Rand note: rand remains around R16.50/USD, with little upside reflected yet by the reforms outlined in the President's speech as markets fear higher debt projections in the MTBPS and rating downgrades

Expected Case: Exchange Rate forecasts

	2020				2021				2022			
	Q1.20	Q2.20	Q3.20	Q4.20	Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22
USD/ZAR	15.38	17.95	16.91	16.50	15.75	15.50	15.50	15.10	15.00	15.20	15.50	15.20
GBP/ZAR	19.64	22.28	21.85	21.52	21.11	20.93	21.24	20.99	21.22	20.98	21.24	20.82
EUR/ZAR	16.95	19.77	19.77	19.31	18.43	18.37	18.76	18.65	18.75	18.54	18.29	17.78
ZAR/JPY	7.12	5.99	6.28	6.39	6.79	6.94	6.84	6.92	6.93	6.91	6.77	6.91
CHFZAR	15.89	18.63	18.38	17.96	16.98	16.77	16.97	16.73	16.61	15.20	15.50	15.20
AUDZAR	10.09	11.79	12.09	11.39	10.79	10.70	10.77	10.57	10.73	10.64	11.01	10.79
GBP/USD	1.28	1.24	1.29	1.30	1.34	1.35	1.37	1.39	1.41	1.38	1.37	1.37
EUR/USD	1.10	1.10	1.17	1.17	1.17	1.19	1.21	1.24	1.25	1.22	1.18	1.17
USD/JPY	109	108	106	106	107	108	106	105	104	105	105	105

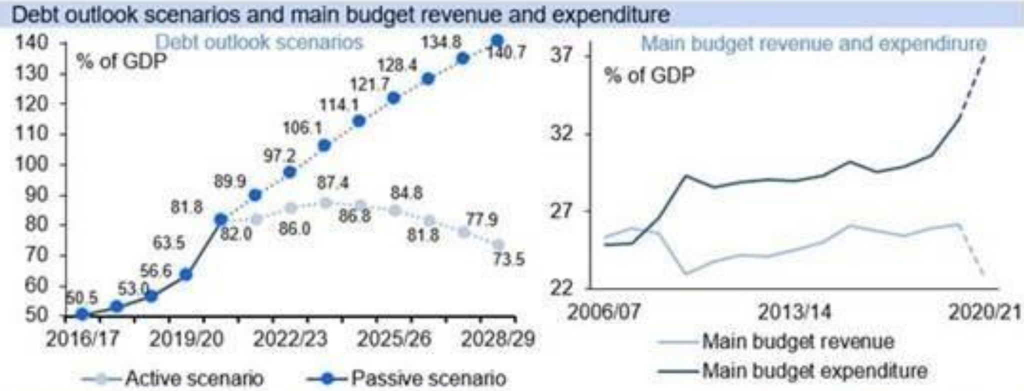
Note: averages, Source: Investec, Iress

Lite Down Case: Exchange Rate forecasts

	2020				2021				2022			
	Q1.20	Q2.20	Q3.20	Q4.20	Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22
USD/ZAR	15.38	17.95	16.91	18.50	19.50	20.00	18.50	17.00	16.50	16.00	15.80	16.00
GBP/ZAR	19.64	22.28	21.85	24.13	26.13	27.00	25.35	23.63	23.34	22.08	21.65	21.92
EUR/ZAR	16.95	19.77	19.77	21.65	22.82	23.70	22.39	21.00	20.63	19.52	18.64	18.72
ZAR/JPY	7.12	5.99	6.28	5.70	5.49	5.38	5.73	6.15	6.30	6.56	6.65	6.56
CHFZAR	15.89	18.63	18.38	20.13	21.03	21.64	20.26	18.83	18.28	16.00	15.80	16.00
AUDZAR	10.09	11.79	12.09	12.77	13.36	13.80	12.86	11.90	11.80	11.20	11.22	11.36
GBP/USD	1.28	1.24	1.29	1.30	1.34	1.35	1.37	1.39	1.41	1.38	1.37	1.37
EUR/USD	1.10	1.10	1.17	1.17	1.17	1.19	1.21	1.24	1.25	1.22	1.18	1.17
USD/JPY	109	108	106	106	107	108	106	105	104	105	105	105

Note: averages, Source: Investec, Iress

Debt outlook scenarios and main budget revenue and expenditure



Source: National Treasury

- The rand continues to average close to R16.50/USD this quarter so far (at an average of R16.57/USD currently), but, with the quarter only having started, there are a number of upcoming events which could drive volatility both globally and locally.
- The rand did not see much movement on last week's Economic Reconstruction and Recovery Plan (ERRP), with markets preferring to mark time and adopt a wait and see

approach, having been disappointed on the delivery of SA's numerous plans and policies in the past decade.

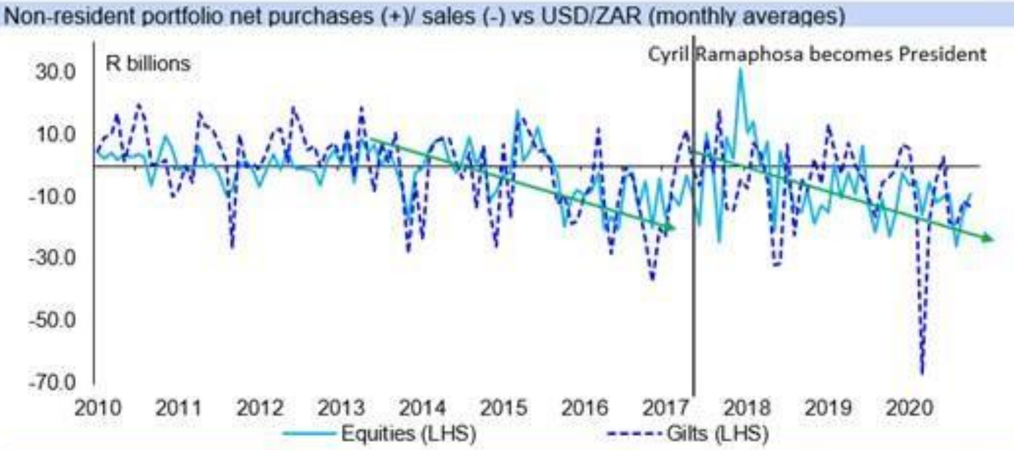
- While the Economic Reconstruction and Recovery Plan will likely be viewed positively by the credit rating agencies, they too have been repeatedly disappointed by insufficient delivery, and plans on their own are insufficient to change the perceived creditworthiness of SA.
- Moody's, Fitch and S&P primarily assess SA on its ability to repay its debt, and both rising borrowings, and rising projections of borrowings, are seen to weaken this ability, with SA already issuing over R2bn a day in government debt.
- While faster GDP growth can lift government revenues and so aid in limiting the amount that is borrowed, as can materially increased efficiencies at SARS, the former is unlikely this year and the substantial number of vacancies at SARS does not indicate the latter will occur soon.
- The ERRP has already seen a significant amount of work done, and a number of factors partially achieved or in process which increases its likelihood of success, but not yet an ability to prevent downgrades. Near term debt stabilisation below 90% of GDP is still needed.
- In contrast, lifting the planned stabilisation point for SA's debt trajectory even higher (with the MTBPS now expected on 28th October at 2pm) to potentially 100% of GDP, instead of 87.4%, will add to substantial pressure for further marked downgrades of SA's credit ratings.
- The rating agencies would not view such a planned deterioration in SA's debt metrics as being outweighed by the ERRP's plans to stimulate economic growth, repair SA's fundamentals and reduce unemployment. Instead plans for fiscal consolidation, not slippage, are key.
- The rand would likely depreciate markedly on shifting to a debt peak of 100% of GDP. A 100% of GDP, or higher, is not deemed at all sustainable for an emerging market, and SA will be viewed no differently. The rise in borrowing costs also reduces debt sustainability.

Rating tier definitions

Moody's Long-term	Moody's Short-term	S&P Long-term	S&P Short-term	Fitch Long-term	Fitch Short-term	Equivalent to SVO Designations NAIC	Rating description	
Aaa		AAA		AAA			Prime	
Aa1		AA+	A-1	AA+	F1+			
Aa2		AA		AA			High grade	
	P-1					1		
A1		A+		A+			Upper medium grade	Investment-grade
A2		A	A-1	A	F1			
A3		A-		A-				
	P-2		A-2		F2			
Baa1		BBB+		BBB+			Lower medium grade	
Baa2	P-3	BBB	A-3	BBB	F3	2		
Baa3		BBB-		BBB-				
Ba1		BB+		BB+			Non-investment grade speculative	
Ba2		BB		BB		3		
Ba3		BB-		BB-				
B1		B+	B	B+	B		Highly speculative	
B2		B		B		4		
B3		B-		B-				
Caa1	Not prime	CCC+					Substantial risks	Non-investment grade AKA high-yield bonds AKA junk bonds
Caa2		CCC				5	Extremely speculative	
Caa3		CCC-	C	CCC	C		Default imminent with little prospect for recover	
Ca		CC						
		C						
C				DDD		6		
/		D	/	DD	/		In default	
				D				

Source: Wikipedia

Non-resident portfolio net purchases (+)/ sales (-) vs USD/ZAR (monthly averages)



Source: Iress, Investec

- South Africa has been more consistent in raising and achieving its higher debt projections, and then exceeding these expectations, than it has been in achieving planned higher growth, revenue collection or substantially reducing unemployment in the past decade.
- SA has already fallen into an unsustainable debt position, its borrowing costs are elevated, and its yield curve is steep, with the short end of the yield curve anchored by low money market rates (the repo rate is at historic lows) and the mid to long-end has risen substantially.
- This steepening in the yield curve reflects higher borrowing costs of longer dated paper and perceived creditworthiness of SA's current borrowings. The deteriorated fiscal metrics already worry domestic and foreign investors on the lack of fiscal consolidation to date.
- Instead of raising the borrowing trajectory, there is a need for a lower debt trajectory. A zero based budget cancelling and reducing previously planned expenditure and reallocating from scratch is expected in the MTBPS with expenditure cuts at least agreed by the ERRP.
- The crux is to lower expenditure to reduce pressure on the need to borrow, and to have a lower projected borrowing trajectory, not a higher one. Advice for a higher debt stabilisation than 87.4% of GDP disregards the lower investor appetite in five year plus debt issuance.
- Lower investor appetite is reflected by investors unwilling to purchase SA's debt at lower borrowing costs. Yields rise to compensate for risk, lifting government expenditure by raising interest payments, with a vicious cycle as still more is borrowed to meet costs.
- The vicious cycle, or debt spiral, is a key concerns of investors who worry that SA is increasingly quickly losing its creditworthiness, a factor which is being reflected by the increasing speed with which SA is being downgraded towards the C grades.
- We expected a downgrade post MTBPS from Moody's Ba1 (BB+ equivalent) to Ba2 (BB equivalent) on 20th November, with Fitch and S&P also likely to downgrade, and the risk is by more than one notch if SA raises its debt peak to 100% of GDP.
- The rand is also at risk of negative market sentiment from external factors, as US fiscal stimulus approval continues to drag, while Brexit and the US elections pose further risk for volatility in the period ahead.

Severe Down Case: Exchange Rate forecasts

	2020				2021				2022			
	Q1.20	Q2.20	Q3.20	Q4.20	Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22
USD/ZAR	15.38	17.95	16.91	19.50	21.00	22.00	23.00	24.00	22.00	20.00	22.00	20.00
GBP/ZAR	19.64	22.28	21.85	25.43	28.14	29.70	31.51	33.36	31.13	27.60	30.14	27.40
EUR/ZAR	16.95	19.77	19.77	22.82	24.57	26.07	27.83	29.64	27.50	24.40	25.96	23.40
ZAR/JPY	7.12	5.99	6.28	5.41	5.10	4.89	4.61	4.35	4.73	5.25	4.77	5.25
CHFZAR	15.89	18.63	18.38	21.22	22.65	23.81	25.19	26.58	24.37	20.00	22.00	20.00
AUDZAR	10.09	11.79	12.09	13.46	14.39	15.18	15.99	16.80	15.73	14.00	15.62	14.20
GBP/USD	1.28	1.24	1.29	1.30	1.34	1.35	1.37	1.39	1.41	1.38	1.37	1.37
EUR/USD	1.10	1.10	1.17	1.17	1.17	1.19	1.21	1.24	1.25	1.22	1.18	1.17
USD/JPY	109	108	106	106	107	108	106	105	104	105	105	105

Note: averages, Source: Investec, Iress

Up Case: Exchange Rate forecasts												
	2020				2021				2022			
	Q1.20	Q2.20	Q3.20	Q4.20	Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22
USD/ZAR	15.38	17.95	16.91	16.00	15.00	14.00	13.50	13.00	12.50	12.40	12.50	12.60
GBP/ZAR	19.64	22.28	21.85	20.86	20.10	18.90	18.50	18.07	17.69	17.11	17.13	17.26
EUR/ZAR	16.95	19.77	19.77	18.72	17.55	16.59	16.34	16.06	15.63	15.13	14.75	14.74
ZAR/JPY	7.12	5.99	6.28	6.59	7.13	7.68	7.85	8.04	8.32	8.47	8.40	8.33
CHFZAR	15.89	18.63	18.38	17.41	16.18	15.15	14.78	14.40	13.85	12.40	12.50	12.60
AUDZAR	10.09	11.79	12.09	11.04	10.28	9.66	9.38	9.10	8.94	8.68	8.88	8.95
GBP/USD	1.28	1.24	1.29	1.30	1.34	1.35	1.37	1.39	1.41	1.38	1.37	1.37
EUR/USD	1.10	1.10	1.17	1.17	1.17	1.19	1.21	1.24	1.25	1.22	1.18	1.17
USD/JPY	109	108	106	106	107	108	106	105	104	105	105	105

Note averages, Source: Investec, Iress

Extreme Up Case: Exchange Rate forecasts												
	2020				2021				2022			
	Q1.20	Q2.20	Q3.20	Q4.20	Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22
USD/ZAR	15.38	17.95	16.91	15.00	14.00	13.50	13.00	12.50	12.00	11.50	11.00	10.90
GBP/ZAR	19.64	22.28	21.85	19.56	18.76	18.23	17.81	17.38	16.98	15.87	15.07	14.93
EUR/ZAR	16.95	19.77	19.77	17.55	16.38	16.00	15.73	15.44	15.00	14.03	12.98	12.75
ZAR/JPY	7.12	5.99	6.28	7.03	7.64	7.96	8.15	8.36	8.67	9.13	9.55	9.63
CHFZAR	15.89	18.63	18.38	16.33	15.10	14.61	14.24	13.85	13.29	11.50	11.00	10.90
AUDZAR	10.09	11.79	12.09	10.35	9.59	9.32	9.04	8.75	8.58	8.05	7.81	7.74
GBP/USD	1.28	1.24	1.29	1.30	1.34	1.35	1.37	1.39	1.41	1.38	1.37	1.37
EUR/USD	1.10	1.10	1.17	1.17	1.17	1.19	1.21	1.24	1.25	1.22	1.18	1.17
USD/JPY	109	108	106	106	107	108	106	105	104	105	105	105

Note: averages, Source: Investec, Iress

Economic Scenarios: note updated forecasts – the slight reduction in the severe down case probability by 1% (and lift in the up case probability by 1%) reflects the improved outlook for global economic recovery, and NOT any reduction in the likelihood of further credit rating downgrades for SA

		Q1.20	Q2.20	Q3.20	Q4.20	Q1.21	Q2.21	Q3.21	Q4.21
Extreme Up case 1%	USD/Rand (average)	15.38	17.95	16.91	15.00	14.00	13.50	13.00	12.50
	Repo rate (end rate)	5.25	3.75	3.50	3.00	3.00	3.00	3.00	3.00

Impact of Covid-19 pandemic very rapidly resolved - economic growth of 3–5%, then 5-7% for SA. Good governance, growth-creating reforms (structural constraints overcome), strengthening of property rights - individuals obtain title deeds in EWC – no nationalisation. High business confidence and fixed investment growth, substantial FDI inflows, strong fiscal consolidation (government debt falls back to low ratios of 2000s). Strong global growth, commodity boom. Stabilisation of credit ratings, then credit rating upgrades.

		Q1.20	Q2.20	Q3.20	Q4.20	Q1.21	Q2.21	Q3.21	Q4.21
Up case 3%	USD/Rand (average)	15.38	17.95	16.91	16.00	15.00	14.00	13.50	13.00
	Repo rate (end rate)	5.25	3.75	3.50	3.25	3.25	3.50	3.50	3.50

Quick rebound from Covid-19 pandemic, rising confidence and investment levels - structural problems worked down. No further credit rating downgrades, rating outlooks move to stable and eventually positive, strong fiscal consolidation (government debt projections fall substantially). Global risk-on, global demand quickly returns to trend growth. Limited impact of expropriation without compensation) to abandoned, unused, labour tenants" and government land (individuals are new owners and receive title deeds) does not have a negative effect on economy - no nationalisation.

		Q1.20	Q2.20	Q3.20	Q4.20	Q1.21	Q2.21	Q3.21	Q4.21
Base case 47%	USD/Rand (average)	15.38	17.95	16.91	16.50	15.75	15.50	15.50	15.10
	Repo rate (end rate)	5.25	3.75	3.50	3.50	3.75	4.00	4.25	4.25

Recovery from the sharp global economic slowdown – sufficient global and domestic monetary and other policy supports to growth and financial markets occur and risk sentiment stabilises then improves. South Africa exits recession in Q3.20. Expropriation of private sector property is limited and does not have a negative impact on the economy or on market sentiment. SA remains in the BB category rating bracket for Moody's – fiscal consolidation (debt to GDP stabilisation) occurs.

		Q1.20	Q2.20	Q3.20	Q4.20	Q1.21	Q2.21	Q3.21	Q4.21
Lite (domestic) Down case 46%	USD/Rand (average)	15.38	17.95	16.91	18.5	19.50	20.0	18.5	17.0
	Repo rate (end rate)	5.25	3.75	3.50	3.75	4.00	4.00	4.25	4.25

The international environment (including risk sentiment) is that of the base case. South Africa fails to see its debt projections stabilise and falls into single B credit ratings from all three agencies for local and foreign currency. More severe recession in SA than in the expected case. Expropriation of some private commercial sector property without compensation, with some small negative impact on the economy. Business confidence depressed, rand weakness, significant load shedding and weak investment growth. Substantial fiscal consolidation ultimately occurs, preventing ratings falling into CCC grade.

		Q1.20	Q2.20	Q3.20	Q4.20	Q1.21	Q2.21	Q3.21	Q4.21
Severe down case 3%	USD/Rand (average)	15.38	17.95	16.91	19.50	21.00	22.00	23.00	24.00
	Repo rate (end rate)	5.25	3.75	3.50	4.00	4.25	4.25	4.75	5.25

Lengthy global recession, global financial crisis – insufficient monetary and other policy supports to growth domestically and internationally. Depression in SA, unprecedented rand weakness. Nationalisation of private sector property (title deeds not transferred to individuals). SA rated single B from all three key agencies, with further rating downgrades eventually occurring into CCC grade and lower as government finances deteriorate (debt projections elevate even further - fail to ever stabilise. Government borrows from increasingly wider sources as it sinks deeper into a debt trap), eventually include widespread services load shedding, strike action and civil unrest.

Note: Event risk begins Q4.20. Source: Investec