

strategy&

Part of the PwC network

South Africa Economic Outlook

Local companies
embracing international
opportunities

30 August 2022



About this document

In this edition of the South Africa Economic Outlook, we focus on local companies finding growth opportunities abroad. This could range from exports to direct investment deals.

While export volumes have been under pressure in recent months due to several factors, the outlook for significant investment in local port infrastructure is a positive development for the medium- to long-term outlook.

Offshore investment is nothing new for South African companies; in fact, during the second quarter of 2022, South Africa recorded a record-high value of R222bn of outward merger and acquisition (M&A) deals. While the global economic outlook is uncertain, previous PwC research found that deals made during a downturn are often the most successful.

Key content in this edition includes:

- Global macro environment: Update on key international factors and their local impacts ([page 3](#)).
- Export trends: Container shipments decline in 2022Q2 but planned port investments provides some optimism ([page 4](#)).
- Offshore investment: South African companies make record-high international M&A deals during 2022Q2 ([page 5](#)).
- Where investors are looking: Long-term economic growth outlook in key export and investment destinations ([page 6](#)).
- International market entry strategy: Asking the right questions to find the right opportunities ([page 7](#)).
- Featured PwC research: Deals made during a downturn are often the most successful ([page 8](#)).

The report is produced by the PwC South Africa Strategy& Economics team. It includes some of PwC South Africa's core macroeconomic views for the country while other data is reserved for internal purposes and client services. Our forecasts are updated on a monthly basis though revisions could occur more frequently due to major economic data releases or key influential events. For more information on the data, the Economics team, and related services (including international market entry strategy), see the [last page](#) of this document.

Baseline	2020	2021	2022f	2023f
ZAR/USD	16.46	14.78	16.00	16.50
Consumer price inflation (%)	3.3	4.6	6.6	5.4
Repo rate (end-of-period)	3.50	3.75	5.75	6.75
Real GDP growth (%)	-6.4	4.9	2.0	1.7
Unemployment rate (%)	32.5	35.3	35.5	35.9
Probability weighted average	2020	2021	2022f	2023f
ZAR/USD	16.46	14.78	15.98	16.48
Consumer price inflation (%)	3.3	4.6	6.7	5.5
Repo rate (end-of-period)	3.50	3.75	5.85	6.73
Real GDP growth (%)	-6.4	4.9	1.9	1.6
Unemployment rate (%)	32.5	35.3	35.5	36.0

Global macro environment: Update on key international factors and their local impacts.



South Africa Economic Outlook August 2022



Global economy

The International Monetary Fund (IMF) World Economic Outlook July 2022 highlighted the extent of challenges in the global economy. These include: a decline in economic output in some major economies (e.g. China and Russia), decade-high inflation rates in many countries, accelerated monetary policy tightening across the globe, global supply chain disruptions exacerbated by zero-COVID-19 lockdowns in China, a growing food crisis due to a drop in exports from Ukraine; energy price spikes (specifically natural gas); rising sovereign bonds costs, declines in stock market and private equity valuations, and weaker investor appetite.

Looking ahead, the IMF said in July that, given the elements above, **the current outlook for the global economy is “extraordinarily uncertain”**. The IMF’s forward-looking baseline and alternative scenarios are available [here](#) and are definitely worth a read to understand the extent of the economic outlook uncertainty.



Oil and fuel prices

The price of Brent crude peaked at \$120/barrel in early June. Energy prices eased subsequently and **Brent declined to \$95/barrel in the first week of August** as a result of rising fears about a global recession. Apart from some signs that fuel sales may be slowing in the US during the summer driving seasons, energy experts commented that there was no change in oil market fundamentals during this period — it was all about the global economic outlook.

Oil prices resisted trading much lower during the remainder of the month on the back of a slightly improved demand outlook. In mid-August, the International Energy Agency (IEA) increased its global demand forecast for oil. It now expects demand to grow by 2.1 million barrels a day (up 380,000 from its previous forecast) due to heatwaves in the Northern Hemisphere and skyrocketing natural gas prices boosting demand for fuel products. Furthermore, the IEA does not expect the OPEC+ grouping to increase output in the coming months due to limited spare capacity.



Food prices

The Food and Agricultural Organisation (FAO) Food Price Index declined by 13.3 points (8.6% m-o-m) in July, marking the fourth consecutive monthly decline. Nevertheless, it remained 16.4 points (13.1% y-o-y) above its value in the corresponding month last year.

On July 22, Russia and Ukraine signed a major deal to facilitate the export of grain from Odessa, Chornomorsk and Yuzhny ports. These ports have all been severely disrupted by the conflict, substantially pushing up global prices and raising fears of global grain shortages. The deal aims to facilitate the export of 22 million tonnes of wheat, corn and other crops. By August 18, 622,000 tonnes of grain had been shipped on 25 vessels from Ukrainian ports.

However, **food prices will not return to pre-conflict levels due to higher fuel and transport costs**, greater demand from China, and reduced agricultural production due to fertiliser shortages (also linked to the conflict).



Interest rates

Central banks around the world are tightening monetary policy to try and tame inflation. Data from Trading Economics shows that, following its most recent monetary policy meetings, central banks lifted interest rates for 84 countries, kept them on hold for 75 others, and lowered lending rates for just nine economies.

Higher interest rates have adverse effects on economies through many channels, including higher household debt service costs. However, policymakers cannot delay responding to the current significant increase in the cost-of-living in most countries.

The South African Reserve Bank (SARB) forecast in July that **G3 (euro area, the US and Japan) interest rates will increase from an average of 0.1% in 2021 to 1.2% this year and 3.0% in 2023**. Reflecting the recent acceleration in interest rate expectations, the 3.0% figure for next year is nearly double the 1.6% projection the SARB made in May.



Trade and supply chains

The IMF said in July it expects the global volume of goods and services trade to grow by 4.1% this year. This projection is 0.9 percentage points lower than its expectations in April. Furthermore, the IMF expects 2.2% growth in trade by Emerging Market and Developing Economies (EMDE) — down 1.8 percentage points from earlier in the year.

The decline in trade growth expectations is linked to weaker global economic growth but also, crucially, supply chain disruptions. The latter is strongly associated with the ongoing Russia-Ukraine conflict as well as periodic lockdowns in China associated with the country’s zero-COVID-19 policy.

Recent movements in the New York Fed’s Global Supply Chain Pressure Index (GSCPI) suggest that, while global supply chain pressures have certainly been decreasing in recent months, they remain at historically high levels.

Impact on South Africa

Uncertain times are almost always bad news for emerging markets. **South Africa’s exchange rate, stock market indices and bond valuations have deteriorated of late** and could continue on this weaker footing for some time given the current “extraordinarily uncertain” global outlook.

Despite a weaker rand and the end of a R0.75/litre reprieve on the general fuel levy, the easing in global oil and fuel prices during July resulted in local petrol and diesel prices declining by R1.32/litre (4.9% m-o-m) and up to R0.91/litre (3.5% m-o-m), respectively, in early-August. At present, **we expect the retail petrol price to decline further at the start of September by around R2.20/litre.**

Retail food inflation was measured at 10.1% y-o-y in July, including a 13.7% y-o-y increase in the staple ‘bread and cereals’ category. However, on the production side, food products cost 15.1% y-o-y more to produce in July, with grain mill products costing 22.5% y-o-y more. This signals **more upstream pressure on local retail food prices.** The SARB said in July it expects food price inflation to average 7.4% in 2022 and 6.2% next year.

The SARB has joined other central banks in accelerating monetary policy normalisation. While the SARB does not target a specific exchange rate level, it is necessary for the monetary authority to ensure that local interest rates offer an attractive premium to investors in order to boost the attractiveness of local assets — and, by implication, the value of the rand.

The new sales orders index of the Absa Purchasing Managers’ Index (PMI) declined from 58.5 in May to 46.3 in June and 35.4 in July, partly ascribed to weaker exports. **Export flows are also challenged by long-standing inefficiencies at our land and sea ports.** There is, however, some light at the end of the tunnel — see next page.

Export trends: Container shipments decline in 2022Q2 but planned port investments provide some optimism.



South Africa Economic Outlook August 2022

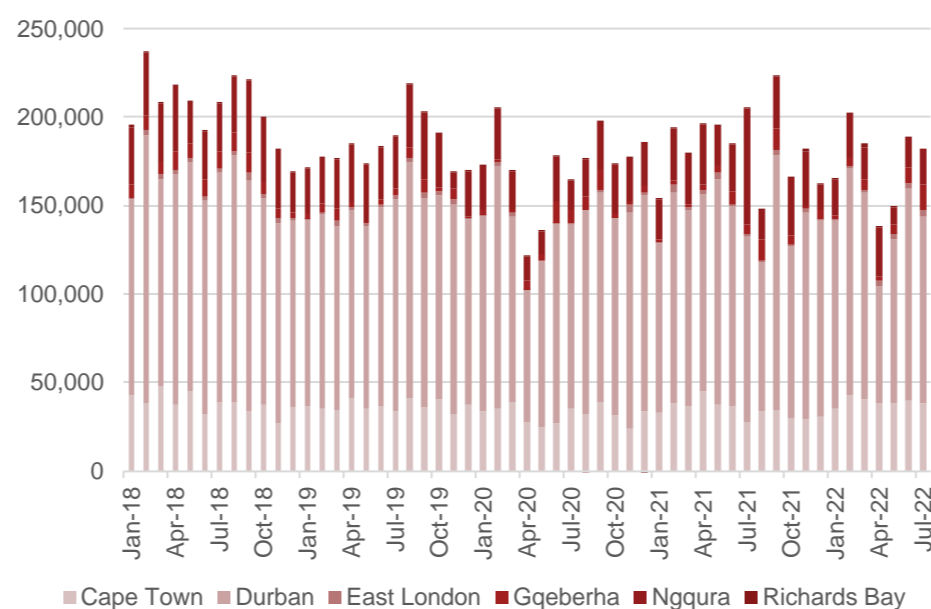
Container exports decline 17.5% y-o-y in second quarter as local and international factors weigh on shipment volumes.

Mining production and mineral exports were among the key drivers of South Africa's economic recovery following the worst of the COVID-19 impacts in 2020. The value of mineral sales (covering both exports and domestic use) increased by 3.9% y-o-y in the first half of this year. The local currency prices received on ore and mineral exports increased by an average of 25.0% y-o-y in the first six months of 2022. Coal shipments, for example, fetched prices that were 48.6% y-o-y higher during the January-June period. European demand for coal has jumped in recent months and is expected to increase by 7.0% this year as the European Union reduces its consumption of Russian natural gas and increases coal-fired power generation. However, it is not just South Africa's primary minerals that are currently garnering high prices abroad. Processed products like coke oven and refined petroleum products (+46.1% y-o-y in June), products of iron and steel (+20.1% y-o-y), and other semi-finished metal products (+14.2% y-o-y) have also seen notable price gains over the past 12 months.

South Africa's container exports increased by 5.1% y-o-y during the first quarter of 2022 on the back of a continued recovery in global demand conditions. Early in the year, as the world shook off the worst effects from the Omicron COVID-19 variant, countries' appetite for imports continued to improve. However, local container shipments declined by 17.1% y-o-y during the second quarter of 2022 due to the adverse effects of the Russian invasion of Ukraine and lockdowns in China reducing global shipping activity. In turn, domestic load-shedding and flooding in KwaZulu-Natal reduced activity at the Port of Durban where exports fell by a third during April and May compared to the same months last year. The country's total container volumes fell by

100,000 (17.5% y-o-y) in 2022Q2. Most recently, South Africa exported 182,421 containers in July, a decline of 3.1% m-o-m 11.2% y-o-y. The latest Absa Purchasing Managers' Index (PMI) report also indicates that local manufacturing businesses experienced a m-o-m decline in exports during July.

Figure 1: Twenty-foot equivalent unit (TEU) container exports



Source Transnet

Apart from the transient supply chain challenges experienced, South African ports are beset with operational inefficiencies. For example, at the start of this year, cargo ships entering Cape Town had to wait for up to two weeks to berth before customs and offloading could commence. The recently released World Bank Container Port Performance Index (CPPI) 2021 ranked Durban, Cape Town and Ngqura in the bottom ten ports out of the 370 locations analysed globally. This is based on the average time spent by a ship in these locations which, in turn, is reflective of factors like the availability and quality of infrastructure, layout of the harbour, and the expertise of the employees, amongst others.

Transnet plans R14bn investment over the next five years to improve the quality of port operations and infrastructure.

Operation Vulindlela — a joint initiative by the presidency and National Treasury — has made some progress of late regarding its objective (among others) of creating a “competitive and efficient” freight transport system in the country. The initiative counts among its successes to date 1) establishing the National Ports Authority as an independent subsidiary of Transnet, 2) finalisation of the White Paper on National Rail Policy, and 3) corporatisation of the Transnet National Ports Authority (TNPA).

Transnet was expected this month to release a request for proposals to set in place private partnerships for container terminals at the Ports of Durban and Ngqura from January 2023. This will enable private investment in, and management of, poorly performing container terminals. Accounting separation of Transnet Freight Rail has also been completed to enable third-party access to the rail network. To this end, a request for proposals was released by Transnet for available slots on the Durban-City Deep and Pretoria-East London lines with responses due this month.

Looking ahead, the National Assembly will soon vote on the Economic Regulation of Transport Bill. If passed, the bill will provide for open and non-discriminatory third-party access to the rail network as well as the establishment of a Transport Economic Regulator. Transnet also plans to invest R14bn over the next five years to improve the quality of ports. Western Cape harbours (Cape Town, Saldanha and Mossel Bay) are already undergoing upgrades under the TNPA's R16bn capital investment programme. Additionally, the TNPA has sought private sector assistance to secure energy supply for the purpose of port operations.

All of these already-achieved reforms in the rail and port space, as well as ongoing and planned developments in these areas, are aimed at improving rail and port performance to the benefit of South African companies and their export businesses.

Offshore investment: South African companies make record-high international M&A deals during 2022Q2.

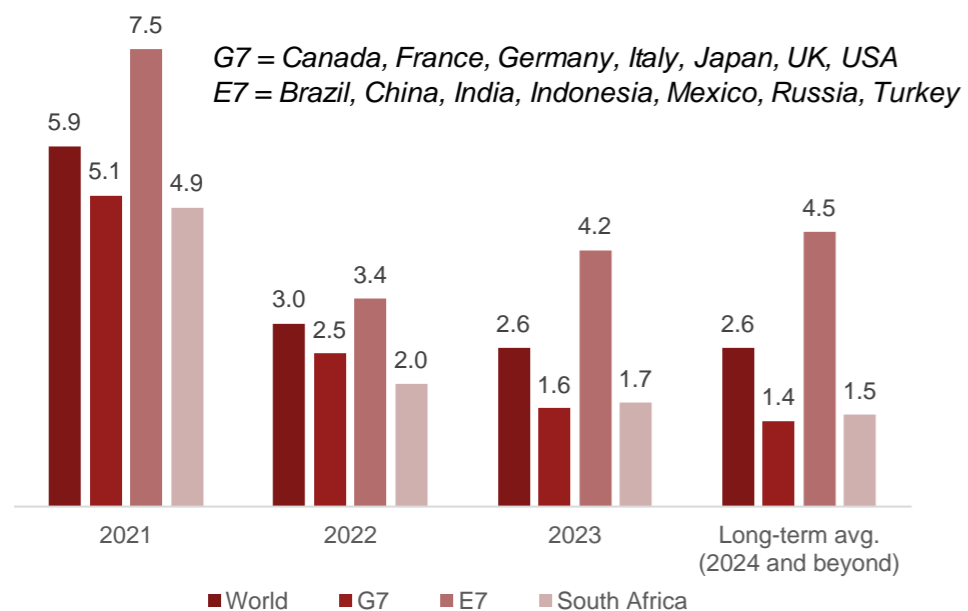


South Africa Economic Outlook August 2022

If economic growth was a car, South Africa will be driving at 60 km/h while the global average is above 100 km/h.

South Africa's economic growth is slowing once more. After the 2020 recession, the economy bounced back in 2021 as GDP expanded by 4.9%. However, even before the Russian invasion of Ukraine, we warned that local economic growth would moderate to a significantly lower level over the medium term. From a forecast real GDP growth rate of 2.0% this year, we expect economic growth to converge at around 1.5% p.a. over the longer term. This is the country's potential economic growth rate given current fundamentals and structural constraints. In turn, we expect the global economy to grow at a healthier long-term rate of 2.6% p.a. If these growth rates could be translated into the speed at which a car travels, South Africa would be driving at 60 km/h while the global average is above 100 km/h.

Figure 2: Global and regional real GDP growth (%)



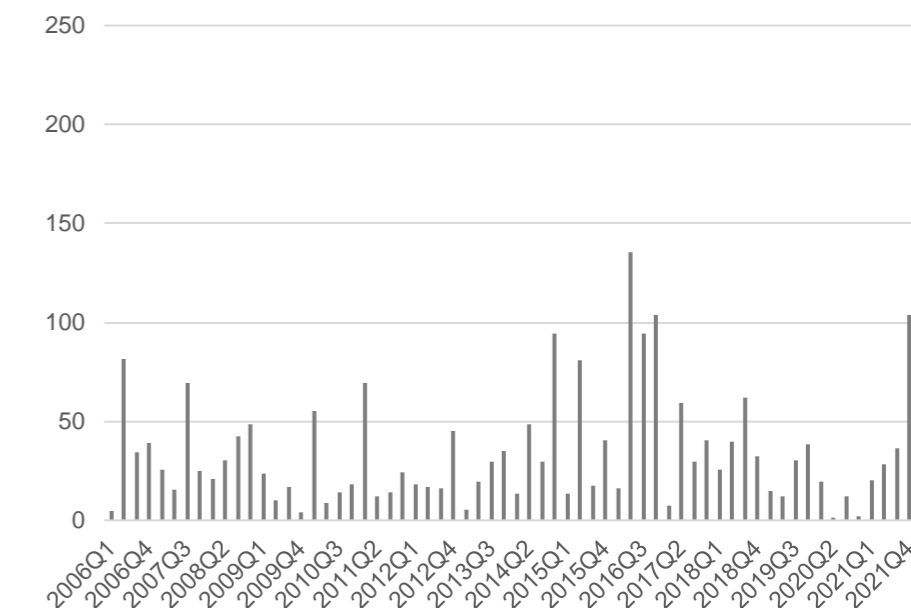
Source PwC Strategy&

Local companies made deals worth R222bn in 2022Q2 to further increase the country's outward FDI stock.

The G7 developed economies are expected to record real GDP growth of 2.4% in 2022 and 1.6% in 2023 as their post-pandemic recoveries continue. The long-term growth outlook for this grouping is an average expansion rate of 1.4% p.a. — very similar to South Africa's long-term trend. The E7 emerging economies are forecast to grow by a healthier 3.4% this year and 4.2% next year. This group's long-term growth outlook is higher at 4.5% p.a. despite the inclusion of Russia within this cohort. The E7 includes some of the largest emerging markets, many with growing middle classes and resource wealth to drive their future economic development. If South Africa is cruising at 60 km/h over the long term, this group would be speeding ahead at 180 km/h.

Clearly, there are faster-growing markets (compared to the local economy) available to South African firms who are willing to look abroad. Some years ago, around two-thirds of the earnings reported by the Johannesburg Stock Exchange (JSE) Top 40 came from foreign currencies. And the offshore investment trend is certainly picking up steam. The value of South Africa's outward FDI stock reached R3.1tn in 2019 (most recent comparable data) which was double the value seen in 2012. Data from White & Case shows that the value of outward M&A activity by South African companies, i.e. deal activity by local businesses into the rest of the world, reached R222bn in the second quarter of 2022. This was the highest on record based on data going back to 2006. While this large sum was certainly linked to a few mega deals (worth R114bn), outward M&A excluding mega deals (valued at R107bn) was also the highest in six years.

Figure 3: South Africa outward M&A activity by value (Rbn)



Source PwC calculations based on data from White & Case

According to the SARB, the market value of South Africa's net foreign assets (increased by 7.7% q-o-q in the fourth quarter of 2021, with the net international investment position (IIP) measured at R8.8tn. This includes direct (e.g. outward FDI), portfolio and other investment assets, and indicates that South Africa's stock of foreign assets are larger than foreigners' stock of local assets.

R3.1tn

The value of South Africa's outward foreign direct investment (FDI) stock reached R3.1tn in 2019 – doubling in value since 2012.

Where investors are looking: Long-term economic growth outlook in key export and investment destinations.



South Africa Economic Outlook August 2022

We highlight a few of the countries (India, Mexico and the United Kingdom) offering business opportunities not just for South African companies but also from other emerging markets seeking new opportunities. These bullet points are illustrative of some positive attributes and definitely not a thorough review of fundamentals.

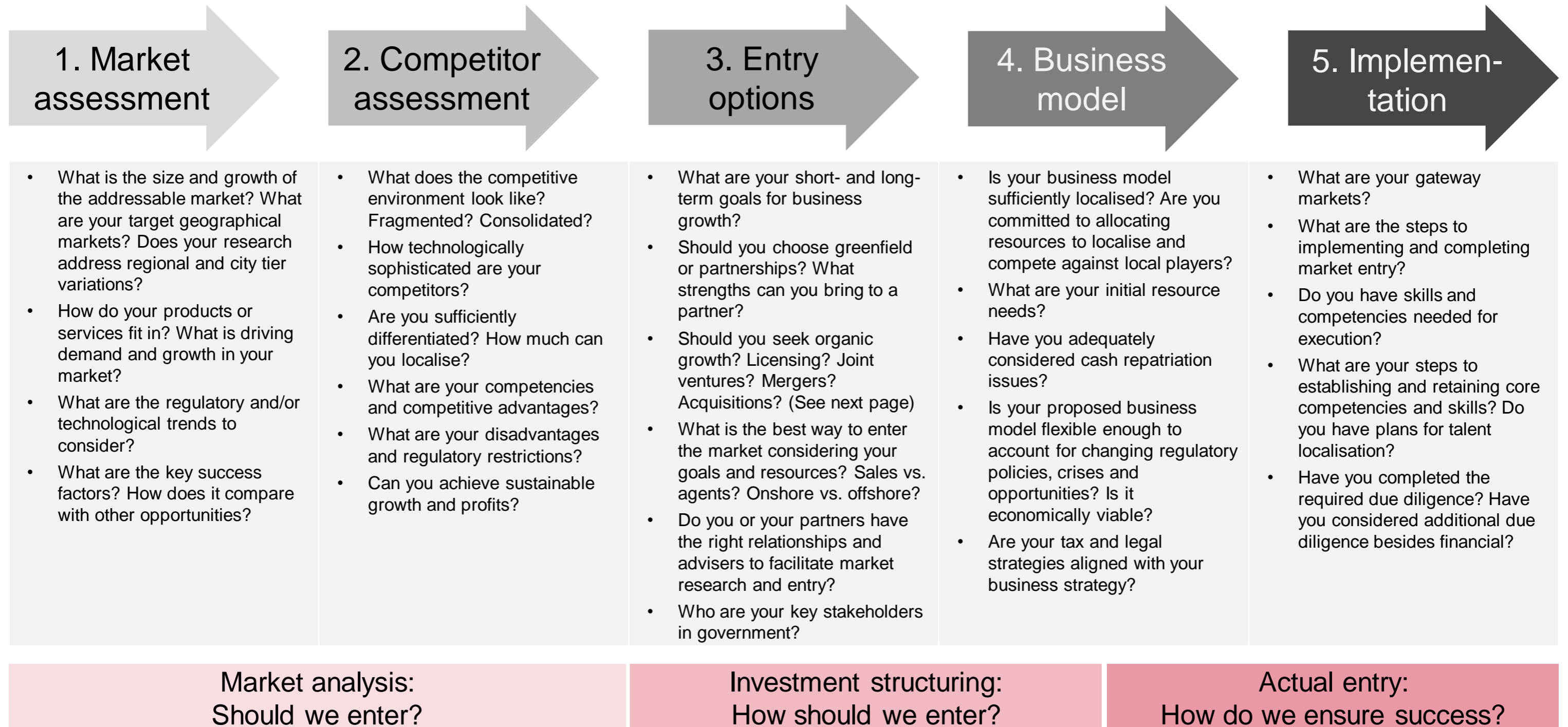
Country	Selected market attractiveness features	Size of the economy (global ranking)	SA outward FDI stock ranking (2019)	SA export market ranking (2017-2021)	Long-term real GDP growth (beyond 2023)
Australia	<ul style="list-style-type: none"> Long-term real GDP growth forecast at 6.7% p.a. — this will be the highest growth rate among the world’s major economies. 	12	5	24	2.4
Brazil		13	32	37	2.1
Canada		9	11	44	1.7
China		2	44	1	4.9
France		7	20	25	1.5
Germany	<ul style="list-style-type: none"> The government regularly reviews its FDI policy and periodically makes significant changes to keep up with local and global investment developments. 	4	15	3	1.3
Greece		25	30	69	1.6
India	<ul style="list-style-type: none"> Apart from national incentives, each state government provides additional investment incentives, including subsidised land prices, tax concessions, etc. 	6	21	6	6.7
Indonesia	<ul style="list-style-type: none"> Gateway to both Latin America to the south and North America (US and Canada) due to its geographic location. 	16	57	28	5.4
Ireland		21	23	55	3.3
Italy	<ul style="list-style-type: none"> Amongst emerging market economies, it is one of the most open towards trade and foreign investment. 	8	22	21	1.0
Japan		3	49	5	0.6
Mexico	<ul style="list-style-type: none"> Free trade agreements with approximately 50 countries across the globe enable the country to conduct trade without incurring substantial costs on goods. 	15	38	46	1.9
Netherlands	<ul style="list-style-type: none"> The country’s large geographical area has an extensive logistics network (roads, rail, air and shipping routes). 	17	1	10	1.6
Nigeria		22	18	32	2.9
Poland	<ul style="list-style-type: none"> Legal, regulatory, and accounting systems are transparent and consistent with international norms. 	20	48	48	3.3
Portugal		24	45	50	2.1
Russia		11	53	39	1.0
Saudi Arabia		18	78	42	2.7
South Korea		10	75	15	2.4
Spain	<ul style="list-style-type: none"> Lowest corporate tax rate in the G20; performance of the tax system ranked 27th out of 190 economies 	14	47	19	2.1
Turkey		19	69	36	3.4
United Kingdom	<ul style="list-style-type: none"> Eight freeports centred around air, rail or sea ports offering tax benefits, simplified customs and other government support. 	5	2	4	1.8
US	<ul style="list-style-type: none"> 130% capital allowances against taxable profit on qualifying plant and machinery investments (temporary until March 2023) 	1	3	2	1.6

Sources: PwC, United Nations Conference on Trade and Development (UNCTAD), International Trade Centre (ITC)

International market entry strategy: Asking the right questions to find the right opportunities.



South Africa Economic Outlook August 2022



Featured PwC research: Deals made during a downturn are often the most successful.



South Africa Economic Outlook August 2022

Deals launched during a downturn can achieve outsized growth and better returns for buyers.

At the start of 2022, dealmakers worldwide were riding high from the best year on record for global mergers and acquisitions (M&A), with more than 60,000 publicly disclosed deals. We predicted that this year was not likely to top 2021 in the face of growing headwinds — but the market expected M&A to continue to prosper. Fast-forward to mid-year: not only have the headwinds grown stronger, but new ones have emerged, including rapidly accelerating inflation and interest rates, lower stock prices, and an energy crisis deepened by the Russia–Ukraine conflict.

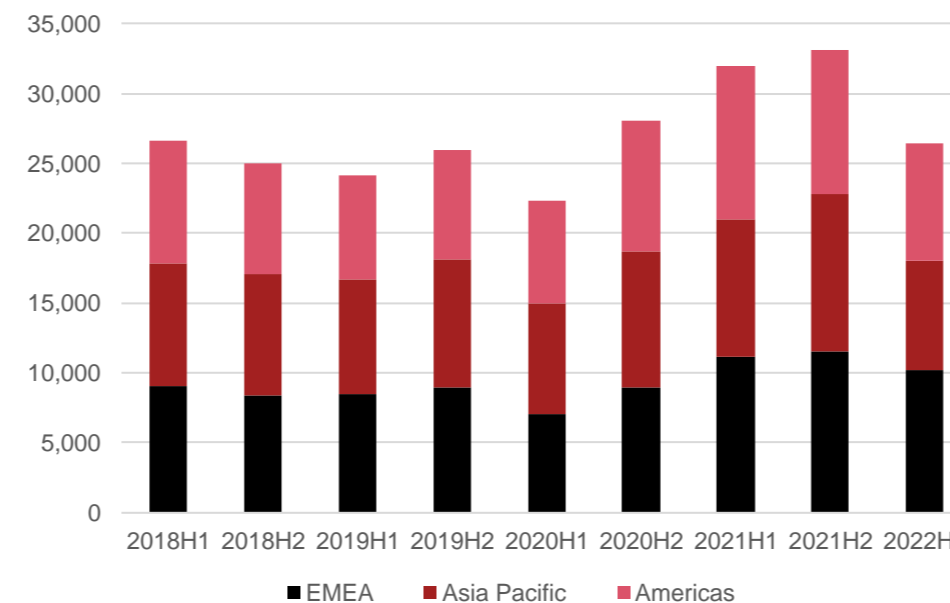
[PwC's Global M&A Industry Trends: 2022 Mid-Year Update](#) reports that M&A activity in the first half of 2022 was lower than during the same period last year.

- Europe, Middle East and Africa (EMA): Deal volumes and values are down 12% and 33%, respectively, as countries face higher energy costs and lower investor confidence.
- Asia Pacific: Deal volumes and values have both declined by more than 30%, due mainly to macroeconomic headwinds and recent pandemic-related restrictions imposed across several major cities in China.
- Americas: Deal volumes and values have declined by 18% and 22%, respectively, mainly due to concerns around inflation and rising interest rates.

However, the numbers are not catastrophic at all: they are in line with healthy, pre-pandemic levels. M&A volumes and values tend to rise during periods of economic growth and favourable markets, and decrease during times of uncertainty and market volatility. We saw this happen in early 2020 at the Strategy&

onset of the COVID-19 pandemic. We have seen similar trends in prior economic recessions, such as the global financial crisis and the dot-com bust. It should be no surprise therefore that M&A softened during the first half of 2022. Dealmakers are facing higher costs of capital and increasing pressure on returns. And their boards and investment committees may be advocating for caution, even delays, in M&A pipelines, as rising inflation, concerns over energy supply, labour shortages and supply chain disruptions put pressure on balance sheets and put longer-term priorities, such as deals, on hold.

Figure 4: M&A deal volumes (number of transactions)



Source: PwC

The good news is that deals done during a downturn or otherwise challenging markets are often the most successful. A PwC analysis ([M&A cycles: Fundamental drivers and valuation impacts](#)) found better returns for buyers during a downturn and shows how deals launched during such times can achieve outsized growth. We believe that dealmakers who are bold — and strategically pursue M&A with a strong capabilities fit — will be best positioned to create value for the longer term. What's

more, the factors that underpinned the M&A market in the first half of this year will remain influential for deal-making in the latter half: supply chain resilience; portfolio optimisation; environmental, social and governance (ESG); and, above all, the competition for badly needed technology.

In many countries, inflation is at a multi-decade high. This is expected to persist through the remainder of 2022. A generation of business leaders who have never operated in an inflationary market are facing a paradigm shift in the economic landscape. As inflation represents a threat to company earnings and erodes shareholder returns in real terms, the historical due diligence dealmakers have become accustomed to needs to be approached differently. Dealmakers need to take into account both present and expected future inflation in their valuations. This involves forecasting different inflation scenarios and using real-time analytics to assess the impact of inflation on the company's operations and earnings. Pricing, cost management and cash flow are part of a company's response to operating in an inflationary environment, and require an understanding of the wider implications on market share, price elasticity, customer and supplier relationships, and employee compensation and retention.

Dealmakers are adapting to a new business climate — one where inflationary pressures, rapidly rising interest rates, short-term volatility in financial markets, supply chain disruptions and geopolitical tensions all appear to be developing into longer-term trends. As such, now is not the time to sit things out. On the contrary, we believe this is exactly the time for business leaders and dealmakers to make bold moves and set the stage for the next five years, winning the targets that matter most to their businesses or portfolios. PwC believes using M&A to pursue opportunities can deliver value in a challenging economy. We remain optimistic that the need for both speed and agility to navigate the current challenges will ensure M&A remains a strategic priority, helping companies to transform, grow and build a new foundation for their future success.

PwC Economics services and contacts.

South Africa Economic Outlook August 2022

How can we help?

Market entry strategy

The South African economy is cruising at a speed of 60 km/h while the global economy is accelerating at 100 km/h. Many South African companies have expanded outside local borders in search of higher-growth opportunities. Some have focused on neighbouring countries, deeper expansion into the rest of Africa, or beyond — to Western Europe, North America or Asia-Pacific. As listed on [page 7](#), the range of questions that need answering for a South African company to successfully expand abroad into such markets is long. And none of these questions are quick or easy to answer. Each company's internationalisation route is different and we have walked this road with many clients. This journey most often combines multiple business units within PwC working together to assist our clients in reaching their expansion destination.

The first step we take on this voyage is the market assessment. We start by asking questions like 'What is the size and growth of the addressable market?' and 'What are your target geographical markets?' Some of this data is available in the public realm. For example, our recently released [Global Entertainment & Media \(E&M\) Outlook 2022–2026](#) provides five-year projections of consumer and advertiser spending data across 14 E&M segments in 52 territories. We found that at a regional level, North America commands by far the highest E&M spend per capita at about R33,500. This is nearly double Western Europe's R17,000. In contrast, Asia-Pacific, which was the largest E&M region by total revenue in 2021, has per capita spend of only about R3,500.

This type of information provides only an introductory answer to the initial questions that a South African company needs to answer when it comes to profiting from international markets. Thereafter, the questions and answers become much more nuanced and intrinsically bespoke for each company.

Our services

The PwC South Africa Strategy & Economics team is a specialised unit of economists who serve our clients in a variety of ways. Our services include:

Measure your impact on the economy and society

- Environmental, Social and Governance (ESG) and Just Transition
- Economic Impact Assessment (EIA)
- Socio-Economic Impact Assessment (SEIA)
- Regulatory Impact Analysis (RIA)
- Total tax contribution
- Localisation calculations

Make decisions about risk and investment

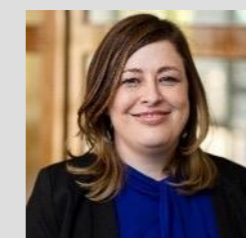
- Macroeconomic research
- Market entry analysis
- Country and industry risk assessments
- Commercial due diligence assistance

Plan for future economic scenarios

- ESG scenario planning
- Economic and political scenario planning
- Industry and macroeconomic modelling
- IFRS 9 audit assist

Please visit our website to learn more:

<https://www.pwc.co.za/en/issues/economy.html>



Lullu Krugel

Partner and Chief Economist

lullu.krugel@pwc.com

+27 (0) 82 708 2330



Jeunes Viljoen

Senior Manager

jeunes.viljoen@pwc.com

+27 (0) 82 634 2036



Salome Ntsibande

Senior Manager

salome.ntsibande@pwc.com

+27 (0) 72 210 1013



Dirk Mostert

Senior Manager

dirk.mostert@pwc.com

+27 (0) 82 800 9326



Christie Viljoen

Senior Manager

christie.viljoen@pwc.com

+27 (0) 82 472 8621