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ABOUT THE COMPANY

DaMina is a preeminent independent frontier markets political risk, research, due diligence, M&A transactions and strategic consulting firm.

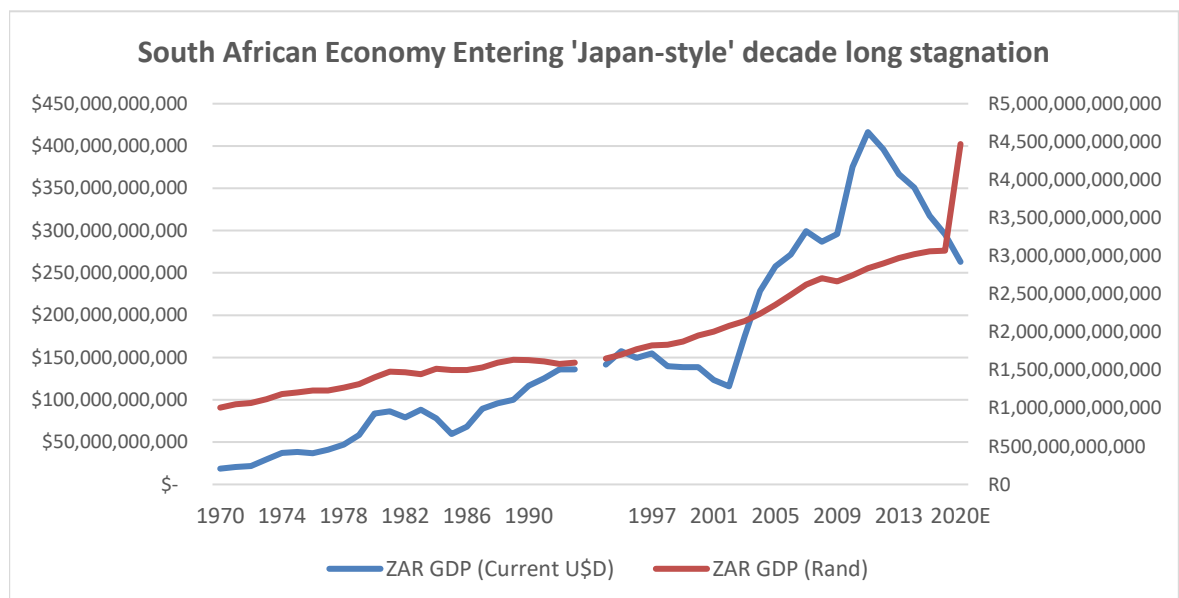
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South Africa faces decade-long Japan-style deflationary economic spiral

SARB will ultimately make 180° turn and cut rates to forestall recession, social unrest

A deadly combination of demographic, structural, policy and global financial factors are pushing South Africa into a possible *decade-long Japan style deflationary economic spiral*. The current South African central bank hawkish policy is increasingly politically untenable ahead of the 2019 elections as both the CPI and GDP price deflators continue to deflate. The central bank is likely to reverse course ahead of the tight early 2019 general elections in a bid to nip the growing cry for a nationalization of the central bank. Ultimately in the medium-term, the South African Reserve Bank (SARB) will have to adopt extraordinary measures like those being undertaken in Japan if the country's decelerating economy is to avoid a decade-long recessionary trap which could ferment serious social unrest and see the ruling African National Congress (ANC) booted from power. With manufacturing, construction, mining, the agricultural sector and consumer spending contracting, or experiencing anemic growth, South Africa's structural inflationary pressures are fast receding. Even the SARB's worry about crude import prices may be unfounded as the forward curve of CME Brent oil futures implies much lower crude prices into 2025. Eskom's recent forecasts that domestic electricity in South Africa will continue to contract are some of the starkest signs of a growing economic deflationary risk.



Source: UN Stats/DaMina Advisors

South Africa's economy faces multiple headwinds: a more hostile international trade environment, a decelerating Chinese economy which will demand less natural resources imports from Africa, new fears around a new land reform program which threatens to curb future fixed capital investment, and social challenges which are partly the legacy of the HIV-AIDS epidemic and Apartheid. With the global mining sector pivoting away from new major investments in Africa and the South African manufacturing sector continuing to contract, the country's financial and services sector remains one of the few remaining bright spots into the future. However capital outflows following the recent Turkish Lira crisis may signal that risks to South Africa's financial services sector are growing.

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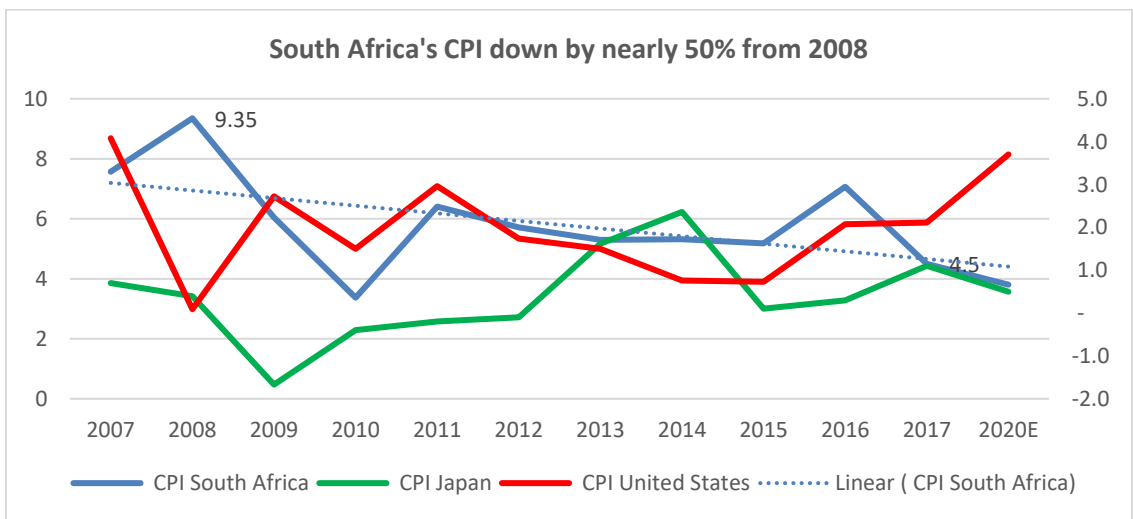
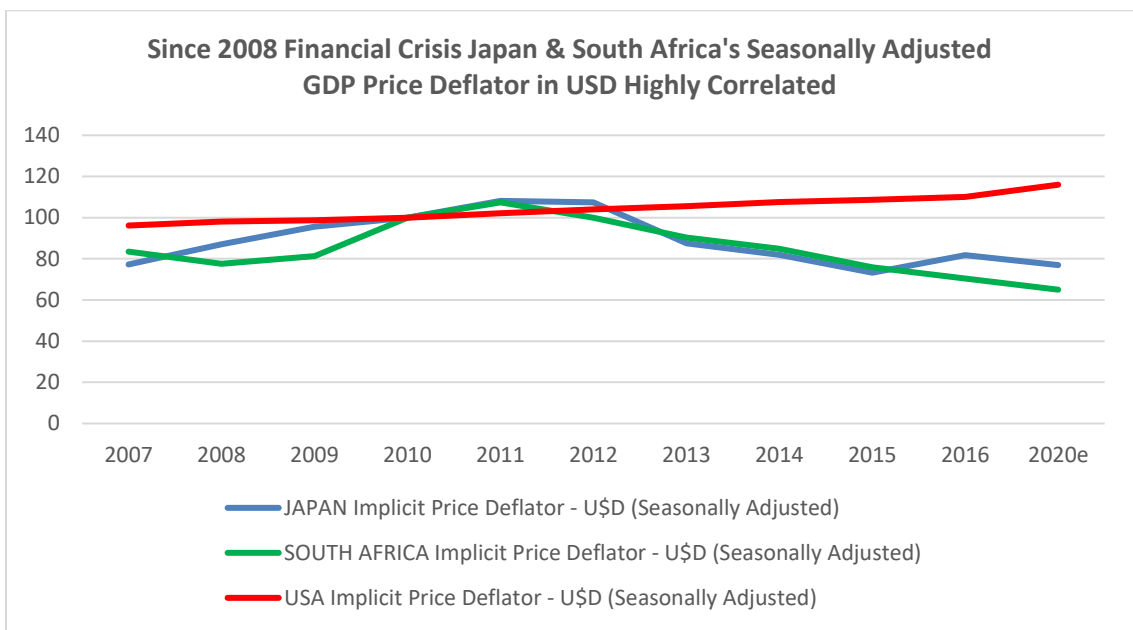
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While the country's banks are stable and well above their required Basel III commitments, the unknown derivative risks to bank collateral and balance sheets stemming from the ongoing land reforms may very well see the country witness another era of rapid capital flight as happened in the late 1990s sometime later this year ahead of the 2019 polls when the tactical alliance between the radical Economic Freedom Front (EFF) and the ruling African National Congress (ANC) is formally announced.

While separated by over 13,500km, South Africa's economy is beginning to mimic Japanese deflationary patterns. While the media headlines around inflation often cite the CPI, the seasonally adjusted GDP price deflator is a broader and better gauge of structural deflationary pressures within the South African economy. Either way both readings have broadly trended negative since 2008 and are mimicking Japan. Japan and South Africa's fundamental deflationary trends have had more in common since 2008 than publicized. Both countries have seen long term price trends decelerate and pull away from the US. South Africa is showing all the signs of oncoming deflation spiral.



Source: UN Stats/DaMina Advisors

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To schedule in-depth Q&A on this note

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