



Global outlook: April 2009

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The current economic, business and investment environment remains extremely challenging.

The biggest concern is the escalation in job losses which could substantially worsen an already dire situation. The global recession is occurring in “fast forward”.

Fortunately, massive policy support is now being provided to try and lift the global and local economy. Realistically, output declines are likely to persist for most of 2009 but the current policy stimulus should allow for at least a modest economic recovery during 2010.

All major economies are in a recession

During the first quarter of 2009 economic data from the US, Euro-area, UK and Japan has been alarmingly weak. Economic activity has declined at its fastest pace since the 1940s, while unemployment is moving sharply higher on a global scale.

Currently all the major developed economies are in recession.

The weakness in global economy has been sudden, severe and widespread. Unsurprisingly, the International Monetary Fund (IMF) has again revised their world growth forecast, from +0.5% in late 2008 to -0.5%. As expected, most central banks around the world continued to cut interest rates in the first quarter.

Equity prices continue to fall

Since the beginning of 2009 the US and global equity prices have continued to fall. By the middle of March the S&P 500 was down around 13% (in early March the equity market had lost a dramatic 25%). This follows a loss of around 38% in 2008. Residential property prices continue to decline.

USA: consumer debt falls and savings rises

Consumer debt in the US, which excludes mortgage debt, fell by a very significant \$20.9 billion towards the end of 2008. This extremely rare event was expected to have continued into 2009. This trend is shown in the increased personal savings rate in the US, which rose from essentially 0% of disposable income in early 2008 to the current level of 5.0% of disposable income; the highest ratio of personal savings in more than a decade.

Although US consumers have lost \$11.3 trillion in asset values over the past year, the net worth of US households totalled a still impressive \$51.5 trillion at the end of 2008. This equates to a respectable 483% of disposable income (4.83 times annual income after tax) compared to an average of 490% since 1960.

Looking forward: two main risks

There is a risk that house and equity prices continue to decline significantly. This would further destroy a significant amount of household wealth and weaken the already fragile US banking system.

The second risk is that job losses of over 650 000 a month continue, putting pressure on the ability of consumers to service their debt. This would aggravate asset prices and weaken the banking sector.

USA shows tentative signs of improvement

Fortunately recent key US economic data has shown tentative signs of improvement towards the end of the first quarter of 2009. The Federal Reserve has indicated that it will continue to purchase mortgage-backed securities as well as US government bonds. This, together with the record low federal funds rate, should keep mortgage rates relatively low and encourage an increase in housing activity. US mortgage applications have started to move up while the Volatility Index (VIX) has eased.

Economic activity in South Africa has slowed substantially

Against the backdrop of a sharply weakening global economy, economic activity in SA has slowed substantially in recent months, especially manufacturing and export activity. The manufacturing sector is in recession and under enormous pressure due to slowing exports, a very weak motor industry, excess inventories and a slowdown in general domestic activity, including the building industry.

This slump in activity is reflected in the Q1 2009 Business Confidence index, which fell by a further 6 index points to 27, its lowest level in 10 years. For 2009 we forecast GDP to slump to only 0.5% year-on-year, with most key sectors of the economy expected to be either in recession or on the brink of recession.

Performance of SA asset classes

During 2008 the domestic bond market was the best-performing asset class in SA, yielding 17%. Most of that gain was achieved in the last quarter of 2008, after a dismal first half performance. The market has since declined a few percentage points due to concerns about a massive increase in the public sector borrowing requirement.

In contrast, the SA equity market declined by a massive 23.2% in 2008, making 2008 the second worst annual (calendar) equity performance since 1960. The equity market continued to decline in early 2009 and by mid-March was down around 10%.

Concern about job losses

Many companies are facing earnings pressure given increased costs and slowing revenue growth. There is therefore growing concern that the economy will experience significant job losses. Hopefully, given SA's substantial skill shortage, most companies will be hesitant to cut employment extensively.

Impact of monetary and fiscal incentives will take time

Consumer inflation is expected to drop during the course of 2009. The sharp drop in the oil price, together with the slowdown in domestic demand, has significantly eased domestic inflationary concerns. This should allow for further interest rates cuts during 2009.

Interest rates take time to take effect and it is unrealistic to expect a significant response to this monetary stimulus before the end of 2009. In addition, the increased fiscal stimulus in the form of personal tax cuts and increased government spending, will also take time to have a positive impact.

** All figures quoted as at 28 February 2009, unless otherwise stated