SEPTEMBER 2023

ECONOMIC NEWSLETTER

SPEKTRA FINANCIAL SERVICES

WHEN IN A (JACKSON) HOLE, STOP DIGGING

Summary

- Consumer Price Inflation in the US is currently running at 3.2%, well above the 2.0% target.
- The Fed may be forced to keep interest rates “higher for longer” to curb inflation.
- Narratives predicting a full-blown recession in the US may be overblown, however there are still risks present.
- The 15th BRICS meeting saw 6 new members added to the bloc. Any talk of a centralised BRICS currency is highly exaggerated and a long way off from any material development.

CENTRAL BANKERS DECEND ON JACKSON HOLE

Late August saw Central Bankers from across the world meet in Jackson Hole, Kansas City, for the annual Jackson Hole Economic Symposium. Hosted by the US Federal Reserve (the Fed), the conference is attended by central bankers to discuss world events and financial trends – the most important of which is centred around the likely direction of global interest rates.

For the last 18 months, inflation and interest rates in the United States has been the focal point of nearly every forward-looking economic discussion. During the Covid era, the Fed injected an estimated 3.7 trillion dollars into the US economy as part of its stimulus program in an effort to prevent the economy from falling into recession. Once the Covid lockdown restrictions were lifted, consumers deployed this excess cash in quick fashion, resulting in increased demand for goods and services, thereby pushing up prices and fuelling inflation.

Hiking interest rates, whilst effective for combating inflation, is more akin to a bludgeon than a precision instrument when assessing the impact on an economy, and risks inducing a recession. With US interest rates having been raised by over 5.0% since March 2022 to a level not seen since the early 2000’s, and with inflation currently poised at 3.2%, still well above the 2.0% target, the Fed now finds itself in a precarious position; continue raising interest rates and potentially push the US economy into recession, or keep interest rates unchanged and live with higher inflation. During the Jackson Hole Symposium, Jay Powell, chairperson of the US Fed, warned that inflation “remains too high”, and reinforced the Fed’s goal to bring inflation down to the 2.0% target. “We are prepared to raise rates further if appropriate, and intend to hold policy at a restrictive level until we are confident that inflation is moving sustainably down toward our objective,” he added.

Despite the hawkish narrative, the Fed is widely expected to keep interest rates unchanged at its next meeting in September. Market bulls propose that that the Fed has already reached the end of its rate-hiking cycle and will opt to keep rates steady for the next 6-12 months, with the first rate cuts expected in the second half of 2024. If inflation remains contained during this period it is highly likely that the US economy will avoid falling into recession and a “soft landing” scenario will play out – characterised as a cyclical slowdown in economic growth that avoids recession. The more bearish narrative involves inflation remaining meaningfully above the 2.0% target, forcing the Fed to engage in subsequent rate hikes, resulting in a “hard landing” scenario and the onset of recession.

CITYWIRE SOUTH AFRICA
SOUTH AFRICAN DFM OF THE YEAR 2022
analytics

CENTRAL BANKERS DECEND ON JACKSON HOLE CONTINUED

Whilst there is evidence to support both the bull and the bear scenario, there appears to be more favour for the soft landing at this stage. Investors should anticipate for rates to remain high for some time, which can be expected to bring increased volatility to markets, however the prediction of a full-scale recession appears to be slightly overstated at this stage.

Currently, with bonds in the US offering very attractive real yields, investors are well-placed to capitalise on higher returns offered by global fixed income instruments. Global portfolios with an allocation to short-term and floating rate bonds would have done well this year without needing to take on excessive duration.

Speaking at the symposium on behalf of South African inflation, our local reserve governor, Lesetja Kganyago also reinforced the need to keep our inflation within an acceptable range. With South African interest rates currently steady at 8.25%, our inflation sank to a two-year low of 4.7% in July, well within the target range of between 3-6%. That being said, Kganyago highlighted pressures which could keep local inflation at elevated levels, chief among them being the performance of the rand. “On the horizon we actually see the exchange rate as one of the risks to the inflation outlook. So if there was to be a weakness in the currency, it does have implication for the inflation outlook,” he said.

SOUTH AFRICA HOSTS BRICS SUMMIT

South Africa hosted the 15th BRICS summit in Johannesburg from 22 to 24 August. Undoubtably the most noteworthy outcome from the conference was the inclusion of six new members into the BRICS bloc; Argentina, Egypt, Ethiopia, Iran, Saudi Arabia and the United Arab Emirates. With the addition of its new members, the BRCIS bloc now represents 29% of world GDP and around 46% of the global population. Despite its notable size and long history, the BRICS group has little to show from its tenure. Since its inception, the only noteworthy development of the bloc has been the founding of New Development Bank. Established by the original BRICS members in 2015, the bank facilitates the lending of resources for infrastructure and sustainable development projects in emerging markets.

While there has been lots of noise surrounding the creation of a BRICS currency, at this stage it appears to be no more than news hype. A BRICS currency didn’t feature on the summit’s agenda at all, and many have called the idea of a centralised currency “unfeasible” at best, and “embarrassing” at worst. Sensational news headlines aside, it is fair to say we are still a very long way off from any form of consolidated currency within the BRICS bloc.

The information and opinions contained in this document are recorded and expressed in good faith and in reliance on sources believed to be credible. No representation, warranty, undertaking or guarantee of whatever nature is given on the accuracy and/or completeness of such information or the correctness of such opinions. Portfolio Analytics (“Analytics”) will have no liability of whatever nature and however arising in respect of any claim, damages, loss or expenses suffered directly or indirectly by an investor acting on the information contained in this document. The information in this document is for factual information and marketing purposes only and does not constitute any form of advice, guidance or recommendation. Furthermore, due to the fact that . Analytics does not act as your financial advisor, we have not conducted a financial needs analysis and will rely on the needs analysis conducted by your financial advisor. We recommend that you take particular care to consider whether any information contained in this document is appropriate given your objectives, financial situation and particular needs in view of the fact that there may be limitations on the appropriateness of the advice provided. No guarantee of investment performance or capital protection should be inferred from any of the information contained in this document. Portfolio Analytics (Pty) Ltd, FSP No 631, is an authorised financial services provider. Telephone: (011) 463-9600 Fax: (011) 463-8279. Website: www.analytics.co.za. Spektra Financial Services is an Authorised Financial Services Provider. FSP No.10679 Tel: 012-5675502 Web: www.spektra.co.za