1-percentage-point-20200414

14 Republic of South Africa, National Treasury, *2020 Budget: Consolidation, Reform, and Growth* (26 February 2020), available at: http://www.treasury.gov.za/documents/National%20Budget/2020/2020%20Budget%20presentation.pdf

Financial impacts:

- Stock market collapse (this has already happened).
- South African government and other bond yields rising if investors perceive these bonds to be riskier as a result of real economy impacts (this has already happened to government bonds, and is not specific to South Africa, although perceived risk of South Africa may be heightened by weak fundamentals prior to the pandemic; Moody's government credit ratings downgrade confirmed these perceptions).
- Rand depreciation (this has already happened, also not specific to South Africa).
- Liquidity shortages globally and in South Africa.
- Silver linings: lower repurchase agreement (repo) rate (has already happened and may happen again), lower oil prices and lower domestic inflation.

Impacts on consumer confidence (further affecting demand)

- According to Investec's economic outlook on 17 March 2020, consumer confidence for 2020 has dropped, with average numbers similar to those towards the end of the Zuma presidency (from 2015 to 2017).[15]
- Perceived appropriateness of the present time to buy durable goods (e.g. vehicles, furniture, household appliances and electronic goods) fell to −26 in Q1 2020, a thirty-three-year low.[16]

Potential abuses:

- The Competition Commission and the National Consumer Commission are investigating companies for price gouging on items such as face masks and hand sanitizer.[17]

Mitigation

It is difficult for a government to manage an international supply shock. If components cannot be imported or replaced by domestic alternatives, domestic production must stop when local inventories run out. These inventories tend to be small given the prevalence of 'just-in-time' inventory management.

It may be easier to mitigate the effects of a local lockdown. Responses include fiscal and monetary programmes (e.g. cash transfers, interest-rate reductions and central bank support of government bonds) and other forms of support to businesses, particularly smaller businesses and workers who lose their jobs.

South Africa has taken or announced several such measures. The opportunity costs of fiscal support measures are likely to be significant and measurable; their benefits will be far harder to measure.

Measures already taken include:[18]

- The R500bn stimulus package discussed in the introduction to this document.
- The SARB has cut the repo rate by 200 basis points since March, to 4.25 percent, which is the lowest level since 1973.[19]
- The Department of Agriculture has set aside R1.2bn.[20]
- A Temporary Employee Relief Scheme has been established aimed at supporting payrolls and avoiding retrenchment.
- A national disaster benefit will be linked to the R3,500 monthly minimum wage. It will be paid for whatever period is shorter: a company's shutdown or three months. The national Unemployment Insurance Fund has surplus of more than R160bn.

15 Investec, "Consumer Confidence: drops to -9, two index points below the last print, and now at thee average of the latter Zuma years of 2015 to 2019" (16 March 2020), available at: https://www.investec.com/content/dam/south-africa/content-hub/annabel-bishop/sa-economics/documents/Consumer%20Confidence%20Q1.20%20docx.pdf
16 Ibid.
17 van der Merwe, Marelise, "Spar, Makro, Pick 'n Pay named in coronavirus price gouging crackdown", fin24 (25 March 2020), available at: https://www.fin24.com/Companies/Retail/spar-makro-pick-n-pay-named-in-coronavirus-price-gouging-crackdown-20200325
18 Most of these are listed in Merten, Marianne, "Lockdown: Details trickle out on economic support and essential services", Daily Maverick (25 March 2020), available at: https://www.dailymaverick.co.za/article/2020-03-25-lockdown-details-trickle-out-on-economic-support-and-essential-services
19 Tshwane, Tebogo, "Sarb cuts interest rates by another 100 basis points", Moneyweb (14 April 2020), available at: https://www.moneyweb.co.za/news/south-africa/breaking-sarb-cuts-interest-rates-by-another-100-basis-points/
20 Phakathi, Bekezela, "Farming sector to get more financial help amid Covid-19 outbreak", Business Day (24 March 2020), available at: https://www.businesslive.co.za/bd/national/2020-03-24-farming-sector-to-get-more-financial-help-amid-covid-19-outbreak/

- A Solidarity Fund, which has raised R500 million from across sectors of South African society, including government, was initially aimed at alleviating cash-flow problems at small businesses but now aims to support the healthcare system and vulnerable households and communities.[21]
- A Debt Relief Fund for South African-owned businesses that employ at least 70 percent South African citizens. Preference is for companies owned by women and the youth. This is also a safety net for informal businesses.
- R500 million of a R3bn Industrial Development Corporation facility is allocated for trade finance to import essential medical supplies. R700 million of the facility is for working capital, machinery and equipment.
- The Ministry of Tourism has earmarked R200 million for enterprises in the sector with annual turnover less than R2 million.
- Several competition law exemptions have been granted (healthcare, banking, retail property) to make allowance, for example, for banks to discuss payment holidays, debt relief, a halt on asset seizures and credit extensions to both businesses and individuals. Additional measures by government include allowing shopping malls and their tenants negotiate rental holidays and a halt to evictions.[22]
- Regulations have also been published recently aimed at tackling instances of price gouging with reference to excessive pricing in competition law and unfair pricing in consumer protection law.[23]
- South African Revenue Service will fast-track the payment of employment tax incentive reimbursements from twice a year to monthly to get cash into the hands of compliant employers.

What has happened elsewhere?

We can get a sense of the severity of this crisis by looking at Asian countries. In China, industrial production in January–February 2020 was nearly 15 percent lower year-on-year, while retail sales were more than 20 percent lower.[24]

A survey[25] of Chinese businesses provides another view of these impacts. Nearly 60 percent of the firms surveyed reported that their revenues had declined by 20 percent or more between January and February 2020, with half of that group reporting declines of 50 percent or more.

China's exports also collapsed during this period, falling over 17 percent between 20 January 2020 and 5 February 2020.[26]

Consequently, China's first quarter growth was –6.8 percent, the first contraction since China began reporting quarterly data in 1992.[27] Some losses could be recuperated before year-end: domestic consumption demand may rebound, and manufacturing capacity can be expanded quite easily in many instances. But demand for Chinese exports may not rebound for another few months, particularly in the US, so the scope to make up lost production will be limited. A recent Reuters poll suggests that China's 2020 GDP growth will be the lowest the country has achieved in nearly forty-five years; the median forecast in the poll was 2.5 percent (2019 growth was 6.1 percent).[28]

About five million jobs were lost in China in January and February 2020.[29] The International Labour Organization[30] has suggested that up to twenty-five million jobs could be lost worldwide.

Singapore's first-quarter GDP figures provide further insight. Advanced estimates released by Singapore's statistics agency (Singstat) on 26 March 2020 suggest that the economy contracted by 2.2 percent over Q1 2019.[31] On a seasonally adjusted and annualised basis, the economy contracted by 10.6 percent over Q4 2019—but this latter figure is less alarming than it appears if one assumes that conditions will normalise through the second and third quarters and that some lost production will be recuperated.

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21 Planting, Sasha, "Solidarity Fund: Stronger Together", Daily Maverick (31 March 2020), available at https://www.dailymaverick.co.za/article/2020-03-31-solidarity-fund-stronger-together.
22 Naidu, Lerisha, & Nxumalo, Sphesihle, "South Africa: Competition Law Exemptions and Regulations applicable during COVID-19", Baker McKenzie (24 March 2020), available at: https://www.bakermckenzie.com/en/insight/publications/2020/03/south-africa-competition-law-covid19
23 See Government Gazette Notice numbers 43116 (19 March 2020) and 43205 (3 April 2020).
24 Berger, Helge, Kang, Kenneth, & Rhee, Changyong, "Blunting the Impact and Hard Choices: Early Lessons from China", International Monetary Fund (20 March 2020), available at: https://blogs.imf.org/2020/03/20/blunting-the-impact-and-hard-choices-early-lessons-from-china/
25 Zhu, W, J Liu, W Wei and L Ouyang (2020), "COVID-19 and Impacts on SMEs: Survey Evidences", *CEIBS Business Review*.
26 Ibid.
27 Cheng, Jonathan, "China Records First Ever Contraction in Quarterly GDP on Coronavirus", Wall Street Journal, available at https://www.wsj.com/articles/china-set-to-report-plunge-in-first-quarter-gdp-11587086697.
28 Zhang, Lusha, & Yao, Kevin, "China's 2020 GDP growth set to sink to 44-year low as coronavirus cripples economy: Reuters poll", Reuters (14 April 2020), available at: https://www.reuters.com/article/china-economy-poll-idUSL3N2C11I4
29 Cheng, Evelyn, "Roughly 5 million people in China lost their jobs in the first 2 months of 2020", CNBC (16 March 2020), available at: https://www.cnbc.com/2020/03/16/china-economy-millions-lose-their-jobs-as-unemployment-spikes.html
30 International Labour Organization, "Almost 25 million jobs could be lost worldwide as a result of COVID-19, says ILO", press release (18 March 2020). https://www.ilo.org/global/about-the-ilo/newsroom/news/WCMS_738742/lang--en/index.htm
31 Ministry of Trade and Industry Singapore, "Singapore's GDP Contracted by 2.2 Per Cent in the First Quarter of 2020. MTI Downgrades 2020 GDP Growth Forecast to "-4.0 to -1.0 Per Cent", press release, https://www.singstat.gov.sg/-/media/files/news/advgdp1q2020.pdf

Nevertheless, Singapore did not implement a full lockdown, as South Africa is doing currently, and this will still be Singapore's worst-ever quarterly contraction. The Ministry of Trade and Industry confirmed in a statement on 26 March 2020 that Singapore's economy is now expected to shrink by between 1 percent and 4 percent this year—the first full-year recession in twenty years.[32] It is worth remembering that forecasted full-year growth rates would have been positive before this crisis began, so the annual production lost will be larger than the magnitude of the contraction.

Stimulus packages offer another way of thinking about the magnitude of potential impacts. Singapore announced a $6.4bn package in February and added a further $48bn on 26 March 2020. This equals nearly half the 2020 annual budget and more than double the 2009 GFC package.[33] The stimulus package recently approved by the US Congress, estimated at approximately $2 trillion, is more than double the estimated value of the GFC package passed in 2009.

These measures are not aimed primarily at supporting banks, but rather at supporting workers and businesses overcome by short-run problems. They are cash transfers rather than loans to banks, with the hope being that the former obviates the need for the latter. Nevertheless, knock-on problems for credit markets will be a reality of this crisis. As noted by the IMF, Chinese authorities had to intervene early on in interbank markets and implemented targeted cuts to bank reserve requirements.[34]

32 Lee, Yen Nee, "Singapore expects its economy to shrink in 2020 due to the coronavirus pandemic", CNBC (25 March 2020), available at: https://www.cnbc.com/2020/03/26/coronavirus-singapore-releases-first-quarter-gdp-advance-estimates.html

33 Sim, Royston, "Singapore Govt pumps in $48b more to fight Covid-19 fallout, on top of $6.4b already announced", *The Straits Times* (26 March 2020), available at: https://www.straitstimes.com/politics/singapores-aviation-and-tourism-sectors-most-badly-hit-by-coronavirus-pandemic-dpm-heng

34 Berger et al. (2020), *op cit.*

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Conclusions

The latest SARB forecast for South African GDP growth in 2020 is negative 6.1 percent[35]; this is a significant change from the April Monetary Policy Review, which was published on 8 April 2020, and forecast a contraction of between 2 percent and 4 percent. The updated forecast accounts for the extended lockdown period were announced over the Easter weekend.

These expectations align with past experience in Asian economies that are 'further along' the path of the epidemic. China's GDP growth forecast for 2020 is the lowest in forty-four years, and Singapore's is negative for the first time in twenty years.

The last time South Africa's economy contracted was in 2009, during the GFC. That contraction was much smaller at 1.5 percent, and the economy rebounded sharply, posting 3 percent growth in 2010 and 3.3 percent in 2011. It is not clear yet whether the economy will rebound sharply from the current crisis. It will depend on how soon the lockdown is lifted, how we will operate as a society after the lockdown ends, and the extent to which demand recovers both domestically and in major trading partners. The longer the lockdowns in South Africa and its major trading partners continue, the more jobs and businesses will be lost, and the lower the probability will be of a sharp recovery.

35 White, Ray, "Reserve bank cuts repo rate to 4.25%", EWN (14 April 2020), available at: https://ewn.co.za/2020/04/14/reserve-bank-cuts-repo-rate-to-4-25

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