NWU Business School

Policy Uncertainty Index (PUI)

4Q 2020

EMBARGOED UNTIL

11 January 2021

EXECUTIVE SUMMARY

- The NWU Business School Policy Uncertainty Index (PUI) at 56.7 for 4Q 2020 remained on a high plateau deep in negative territory, compared with 58.0 in 3Q 2020 (baseline 50).
- As 2020 drew to a close many parts of the world as well as SA again grappled with the seismic impact on lives and livelihoods of renewed surges in Covid-19. Global growth is still expected to be in positive territory this year, rebounding to about 5%, after being strongly negative in 2020. Several uncertainties remain and depend heavily on how quickly vaccines can be distributed internationally to combat the virus.
- Regarding the SA economy, although the recent return to adjusted Level 3 restrictions announced on December 28 will have some negative impact on growth, on present evidence the GDP growth rate in 2021 is likely to 'rebound' to about 3%.
- This recovery still needs to be urgently underpinned by economic reform policies which strengthen investor confidence and boost *sustained* job-rich growth.
- Six actions to minimize policy uncertainty and support economic recovery include:

  (a) coordinating the twin policy pillars of sustainable economic growth

  (b) the SONA and main Budget in February must build credibility

  (c) emphasis on an 'implementation-led' economic recovery

  (d) taking the tough economic and political decisions required in 2021

  (e) cutting borrowing costs further

  (f) expediting SA's access to vaccines
- 'I don't know how to explain this anymore.... Economic agents: investors, businesses, consumers, buyers and sellers of goods, farmers, the market etc, need policy certainty. FUNDAMENTAL. I invest because I will harvest in X-years in the forward market. CONFIDENCE! (*Finance Minister Tito Mboweni, 22/11/2020).*

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NWU BUSINESS SCHOOL POLICY UNCERTAINTY INDEX (PUI) AT 56.7 IN 4Q 2020 REMAINS DEEP IN NEGATIVE TERRITORY, COMPARED TO 58.0 IN 3Q 2020 (BASELINE 50)

NWU BUSINESS SCHOOL POLICY UNCERTAINTY INDEX (PUI)

1. INTRODUCTION

As outlined when the PUI was launched in early 2016, the role of policy uncertainty has loomed large in much of the recent economic debate in SA. It is seen to have important implications for business confidence and the investment climate in the country. Hardly any recent economic assessment or media release from international or local financial institutions, business lobbies, economic analysts, financial journalists or credit rating agencies appears without the inclusion of the words 'policy uncertainty' occurring in them.

The design of a policy uncertainty index for SA has nonetheless been spurred not only by economic circumstances in the country, but also by the increasing academic and policy interest globally around the cause, effect, measurement and definition of policy uncertainty. There is now a ‘World Uncertainty Index’ (WUI) created recently by the IMF and Stanford University to calibrate rising levels of policy uncertainty in the global economy.

There have been many manifestations of policy uncertainty in SA over the years. The institutional setting and policy making environment clearly influence the extent to which negative shocks and developments lead to bad outcomes and tough policy challenges. It seemed that the time had arrived to craft a more accurate measurement of this recurrent factor in SA's economic outlook. A deeper understanding of how uncertainty 'shocks' affect the SA economy helps policy makers to assess how future shocks will impact markets and business. The outcome of this research will now be made regularly available on a quarterly basis to hopefully fill a gap in our monitoring of the economic environment.

Interesting correlations have been found of the policy uncertainty index with economic outcomes. Empirically it shows that when economic policy uncertainty is strongly present in the environment, it indeed lowers investment, employment and output. High levels of such policy uncertainty inhibit meaningful investment and consumption. Elevated policy uncertainty in many countries contributes to sluggish growth. Economic policy uncertainty then has actual consequences for the economy.

Research suggests that uncertainty is very different across economies. Developing countries seem to have about one-third more macro-economic uncertainty than developed countries. However, this is now changing with events such as Covid-19, the controversial policies of US president Donald Trump as well as other geo-political tensions.

The PUI is published in January, April, July and October of each year. An increase beyond 50 reflects heightened policy uncertainty; a decline in the PUI means reduced uncertainty. The value of the PUI as a proxy for policy uncertainty will lie in tracking changes in policy uncertainty over time.

2. PUI RESULTS FOR 4Q 2020 - WHAT DOES IT SAY?

The PUI is the *net* outcome of *positive* and *negative* factors influencing the perceptions of policy uncertainty over the relevant period. The outcome for 4Q 2020 shows an average score of 56.7, compared to 58.0 in 3Q 2020. Thus, although levelling off, for now the PUI remains on a high plateau in negative territory.

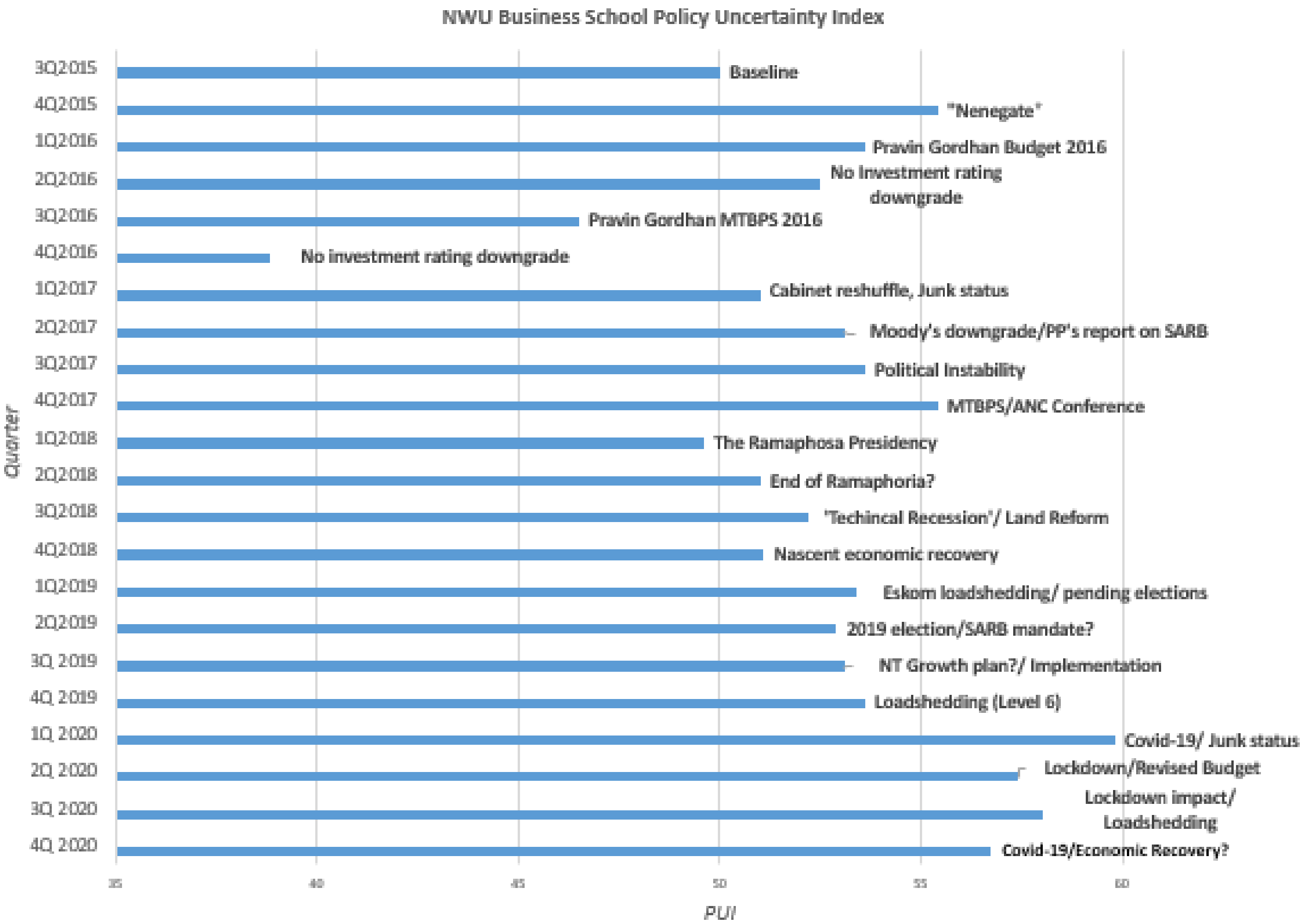
NOTE: It should be pointed out that the usual inputs to the PUI were received *before* the reintroduction of the adjusted level 3 lockdown restrictions announced by President Cyril Ramaphosa on December 28.

Unpacking the three elements of the latest index shows the following:

2.1 in the *media data* there was a slightly lower level of reference to economic/policy uncertainty as compared with 3Q 2020.

2.2 the *survey of economists* still reflected high levels of policy uncertainty.

2.3 the University of Stellenbosch's Bureau for Economic Research *survey of manufacturers* experiencing policy/political uncertainty declined marginally from 85 to 81.



3. NARRATIVE ON SOME FACTORS INFLUENCING ECONOMIC/POLICY UNCERTAINTY

3.1 The Global Economic Outlook

It was evident that, as 2020 drew to a close, in many parts of the world as well as in SA, both again grappled with the seismic impact on lives and livelihoods of renewed surges in Covid-19. Travel links and supply chains have again been placed under severe strain. In the face of the recent renewed surges in the pandemic, Covid-19 exit strategies are, more than ever before, a complex process of balancing trade-offs, handling fears and maintaining trust - all on the basis of shifting evidence and imperfect information, but with profound economic implications

Although the global pandemic to a greater or lesser extent has disrupted economic and business links worldwide over the past year its economic impact has varied across regions. The consequences have been largely dependent on a region's economic position and this has again become apparent with the 'second wave' of Covid-19. Towards the end of 2020 several countries began to climb from depths of the Covid-19 towards a degree of 'normality' but this has now been jeopardized by the pandemic's recent aggressive resurgence.

In October 2020 the IMF even made an upward revision of its 2020 global growth forecast to -4.4% (from -5%). World growth is still projected by the IMF to rebound to 5.2% in 2021 but with wide differences between regions. Overall global economic growth this year is therefore still expected to regain positive territory, yet with several uncertainties prevailing. In this process global value chains are also undergoing profound changes.

As the world moves into year two of the pandemic there remain several unknowns about the future trajectory of the virus. But despite the spike in many parts of the world, how well countries will fare will still be eventually determined by how quickly their economies and societies recover from their respective lockdowns and by the success or otherwise of the policies they have followed so far. Painful lessons are being learned about an unprecedented pandemic that has created enormous challenges for policy makers around the world.

Above all, the most important hope for the world economy lies in the early availability of vaccines. The ability to move beyond Covid-19 sooner rather than later now depends on how soon vaccines become widely available. It is indeed a race against time to get effective vaccines distributed throughout the world as rapidly as possible, and on an equitable and affordable basis.

Finally, on the global front there is now the Brexit 'deal' between the UK and the EU which was settled just before the transitional deadline of December 31. It was rather overshadowed by the preoccupation with Covid-19 but nonetheless remains an historic watershed moment for future economic and other relations between the UK, the EU and even third party countries like SA doing business with those two important economic entities.

SA must remain alert to any possible unintended trade or supply chain consequences arising from the new complex 'Canada-style' UK/EU free trade agreement now in operation.

3.2 The South African Economy

It is no surprise that the 4Q 2020 PUI remained well in negative territory. Although there was generally better high frequency economic data in 4Q 2020, a large 'bounce back' in 3Q 2020 growth, as well as the important message of the Medium Term Budget Policy Statement (MTBPS) in October, negative factors continued to outweigh the positive ones, including the gradual lockdown exit strategy. However, with the inputs to the latest PUI having been made before the return to adjusted Level 3 restrictions were announced on December 28, would prior knowledge thereof have made the 4Q 2020 PUI a little higher or not?

It must be recalled that it was previously agreed in 2020 that it was essential for SA to already look beyond the pandemic. The SA economy was extremely vulnerable even before Covid-19 shock and the initial drastic and prolonged lockdown simply reinforced the existing fault-lines of unemployment, poverty and inequality in SA. Whereas for most other economies the coronavirus interrupted a positive growth cycle, for SA it widened and deepened an existing recession.

SA therefore has faced a double challenge: to contain and manage Covid-19 outbreaks while simultaneously implement policies and projects to promote *sustainable* inclusive growth. To do so successfully policy reform and essential infrastructure projects needed to be kick-started, even before the pandemic was over. Hence the formulation of various growth and fiscal plans in 2020. These have nonetheless continued to be beset with an ambiguous sense of economic direction, weak implementation and poor policy coherence, thus perpetuating policy uncertainty

The latest sudden return to adjusted Level 3 lockdown restrictions on December 28 in response to the recent renewed surge in the coronavirus was clearly a necessary step but will have economic consequences. They are likely to have some negative impact on growth in 2021, and might delay the anticipated modest economic recovery until the second half of the year. The pace of SA's economic revival in 2021 will therefore to a large extent depend on whether the Level 3 restrictions are extended beyond January 15 or even tightened, whether economic support measures are extended, and ultimately on how quickly the vaccine is available in SA this year

Overall, in the absence of real structural reforms the economic revival this year is unlikely to be more than a short-term 'rebound' of about 3% GDP growth. Among the bright spots on SA's economic horizon this year will also be the strong performance of the agricultural sector and certain commodity exports, both of which will help to push growth into positive territory. But what else should be done to help reduce economic uncertainty and strengthen recovery in 1Q 2021?

Six actions in the near future which could be 'game-changers' in lessening policy uncertainty and supporting an economic revival include:

- Coordinating the twin policy pillars of sustainable economic growth

The twin policy pillars on which hopes of sustainable job-rich growth now rest are the urgent implementation of the Economic Reconstruction and Recovery Plan (the growth plan) and the Medium Term Budget Policy Statement (the fiscal plan). These two plans must in 2021 now clearly 'speak to each other' in official 'messaging' and decision-making so as to project a coherent and balanced overall economic strategy

- The SONA and main Budget must build credibility

Two upcoming events (given their early time slot in 2021) in February have the potential to ameliorate policy uncertainty and boost confidence in the country's future economic direction. They are the state-of-the nation address (SONA) and the main Budget. There remains a serious credibility 'gap' to be overcome in 2021 and these key policy statements must be actively and creatively used to help close this gap, particularly also in wanting to ward off further investment rating downgrades

- Emphasis on an 'implementation-led' economic recovery

President Cyril Ramaphosa's recent reference to 'implementation, implementation, implementation' as the dominant mantra for SA's policies and projects must start to take tangible shape early this year. Drift and procrastination are the enemies of delivery and undermine policy certainty. The ever-present implementation risks must therefore be visibly reduced in 2021.

- Taking the tough economic and political decisions required in 2021

Tough decisions, such as what to do about the inflated public sector wage bill, need to be taken soon. Early evidence is needed that troubled and costly state-owned enterprises will be decisively restructured and the country's energy supply secured. The longer remedial action reform is delayed the more difficult the problems become to resolve. And the longer SA remains on its present path, the more policy uncertainty will persist and the longer it will take to recover.

- Cutting borrowing costs further

The next meeting of the Monetary Policy Committee (MPC) is on January 21. Although monetary policy cannot do the heavy lifting on growth, in current economic circumstances the MPC could now consider offering some additional support to business and consumers by further lowering borrowing costs. With the present combination of subdued inflation, a strong rand and weak growth there is room to contemplate another cut in interest rates in 1Q 2021.

- Expediting SA's access to vaccines

SA's access to one or more of the Covid-19 vaccines now available must be urgently expedited. It has now become an imperative factor for securing lives and livelihoods. Firm timelines for the delivery of vaccines would strengthen confidence and reduce uncertainty. The UK government, for example, has appointed a 'Minister for Vaccine Deployment' to specifically oversee the rapid distribution of the vaccines in that country. SA should perhaps also consider a similar dedicated appointment for this task. It is ultimately through speedy vaccination that the vaccine can be 'weaponized'.

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North West University Business School
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