



Recovering from COVID-19

Considering economic scenarios
for resilient leaders

Overview and approach

The outbreak of COVID-19 has necessitated the implementation of stringent policy measures, setting off a global economic crisis of unprecedented magnitude. As part of the firm's commitment to support its clients, Deloitte Africa has implemented a COVID-19 recovery framework to help businesses and governments navigate these extremely uncertain times.

The COVID-19 pandemic challenges leaders to stabilise their organisations amidst a crisis and prepare for a newly uncertain future. Compounding the body blows the economy has been enduring from the COVID-19 forced economic shutdown is the fiscal weakness that South Africa finds itself in. Not possessing the "fiscal space", the state is unable to allocate sizeable funding to support industry and preserve consumer spending power.

Our firm has set out a broad framework that consists of three facets: **Respond** (how to react to the crisis); **Recover** (how to position for the rebound); and **Thrive** (how to ensure success in the post-COVID-19 world).

As part of the effort to support our clients, we are providing high frequency commentary, real-time monitoring of health, economic, and financial statistics, and recurrent updates on the evolving outlook. In light of the unprecedented uncertainty that we are facing, we have also developed three plausible scenarios, each outlining a potential path for the South African and global economies depending on how the pandemic evolves.

Our past outlooks and commentary have emphasised the benefits of scenario planning. Such an approach is particularly helpful in the current climate of extreme volatility and elevated uncertainty regarding the future. Scenario-based strategic planning, when executed against a range of plausible outcomes, allows organisations to prepare for various outcomes, helps executives identify key decision points and positions the organisation to take advantage of opportunities during the recovery (which will come).

Scenario 1 is a scenario where pandemic containment efforts prove successful, but manifest in a dramatic but short-lived economic contraction that is followed by

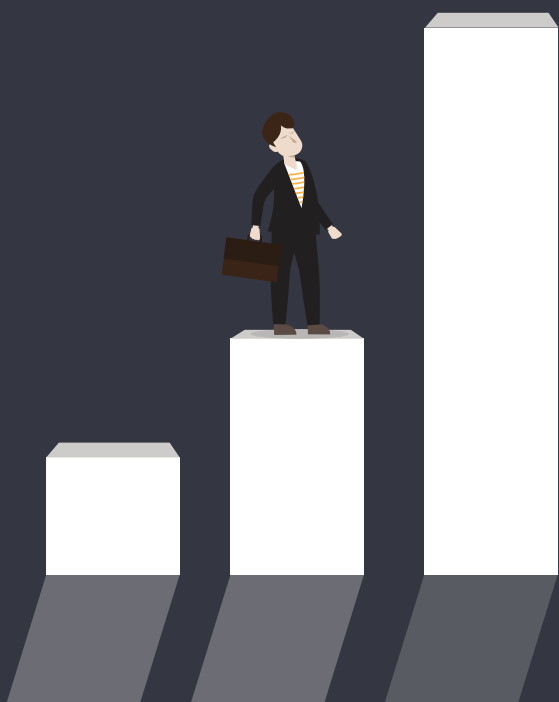
a gradual recovery reflecting the long-lasting legacies of the economic plunge. This outcome results in a drop in GDP of more than 1.5 times what we saw during the Great Recession of 2008-09.

In **Scenario 2**, the pandemic lasts longer with waves of infection lasting through mid-year and into the third quarter of this year. There is also a resurgence of the virus heading into 2021. In this scenario, the South African economy is faced with a prolonged shutdown extending into the beginning of 2021.

Scenario 3 models a worst-case scenario. In this scenario, containment of the virus fails as the virus continues to mutate preventing the development of a successful vaccine. The global and South African economies experience a long-lasting decline in GDP (i.e. depression).

This document summarises the three distinct global scenarios of varying magnitude and discusses the associated paths for the South African economy. In each scenario, we outline key domestic and global assumptions.

The decisions businesses make in the near term will drive how companies sustain themselves in the long term. It is critical that leaders take decisive action to soften the shocks we know are yet to come as they prepare for what may change in the months ahead.



Deloitte's Resilient Leadership framework defines three timeframes of the crisis...



This document is designed to guide leaders in strategic, financial and operational planning over the next 18-24 months as the **Respond** time frame emerges into **Recover**.

Each of the economic cases posits a future economic state – including trends in health, society, technology, policy and the environment – leading to corresponding economic implications. These economic cases are not predictions about what will happen; they are hypotheses about what could happen, designed to frame planning discussions in light of global conditions as well as those in South Africa.

The focus of this document is to set out **three Near-Term Scenarios**. These distinct scenarios are intended to guide leaders through to the end of 2021.

As you read through these scenarios, please consider:

- Which of your previous expectations need to be rethought? What prospects that seemed unlikely or years away could be accelerated?
- What might consumers value in particular in these different worlds? How might that vary across key variables (for example regions and industries)?
- What are the biggest threats to your current business in these worlds?
- What new providers, companies, business models, and ecosystems might emerge? Which existing companies are best positioned to succeed?
- What capabilities, relationships, and assets are important in these worlds?

Scenario 1: A steep but short-lived downturn

What if the pandemic eases sooner than experts anticipate? The BBC reported that “so far, and against most predictions, South Africa’s hospitals remain quiet, the anticipated ‘tsunami’ of infections that many experts here have been waiting for has yet to materialise.” Has South Africa’s pro-active response to the pandemic worked to save countless lives and succeeded in “flattening the curve” of infections to manageable proportions?

What if effective Government measures combined with increased testing to contain the virus lead us out of the crisis phase in the next few months? This will lead to a relatively fast economic recovery. Small and medium-sized businesses are surely being hurt and the economic impact cannot help but be notable. But something like “normal” returns, even if it is not quite the same as before. This scenario anticipates a relatively quick normalisation of conditions.

More business and social activity has moved online and stays there. The crisis has boosted e-commerce plays and has changed the face of formal retail forever. Perhaps there is growing respect for public sector institutions following their pro-active response to contain the pandemic crisis, the medical expertise of both our private and public sectors working in unison, and a new appreciation for reliable data and information when lives are on the line.

And as we come out of our homes so that life on the street returns, the new appreciation for our friends and neighbours and even the loss of some treasured local shops, reminds us not to take those things for granted....

After declining sharply in the first half of the year, global economic activity begins to rebound from mid-year.

While the recovery is initially slow, it speeds up in the second half of 2021 as consumers become more confident. The recessions in the European Union and the United States are deep but quick. Global growth slows to zero in 2020 while the US experiences a 5% contraction. Small and medium-sized businesses are disproportionately impaired. Substantial fiscal programmes in the EU and the US help to limit the damage.

Overall, we expect South African GDP to decline sharply in 2020 followed by a gradual improvement in 2021. While the downturn will be short-lived, the annual decline could well turn out to be more than three times the decline experienced during the Great Recession of 2008-09.



Health

- Current measures are largely successful in preventing the spread of the virus
- As South Africa enacted restrictions relatively quickly, it effectively contained the virus and is able to open its domestic economy sooner
- Relatively constrained disease dynamic and a rapid response by the health system - private supporting public
- Warmer weather in the northern hemisphere helps to contain COVID-19 and limit further outbreaks in the regions which first suffered the outbreaks of infection
- Revival of the virus later in the year is dealt with through improved testing and tracking rather than shutting down economic activity
- Overall, stifled (or at the very least reduced) human movement limits the spread of the virus



Society, Technology, Policy, Environment

- Despite the negative impact on small business, there is increased social cohesion witnessed emerging from the period of shutdown
- Acceleration in tech development, with more businesses' models shifting online, in particular retail. This is a tailwind to the logistics sector
- Global supply chains recover but there is an increased tendency toward local procurement, if only to promote local growth in damaged societies
- A far greater sense of collaboration between public and private sector, including unions
- Growing respect for public sector institutions as their efforts appear to have slowed the pandemic

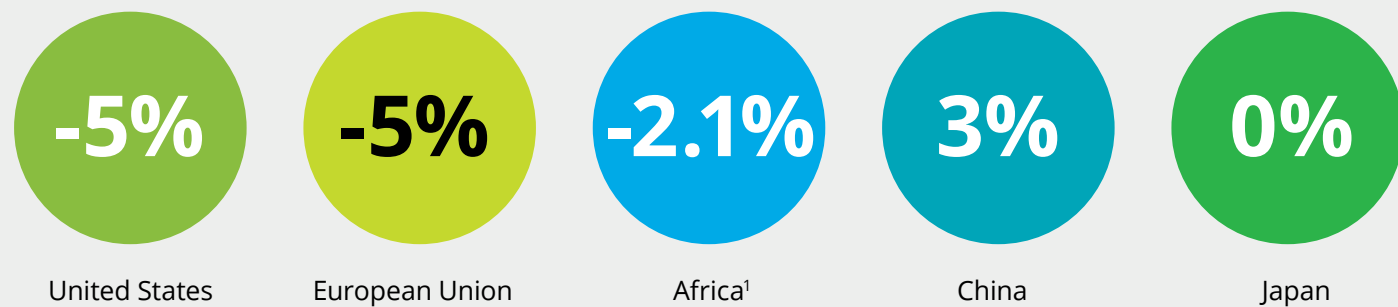


The Economy

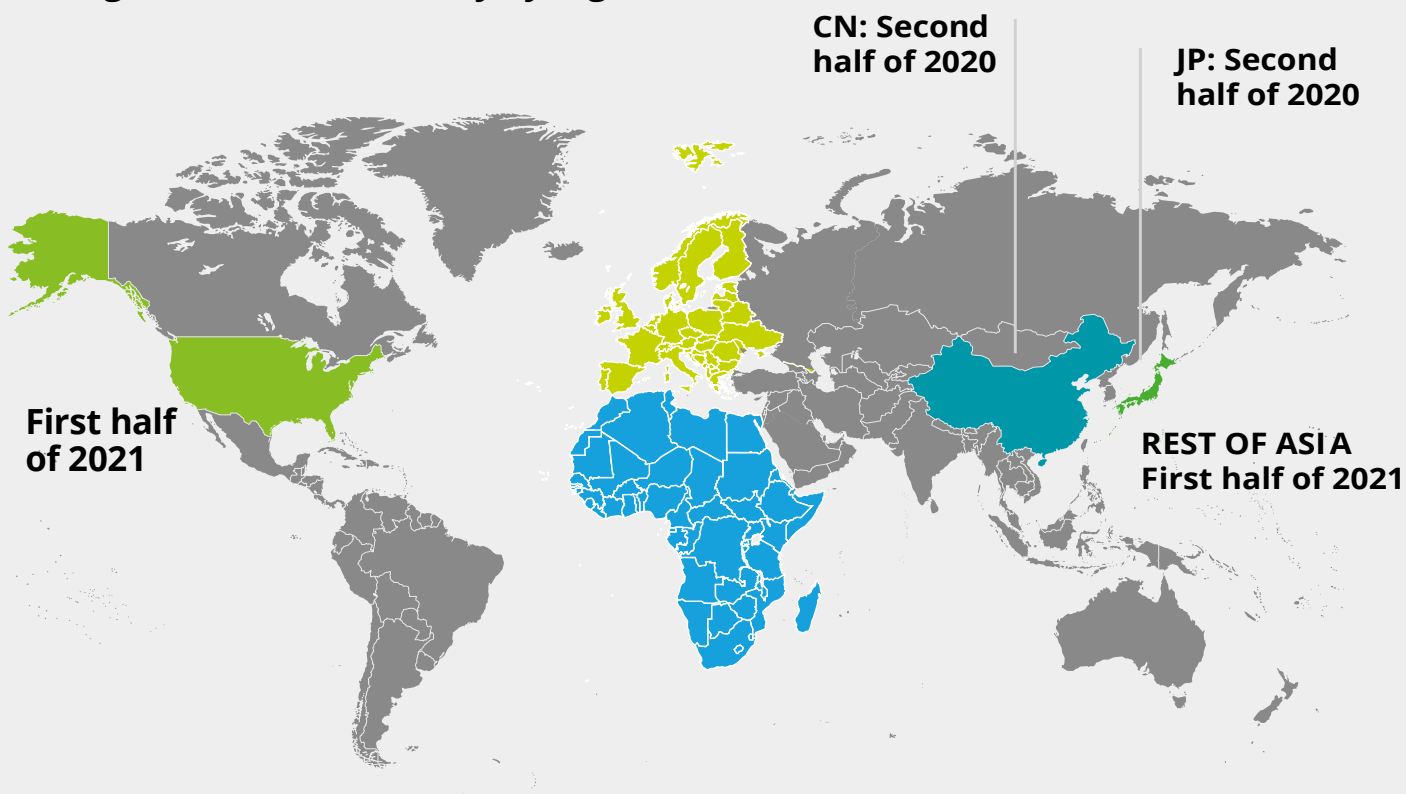
- Economic activity rebounds in late 2020 as the virus dissipates. The recovery is initially slow but picks up in the second half of the year as consumers become more confident
- China's relatively quick recovery and stimulus spend has an inflationary impact on commodity prices, supporting commodity exporting countries like South Africa
- Commodity exports are expected to decline in the second quarter but largely rebound later in the year
- Non-commodity exports see a large decline due to suppressed global demand for manufactured goods, in particular automotive
- Deep but quick recessions in the European Union and the United States; small & medium businesses disproportionately impaired
- Substantial fiscal programmes in the European Union and the United States help in limiting the damage in the wider global economy
- Low oil prices provide some relief to the South African economy and consumer
- Commercial real estate is hit by increased business bankruptcies, rising vacancy rates and a permanent increase to remote work
- Despite some return to growth late in 2020, exports will be suppressed by ongoing weak demand and low business investment
- Travel and leisure services fall dramatically in the second quarter. A slow recovery thereafter
- Spending growth will return in the third quarter as stores reopen but there is ongoing weakness. This weakness will be driven by a deterioration in household finances
- Consumers exit the downturn with higher debt burdens and a negative wealth effect from the stock market correction
- Interest rates are projected to remain at current lows until early 2022
- In this scenario, equities are projected to start to rebound in late 2020



Real GDP growth in 2020



Timing of economic recovery by region



¹World Bank Forecast

Scenario 2: Prolonged pandemic and delayed rebound

What if the pandemic lasts longer than what we are ready for, with waves of infection lasting throughout the year keeping us in crisis mode for months to come? A prolonged recession with weak supply and weak demand, combined with financial system shocks, wreaks havoc on social and economic life. But maybe not all countries suffer to the same degree. Those which faced it sooner and reacted more aggressively return to normality faster, while those slower or less consistent in their responses are hurt more deeply and for longer.

Before long, virtual life is real life in many places. Will those companies that can still invest accelerate their investments in AI, robotics and other technologies to reduce their reliance on human labour, subject to the disease? Or will the need to rebuild the economy and restart consumption favour policies that promote getting people back into

employment in 2021? This may be a clear case of technology versus labour as to which is prioritised.

In this scenario, the Chinese economy rebounds slowly. There is a deep and prolonged recession in Western economies, affecting supply chains and consumer demand. Fiscal stimulus limits business failures but does not boost spending. There is a deep drop in output as supply chains are disrupted. There is a severe decline in global demand and financial stress akin to 2008-09. In all, the recession lasts nine quarters long with the recovery beginning in the second half of 2021.

The South African economy – mimicking other emerging markets – experiences a sharp contraction and a decline in South African GDP of up to 10% in 2020 has been projected.² After a second containment, a rather gradual recovery begins in the second half of 2021. The pattern



of economic growth would have characteristics of a 'W' double dip. This outcome could be achieved without the second round of the virus and containment and is a downside risk to the economy from the legacies of the 2020 contraction. The longer and more extensive economic downturn leads to extensive liquidity and balance sheet pressures causing high levels of business failure and strains on the financial system.

Health

- The current measures are initially successful in preventing the spread of the virus
- The outbreak in China is mostly contained, but some revival due to returning inbound travel
- The second viral outbreak is worse than the first one as people are less willing to follow the restrictions
- South Africa which had a strong containment effort in the first wave will see the biggest resurgence due to a low build-up of immunity
- The European Union and the United States have severe outbreaks which return in waves and last until early 2021
- Restrictions in select areas are put in place through the first quarter of 2021
- Contagion of COVID-19 in South Africa and the region becomes deeply problematic for the healthcare sector to manage



²Business South Africa

Society, Technology, Policy, Environment

- Extended and severe virus leads to all things virtual as the norm with increasing comfort with life online, even among previous holdouts
- The African Continental Free Trade Area (AfCFTA) agreement is no longer a priority of African governments
- Technologies of the Fourth Industrial Revolution (4IR) accelerate in development due to greater demand
- Mixed environmental impact
- Limited cooperation between countries, growing tendency toward nationalism rather than regionalism
- Rise in centralised surveillance mechanisms

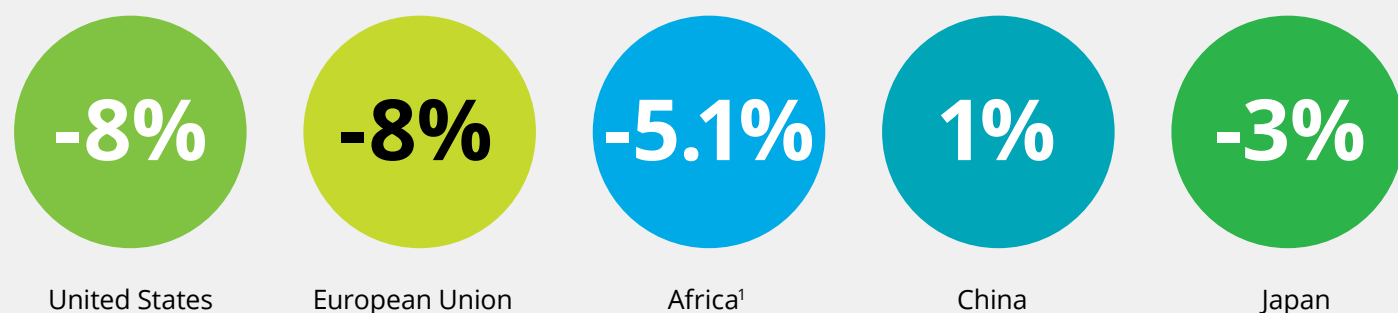


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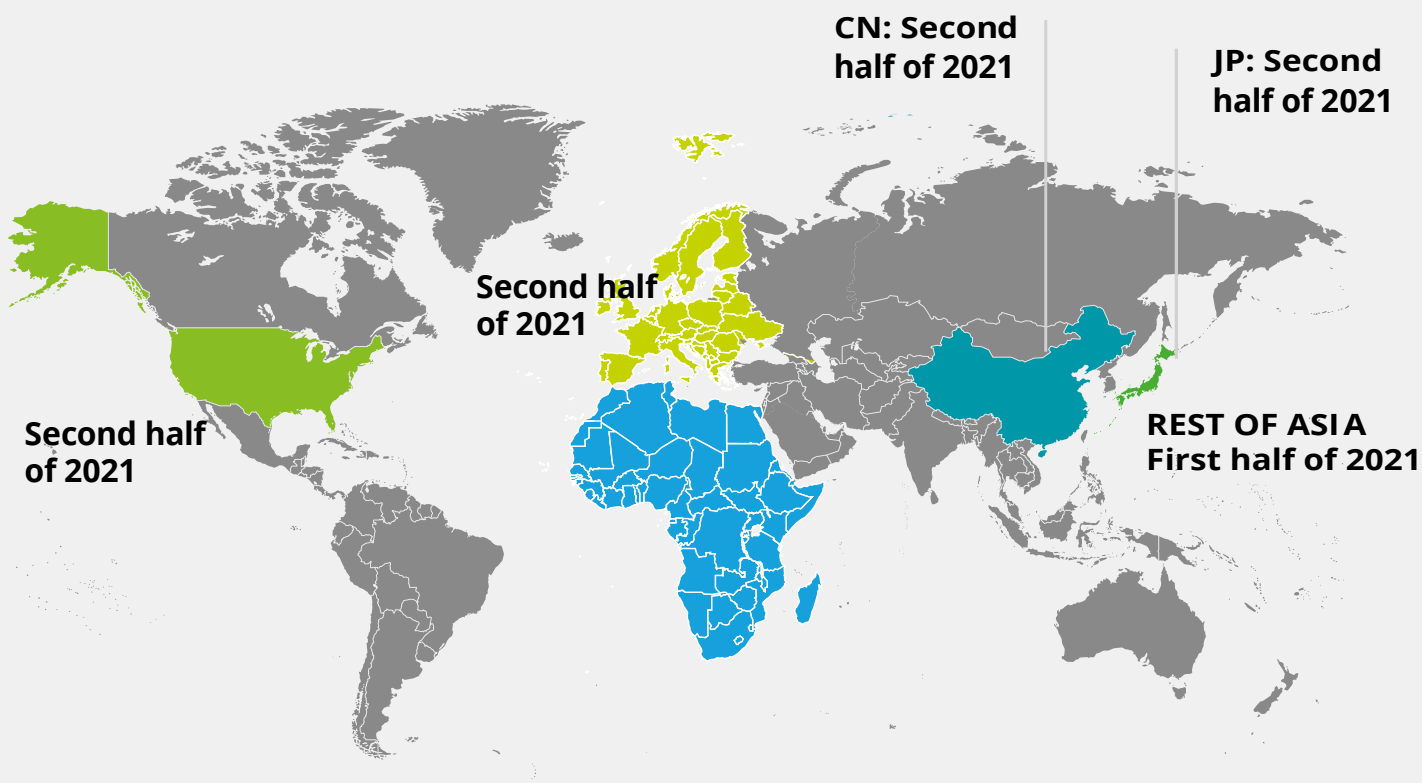
- The virus follows a wave pattern, abating and then peaking again in multiple global geographies.
- Economic recovery begins late 2021. Recovery is slow in early 2022 and picks up by the second half of 2022
- China's economy rebounds slower than expected, resulting in subdued commodity prices as a result
- Deep and prolonged recession in West, affects supply chains and consumer demand
- Inflation in the supply chain due to high production cost and lesser competition
- Fiscal stimulus limits business failures, but does not boost spending
- Rising structural unemployment in South Africa increases to 40%
- Commercial real estate experiences acute weakness
- Manufactured exports are expected to see a substantial decline
- The continuance of the virus will result in a large decline in consumer spending due to deteriorating household finances
- The steep decline in GDP places significant stress on the public sector, already in a precarious fiscal situation
- Interest rates are projected to remain at current lows until mid-2022
- Despite low interest rates, some prices could see a boost in inflation such as food
- In this scenario, banks run into rising defaults which place stress on their balance sheets
- Equities start to rebound in late 2020, but are pushed down again as the economy falters and does not show signs of a recovery in the short term



Real GDP growth in 2020



Timing of economic recovery by region



Scenario 3: The worst case scenario

What if the pandemic fools us into thinking we are making gains when in fact we have mistaken the foothills for the mountain? What if the countries that today seem to have things under control face a return of the virus, while those still struggling today find that the pandemic outruns every effort at containment? And what if we discover that the world is just too big, as the virus cycles (and mutates) between wealthier nations and the emerging economies they trade with. Will even the most aggressive fiscal and monetary interventions in history fall short? Large parts of the global economy move from economic recessions into a state of depression.

Yes, technology adoption will grow, but so will distress and suspicion. Is privacy – about our health, our whereabouts, the people we have been near – a luxury we can no longer afford? How would our calculus of trust change?



In this scenario, the financial system breaks down despite central bank efforts. Fiscal stimulus is substantial at first but fails to boost private consumption. There are many business failures and household disruptions. There is a severe drop in output as supply chains break down. As government attempts to maintain production in the economy, there is a widespread and enduring nationalisation of industries.

The global economy experiences a severe decline in demand and many sizeable business failures. The global

economic recovery does not take hold until early 2022.

In this scenario, the South African economy experiences continued economic contraction in 2021 beset with structural constraints to growth. At first, this is broadly similar to the previous scenarios but the economy continues to languish for a prolonged period. The large increase in business and household debt that has occurred also has a large and persistent impact on the economy throughout 2021 and 2022.

Health

- The current measures are unsuccessful in preventing the spread of the virus
- Smaller but frequent virus outbreaks keep occurring throughout 2020 and intensify as the flu season arrives
- Outbreak returns to North Asia, with negative economic repercussions globally
- The second and third viral outbreaks are worse than the first one as people are less willing to follow the restrictions as economic hardship leads to social unrest
- More people contract the virus with every outbreak causing the health system to be severely disrupted
- The European Union and United States outbreaks are prolonged, coming in multiple waves
- Severe outbreak in emerging countries; possible negative feedback loop to the West
- South Africa which had a strong containment effort in the first wave, will see the biggest resurgence with intermittent periods of restrictions
- Containment is achieved by late 2021, largely due to crowd immunity



Society, Technology, Policy, Environment

- Social cohesion begins to unravel; suspicion of others becomes the norm and xenophobia rises
- Isolationism is practiced globally – strict border controls and shortened supply chains
- Flows of people, services, goods and capital are reduced in a de-globalising world
- The African Continental Free Trade Area agreement is ignored by African governments which have shunned multilateral collaboration, instead closing their borders to trade
- Technology advances to meet society's virtual demands; government obliges data sharing from the citizenry
- At a global level, economic recovery is prioritised over fighting climate change

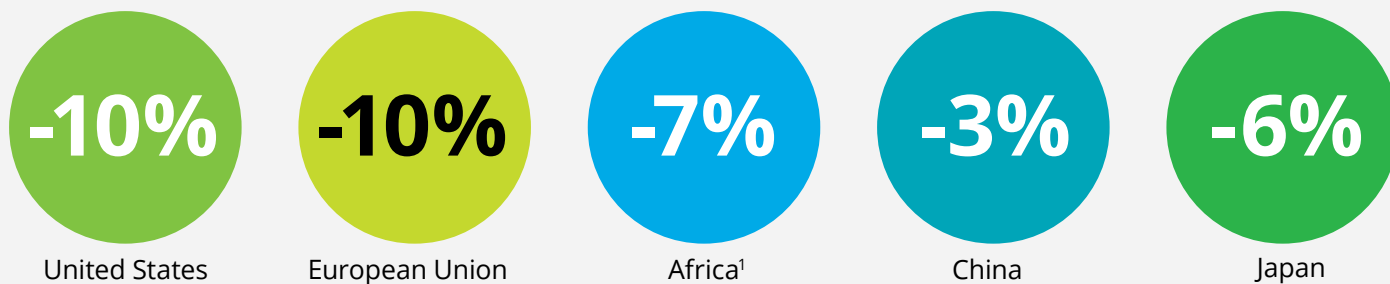


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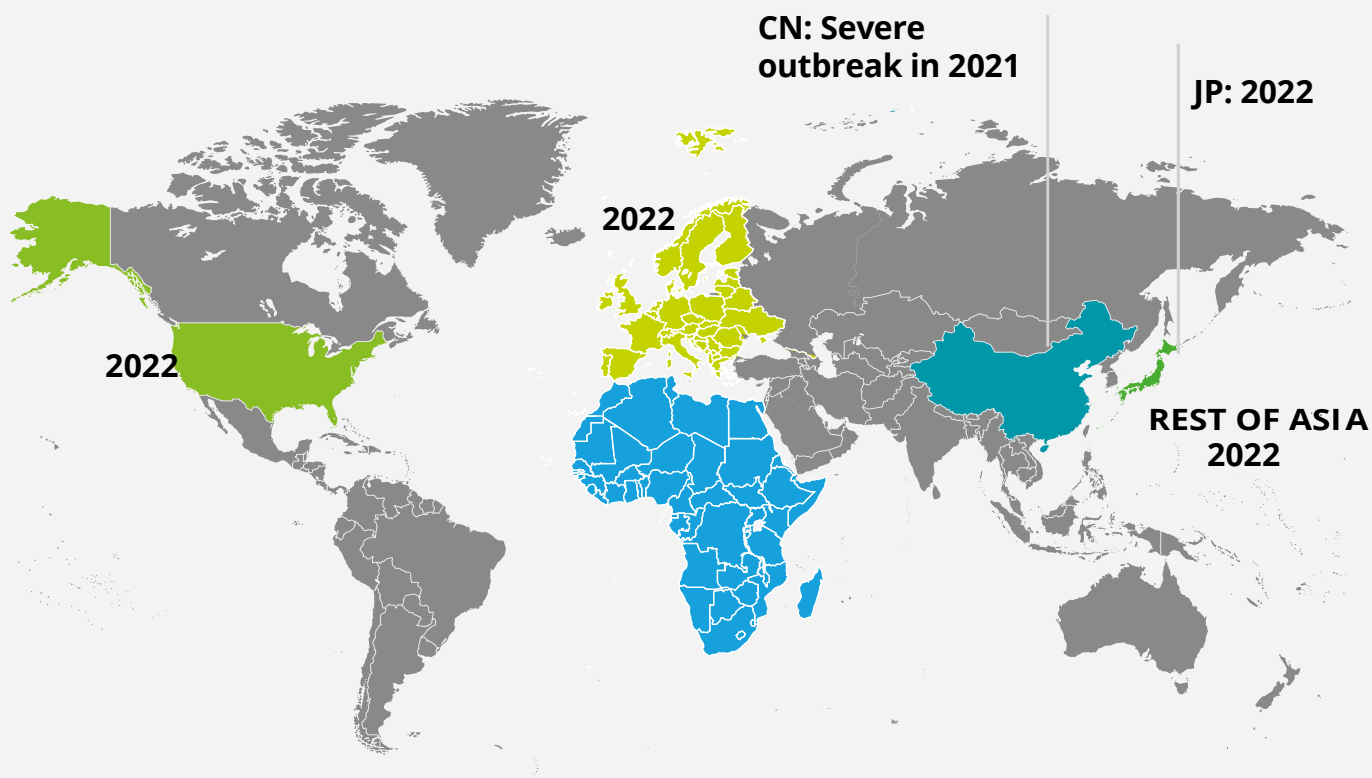
- The epidemic continues with severe infections into 2021 until either crowd immunity and/or a vaccine reduces the virality. Economic recovery begins by mid-2022. Significant risk of cascading outbreaks with feedback loops, limiting economic recovery
- Global depression – major global economies decline by 10% or more in real GDP for two or more years
- Financial system breaks down despite central bank efforts causing banking crises in many economies, in particular emerging markets
- As the capital stock is depleted, commodity exports continue to decline
- Manufactured exports undergo a substantial decline
- When the new waves of the virus hit, exports for non-essential items decline severely
- After considerable declines, imports are limited to essential goods
- Inflation is not contained with high volatility in food, fuel, shelter, and discretionary goods inflation. Deflation takes hold
- Net export balance is a drag to the overall economy
- There is a permanent negative wealth shock
- As the economic downturn extends, public sector fiscal accounts come under significant strain
- Chronic structural unemployment in South Africa increases to 50%
- Many business failures across the board and household disruptions occur
- Widespread and enduring nationalisation of industries by the state
- In this scenario, rising defaults stress banks' balance sheets as their capital base is eroded. There is the risk of extreme financial system stress as businesses fail



Real GDP growth in 2020



Timing of economic recovery by region



Looking beyond 2020

There are numerous macro-economic uncertainties that affect any near-term economic cases, many of which present either additional upside opportunities and/or downside risks beyond the accompanying economic cases. We have presented some additional thoughts centred around key thematic issues as to how the future may transpire.

As noted, these scenarios suggest a range of possible outcomes as the COVID-19 crisis rapidly evolves. It is too soon to tell which of these scenarios will emerge, but resilient leaders are preparing now for what the future may hold.

Upside Opportunities

- Social cohesion is improved coming out of the crisis as people develop a heightened sense of appreciation of relationships following periods of quarantine
- Virtual learning becomes more prominent resulting in increased access and affordability of education
- The Future of Work is fundamentally different with employers realising the benefits and cost effectiveness of virtual work teams, particular in the professional sector
- Step change increase in corporate social responsibility consistent with Business Roundtable tenets



Society

Downside Risks

- Increased tensions between younger and older generations as retirement ages are pushed out to recover lost wealth
- Rising xenophobia against foreigners and groups of perceived difference with populations adopting prejudice against others
- Rising frictions between the haves and have nots in society and wealth differentials
- Increase in crime and social discord due to heightened rising inequality

- Ubiquitous deployment of connectivity and 5G leads to rapid digitalisation of business and society
- There is a significant investment in remote conferencing and virtual reality applications
- Virtual “hangout” sessions become the norm helping to keep family and friends connected regardless of distance
- Telemedicine becomes the “frontline” of medicine enabling far wider healthcare penetration



Technology

- There is an increased prevalence of states’ obliging their citizens to share data and privacy laws are rolled back
- Increased stress amongst workforces who find that work-life balance is no longer possible with heightened connectivity
- With increased reliance on technology, society finds itself increasingly vulnerable to cyber attacks

Upside Opportunities

- An increased sense of collaboration and partnership between public and private sectors in a post-COVID-19 world
- International organisations see a rise in relevance as people become more aware of their role and activities
- As Asia recovers more rapidly than Western economies, East Asian countries begin to assume more leadership roles in global institutions

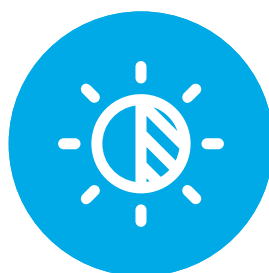


Politics

Downside Risks

- Countries turn to isolationism and the trend is toward de-globalisation with a reduction in flows of good, services, labour, and capital
- Nations put strict control on foreigners and force supply chains home in the name of national security
- Global coordination institutions such as the UN, WTO and others become increasingly ineffective

- Renewed efforts to combat climate change are undertaken as successful global collaboration around COVID-19 now serves as model to also act on multilateral climate issues



Environment

- Declines in pollution are seen from increased “stay at home” measures, the economic challenges lead to an overall decline in emphasis on climate change and investment in renewable energies
- Countries tend toward withdrawing from climate change agreements to focus on short-term economic recovery

Contacts

Dr Martyn Davies

MD, Emerging Markets & Africa
Deloitte Africa
+27 83 459 8880
mdavies@deloitte.co.za

Andre Dennis

Consumer Industry Leader
Deloitte Africa
+27 82 566 3707
adennis@deloitte.co.za

Nazeer Essop

Government & Public Services Leader
Deloitte Africa
+27 82 827 8607
nessop@deloitte.co.za

Mark Joseph

Technology, Media and Telecommunications
Industry Leader
Deloitte Africa
+27 83 260 4538
marjoseph@deloitte.co.za

Andrew Lane

Energy, Resources & Industrials
Industry Leader
Deloitte Africa
+27 83 326 2849
alane@deloitte.co.za

Nina le Riche

Financial Services Industry Leader
Deloitte Africa
+27 82 331 4840
nleriche@deloitte.co.za

Ashleigh Theophanides

Life Sciences & Health Care Leader
Deloitte Africa
+27 72 698 9886
atheophanides@deloitte.co.za



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