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SOUTH AFRICA AT A TIPPING POINT

SOUTH AFRICA'S financial prospects, already very uncertain following downgrades by two international ratings agencies—Fitch and S&P—took a turn for the worse when pres. Jacob Zuma unexpectedly fired finance minister Nhlanhla Nene on Wednesday evening after only 19 months in the job, replacing him with an unknown ANC cadre Des van Rooyen.

Financial markets were plunged into turmoil at this news as Nene was considered to be one of the few last bulwarks against further financial profligacy by the ANC government. He showed his independence earlier this month when he turned down a request for more financial assistance by cash-strapped state-owned airline SAA. This decision might have cost him his career.

The market reaction to this announcement was as brutal as it was immediate.

The rand dropped from R14,60 to R15,40 at one stage, but settled down at R15,20 at the time of writing. Against the British pound the rand dropped to R22,70 and almost R16 against the euro.

Pres. Zuma gave no reason for replacing Nene with Van Rooyen but earlier this week the political rumour mills were suggesting that Nene's head was on the chopping block after turning down the SAA deal as well as resisting the funding requests for the proposed nuclear reactor deal with Russia, estimated to cost in excess of R100 billion.

Several international and local commentators have been warning that South Africa should do everything in its power to avoid a downgrade to junk status by any one of the three international credit ratings agencies. Even former ANC minister and Reserve Bank Governor Tito Mboweni earlier this week spoke of a "red mist, a fog" that has descended on the country.

A credit downgrade sometime during 2016, which now looks like a certainty, will have a massive spill-over effect on financial markets and could, in addition to causing further weakness in the currency, lead to a spike in capital market rates, higher retail interest rates as well as an outflow of capital from the Johannesburg Stock exchange.

In all, the likely outcome is not bound to be good.

The timing of Nene's firing could not have come at worst time, barely two months before the tabling of the 2016/17 National Budget. One of the issues the former finance minister has already been grappling with has been the cost of the massive increase in salaries and wages for the bloated civil service (an estimated unplanned cost of R63 billion over the next three years).

Fortunately for Brenthurst Wealth clients we have been advocating offshore investments for longer than 5 years now and a great percentage of our total portfolios are either directly offshore or in rand-based asset swaps. Some of our local asset swaps, such as the MI Plan Global Opportunity Fund, has returned 100% over the past 18 months and is the number one fund in the country over this period.

This fund has been set up as a low-cost asset swap in conjunction with MI Plan and is exclusive to clients of Brenthurst Wealth.

The firing of Nene and the expected longer-term financial fall-out this could cause reinforces this recommendations to an even greater extent. Many clients have resisted our efforts to take some money offshore or consider asset swaps within rand-based portfolios, such as pension, provident and living annuity funds. We think this still remains our best-case scenario as a combination of lower (or no growth), rising budget and current accounts deficits plus a rapidly slowing down revenue collection effort, does not augur well for capital growth of local assets.

As it is, the best returns during the past 5 years have been offshore equity and property markets, with the United States market for instance, growing at a rate of almost three times that of the local JSE.

We don't think this trend is likely to change soon and could even accelerate.

There is also a danger that government might cancel the current foreign investment allowance. There have been voices in the ANC recently saying that allowing private individuals to remit capital offshore is negative for the country and effects badly needed foreign exchange reserves.

Currently individuals are allowed R1m per calendar year in terms of the annual offshore allowance, for which no SARS clearance is needed, plus an additional R10m per calendar year for which SARS clearance is required.

It is therefore possible to remit money offshore before the end of the 2015 calendar year and then again in the first weeks of January 2016 to benefit from the allowance for the following year.

Please speak to your allocated Brenthurst Wealth investment advisor.
Please note our offices are open until the 18th December 2015.

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