



Trouble Ahead for Zuma and the ANC:

Negative Credit Outlooks and Possible Electoral Upset

Rocio Diaz

rmd@nwpcapital.com
414.775.0461 ext.107

K.P. O'Reilly, JD, PhD

kpo@nwpcapital.com
414.755.0461 ext.110

172 N. Broadway, Suite 300
Milwaukee, WI 53202

Economic Overview

2016 has been economically challenging for South Africa in light of declining metal prices and Chinese economic deceleration—its largest export market. The South African central bank projection for economic expansion is 0.6%, the lowest level since 2009.¹ More recently, the IMF adjusted downward its earlier growth forecast of 0.6%, now predicting 0.1%.² South African Finance Minister, Pravin Gordhan, while telling investors that the economic situation is stabilizing, noted that the country remains in a low growth trap.³

Figure 1. South Africa GDP Growth 2011-2016



Source: Trending Economics.Com

Despite current economic woes, South Africa, judged by emerging market standards, has a developed financial system, with a deep local government bond market and a fully convertible and deliverable currency. The government's debt-to-GDP stands at 49.4%, which the government primarily funds by borrowing in local currency (approximately 87%), leaving it with a small external debt burden of less than 14% of GDP in hard currency borrowing.⁴

Nevertheless, the economic challenges facing the country are aggravated by current political developments, notably ongoing friction between the President and Finance Minister as well as upcoming municipal elections. These political events warrant close attention as they pose short-term risk, with the potential to trigger a credit downgrade to junk status.

Credit Rating Secure for Now

This spring, Moody's and Standard and Poor's left unchanged their long-term credit ratings for South Africa (Baa2 and BBB- respectively). Both agencies did, however, offer negative outlooks. They highlighted concern about political dysfunction potentially undercutting necessary policies to stimulate economic growth.

An ongoing political storyline is the uneasy pairing of President Jacob Zuma and Finance Minister Gordhan. Zuma remains unwilling to embrace Gordhan given his desire to exert greater control over economic and fiscal policy. Simply put, while favored by investors, Gordhan is not the president's man. Zuma continues to voice support for the failed appointment of African National Congress (ANC) loyalist David van Rooyen, which was vehemently rejected by investors last December. Not surprisingly, when news broke about rumors of an arrest warrant issued for Gordhan, in connection to alleged spying on taxpayers by the South African Revenue Service (SARS), some speculated that the president's office was behind the story.⁵

More troublesome for investors is the apparent lack of coordination between the President and the Finance Minister. This point was driven home recently by conflicting statements given by each official regarding the possible privatization of South African Airlines (SAA).⁶ This discontinuity at the highest level of government generates doubts about its overall ability to implement necessary reforms to help the economy. For now, the pair appears stuck with one another. Any effort by Zuma to remove Gordhan would likely trigger another crisis of confidence with investors as well as a credit re-evaluation.

ANC Facing Voter Defection in August Elections

Reports indicate growing voter dissatisfaction with the government heading into the upcoming nation-wide municipal elections scheduled for August 3rd. The ANC faces tight contests across the country, with several traditional party strongholds projected as toss-ups.⁷ These elections are viewed as a referendum on the party and President Zuma, who has two years remaining in office.

Zuma has become a lightning rod for criticism by ANC opponents after a series of scandals. The Constitutional Court's ruling against Zuma in the Nkandla scandal, regarding taxpayer-funded improvements to Zuma's personal residence, prompted an opposition motion for impeachment which was quickly squashed by the ANC majority. However, the party also appears to be out of step with its supporters. A controversial choice to back a long-time party loyalist to run for the mayor of Pretoria, instead of a popular local candidate, has sparked anti-party protest and rioting.

Nevertheless, opposition parties appear limited in challenging the ANC's control of the national parliament. The strongest potential contender is the Democratic Alliance (DA) party, which only holds 22% of the chamber (89 seats). Rather than a wholesale rejection of the ANC, a party shake-up, rejecting the current pro-Zuma leadership, fueled by negative voter sentiment, seems a more likely result.

The Future of Zuma and the ANC

Over the past months, public discontent with Zuma has grown. The Afrobarometer opinion poll found that public distrust of him increased from "37% in 2011 to 66% in 2015 [...] and public approval of his performance dropped from 64% in 2011 to 36% this year."⁸ Despite falling poll numbers, Zuma supporters argue that he remains popular. Inside the party, the leadership appears to be closing ranks in support of Zuma, having sought to quell the few incidents of dissent that have occurred. Critics contend, however, that Zuma's days are numbered, predicting that he will not serve

out the remainder of this terms through the end of 2019. They suggest efforts are already underway to recall Zuma, delayed only until after the August local elections to avoid losing votes in areas where he remains popular.

Removing Zuma would not be an easy process. The ANC's constitution requires five provinces to request a special conference before the party's executive committee can convene one for the purpose of electing a new ANC president.⁹ Should the party go forward with recalling President Zuma; the larger question remains of who would replace him as party leader? Several potential successors are currently jockeying for the position, but no clear frontrunner has emerged.

NWP's Outlook

Overall, low growth continues to impede the South African economy. However, lacking any further erosion of economic conditions, we do not foresee a near-term credit downgrade. Rather than economic conditions, the real driver of any potential credit downgrade looks to be South Africa's domestic politics. The government's current inability to tackle major policy initiatives to aid the economy might be further undermined by upcoming national municipal elections. We anticipate the ANC losing majority status in traditional party strongholds including losing in at least two out of three among Tshwane, Johannesburg, and Nelson Mandela Bay. While not directly impacting the national government, the elections could ignite a disruptive intra-party leadership contest further derailing legislative action.

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¹ Xinhua. "Rounduo: South Africa's Central Bank Cuts 2016 growth forecast to 0.6pct." China.org.cn. May 20, 2016. Accessed July 8, 2016. http://www.china.org.cn/world/Off_the_Wire/2016-05/20/content_38493477.htm

² Gumede, Arabile. "IMF Cuts South Africa 2016 Growth Forecast to 0.1% From 0.6%." Bloomberg.com. July 7, 2016. Accessed July 08, 2016. <http://www.bloomberg.com/news/articles/2016-07-07/imf-cuts-south-africa-2016-gdp-growth-forecast-to-0-1-from-0-6>.

³ Gumede, Arabile. "South Africa to Avoid Recession as Growth Dips, Gordhan Says." Bloomberg.com. July 26, 2016. Accessed July 28, 2016. <http://www.bloomberg.com/news/articles/2016-07-26/south-africa-to-avoid-recession-as-growth-dips-gordhan-says>.

⁴ Bloomberg Terminal – Republic of South Africa (SOAF). Debt Distribution Function (DDIS). Accessed June 30, 2016.

⁵ Olifant, Nathi, Qaanitah Hunter, and Thanduxolo Jika. "Pravin Gordhan Faces 'imminent Arrest'" Sunday Times. May 15, 2016. Accessed May 23, 2016. <http://www.timeslive.co.za/sundaytimes/stnews/2016/05/15/Pravin-Gordhan-faces-imminent-arrest>.

⁶ Gumede, Arabile. SA's Ratings Relief Tarnished by Politics | IOL. SA's Ratings Relief Tarnished by Politics | IOL. June 6, 2016. Accessed June 07, 2016. <http://www.iol.co.za/business/news/sas-ratings-relief-tarnished-by-politics-2031232>.

⁷ Toyana, Mfuneko. "Opinion Polls Show ANC Losing Control of Major Metros after Polls." Business Day Live. July 27, 2016. Accessed July 28, 2016. <http://www.bdlive.co.za/national/politics/2016/07/27/opinion-polls-show-anc-losing-control-of-major-metros-after-polls>.

⁸ "After Zuma, Another Zuma?" The Economist. January 09, 2016. Accessed May 20, 2016. <http://www.economist.com/news/middle-east-and-africa/21685324-giving-presidency-his-ex-wife-might-be-jacob-zumas-best-shot-avoiding>.

⁹ Hunter, Qaanitah, and Thanduxolo Jika. "Operation Exit Zuma: Top ANC Leaders Driving Secret Plan." Sunday Times. April 17, 2016. Accessed May 20, 2016. <http://www.timeslive.co.za/sundaytimes/stnews/2016/04/17/Operation-exit-Zuma-Top-ANC-leaders-driving-secret-plan>.