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Covid-19 relief: R500bn in phase II

- President Ramaphosa announced a R500bn package to curb the economic impact of the COVID-19 pandemic. Government regards this as the second of three phases of its economic response to the crisis: the initial phase included the tax relief, release of disaster relief funds, UIF wage support and SMME funding announced when a national disaster was declared; this (second) phase includes a significant increase in the health budget, hunger and social disaster relief, support for companies and workers, and a phased opening up of the economy to stabilise the economy, address lower demand and supply and protect jobs; and the third phase will be the economic recovery strategy, which will include stimulating demand and supply through interventions such as an infrastructure build programme and "speedy" implementation of economic reforms.

- We interpret the R500bn as comprising: R130bn of reprioritised fiscal spending, a R200bn loan guarantee scheme, R70bn of tax relief measures, and R100bn to protect and create jobs (see detail overleaf). Furthermore, government estimates that the SARB's rate cuts unlock at least R80bn in the real economy. While the entire R500bn of announced interventions are geared towards alleviating the economic impact of the pandemic, it isn't all additional stimulus: R130bn is redirected spending, and a large part of the R70bn of tax relief are deferred tax payments rather than permanent savings. We assume that the R100bn to protect and create jobs will be funded from the Unemployment Insurance Fund (UIF). The immediate fiscal impact thus appears to be small relative to the total package, though the ultimate total cost will partly depend on the performance of the guaranteed loans. While the R500bn total package is larger than we expected at this stage, the modest fiscal impact is in line with our expectations given the dismal fiscal prognosis even before the crisis.

- Treasury is working with the World Bank, IMF, New Development Bank and African Development Bank on various funding transactions. As we've indicated before (see From the crisis, a rare opportunity for reform), we expect SA to utilise the IMF's rapid financing instrument, from which SA can get up to about R70bn this year, with very little conditionality and at a very low interest rate. It is thus not surprising that the ANC government and Cosatu endorsed such a loan, notwithstanding their usual IMF aversion. The bond market will be relieved about the immediate funding relief provided by such loans and also that government mobilised such large resources to curb the economic impact of the crisis with relatively little additional fiscal impact. However, ultimately, the crux for the currency and bond prognoses is whether the next announcements will ease fears about the lack of debt stabilisation in the medium term. Announcements on the post-lockdown easing of economic restrictions (due on Thursday) and government's final wage settlement (with arbitration for the FY20/21 wage increase reportedly scheduled for 28-30 April, and the next multi-year negotiations likely much later) will obviously have a material bearing on the fiscal trajectory (see some simulations in Fiscal scenarios highlight need for reform). However, the crux will be whether the third phase economic recovery interventions convincingly lift trend growth adequately to support debt stabilisation. President Ramaphosa said that he will outline the growth interventions "in the coming days", indicating that this will "accelerate the structural reforms required to reduce the cost of doing business, to promote localisation and industrialisation, to overhaul SOEs and to strengthen the informal sector". This is consistent with the core view in our recent report From the crisis, a rare opportunity for reform that the crisis will finally compel government to accelerate key reforms (even if select reforms will be delayed as a result of the crisis). This is a critical assumption underpinning our forecast for material rand and bond gains in the medium term (see Lockdown hits growth, prevents bigger crisis and Bonds: weak basics, punishing premium).

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- Government's new package includes the following spending measures: R20bn to fund the health response to coronavirus (including personal protective equipment for health workers, community screening, an increase in testing capacity, additional beds in field hospitals, ventilators, medicine and staffing); R20bn for municipalities to provide emergency water supply, increased sanitisation of public transport and facilities, and food and shelter for the homeless; and a R50bn increase in social grant payments for the next six months, including temporary increases in all the existing grants and a special COVID-19 social relief of distress grant of R350 per month for six months to individuals who are currently unemployed and don't receive any other form of social grant or UIF payment; and food assistance through vouchers and cash transfers.

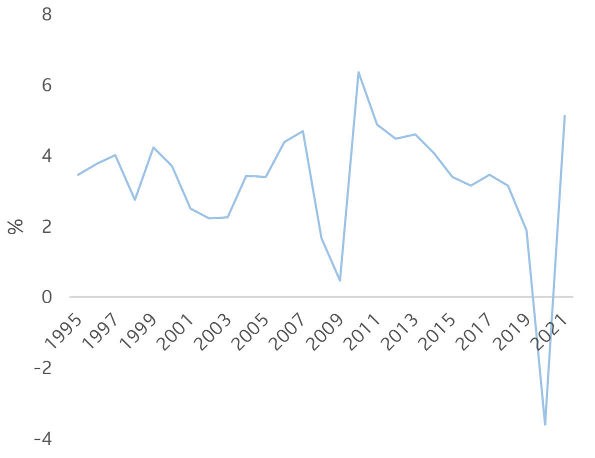
- The new R200bn loan guarantee scheme will be in partnership with the major banks, the Treasury and the SARB, to assist enterprises with operational costs (such as salaries), rent and the payment of suppliers. Initially, companies with a turnover of less than R300mn per year will be eligible; government expects the scheme to support 700 000 firms and 3 million employees.

- Tax relief includes a 4-month holiday for skills development levies, fast-tracking VAT refunds, a 3-month delay for filing and first payment of the carbon tax, an increase in the turnover threshold for tax deferrals to R100mn a year with the portion of PAYE payments that can be deferred increased to 35%, and tax deductibility of donations to the Solidarity Fund. Government expects these changes to provide around R70bn of relief. Most of these measures are deferrals and should thus have only a modest permanent fiscal impact. We have included this in our fiscal forecasts.

- We currently foresee a 5% real GDP contraction in 2020, followed by a sizeable rebound in 2021 (see Lockdown hits growth, prevents bigger crisis). The relief measures announced by government temper the downside risk to our 2020 forecast somewhat, with growth also supported by elevated terms of trade (see charts overleaf), particularly in light of the collapse in oil prices (though the benefit will ultimately depend on the sustainability of this retreat). The GDP rebound that we foresee in 2021 is supported by the bounce forecast for SA's export destinations (see charts overleaf), although this assumption, like the sustainability of favourable terms of trade, is subject to exceedingly high forecast risk. Growth should also in 2021 benefit from the lagged impact of easier monetary policy.

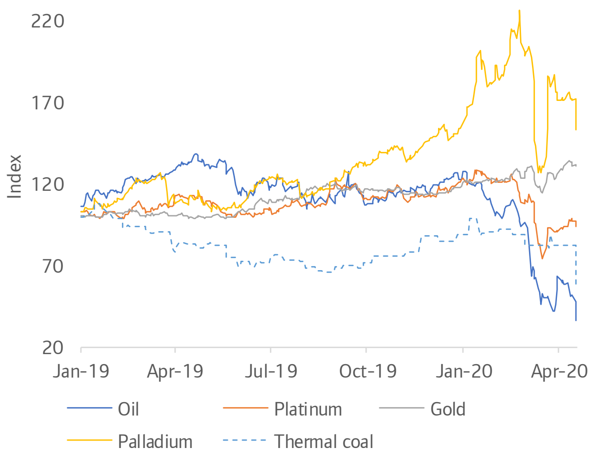
- We foresee a fiscal deficit around 11% of GDP in 2020. The sizeable spending that was reprioritised in FY20/21 (as discussed above) is probably a combination of permanent savings and some delays. The permanent savings should support quicker medium-term fiscal consolidation than what we expected prior to the announcement. Our forecasts don't at this stage incorporate any tax hikes next year, though this would presumably to a large extent depend on the strength of the economy at the time.

Figure 1: Strong rebound in SA's (weighted) export destinations in 2021 should support local growth



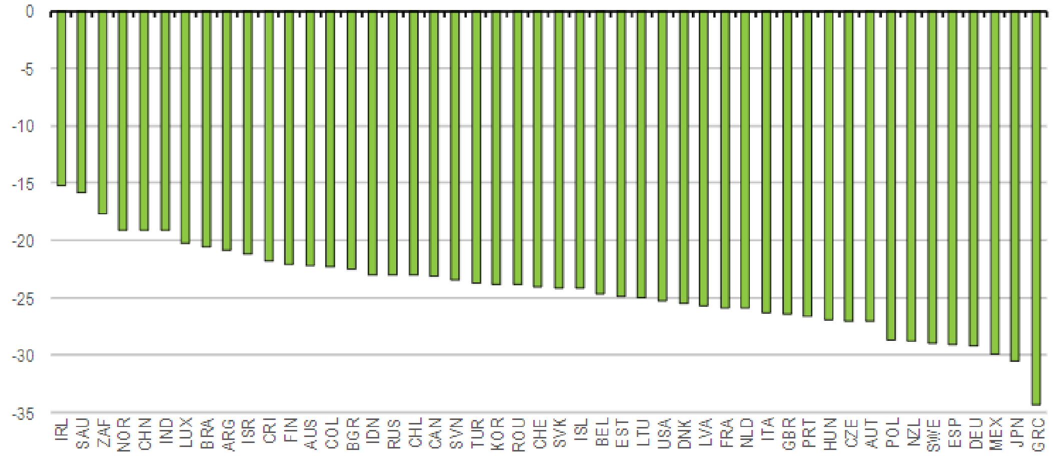
Source: IMF, Standard Bank Research

Figure 2: Elevated terms of trade currently growth supportive



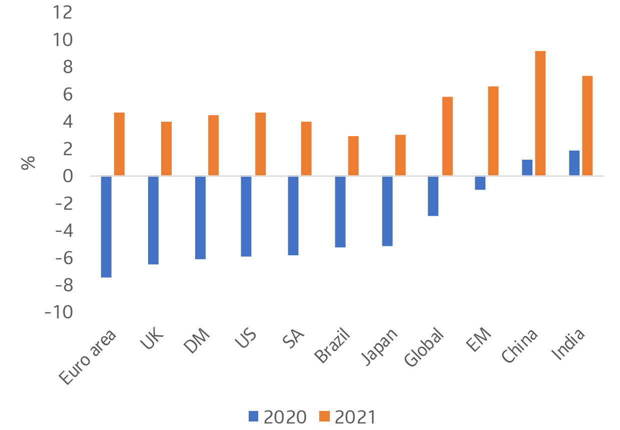
Source: Bloomberg, Standard Bank Research

Figure 3: OECD expects SA growth impact from lockdowns to be relatively small vs peers, though this partly reflects OECD assumptions



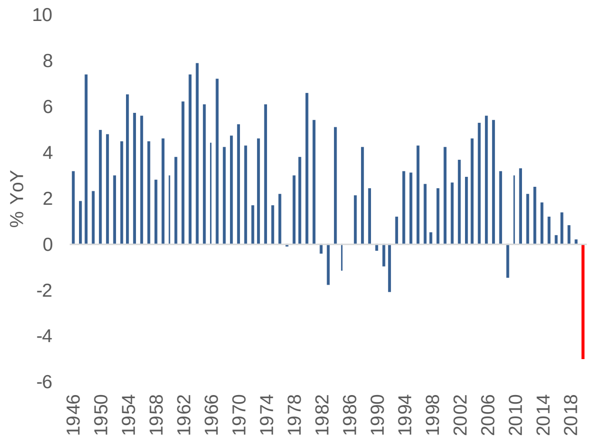
Source: OECD

Figure 4: IMF expects SA to be middle of the pack in terms of growth amid coronavirus pandemic (which appears more reasonable to us than OECD optimism above)



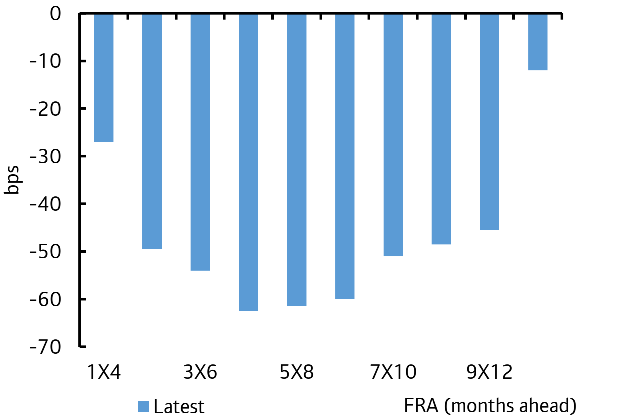
Source: IMF

Figure 5: We foresee the worst SA GDP contraction on record (data starts in 1946)



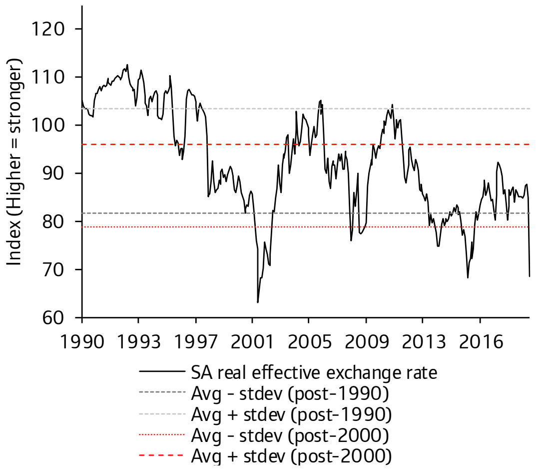
Source: SARB, Standard Bank Research

Figure 6: We concur with the money market that the SARB will cut interest rates further



Source: Bloomberg, Standard Bank Research

Figure 7: Rand undervalued, but rebound requires credible policy reform



Source: Bloomberg, Standard Bank Research

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