

OLD MUTUAL MULTI-MANAGERS
MARKET MATTERS

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WINDS OF CHANGE



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Even by its usual windy standards, Cape Town was particularly blustery last week when the Budget Speech was delivered. This is especially considering that the event was held in a temporary dome – essentially a giant tent – while repairs to the fire-damaged Parliament building are ongoing. Metaphorically speaking, the winds of change are also blowing. The global economic and geopolitical environment is facing its biggest upheaval in years, perhaps decades, while locally, coalition politics brings a new dynamic to the budgeting process.

The latter cannot escape the former. SA-US relations have fallen to the lowest point in years. Already, US President Donald Trump has slashed spending on foreign aid. This leaves South Africa with a gap of around R8 billion a year to fill, particularly for treating tuberculosis and Aids, though there was no explicit allowance for this in the Budget. With the US imposing tariffs on friends and foes alike, it is very likely that duties on South African imports will go up at some point. This does not automatically translate into lower revenues for South African exporters, but some might be forced to cut prices to remain competitive in the US market.

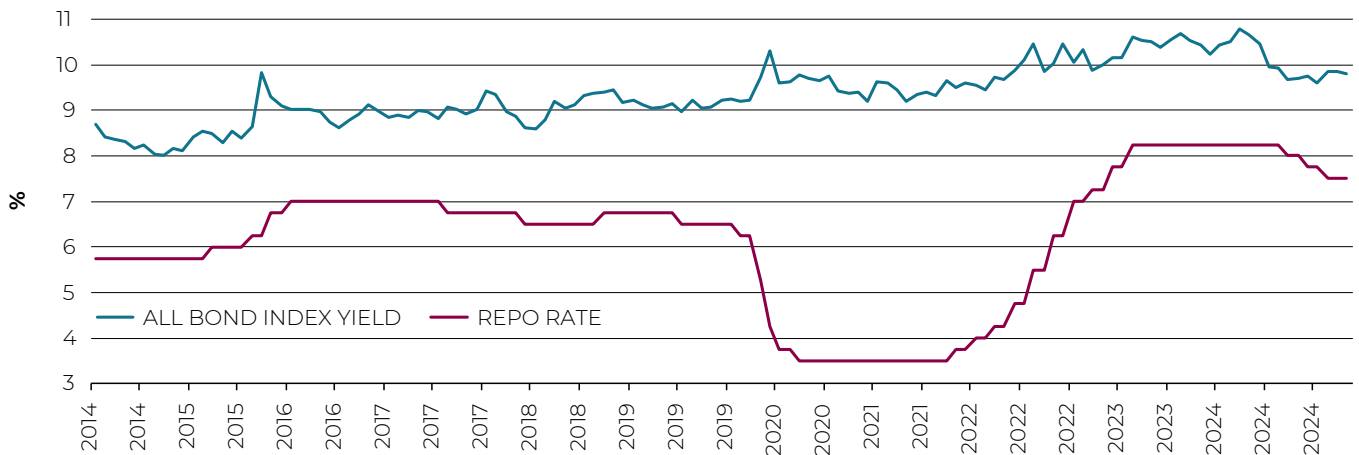
Beyond the direct impact on US-South Africa trade is the overall health of the global economy. If global economic growth comes under pressure due to US tariffs, South African exports to China, Europe and elsewhere might also be affected. This could be somewhat offset by the positive impact of Beijing's stimulus efforts, and Europe's planned increases in defence spending.

SENSITIVE

Above all, South Africa is very sensitive to shifts in global market sentiment and commodity prices. The country imports capital and exports commodities. It is notable that the rand has been relatively stable despite recent market jitters. This is due to a weaker dollar as markets sense a weakening US economy and potentially more rate cuts. But rand stability cannot be taken for granted, which complicates the picture for the Reserve Bank's Monetary Policy Committee (MPC) when it meets next week. It might still reduce the repo rate by 25 basis points, despite some upward inflationary pressure from VAT increases. This doesn't help the government, however, since it borrows longer-term in the bond market at much higher interest rates of around 10%.



CHART 1: ALL BOND INDEX YIELD AND REPO RATE



Source: LSEG Datastream

This means that whatever combination of government spending and revenue we end up with, it is very important that overall government borrowing levels are stabilised. South Africa does not have as much government debt relative to national income as the likes of the US or UK, but they borrow at much lower interest rates than we do. This means that our debt burden compounds much quicker. As it stands, the South African government spends more on interest payments than on social grants or education, and its interest burden keeps rising. It also spends more on interest than

most of our peers. Apart from squeezing out important areas of spending, it also means there is limited room to respond to shocks. In other words, 'fiscal consolidation' remains crucial. We need discipline on the spending side, and efforts to raise government's tax revenue. For the latter, only faster economic growth can deliver on a sustained basis. There is a limit to how many tax rate increases the economy is able to absorb, and taxpayers are willing to tolerate.

Indeed, that was the main message of the Budget Speech – economic growth and fiscal consolidation.

VAT ATTENTION

However, within an overall framework of fiscal consolidation, without borrowing more in other words, the finance minister proposed additional spending on key areas: accommodating the public sector wage increase, more infrastructure spending, above-inflation social grant increases and frontline service delivery support (more teachers and nurses). SARS will also get an additional allocation, which should pay for itself over time by improving tax collection.

The above does mark a shift after several years of spending curtailment. To fund this, the failed February Budget proposed a 2% VAT increase that was shot down by other parties in the GNU.

The second attempt at a Budget proposes a 0.5% increase in the VAT rate this year and next. This will ultimately raise the VAT rate to 16%. This remains a politically contentious

issue, however. Unlike in February, there is no bracket creep relief, and also no upward adjustment of medical aid credits. One positive for consumers is that there is still no fuel levy increase, despite the rand price of Brent crude oil falling almost 10% since the start of the year.

The VAT increases will temporarily add to inflation. About two-thirds of the CPI basket is VAT-able, so the full 0.5% increase in the VAT rate will not show up in inflation. Some companies might even absorb the increase to not raise the final price to the consumer. The previous VAT rate increase in 2018 saw very limited passthrough.

Overall, the tax changes will net an additional R28 billion in the coming fiscal year, but this is half of what was proposed in February. Accordingly, the spending increases are also scaled back.

SPENDING REVIEW

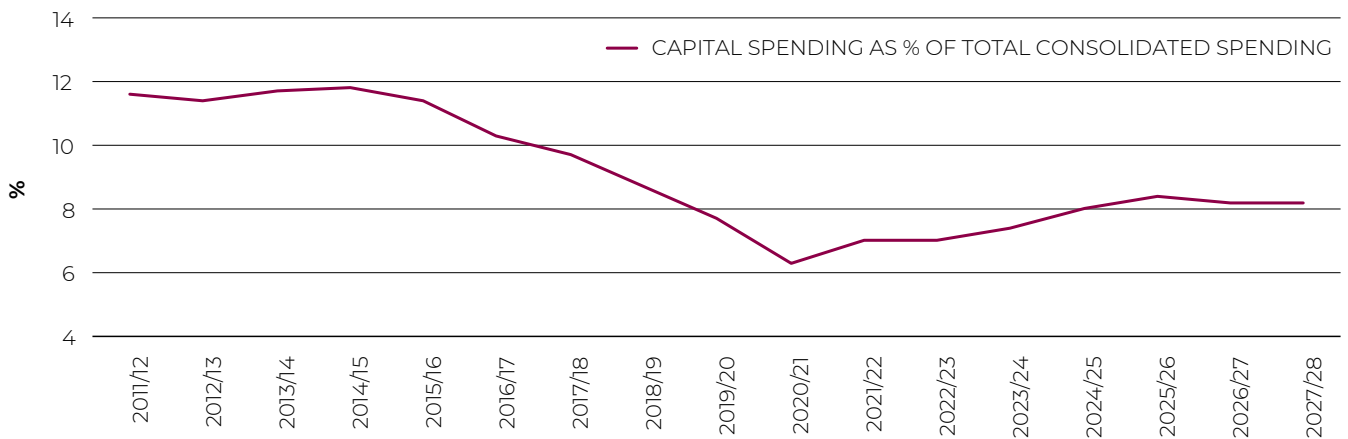
The spending side of the Budget contains dozens of pages full of details, but two things are worth highlighting here. Firstly, the public response to the proposed 2% VAT increase in February was overwhelmingly negative, with a chorus of voices calling for spending cutbacks instead. This was also the view of some GNU member parties.

Importantly then, unlike in February, the latest Budget Speech notes that spending reviews conducted by Treasury over the years will be consolidated and presented to Cabinet next month. It will also conduct an audit of ghost workers. This will presumably form the basis of much of the Budget negotiations within the GNU. A committee will be established between the Presidency and Treasury to identify waste,

inefficient and underperforming programmes. Savings from these initiatives are not factored into spending projections yet, but if done thoroughly and with political will, a lot of money can be found.

Secondly, there is an ongoing, though gradual shift in the mix of current and capital spending. The share of capital spending declined notably over the past decade, but the situation has started turning around. This is important, since capex will support economic activity over time. The government still spends a larger share of revenues on salaries compared to our peer group, but this is stabilising. Meanwhile, public infrastructure spending over the next three years will amount to more than R1 trillion.

CHART 2: CAPITAL SPENDING AS A SHARE OF TOTAL CONSOLIDATED SPENDING



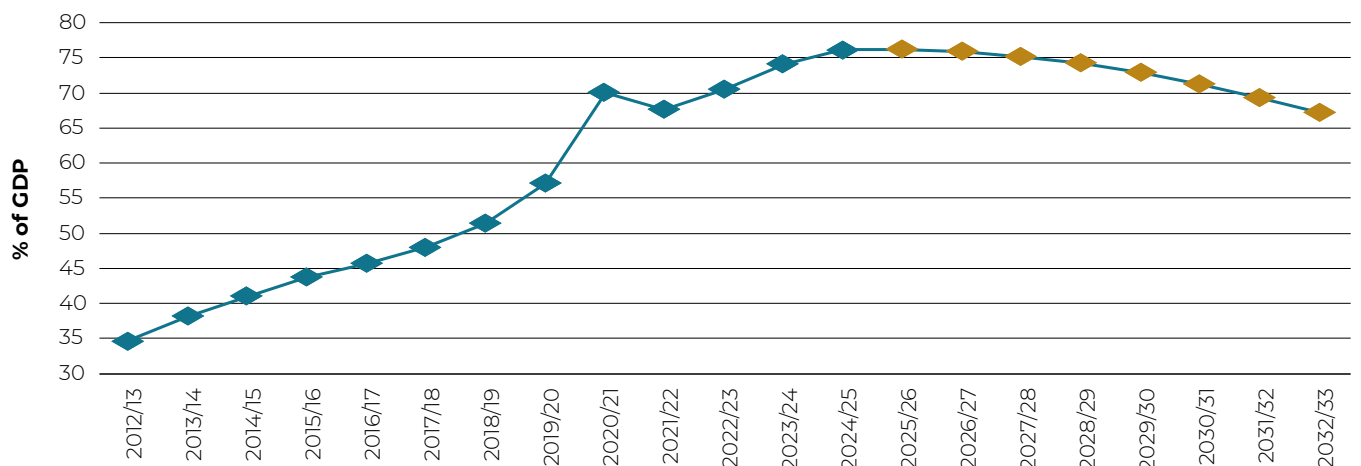
Source: National Treasury

DEFICIT TO SURPLUS

The difference between projected tax revenues and spending is the budget balance. This is usually expressed as a share of national income (GDP) and has been in deficit every year since 2008. It is expected to be in deficit to the tune of 4.6% of GDP in the 2025/26 fiscal year, narrowing to 3.5% by 2027/28. Notably, however, the balance between non-interest

spending and tax revenues – the ‘primary’ balance – has shifted from deficit to surplus and will rise over the next three years. This is an important step to stabilising debt levels. It means that tax revenues cover non-interest spending, while borrowing is only needed to make interest payments.

CHART 3: GOVERNMENT GROSS DEBT-TO-GDP RATIO, ACTUAL AND PROJECTED



Source: National Treasury

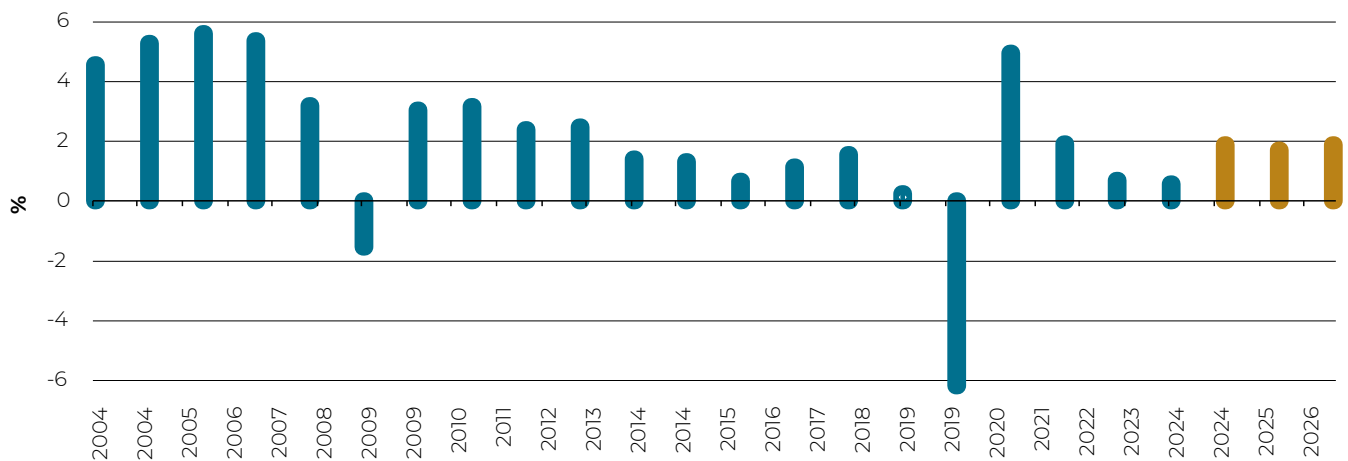
Government debt as a percentage of GDP is projected to peak at 76% the coming fiscal year and drift lower thereafter. This excludes government's guarantees of state-owned enterprises and other 'contingent' liabilities, which amount to around 10% of GDP. However, ratings agencies already include these in their assessments.

The expected peak in the debt ratio has been pushed out every year for the past decade, so seeing will be believing. Already, one ratings agency, Fitch, has indicated it doesn't think the ratio will peak soon. But if achieved, it will be worth cheering. Since growth reduces the need to borrow more (the numerator) while also raising the denominator of the

debt ratio, the faster the economy grows, the quicker it will decline.

Treasury expects real economic growth to average 1.8% over the next three years, a considerable improvement from 0.6% in 2024. In fact, excluding the Covid rebound, the last time the economy averaged growth of 1.8% over a three-year period was 2012-14. Ever since, growth persistently undershot Treasury's forecasts, so some scepticism would be natural, particularly given the uncertain global environment noted above. Nonetheless, the ingredients of a cyclical upturn – lower inflation, falling interest rates, improved confidence and rising private investment – are in place.

CHART 4: SOUTH AFRICA REAL ECONOMIC GROWTH WITH FORECASTS



Sources: Stats SA, National Treasury

To further stimulate economic growth, there is an emphasis on infrastructure spending. Beyond the planned above-mentioned R1 trillion in infrastructure spending by the public sector, there are several initiatives to crowd in private spending. This includes new regulations to simplify the processes for public-private partnerships (PPPs) and create capacity to support and manage them. New rules will also allow for unsolicited bids from the private sector. A credit guarantee mechanism will be set up to reduce risks faced by private sector investors. And the Budget Facility for

Infrastructure (BFI) will run multiple bid windows instead of just one annually. In these bid windows, private or public investors can submit requests for funding for large infrastructure projects. Instead of offering direct support to Transnet, for instance, the company will be able to tap the BFI for specific projects.

Notably, government will also sell its first infrastructure bond in the coming year, a way for pension funds and other investors to get direct infrastructure exposure.

COALITION COMPLICATIONS

The complication with all the above is getting agreement within the government of national unity (GNU). The DA, the second largest party in the GNU, opposes the VAT increase, unless it is paired with a comprehensive spending reduction (reportedly, it also seeks concessions unrelated to the Budget). This is where the winds of change of coalition politics will potentially be felt. This year, and perhaps in the years ahead, the Budget might be less of an event and more of a process.

The formal procedure is that the finance minister tables the Budget framework and accompanying bills in Parliament. The finance committees of both the National Assembly

and the National Council of Provinces must accept or amend the proposed fiscal framework within 16 days, before it can be adopted by the National Assembly. Over the past 30 years, the ANC majority meant that in practice, Parliament almost always accepted the Budget as tabled. Now that no party has a majority, the compromise that was not reached within the GNU Cabinet before the Budget Speech must be found in this Parliamentary process. It is still likely that it will as the parties are not particularly far apart. It does, however, introduce uncertainty since the final product might be somewhat different from what is proposed by National Treasury.

It was always the intention in the Constitution that Parliament provides oversight and input into fiscal policy. However, while Treasury remains a centre of excellence in government, the same cannot always be said of Parliament, so investors will keep a close eye on this shift. Parliament does have a Budget Office to conduct fiscal analysis, but it rarely

SLOW PROGRESS

Remember that whether you consider this to be a “good” Budget will depend on whether you view it from your perspective as a taxpayer, or as an investor. For taxpayers, there is little cheer. For investors, however, there is ongoing, though slow, progress with limiting government borrowing. This should support the valuations of South African bonds and equities over time. The scale of the fiscal and growth challenges means South African assets will probably continue to trade at a discount – the market will continue to price in the risk of a sudden turn to populism. However, it will not

contribute to the public debate, while the constitutionally mandated Fiscal and Financial Commission is equally quiet. The main thrust of fiscal policy should remain unchanged, however, and that is the emphasis on supporting faster growth and stabilising government debt.

be able to ignore evidence of faster growth and sensible policy forever either. As we saw with the recent unexpected rerating in European shares, things don't need to go from bad to good for undervalued assets to rally. They just need to go from bad to less bad; it is the direction of travel, not the destination, that often matters more. Nonetheless, given the increasingly uncertain global climate, effective implementation of economic and fiscal policy reforms is more urgent than ever.

EQUITIES - GLOBAL

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
Global	MSCI World	US\$	3 666.0	-1.98%	-3.65%	-1.13%	8.40%
United States	S&P 500	US\$	5 639.0	-2.27%	-5.31%	-4.13%	9.50%
Europe	MSCI Europe	US\$	2 267.0	-1.18%	2.35%	13.18%	7.59%
Britain	FTSE 100	US\$	11 166.0	-0.44%	0.76%	9.17%	13.07%
Germany	DAX	US\$	2 133.0	0.05%	6.76%	20.99%	26.74%
Japan	Nikkei 225	US\$	249.3	0.05%	1.05%	-1.77%	-4.73%
Emerging Markets	MSCI Emerging Markets	US\$	1 120.0	-0.80%	2.10%	4.19%	6.77%
Brazil	MSCI Brazil	US\$	1 333.0	3.57%	6.64%	13.25%	-19.11%
China	MSCI China	US\$	77.2	-0.13%	6.40%	19.66%	39.47%
India	MSCI India	US\$	924.5	-1.26%	1.92%	-9.72%	-4.50%
South Africa	MSCI South Africa	US\$	482.0	-0.21%	5.93%	12.09%	26.18%

EQUITIES - SOUTH AFRICA (TOTAL RETURN UNLESS INDICATED OTHERWISE)

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
All Share (Capital Only)	All Share (Capital Index)	Rand	87 916.0	-0.74%	2.30%	4.54%	19.87%
All Share	All Share (Total Return)	Rand	16 125.0	-0.54%	2.53%	4.89%	24.18%
JSE Capped SWIX	Capped SWIX (Total Return)	Rand	39 366.6	-0.48%	2.39%	4.61%	23.48%
TOP 40/Large Caps	Top 40	Rand	14 621.0	-0.41%	2.96%	7.33%	24.46%
Mid Caps	Mid Cap	Rand	24 590.0	-0.90%	1.32%	-2.20%	16.12%
Small Companies	Small Cap	Rand	40 930.0	-0.14%	-0.81%	-7.57%	27.66%
Resources	Resource 20	Rand	5 610.3	0.87%	12.43%	24.39%	22.69%
Industrials	Industrial 25	Rand	27 418.0	-1.46%	0.79%	5.32%	26.08%
Financials	Financial 15	Rand	15 414.0	-0.19%	0.07%	-1.83%	25.43%
Listed Property	SA Listed Property	Rand	2 306.9	0.48%	-1.41%	-4.00%	18.06%

FIXED INTEREST - GLOBAL

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
IBOXX Global Government S&P Overall (USD Unhedged)		US\$	75.2	-0.24%	0.23%	1.85%	-0.98%

FIXED INTEREST - SOUTH AFRICA

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
All Bond	BESA ALBI	Rand	1 107.8	0.00%	-0.04%	0.47%	18.70%
Government Bonds	BESA GOVI	Rand	1 091.2	0.00%	-0.02%	0.50%	18.64%
Inflation Linked Bonds	BESA CILI	Rand	379.8	0.05%	0.18%	0.85%	9.91%
Cash	STEFI Composite	Rand	603.9	0.14%	0.29%	1.54%	8.32%

COMMODITIES

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
Brent Crude Oil	Brent Crude ICE	US\$	70.6	0.31%	-3.32%	-5.89%	-16.96%
Gold	Gold Spot	US\$	2 983.0	2.44%	4.41%	14.03%	37.53%
Platinum	Platinum Spot	US\$	1 009.0	4.67%	7.23%	10.27%	9.08%

CURRENCIES

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
ZAR/Dollar	ZAR/USD	Rand	18.47	-1.20%	1.19%	1.99%	1.45%
ZAR/Pound	ZAR/GBP	Rand	23.52	0.38%	0.00%	0.47%	1.57%
ZAR/Euro	ZAR/EUR	Rand	19.78	-0.05%	-1.97%	-1.16%	3.09%
Dollar/Euro	USD/EUR	US\$	1.09	-0.92%	-4.77%	-5.05%	0.00%
Dollar/Pound	USD/GBP	US\$	1.29	-0.11%	-2.59%	-3.36%	-1.04%
Dollar/Yen	USD/JPY	US\$	0.01	0.40%	-1.31%	-5.45%	0.22%

Source: I-Net, figures as at 14 March 2025

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