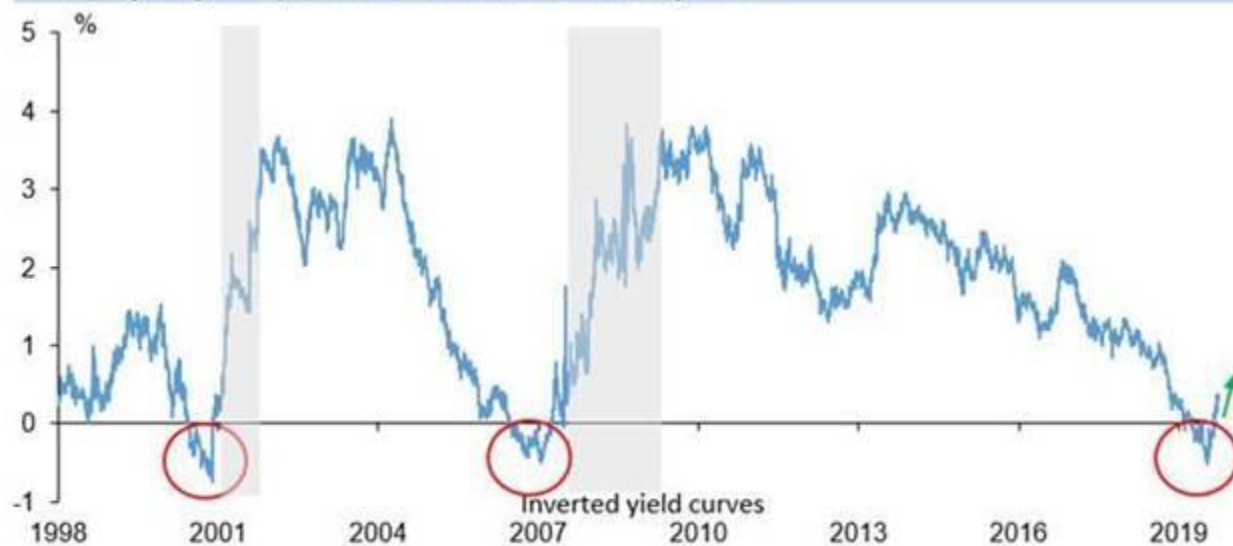


Rand Note

14th November 2019

Rand strengthens somewhat over the course of this week with some risk seen as diminishing as the US 'yield curve' uninverts and the Fed indicates little further on the rate cut front (with markets now having priced in Octobers MTBPS)

US: ten year yield spread over three month treasury rate

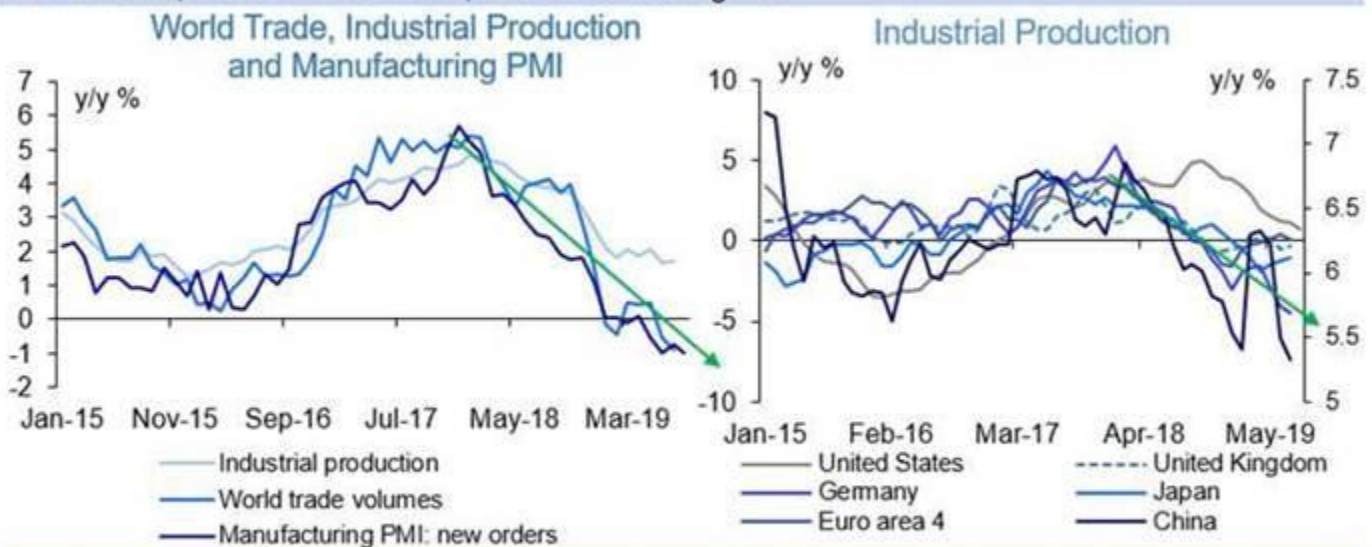


Source: IRESS, Economist

- The rand has reached R14.82/USD, R16.29/EUR and R19.02/GBP today, strengthening somewhat over the course of this week as markets globally quietened somewhat, with the US spread between ten year and three month rates losing the inversion that had prevailed over most of this year.

- Part of the reason for the inversion falling away has been the fairly strong signals that the US is unlikely to cut interest rates further this year, or indeed in H1.20, and this, along with the uninversion, are both being taken by the markets as potentially indicating that the risk of recession is subsiding (that the Fed is less concerned on the growth front as well).
- Fed Chair Jerome Powell this week sounded significantly upbeat on the US economy, highlighting that the Fed “see(s) the current stance of monetary policy as likely to remain appropriate as long as incoming information about the economy remains broadly consistent with our outlook”.
- He specifically added, that “(w)hat we have learned — and what we continue to learn — is that the U.S. economy can operate at a much lower level of unemployment than many would have thought”. The more sanguine approach of the Fed to the jobs market is also being seen by markets as reducing the possibility of further rate cuts in the near term.
- This does not mean that the global economy is no longer at risk of recession, or indeed that it is not experiencing further slowdown, nor does it mean that the US led trade feud, and its effects, are at an end. Recent Chinese retail sales and manufacturing output was weaker than expected, indicating that broad based nature of the slowdown in the economy.
- The rand’s hiatus will prove to be short-lived if the synchronised global economic slowdown accelerates, or indeed persists. Currently however, markets have also gained some cheer on German GDP data showing the EU’s largest economy avoided recession in Q2.19 and Q3.19.
- Nevertheless, evidence of the weaknesses in the global economy persists, and Governor Powell has recognised the feed through into the US, adding that “(i)n particular, sluggish growth abroad and trade developments have weighed on the ... (US)... economy and pose ongoing risks”.

World Trade, Industrial Production, and Manufacturing PMI



Source: CPB Netherlands Bureau for Economic Policy Analysis and IMF

Three-month moving average; year-over-year percent change

- Earlier this month the IMF also warned on spill over effects, specifically into the world’s largest economic block, stating that “(a)s in the rest of the world, European trade and manufacturing have weakened. There

are some signs that this slowdown is spreading into the rest of the economy ... investment is starting to lose steam.”

- “The weakening trade and manufacturing—along with subdued business confidence and elevated trade uncertainty—have started to spill over into investment, especially in many *advanced European* countries. While the services sector has been relatively buoyant, it too has started to soften. Private consumption, however, has stayed relatively robust.”
- “This weakness is primarily driven by machinery and transport equipment—sectors that are particularly relevant for Europe. As a result, economic activity in Europe has slowed, especially in *advanced economies*. *Emerging European* economies outside of Russia and Turkey were a bright spot, with growth remaining strong.”
- “(S)igns of a slowdown are also emerging in labor markets. For example, job openings—a measure of labor demand—are not only falling in the manufacturing sector, but vacancy growth for the overall economy has also slowed since the beginning of the year.”
- “On balance, Europe’s growth is projected to decline from 2.3 percent in 2018 to 1.4 percent in 2019. A modest and precarious recovery is forecast for 2020 due to an expected rebound in external demand that would limit emerging spillovers into investment and services.”
- The IMF concludes that “(a)mid high uncertainty, there are several risks to the outlook, including Brexit-related disruptions, intensifications of protectionism and related uncertainty, abrupt declines in risk appetite, and rising geopolitical tensions.”
- While the central case remains one of no global recession, the probability of this declined (see “Risk note: ... the rising threat of global recession sees the probability of the severe down case somewhat higher”, 11th October 2019, website address below), and the probability of the downside elevated (see also scenario table below).

Economic Scenarios: - note updated table

		Q1.19	Q2.19	Q3.19	Q4.19	Q1.20	Q2.20	Q3.20	Q4.20
Extreme	Rand/USD (average)	14.01	14.38	14.89	11.50	10.30	9.50	8.60	7.90
Up case	Repo rate (end rate)	6.75	6.75	6.50	6.00	6.00	5.75	5.75	5.50
1%	Fast, sustainable economic growth of 5-7% y/y. Change in political will with growth creating economic reforms that structurally lift private sector investor confidence and fixed investment. Global growth boom (including commodities), Trump protectionism removed, SA export and domestic growth boom lifts employment and incomes, poverty eventually eliminated. Property rights strengthened, individuals obtain title deeds in EWC without disruption to economy. Fiscal consolidation, credit rating upgrades to A grade.								
Up case		Q1.19	Q2.19	Q3.19	Q4.19	Q1.20	Q2.20	Q3.20	Q4.20
7%	Rand/USD (average)	14.01	14.38	14.89	13.00	11.50	10.00	9.95	9.90
	Repo rate (end rate)	6.75	6.75	6.50	6.25	6.25	6.25	6.00	6.00
	Persistent growth of 3-5%, higher probability of extreme up case. Better governance, growth-creating reforms (structural constraints overcome), greater socio-economic stability, strengthening in property rights, individuals obtain title deeds in EWC without disruption to economy and can leverage and obtain credit. High business confidence and fixed investment growth, substantial FDI inflows, fiscal consolidation. Strong global growth and commodity cycle, Trump protectionism reduce significantly. Stabilisation of credit ratings, with ultimately credit rating upgrades.								
Base		Q1.19	Q2.19	Q3.19	Q4.19	Q1.20	Q2.20	Q3.20	Q4.20
case	Rand/USD (average)	14.01	14.38	14.89	14.85	14.15	14.45	14.65	14.00
40%	Repo rate (end rate)	6.75	6.75	6.50	6.50	6.50	6.50	6.50	6.50
	Annual growth approaches 2.0% y/y by 2021. Rising confidence and investment levels over the five-year forecast period. SA retains one investment grade (Moody's) rating on its local currency long-term sovereign debt in 2019 and 2020 on a negative outlook. Avoids severe global risk-off environment, neutral to global risk-on. Modestly strengthening global demand to trend growth. Limited impact of EWC (expropriation without compensation) to abandoned & unused land, labour tenets land and government land (individuals are new owners and receive title deeds) does not have a negative effect on economy.								
Lite		Q1.19	Q2.19	Q3.19	Q4.19	Q1.20	Q2.20	Q3.20	Q4.20
(domestic)	Rand/USD (average)	14.01	14.38	14.89	15.80	16.50	16.30	15.50	15.15
Down	Repo rate (end rate)	6.75	6.75	6.50	6.75	7.25	7.25	7.25	7.25
case	SA is rated sub-investment grade by Moody's but substantial repair avoids further marked downgrades. Business confidence depressed, marked rand weakness, significant load shedding and weak investment growth until substantial repair effected. V shaped, credit rating downgrade-related recession. However, a neutral to risk-on global financial market environment (the international environment is that of the base case) lessens the impact of the rating downgrade. Potentially combined with a modest expropriation of some private commercial sector property without compensation, with limited impact on economy.								
37%		Q1.19	Q2.19	Q3.19	Q4.19	Q1.20	Q2.20	Q3.20	Q4.20
Severe	Rand/USD (average)	14.01	14.38	14.89	16.10	18.50	19.50	20.00	19.25
down	Repo rate (end rate)	6.75	6.75	6.50	7.00	7.75	8.50	9.25	10.00
case	Continued global sharp economic slowdown resulting in a global recession, on a marked escalation of the US-China trade war – may include a global financial crisis. SA rated sub-investment grade from all three key agencies, with further rating downgrades. A significantly more severe recession occurs in SA than in the lite down case, marked rand weakness, eventually widespread services load shedding and strike action. Expropriation of private sector property (title deeds not transferred to individuals' and so nationalisation) without compensation – severe negative impact on economy.								
15%									

Note: Event risk begins Q4.19. Source: Investec, Iress historical data

Expected case: Exchange Rates forecasts	2019	2019	2019	2019	2020	2020	2020	2020	2021	2021	2021	2021
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
USD/ZAR	14.01	14.38	14.69	14.65	14.15	14.45	14.65	14.00	13.75	14.05	14.55	14.15
GBP/ZAR	18.25	18.48	18.10	18.39	18.16	18.66	19.06	18.30	18.56	19.25	20.29	19.73
EUR/ZAR	15.92	16.16	16.33	16.04	15.71	16.33	16.77	16.10	16.23	16.86	17.90	17.69
ZAR/JPY	7.86	7.65	7.31	7.34	7.53	7.34	7.20	7.46	7.71	7.54	7.29	7.49
ZARCHF	14.06	14.33	14.90	14.69	14.28	14.71	14.91	14.25	14.18	14.64	15.16	14.74
ZARAUD	9.98	10.07	10.07	9.99	9.83	10.19	10.55	10.22	10.45	10.82	11.35	11.04
GBP/USD	1.30	1.29	1.23	1.26	1.28	1.29	1.30	1.31	1.35	1.37	1.39	1.39
EUR/USD	1.14	1.12	1.11	1.10	1.11	1.13	1.15	1.15	1.18	1.20	1.23	1.25
USD/JPY	110	110	107	108	107	106	106	105	106	106	106	106

Note: averages, Source: IRESS, Investec

Lite Down case: Exchange Rates forecasts	2019	2019	2019	2019	2020	2020	2020	2020	2021	2021	2021	2021
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
USD/ZAR	14.01	14.38	14.69	15.80	16.50	16.30	15.50	15.15	15.10	15.05	15.00	15.05
GBP/ZAR	18.25	18.48	18.10	19.83	21.17	21.05	20.17	19.80	20.39	20.62	20.92	20.99
EUR/ZAR	15.92	16.16	16.33	17.30	18.32	18.42	17.75	17.42	17.82	18.06	18.45	18.81
ZAR/JPY	7.86	7.65	7.31	6.81	6.45	6.50	6.81	6.90	7.02	7.04	7.07	7.04
ZARCHF	14.06	14.33	14.90	15.84	16.65	16.59	15.78	15.42	15.57	15.68	15.63	15.68
ZARAUD	9.98	10.07	10.07	10.78	11.47	11.49	11.16	11.06	11.48	11.59	11.70	11.74
GBP/USD	1.30	1.29	1.23	1.26	1.28	1.29	1.30	1.31	1.35	1.37	1.39	1.39
EUR/USD	1.14	1.12	1.11	1.10	1.11	1.13	1.15	1.15	1.18	1.20	1.23	1.25
USD/JPY	110	110	107	108	107	106	106	105	106	106	106	106

Note: averages, Source: IRESS, Investec

Severe Down case: Exchange Rates forecasts	2019	2019	2019	2019	2020	2020	2020	2020	2021	2021	2021	2021
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
USD/ZAR	14.01	14.38	14.69	16.10	18.50	19.50	20.00	19.25	18.70	18.00	17.50	16.75
GBP/ZAR	18.25	18.48	18.10	20.21	23.74	25.18	26.02	25.16	25.25	24.66	24.40	23.36
EUR/ZAR	15.92	16.16	16.33	17.63	20.54	22.04	22.90	22.14	22.07	21.60	21.53	20.94
ZAR/JPY	7.86	7.65	7.31	6.68	5.76	5.44	5.28	5.43	5.67	5.89	6.06	6.33
ZARCHF	14.06	14.33	14.90	16.14	18.67	19.85	20.36	19.59	19.28	18.75	18.23	17.45
ZARAUD	9.98	10.07	10.07	10.98	12.86	13.75	14.40	14.05	14.21	13.86	13.65	13.07
GBP/USD	1.30	1.29	1.23	1.26	1.28	1.29	1.30	1.31	1.35	1.37	1.39	1.39
EUR/USD	1.14	1.12	1.11	1.10	1.11	1.13	1.15	1.15	1.18	1.20	1.23	1.25
USD/JPY	110	110	107	108	107	106	106	105	106	106	106	106

Note: averages, Source: IRESS, Investec

Up case: Exchange Rates forecasts	2019	2019	2019	2019	2020	2020	2020	2020	2021	2021	2021	2021
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
USD/ZAR	14.01	14.38	14.69	13.00	11.50	10.00	9.95	9.90	9.70	9.65	9.45	9.30
GBP/ZAR	18.25	18.48	18.10	16.32	14.76	12.91	12.95	12.94	13.10	13.22	13.18	12.97
EUR/ZAR	15.92	16.16	16.33	14.24	12.77	11.30	11.39	11.39	11.45	11.58	11.62	11.63
ZAR/JPY	7.86	7.65	7.31	8.27	9.26	10.60	10.60	10.56	10.93	10.98	11.22	11.40
ZARCHF	14.06	14.33	14.90	13.03	11.60	10.18	10.13	10.08	10.00	10.05	9.84	9.69
ZARAUD	9.98	10.07	10.07	8.87	7.99	7.05	7.16	7.23	7.37	7.43	7.37	7.25
GBP/USD	1.30	1.29	1.23	1.26	1.28	1.29	1.30	1.31	1.35	1.37	1.39	1.39
EUR/USD	1.14	1.12	1.11	1.10	1.11	1.13	1.15	1.15	1.18	1.20	1.23	1.25
USD/JPY	110	110	107	108	107	106	106	105	106	106	106	106

Note: averages, Source: IRESS, Investec

Extreme Up case: Exchange Rates forecasts	2019	2019	2019	2019	2020	2020	2020	2020	2021	2021	2021	2021
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
USD/ZAR	14.01	14.38	14.69	11.50	10.30	9.50	8.60	7.90	7.60	7.40	7.10	6.95
GBP/ZAR	18.25	18.48	18.10	14.44	13.22	12.27	11.19	10.32	10.26	10.14	9.90	9.69
EUR/ZAR	15.92	16.16	16.33	12.59	11.43	10.74	9.85	9.09	8.97	8.88	8.73	8.69
ZAR/JPY	7.86	7.65	7.31	9.35	10.34	11.16	12.27	13.23	13.95	14.32	14.93	15.25
ZARCHF	14.06	14.33	14.90	11.53	10.39	9.67	8.75	8.04	7.84	7.71	7.40	7.24
ZARAUD	9.98	10.07	10.07	7.85	7.16	6.70	6.19	5.77	5.78	5.70	5.54	5.42
GBP/USD	1.30	1.29	1.23	1.26	1.28	1.29	1.30	1.31	1.35	1.37	1.39	1.39
EUR/USD	1.14	1.12	1.11	1.10	1.11	1.13	1.15	1.15	1.18	1.20	1.23	1.25
USD/JPY	110	110	107	108	107	106	106	105	106	106	106	106

Note: averages, Source: IRESS, Investec