Economic outlook - hoping for business as usual

By Craig Pheiffer

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If we can get back to "business as usual" soon in the United States, then the damage from the fiscal impasse can be limited. Should that be the case, then Gross Domestic Product (GDP) of 1,6% is forecast for the US in 2013 from 2,2% last year with expectations of a pick-up into 2014 of 2,3%.

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The current fiscal policy uncertainty as well as the change in Fed chairman could well push out the onset of tapering of asset purchases from the current expected start in December to March 2014. Even with the US government going back to work soon, some budget compromises will need to be made in the coming months to appease all parties and that could add additional drag to the economy just as the sequester did at the start of 2013.

The euro area economy emerged from recession in Q2 2013, but for the year a contraction of 0,3% in real GDP is expected before returning to a positive growth rate of 1,3% in 2014 (-0,6% in 2012). Q3 GDP growth is expected to come in slightly lower than that of Q2 and remain fairly subdued with risks to the fragile economy to the downside. The market will watch for developments on the Banking Union front but it could be some time yet before all of the required mechanisms for the Union are agreed upon.

Economic contraction in Q2 2014

In Japan the increase in the VAT rate from 5% to 8% in April 2014 is dominating the economic landscape. Demand from the frontloading of consumer purchases (and business' response) is expected to drive GDP growth in Q4 2013 and Q1 2014 before an economic contraction in Q2 2014 when the new rate comes into effect. The tax increase comes with ¥5 trillion of stimulus measures designed to combat the tighter fiscal policy and growth rates of 1,9% and 1,5% are forecast for 2013 and 2014 respectively (from 2,0% in 2012). By design, inflation has already turned positive and consumer inflation rates of 0,3% and 2,6% are expected in 2013 and 2014 respectively after many years of deflation.

The world's biggest economic engine may be growing at a moderate pace that is supporting global growth but world demand is only expected to expand at a 2,9% pace in 2013 and 3,5% in 2014 (from 3,2% in 2012). Global growth expectations have been revised lower on downward revisions to the expected growth rates of developing economies, most notably in China. While developed economies are expected to advance at a 1,1% pace in 2013 and 1,9% pace in 2014 (from 1,4% in 2012), the developing economies are expected to grow at 4,7% in 2013 and 5,0% in 2014 (from 5,0% in 2012).

In China, the government continues to drive a rebalancing of the economy away from asset investment towards domestic consumption. The accepted trade-off for "elevating China to a new stage of development" is slower growth in the shorter term and the Chinese authorities may well lower their forecast growth rate for the economy in 2014 to 7,0% from 7,5% in 2013. The Barclays team currently forecast growth of 7,6% in 2013 and 7,1% in 2014 from 7,7% in 2012 along with modest inflation and a neutral monetary policy stance.

Slowing growth, tighter global financial conditions

The softer global economy and weak domestic business and household confidence are expected to keep South African GDP growth at levels below potential and insufficient to create desired levels of employment. The International Monetary Fund cautioned in its October release of its World Economic Outlook that "Emerging market economies face the dual challenges of slowing growth and tighter global financial conditions". South Africa is no exception and a GDP growth rate of 2,0% is forecast for 2013 with a marginal pick-up to 2,8% in 2014 (from 2,5% in 2012).

Inflation is expected to decline back into the upper end of the target range from a Q3 peak but remain susceptible to external shocks. Core inflation has been increasing but the South African Reserve Bank is likely to keep interest rates flat for the duration of 2014 for as long as inflation is not demand-driven, consumer and business confidence is low, inflation expectations are well anchored and domestic growth remains pedestrian. The current account deficit and the budget deficit leave the rand vulnerable with potential political noise being added to the melting pot in the run up to the 2014 elections. We remain under the watchful eye of the ratings agencies and developments on the medium-term budget policy front as well as the labour front will be keenly monitored over the coming months.

ABOUT CRAIG PHEIFFER

Craig Pheiffer is head of Private Client Asset Management at Absa. He studied at the University of the Witwatersrand and Unisa graduating with a BSc Computer Science (Wits), BCom - Economics, BCom Hons - Economics and MCom (cum laude) - Economics (Unisa). His master's dissertation on "Capital Flight from Middle Income Countries" won the Economic Society of South Africa's Founders medal for the best dissertation in 2000.

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