

# SA Economics



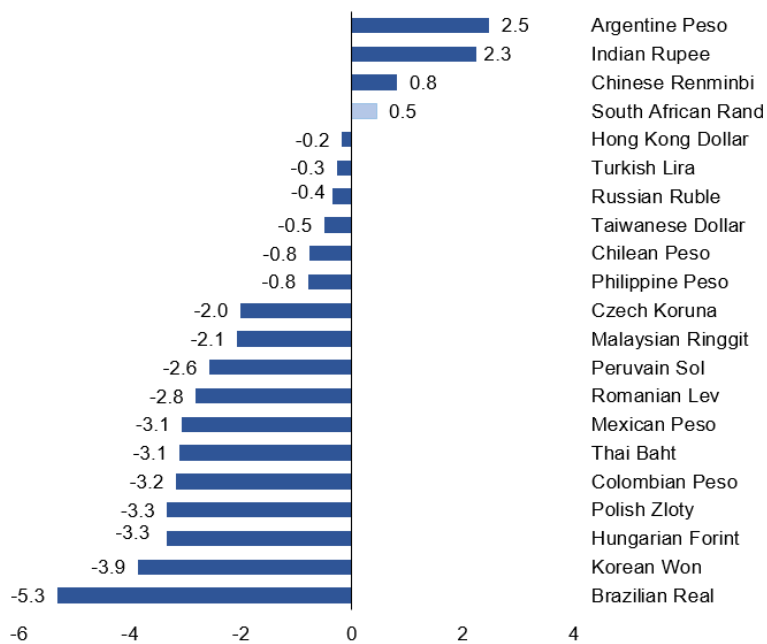
Tuesday 23 March 2021

Rand note: the rand hangs onto some of its gains after its very rapid strength following last week's FOMC meeting, although the prospect of a rate hike and SA's slow vaccine rollout are denting market confidence in SA's economic recovery

Expected Case: Exchange Rate forecasts												
	2021				2022				2023			
	Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.23	Q4.23
USD/ZAR	15.00	15.40	15.50	15.20	15.40	15.50	15.20	15.30	15.40	15.80	16.20	15.70
GBP/ZAR	20.55	21.10	21.24	21.13	21.10	21.24	21.13	21.72	21.87	22.28	22.68	21.98
EUR/ZAR	18.18	18.48	18.76	18.77	18.48	18.76	18.77	19.20	19.25	19.75	20.25	19.63
ZAR/JPY	6.94	6.82	6.77	6.88	6.82	6.77	6.88	6.80	6.88	6.71	6.54	6.75
CHF/ZAR	16.75	16.88	16.97	16.84	16.88	16.97	16.84	17.14	15.40	15.80	16.20	15.70
AUD/ZAR	11.56	11.86	12.01	12.01	11.86	12.01	12.01	12.24	11.55	11.85	12.15	11.78
GBP/USD	1.37	1.37	1.37	1.39	1.42	1.43	1.45	1.43	1.42	1.41	1.40	1.40
EUR/USD	1.21	1.20	1.21	1.24	1.26	1.26	1.27	1.26	1.25	1.25	1.25	1.25
USD/JPY	104	105	105	105	104	104	105	105	106	106	106	106

Note: averages, Source: Investec, Iress

Emerging Markets Carry Return – values as at the 23<sup>rd</sup> March 2021

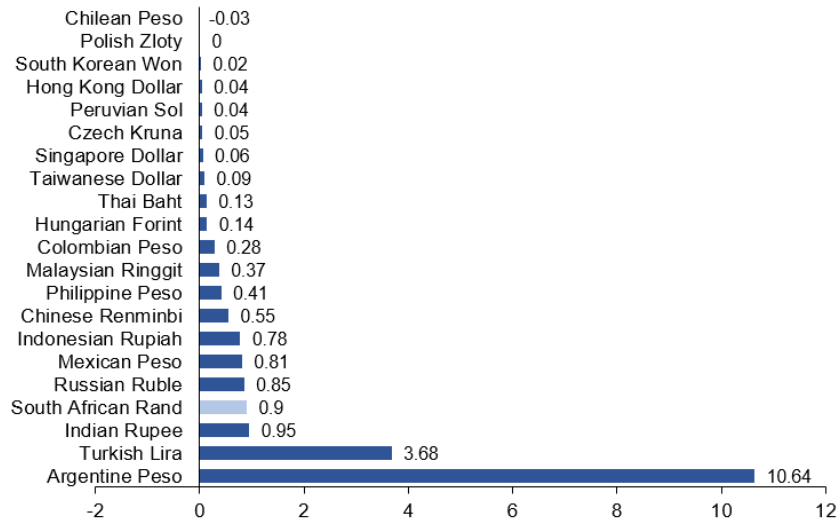


Source: Bloomberg

# SA Economics

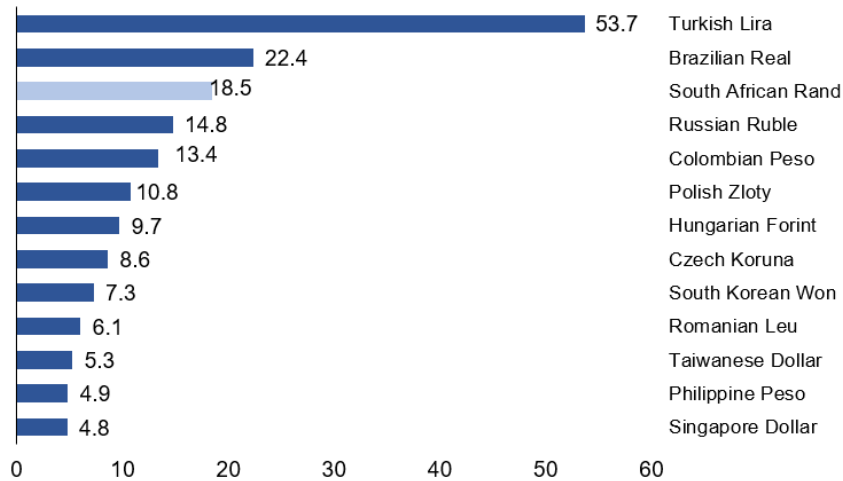


Emerging Markets Interest Return – values as at 23<sup>rd</sup> March 2021



Source: Bloomberg

Emerging Markets Implied Volatilities – values as at 23<sup>rd</sup> March 2021

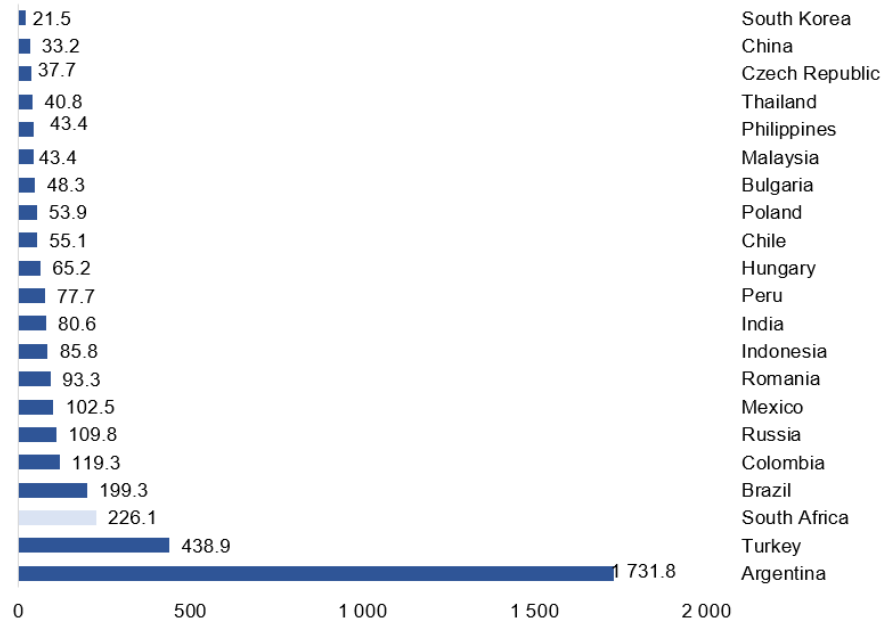


Source: Bloomberg

# SA Economics



Emerging Markets CDS Spreads – values as at 23 March 2021



Source: Bloomberg

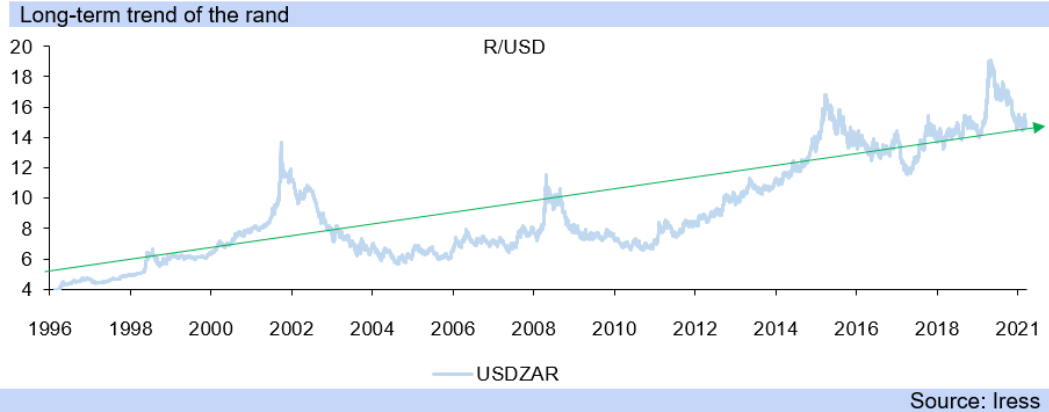
- With South Africa's MPC due to meet this week, worries are growing that it could look to begin hiking interest rates, even though the economy is still exceptionally weak. However, we don't believe the SARB will necessarily lift the repo rate already this month.
- Higher oil prices have added to upwards price pressure this year so far, with another hike in the petrol price due in April of likely over R1/litre. As a consequence, CPI inflation is likely to reach 5.0% y/y by May and could remain around 5.0% y/y for the rest of this year.
- Real interest rates would consequently become negative absent hikes in the repo rate, while a number of other emerging market (EM) economies have begun to increase their rates - SA risks seeing less competitive interest rates for interest rate investors if it does not hike too.
- This could cause some weakness in the rand if the SARB does not hike as other EMs do, and indeed marked weakness in the domestic currency would in turn add to higher inflation pressures as rand weakness has a direct and fairly immediate impact on the petrol price.
- However, the economy is exceptionally weak, and has not recovered either the jobs or the production that was lost in the harsh lockdowns of last year, with only small gains having been made subsequently.
- Furthermore, South Africa's vaccine rollout remains very slow, with only 182 983 vaccines administered to date in a population of 60 000 000 since February. If the vaccine rollout proceeds at this pace (not expected) the economic growth outlook will be at risk.

# SA Economics

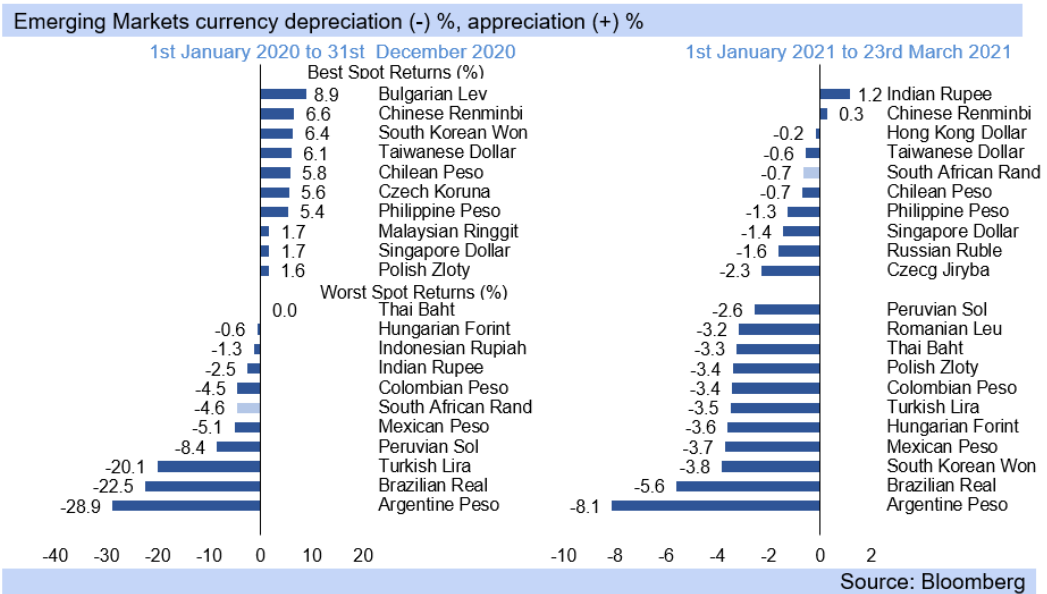
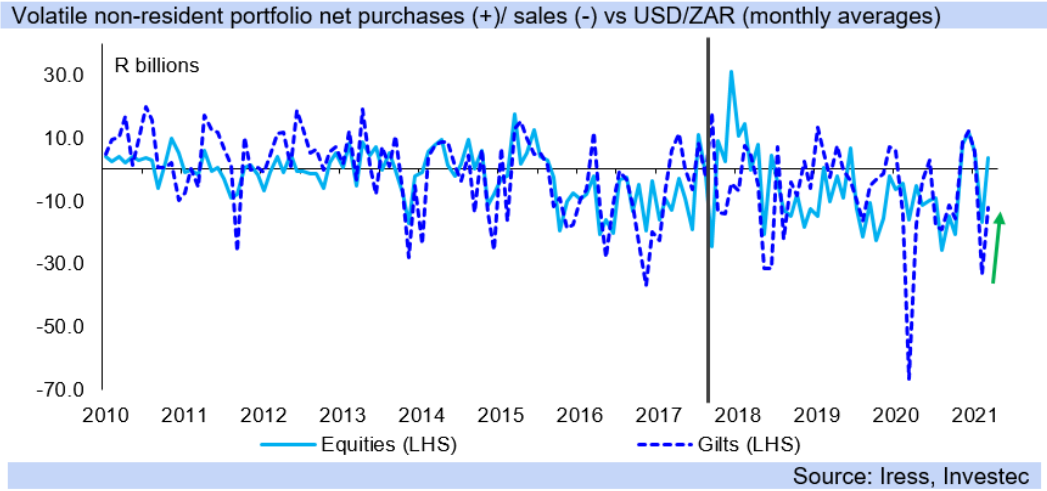


- That is, the probability of the expected case, currently 48% could be lowered towards 45%, and the probability of the up case moved to 1%, if SA does not move out of phase one, and into phase two of its vaccine rollout strategy in early Q2.21.
- A further concern is the very weak nature of the electricity grid, with load shedding having a negative impact on economic activity, and Q1.21's GDP outcome will likely be negatively impacted by this, with risks into Q2.21.
- The rand is still benefitting from the lift in risk-on market sentiment after last week's FOMC meeting which fuelled optimism of US, and so global economic recovery. However, May traditionally is the start of a risk-off period in financial markets and so also for the rand.

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# SA Economics

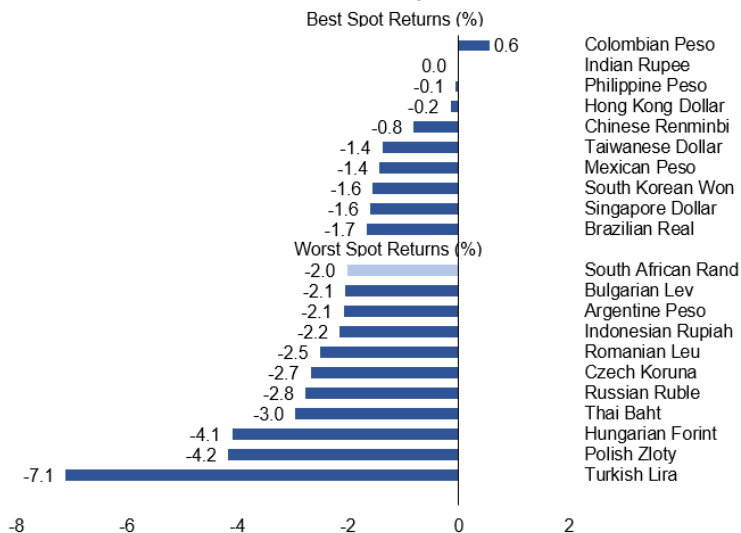


# SA Economics



## Emerging Markets currency depreciation (-) %, appreciation (+) %

24th February to 23rd March 2021



Source: Bloomberg

- The domestic currency will remain erratic, swinging rapidly both stronger and weaker, as global market events continue to impact its direction. However, higher interest rates in EM economies while the SARB sits pat would underlay weakness in the rand.
- While there have been recent announcements of planned improvements in South Africa's electricity regulations in order to allow substantial private sector participation in supplying to the grid, these will not have an immediate impact on supply and so H1.21 economic growth.
- The lengthy nature of these projects mean they will not solve the electricity demand supply gap in SA by H2.21 either. Consequently, the economic outlook for 2021 is at risk, and despite the recent base effects from Q4.20 GDP, we are keeping our forecast around 3.0% y/y.
- Yesterday the President wrote a number of "companies ...successfully bid to supply 2,000 megawatts of emergency power to address the gap in capacity". "The power will be produced from a range of sources including solar, wind, liquified natural gas and battery storage."
- "These projects will involve an investment of around R45 billion by the private sector. Around half of all the materials used in the construction will be locally sourced. The projects should be providing power to the nation by August next year."
- He also referred to the fact that "last week, government released a request for proposals for the procurement of a further 2,600 megawatts of renewable energy ... the fifth 'bid window' in the country's ... programme to buy renewable energy from independent power producers."

# SA Economics



- He added that “(o)ver the course of the next year, government plans to release four more requests for proposals for new power generation projects, in renewable energy, gas, coal and battery storage respectively ... expected to provide over 7,000 megawatts of electricity.”
- These plans are extremely positive, and stem from the 2019IRP, but they should have already begun being implemented in 2019, and over 2020. The extremely slow pace to bring in these reforms has needlessly weakened SA’s economic growth instead from this perspective.
- SA entered a structural recession in H2.19 which continued into Q1.20. The strangulation of the economy in Q2.20 by the lockdown regulations saw economic growth weak enough to be satisfied by the low electricity supply, but now low supply is hamstringing economic recovery.

# SA Economics



## Economic Scenarios: change in Q1.21 rand values to reflect the small remaining period of Q1.21

		Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22
<b>Extreme</b> Up case 1%	USD/Rand (average)	14.65	14.00	13.50	13.25	13.00	12.75	12.75	12.50
	Repo rate (end rate)	3.00	3.00	3.00	3.00	3.00	3.25	3.25	3.25
	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). <b>Strong global growth, commodity boom. Stabilisation of credit ratings, then credit rating upgrades.</b>								
<b>Up case</b> 2%	USD/Rand (average)	14.71	14.50	14.50	14.00	13.50	14.00	14.50	13.50
	Repo rate (end rate)	3.25	3.50	3.50	3.50	3.50	3.50	3.50	3.50
	Quick rebound from Covid-19 pandemic, rising confidence and investment levels - structural problems worked down. <b>No further credit rating downgrades, rating outlooks move to stable and eventually positive, strong fiscal consolidation (government debt projections fall substantially).</b> 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.								
<b>Base case</b> 48%	USD/Rand (average)	15.00	15.40	15.50	15.20	15.30	15.70	15.90	15.60
	Repo rate (end rate)	3.50	3.50	3.50	3.75	3.75	4.00	4.50	4.50
	Recovery from the sharp global economic slowdown by 2024 in real terms – <b>sufficient global and domestic monetary and other policy supports to growth and financial markets occur and risk sentiment stabilises then improves.</b> Expropriation of private sector property is limited and does not have a negative impact on the economy or on market sentiment. <b>SA remains in the BB category rating bracket for Moody's – fiscal consolidation (debt to GDP stabilisation) occurs.</b>								
<b>Lite</b> (domestic) Down case 44%	USD/Rand (average)	15.35	16.50	17.00	16.80	16.50	17.00	17.50	17.00
	Repo rate (end rate)	3.75	3.75	3.75	4.00	4.00	4.25	4.75	4.75
	The international environment (including risk sentiment) is that of the base case. <b>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.</b> Recession occurs. Expropriation of some private commercial sector property without compensation, with some 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 the C grades.								
<b>Severe</b> down case 5%	USD/Rand (average)	15.50	17.00	17.50	18.00	17.50	17.80	18.00	17.80
	Repo rate (end rate)	4.00	4.00	4.00	4.50	4.50	4.50	5.00	5.00
	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). <b>SA rated single B from all three key agencies, with further rating downgrades eventually occurring into CCC grade and lower to D (default) as government finances deteriorate (debt projections elevate even further - fail to ever stabilise.</b> 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 Q1.21. Source: Investec



# SA Economics



Up Case: Exchange Rate forecasts												
	2021				2022				2023			
	Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.23	Q4.23
USD/ZAR	14.71	14.50	14.50	14.00	13.50	14.00	14.50	13.50	13.00	13.80	14.00	13.50
GBP/ZAR	20.16	19.86	19.87	19.46	19.17	20.02	21.03	19.31	18.46	19.46	19.60	18.90
EUR/ZAR	17.83	17.40	17.55	17.29	16.94	17.64	18.42	17.01	16.25	17.25	17.50	16.88
ZAR/JPY	7.08	7.24	7.24	7.46	7.70	7.43	7.24	7.78	8.15	7.68	7.57	7.85
CHFZAR	16.43	15.89	15.88	15.51	15.13	15.61	16.15	15.14	13.00	13.80	14.00	13.50
AUDZAR	11.34	11.17	11.24	11.06	10.80	11.20	11.60	10.80	9.75	10.35	10.50	10.13
GBP/USD	1.37	1.37	1.37	1.39	1.42	1.43	1.45	1.43	1.42	1.41	1.40	1.40
EUR/USD	1.21	1.20	1.21	1.24	1.26	1.26	1.27	1.26	1.25	1.25	1.25	1.25
USD/JPY	104	105	105	105	104	104	105	105	106	106	106	106

Note averages, Source: Investec, Iress

Lite Down Case: Exchange Rate forecasts												
	2021				2022				2023			
	Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.23	Q4.23
USD/ZAR	15.35	16.50	17.00	16.80	16.50	17.00	17.50	17.00	17.30	17.50	18.00	17.50
GBP/ZAR	21.03	22.60	23.29	23.35	23.43	24.31	25.38	24.31	24.57	24.68	25.20	24.50
EUR/ZAR	18.60	19.80	20.57	20.75	20.71	21.42	22.23	21.42	21.63	21.88	22.50	21.88
ZAR/JPY	6.78	6.36	6.18	6.22	6.30	6.12	6.00	6.18	6.13	6.06	5.89	6.06
CHFZAR	17.14	18.08	18.62	18.61	18.49	18.96	19.50	19.07	17.30	17.50	18.00	17.50
AUDZAR	11.83	12.71	13.18	13.27	13.20	13.60	14.00	13.60	12.98	13.13	13.50	13.13
GBP/USD	1.37	1.37	1.37	1.39	1.42	1.43	1.45	1.43	1.42	1.41	1.40	1.40
EUR/USD	1.21	1.20	1.21	1.24	1.26	1.26	1.27	1.26	1.25	1.25	1.25	1.25
USD/JPY	104	105	105	105	104	104	105	105	106	106	106	106

Note: averages, Source: Investec, Iress

Severe Down Case: Exchange Rate forecasts												
	2021				2022				2023			
	Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.23	Q4.23
USD/ZAR	15.50	17.00	17.50	18.00	17.50	17.80	18.00	17.80	17.80	18.00	18.50	18.00
GBP/ZAR	21.24	23.29	23.98	25.02	24.85	25.45	26.10	25.45	25.28	25.38	25.90	25.20
EUR/ZAR	18.78	20.40	21.18	22.23	21.96	22.43	22.86	22.43	22.25	22.50	23.13	22.50
ZAR/JPY	6.72	6.18	6.00	5.81	5.94	5.84	5.83	5.90	5.96	5.89	5.73	5.89
CHFZAR	17.31	18.63	19.16	19.94	19.61	19.85	20.05	19.97	17.80	18.00	18.50	18.00
AUDZAR	11.95	13.09	13.56	14.22	14.00	14.24	14.40	14.24	13.35	13.50	13.88	13.50
GBP/USD	1.37	1.37	1.37	1.39	1.42	1.43	1.45	1.43	1.42	1.41	1.40	1.40
EUR/USD	1.21	1.20	1.21	1.24	1.26	1.26	1.27	1.26	1.25	1.25	1.25	1.25
USD/JPY	104	105	105	105	104	104	105	105	106	106	106	106

Note: averages, Source: Investec, Iress

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Extreme Up Case: Exchange Rate forecasts												
	2021				2022				2023			
	Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.23	Q4.23
USD/ZAR	14.65	14.00	13.50	13.25	13.00	12.75	12.75	12.50	12.50	12.30	12.00	11.80
GBP/ZAR	20.07	19.18	18.50	18.42	18.46	18.23	18.49	17.88	17.75	17.34	16.80	16.52
EUR/ZAR	17.75	16.80	16.34	16.36	16.32	16.07	16.19	15.75	15.63	15.38	15.00	14.75
ZAR/JPY	7.11	7.50	7.78	7.89	8.00	8.16	8.24	8.40	8.48	8.62	8.83	8.98
CHFZAR	16.36	15.34	14.78	14.68	14.57	14.22	14.20	14.02	12.50	12.30	12.00	11.80
AUDZAR	11.29	10.78	10.46	10.47	10.40	10.20	10.20	10.00	9.38	9.23	9.00	8.85
GBP/USD	1.37	1.37	1.37	1.39	1.42	1.43	1.45	1.43	1.42	1.41	1.40	1.40
EUR/USD	1.21	1.20	1.21	1.24	1.26	1.26	1.27	1.26	1.25	1.25	1.25	1.25
USD/JPY	104	105	105	105	104	104	105	105	106	106	106	106

Note: averages, Source: Investec, Iress