FG ASSET MANAGEMENT

# SA budget and grey listing update

Recently we have had two significant developments within the South African market which we felt would be useful to provide feedback on.

The new budget was announced, which I am sure you have already received many review pieces on. Without going into too much detail, the key take aways for us were, firstly, that the minister said all the right things, reflecting the Treasury's commitment to debt stabilisation and fiscal discipline. The problem as ever is one of credibility, for example, Treasury is only modelling public sector wages growing by a modest 3.3% annually for the next three years, well below inflation. In addition, there are risks on the revenue collection side, given the significant constraints to the SA economy posed by loadshedding. These two factors are important determinants if the debt and budget deficit targets will be met. The budget deficit (difference between revenues and expenditure) targets have historically been unattainable due to the expectations of revenue and expenses being too optimistic. Despite the questions around the achievability of these targets, the significant importance of Treasury's intention to keep South Africa fiscally prudent especially a year ahead of the 2024 national elections, must not be underappreciated.

Secondly, as has been widely expected, the budget also provided more detail of the plans to support Eskom. National Treasury committed R243bn in debt relief to Eskom over the next 3 years. The bailout will help alleviate Eskom's weak financial position; however National Treasury has put strict conditions on Eskom to 'safeguard public money'. This will free up cash for maintenance and investment in other much needed areas.

Overall, the budget was positively received as there were no unexpected tax increases, more clarity over Eskom's debt support was provided and government reiterated their commitment to maintaining a prudent fiscal stance.

The second development which we wanted to speak to was South Africa's grey listing by the FATF (Financial Action Task Force). It means that South Africa has been identified as country that will come under increased monitoring following serious deficiencies in its anti-money laundering, terrorism, and proliferation financing framework. Government has addressed 59 of the 67 deficiencies that were first identified in October last year, with only 8 remaining deficiencies still to be resolved. The effective implementation of the legislation was identified by the FATF as lacking, however government's request for a formal assessment again in June 2023 could be seen as an indication that progress is expected regarding the enforcement of legislation. Overall, the grey listing does not prevent new investments, although it does increase the cost of doing business in South Africa.

The big question is, do these developments influence our fund positioning in any meaningful way. The answer is 'not really'. There has been a gradual increase in offshore exposure across our fund range, and this is likely to be a longer-term trajectory given significant domestic challenges and our assessment of the risks. Valuation, however, remains an important determinant and a significant amount of bad news appears to be already priced into domestic assets. We continue to rely on the significant skill set we have at our disposal through our underlying managers.