EFFICIENT GROUP

ECONOMIC COMMENTARY

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LESS AND MORE ACCOMMODATION

Talk about reducing the extent of accommodative monetary policy in the United States (US) is becoming increasingly common; a weary sign to cash-hungry US and global markets. Many of the Federal Reserve heads of different US states have voiced their opinion that the US Federal Reserve (Fed) should begin discussions about tapering asset purchase programmes, sooner rather than later. The US asset purchase programme, more commonly referred to as quantitative easing (QE), is currently at $120 billion a month. That means that the Fed buys $120 billion of US treasuries and corporate bonds every month, pushing cash into the US financial system in an attempt to get banks to lend out more and corporates to spend more. Since January 2020, the Fed's balance sheet nearly doubled, from $4.1 trillion to today's $7.9 trillion, as the US used QE to support their economy through the coronavirus pandemic. Because of these asset purchases, as well as fiscal support, US debt has ballooned into what many believe is unsustainable: almost $25 trillion or 130% of their gross domestic product (GDP). Debt is not such a big problem if the US can grow their economy faster, albeit in nominal terms. Note that this is also why the Fed is not too concerned with slightly higher levels of inflation.

US markets received some more unwelcome news when the White House announced that they would be cutting their infrastructure bill from $2.3 trillion to $1.7 trillion. By spending less on investments in broadband, roads and bridges, the Democrats are hoping to win over some much-needed Republican support to push the bill through. Less accommodation from monetary and fiscal policy means that the US, especially its markets, will slowly start to wake up from the daze of easy money that it has grown so accustomed to for more than a decade. Uncertainty, and the volatility it leads to should therefore increase. Less accommodation also means that markets will have to sustain themselves, something that can take them quite some time to do. While this is happening there might be an overall slump in global markets, emphasising the need for active, rather than passive management.

Conversely, in South Africa (SA), markets got exactly what they wanted when the Governor of the South African Reserve Bank (SARB) said that the bank has decided to keep interest rates unchanged at 3.5% (prime, therefore, also remains unchanged at 7%). During his speech, the Governor, Lesetja Kganyago, also explained that the bank still believes that 2021 GDP can reach 4.2%, but they have reduced their inflation forecast from 4.3% to 4.2% (in line with our forecasts). We maintain that the impact of higher oil prices on local inflation will be subdued, and that the rand should remain strong (around R14.50) throughout the next year, albeit with some volatility. Although the SARB's model is still pricing in two interest rate increases of 0.25%, in the second and fourth quarters of 2021, we still believe that only one increase is needed. As long as interest rates remain above inflation, South African monetary policy remains accommodative, supporting consumption at the expense of savers.

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