Key points

- After an exhausting period of negotiations for cabinet positions, with the broadly expected levels of drama and fluff aimed at influencing narratives throughout the process, President Ramaphosa has announced the National Executive for the seventh administration. Notably, while the cabinet appointments have garnered much attention, the individuals serving as Directors General will also play a crucial role.
- The market may initially cheer the spirit underlying the Government of National Unity (GNU) and the reduction in uncertainty following the cabinet announcement, but the real challenges still lie ahead. It is no secret that the GNU faces significant ideological differences that need to be bridged, and realistically, there will be plenty of turbulence along the way.
- Continued reform progress is, however, expected, promising a more favourable economic outlook for South Africa. While the market may remain cautious of getting too optimistic for now, material evidence of continued reforms could trigger significant capital inflows. Of particular importance will be further progress in consolidating SA's fiscus, although the retention of Enoch Godongwana as finance minister suggests that this is likely.
- Even though the rand has recovered notably in recent months and is now trading closer to its risk-adjusted fair value, there is scope for it to record more gains through H2 of this year. It is poised to capitalise on looser monetary conditions in the developed world, with SA's risk profile significantly better than it was just a few months ago.

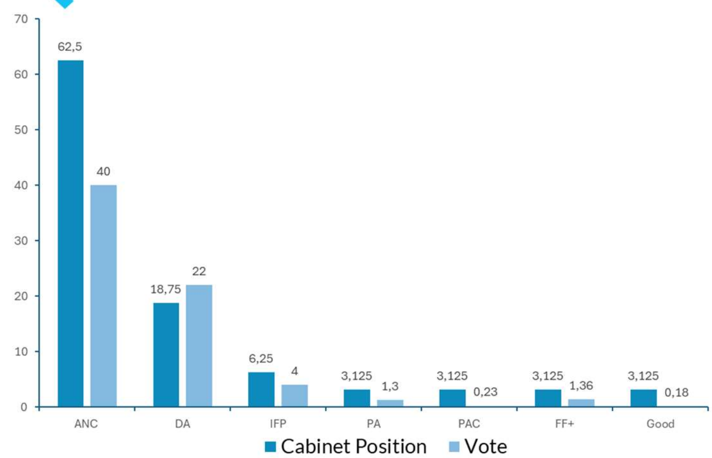
BASELINE VIEW: Six years ago, Ramaphosa promised South Africans the beginning of a new dawn. He adopted an economy facing structural headwinds due to the maladministration of his predecessor, but has gradually been implementing key reforms aimed at crowding in the private sector. Now, the GNU has another opportunity to push forward the 'new dawn' vision. One, perhaps with a more centrist leaning and a business-friendly stance, which will lay the foundations for sustainable, long-term economic growth. In turn, this holds the potential to significantly improve SA's risk profile, which will unlock foreign capital flows and support the ZAR.

Wrapping up the 2024 elections

Thirty-three days post-election, South Africa has a seventh administration. President Cyril Ramaphosa announced the country's most diverse, albeit most bloated, cabinet to date. Cabinet positions were dished out seemingly not on an equal-to-vote basis, but the jockeying for the top spots is now done.

With this finalisation, the markets can breathe a sigh of relief. However, the direction from this moment of optimism will depend on the extent of harmonious co-operation between members of the Government of National Unity (GNU) members.

Political make-up of SA's Cabinet
Share of Cabinet positions vs Share of votes (%)



Source: IEC, SA Gov, ETM Analytics

Who's in?

South Africa's National Executive increased from 30 to 32 cabinet positions (excluding the president and deputy-president), while the number of deputy ministers also rose from 36 to 43. Members from all of the parties within the GNU, bar Rise Mzansi and the United Africans Transformation, received posts as either ministers or deputy ministers.

ANC members are heading 20 ministries, the DA six, the IFP two, and the FF+, PA, PAC, and the Good Party one each. The cabinet is now more reflective of South Africa's diverse political landscape, allowing for different inputs into the national dialogue preceding policy formation.

This is therefore a better outcome for the country's democracy when compared to the one-party state South Africa effectively was under ANC rule since 1994.

The success of the GNU will depend on whether the participating parties can manage to co-operate despite their ideological differences. Several points of contention still need to be ironed out, especially on policy direction. These include the support of/implementation of policies related to the National Health Insurance (NHI) bill, Basic Education Laws Amendment (BELA) bill, and the Land Expropriation bill, to name but a few.

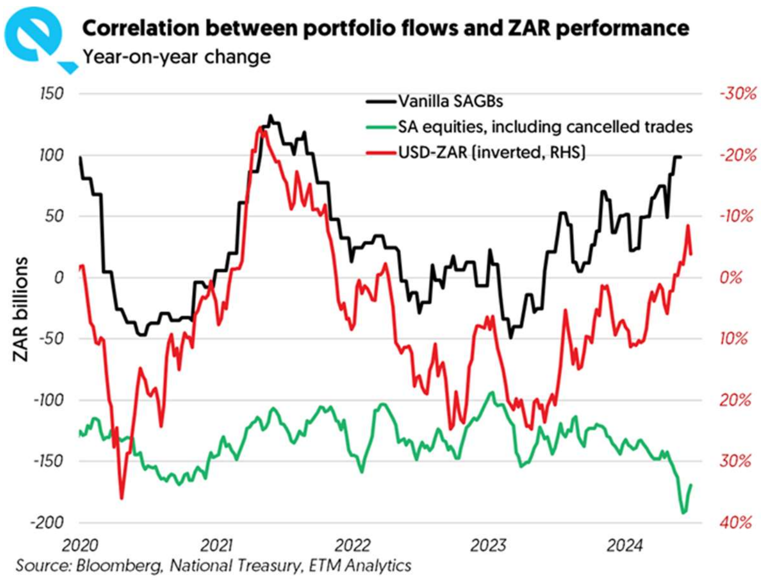
What's next?

Although much has been made of the cabinet appointments, those who occupy positions as Directors General (DG) will also be of significance. Often out of the limelight, so to speak, DGs are mandated to ensure proper administration, policy implementation, strong communication and all the rest of the day-to-day functioning of a department.

They form an integral part of the mechanics of a ministry, and therefore hold much sway in the direction a department is heading. These appointments still need to be revealed, and should be closely watched.

The GNU and reforms

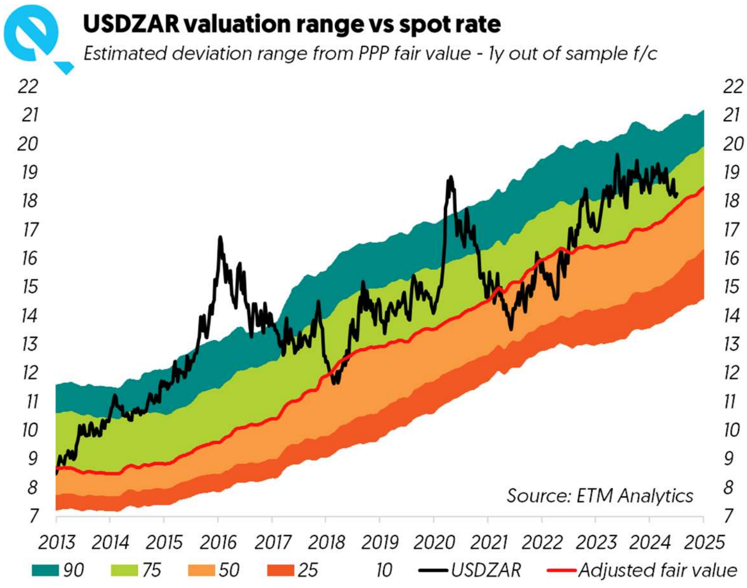
Time will tell the degree to which the ANC will impose its more left-leaning ideology on its new coalition partners rather than negotiating policy plans, and it might well be too much to expect the GNU to survive a full five-year term.



With that being said, significant progress can be made over a few years to solidify and expedite important reforms. Prior to the election, the first Ramaphosa administration had already begun to implement various reforms aimed at better utilising private sector capabilities for developing SA's struggling electricity, ports, and railway infrastructure.

These reform efforts are still in the early, delicate stages and will require more time to have a substantial economic impact. Nonetheless, the election results, solidified by a GNU that excludes the likes of the EFF and MK and is instead formed around an ANC-DA partnership, is a welcome development. The private sector's involvement is expected to increase in the coming years, promising a more favourable economic outlook for South Africa. While the markets may remain cautious of getting overly optimistic for now, material evidence of continued reform progress could trigger capital inflows that would support SAGBs and the ZAR.

ZAR outlook

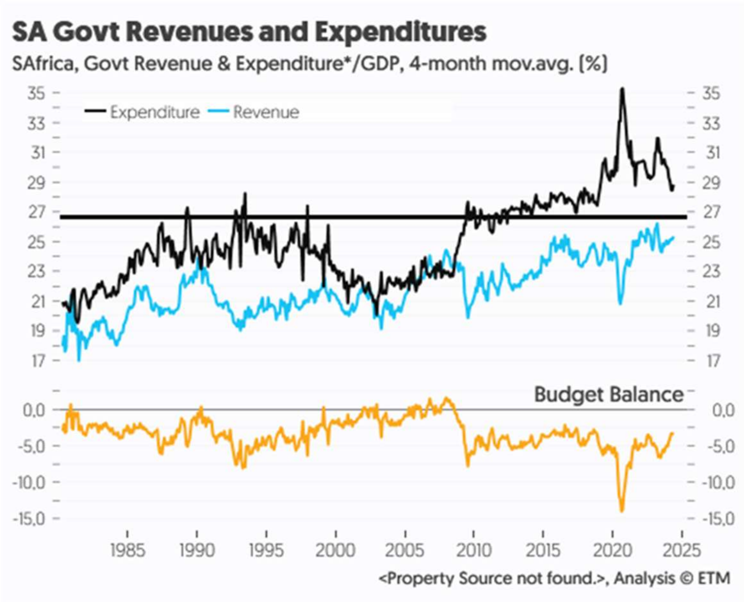


It is worth noting that much of the bad news that was baked into the rand through the early stages of this year has now been priced out. The ZAR was trading deeply in undervalued territory at levels closer to R19.4000/$ in mid-April, but the adjacent chart shows that it has recovered towards its risk-adjusted fair value around the R18.0000/$ handle.

That is not to say that it can't appreciate further, especially if evidence of political stability and meaningful economic reforms emerges. SAGB yields remain highly attractive, especially for carry traders looking to take advantage of the flusher liquidity conditions that will follow an anticipated global rate cut cycle into the end of the year.

As illustrated in the first chart to the top-right, the ZAR's trajectory is closely linked to foreign demand for SAGBs. Moreover, if one adds to SA's rising attractiveness the possibility that the USD could lose ground due to a shift in the US Federal Reserve's monetary policy, then the argument for the ZAR to make a substantial recovery through H2 increases. This environment holds the potential to generate a virtuous cycle that will self-reinforce, suggesting there is scope for continued ZAR strength.

More fiscal consolidation is key



Of particular importance for the outlook of SAGBs and the ZAR is South Africa's fiscal performance. The GNU needs to commit to being fiscally disciplined with taxpayer money, especially when every party has its own spending priorities.

With this in mind, the retention of Enoch Godongwana as finance minister is a very positive outcome. It signals a continuation of fiscal consolidation, with the adjacent chart illustrating a narrowing budget deficit in recent months.

Data published in the SARB's Quarterly Bulletin last week confirmed that for the first time in 15 years, South Africa posted a primary surplus (when revenue exceeds non-interest expenditure) in the 12 months through March.

Minister Godongwana has held a firm line on funding to ailing state companies, and more of the same is likely under the banner of the GNU. Should reforms manifest as expected, there would be a strong case for capital inflows into SA that would support the ZAR.

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