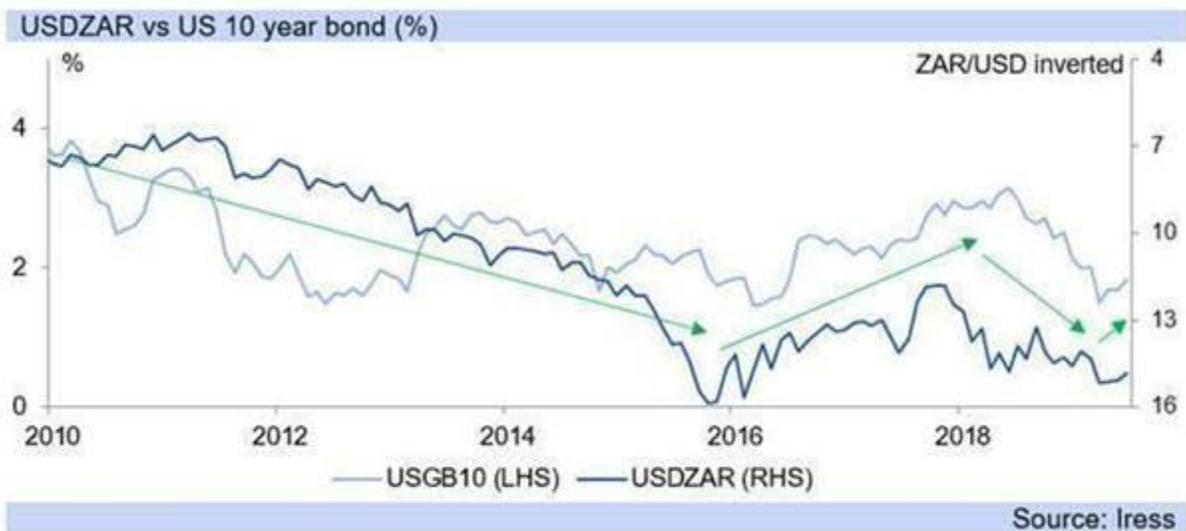


## Rand Note

Monday 18 November 2019

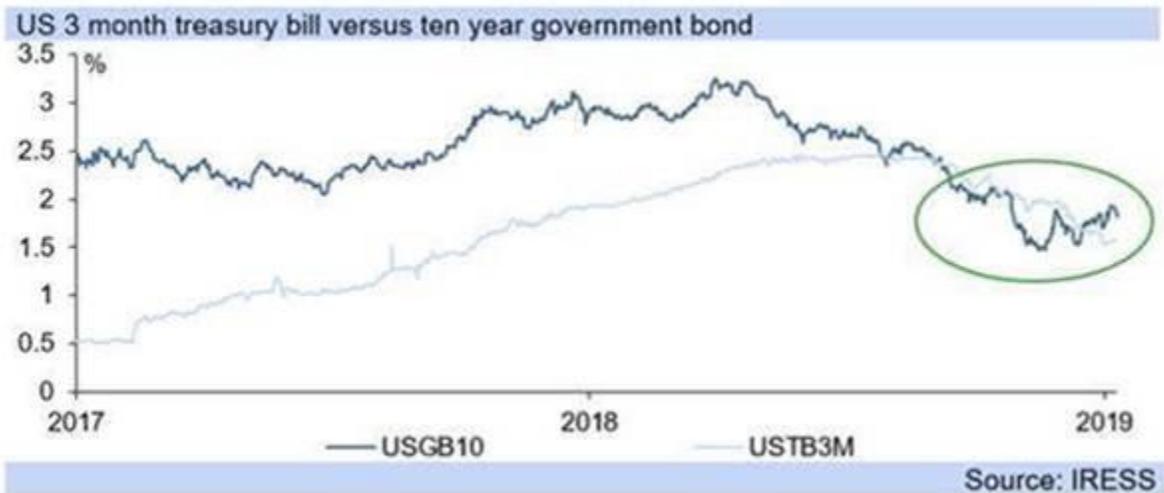
Rand nears our Q4.19 forecast (albeit on a level not on an average basis), gaining from improved market sentiment, with the lift in the US ten year treasury yield reflecting the lift in sentiment



- The rand's strength today to R14.69/USD, R16.25/EUR and R18.99/GBP is nearing our Q4.19 forecasts on a level basis, although more quickly against the US dollar than against the euro and UK pound. The USD has seen some weakness recently as risk aversion subsided, with perceived gains in the US trade deal since October aiding sentiment.
- The US-Sino trade deal continues to be stop start in nature, with the US delaying the signing of the partial deal with China as it (the US) seeks more concessions from China ahead of US 2020 elections. Nevertheless,

a deal is increasingly expected to be signed, which is seen as reducing the chance of global recession, and is cheering markets.

- Specifically, further progress is expected to be made (in the trade negotiations) ahead of the US elections next year, with a completed deal in the US's favour still expected before the elections (to bolster the election outcome in the favour of President Trump), and a winding down of the degree of protectionism to provide a boost to the economic outlook.
- The lowering in risk aversion levels on progress in the trade negotiations has reduced the pressure for safe haven flows, which in particular were focussed into US treasuries, causing their yields subsequently to rise as prices moderated, and aiding in reversing the 'yield curve' inversion (see "Bond Note", 11<sup>th</sup> July 2019, website address below).
- Patchy data out of the global economy continues, but the improvement in some countries' economic metrics (particularly Germany's recent GDP print) has also contributed to improving market sentiment, and so to the lowering of risk aversion, where previously US ten year treasury yields were lower on higher prices supported by demand from safe haven inflows.
- The continued relatively good performance of US GDP, and the US jobs market, has also assisted market sentiment. The performance of the US stock market has also aided inflows, besides those into US treasuries seeking haven investments, which strengthened the US dollar.
- Part of the improvement in US growth has seen the lift in corporate earnings over the past few years, positive wealth effects on the rise in share prices and strengthening in business confidence over the period, although a material reduction in red tape also supported the US economic expansion, along with fairly widespread tax cuts.



- In particular, significant tax cuts for lower and middle income US households, along with increased child and family benefits have added to material GDP strength in the past few years, also supported by with tax reform also seeing lower utility costs as tax savings from these entities are passed through to consumers.
- "The Tax Cuts and Jobs Act includes \$5.5 trillion in gross tax cuts, it also includes \$4 trillion in reforms, including the elimination of special-interest loopholes and protection of important tax benefits ... (and) created the federal Opportunity Zones program" – US Department of the Treasury.

- “Utility (c)ompanies ... (p)assing (t)heir (s)avings (a)long (t)o (c)ustomers (v)ia (l)ower (e)lectric (b)ills, (l)ower (g)as (b)ills (a)nd (l)ower (w)ater (b)ills (f)or Americans. Over 100 utility companies have pledged to pass billions in tax savings to over 22 million of their customers” – US Department of the Treasury.
- Tax cuts to corporates have supported hiring and job creation, higher incomes for workers, improved job opportunities, particularly for blue collar workers with low unemployment. Special development or “opportunity zones” assisted with job creation and economic development in low income areas.
- “Opportunity Zones are located in economically distressed communities ... of every U.S. state and territory. These communities demonstrate average poverty rates of 32 % ... (vs.) the U.S. average rate of 17 % - unemployment rates 1.6 times higher than the average U.S. census tract, ... family incomes averaging 37% below the state median.”
- The rand retreated from the key resistance level of R14.70/USD this morning, but could see further gains, particularly on progress on US-Sino trade negotiations. Any signs of US economic weakness that creep in (see “Rand note”, 14<sup>th</sup> November 2019) are negative for Trump’s election prospects and would likely speed the completion of the trade deal.
- Our expected, or central case remains one of no global recession. The probability of the expected case will rise as the likelihood of a global recession (low probability currently of 15%) falls, which in turn would be driven by the signing of the US Sino first phase trade deal, and further notable progress thereafter. Forecast below are all averages.

**Economic Scenarios: - note updated table**

		Q1.19	Q2.19	Q3.19	Q4.19	Q1.20	Q2.20	Q3.20	Q4.20
<b>Extreme</b>	Rand/USD (average)	14.01	14.38	14.69	11.50	10.30	9.50	8.60	7.90
<b>Up case</b>	Repo rate (end rate)	6.75	6.75	6.50	6.00	6.00	5.75	5.75	5.50
<b>1%</b>	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.								
<b>Up case</b>	Rand/USD (average)	14.01	14.38	14.69	13.00	11.50	10.00	9.95	9.90
<b>7%</b>	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.								
<b>Base case</b>	Rand/USD (average)	14.01	14.38	14.69	14.65	14.15	14.45	14.65	14.00
<b>40%</b>	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.								
<b>Lite</b>	Rand/USD (average)	14.01	14.38	14.69	15.80	16.50	16.30	15.50	15.15
<b>(domestic)</b>	Repo rate (end rate)	6.75	6.75	6.50	6.75	7.25	7.25	7.25	7.25
<b>Down case</b>	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.								
<b>37%</b>									
<b>Severe down case</b>	Rand/USD (average)	14.01	14.38	14.69	16.10	18.50	19.50	20.00	19.25
<b>15%</b>	Repo rate (end rate)	6.75	6.75	6.50	7.00	7.75	8.50	9.25	10.00
	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.								

**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