

## Rand Note

Monday 25 May 2020

Rand continues to strengthen as markets are building up optimism for quicker recovery in some key geographic areas, notably some commodity importers, benefiting the commodity nature of the domestic currency

### Up Case: Exchange Rates 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 |
| USDZAR | 15.38 | 16.00 | 15.00 | 14.00 | 13.50 | 12.00 | 11.50 | 11.00 | 10.80 | 10.60 | 10.40 | 10.65 |
| GBPZAR | 19.64 | 19.76 | 18.53 | 17.54 | 17.17 | 15.35 | 14.93 | 14.67 | 14.47 | 14.31 | 14.14 | 14.59 |
| EURZAR | 16.95 | 17.34 | 16.13 | 15.26 | 14.85 | 13.20 | 12.77 | 12.32 | 12.20 | 12.08 | 11.96 | 12.35 |
| ZARJPY | 7.12  | 6.75  | 7.27  | 7.86  | 8.07  | 8.96  | 9.22  | 9.50  | 9.81  | 10.00 | 10.19 | 9.95  |
| CHFZAR | 15.89 | 16.44 | 15.28 | 14.26 | 13.69 | 12.05 | 11.55 | 11.05 | 10.80 | 10.60 | 10.40 | 10.65 |
| AUDZAR | 10.09 | 9.58  | 8.89  | 8.54  | 8.51  | 7.74  | 7.65  | 7.59  | 7.56  | 7.42  | 7.38  | 7.56  |

Note averages, Source: Investec, Iress

### Extreme Up Case: Exchange Rates 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 |
| USDZAR | 15.38 | 15.00 | 14.00 | 13.00 | 12.00 | 11.00 | 10.00 | 9.00  | 8.00  | 8.00  | 8.00  | 8.00  |
| GBPZAR | 19.64 | 18.53 | 17.30 | 16.29 | 15.26 | 14.07 | 12.98 | 12.00 | 10.72 | 10.80 | 10.88 | 10.96 |
| EURZAR | 16.95 | 16.25 | 15.05 | 14.17 | 13.20 | 12.10 | 11.10 | 10.08 | 9.04  | 9.12  | 9.20  | 9.28  |
| ZARJPY | 7.12  | 7.20  | 7.79  | 8.46  | 9.08  | 9.77  | 10.60 | 11.61 | 13.25 | 13.25 | 13.25 | 13.25 |
| CHFZAR | 15.89 | 15.42 | 14.27 | 13.24 | 12.17 | 11.05 | 10.05 | 9.04  | 8.00  | 8.00  | 8.00  | 8.00  |
| AUDZAR | 10.09 | 8.98  | 8.30  | 7.93  | 7.56  | 7.10  | 6.65  | 6.21  | 5.60  | 5.60  | 5.68  | 5.68  |

Note: averages, Source: Investec, Iress

**Expected Case: Exchange Rates 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 |
| USDZAR | 15.38 | 18.00 | 17.50 | 16.50 | 15.75 | 15.50 | 15.50 | 15.00 | 14.50 | 14.75 | 15.00 | 14.50 |
| GBPZAR | 19.64 | 22.23 | 21.62 | 20.67 | 20.03 | 19.83 | 20.12 | 20.00 | 19.43 | 19.91 | 20.40 | 19.87 |
| EURZAR | 16.95 | 19.50 | 18.81 | 17.99 | 17.33 | 17.05 | 17.21 | 16.80 | 16.39 | 16.82 | 17.25 | 16.82 |
| ZARJPY | 7.12  | 6.00  | 6.23  | 6.67  | 6.92  | 6.94  | 6.84  | 6.97  | 7.31  | 7.19  | 7.07  | 7.31  |
| CHFZAR | 15.89 | 18.50 | 17.83 | 16.81 | 15.97 | 15.57 | 15.57 | 15.07 | 14.50 | 14.75 | 15.00 | 14.50 |
| AUDZAR | 10.09 | 10.77 | 10.37 | 10.07 | 9.92  | 10.00 | 10.31 | 10.35 | 10.15 | 10.33 | 10.65 | 10.30 |

Note: averages, Source: Investec, Iress

**Lite Down Case: Exchange Rates 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 |
| USDZAR | 15.38 | 19.50 | 22.00 | 20.00 | 18.50 | 17.00 | 16.50 | 16.00 | 15.50 | 16.00 | 16.50 | 16.00 |
| GBPZAR | 19.64 | 24.09 | 27.18 | 25.06 | 23.53 | 21.74 | 21.42 | 21.33 | 20.77 | 21.60 | 22.44 | 21.92 |
| EURZAR | 16.95 | 21.13 | 23.65 | 21.80 | 20.35 | 18.70 | 18.32 | 17.92 | 17.52 | 18.24 | 18.98 | 18.56 |
| ZARJPY | 7.12  | 5.54  | 4.95  | 5.50  | 5.89  | 6.32  | 6.42  | 6.53  | 6.84  | 6.63  | 6.42  | 6.63  |
| CHFZAR | 15.89 | 20.04 | 22.42 | 20.37 | 18.76 | 17.08 | 16.57 | 16.07 | 15.50 | 16.00 | 16.50 | 16.00 |
| AUDZAR | 10.09 | 11.67 | 13.04 | 12.20 | 11.66 | 10.97 | 10.97 | 11.04 | 10.85 | 11.20 | 11.72 | 11.36 |

Note: averages, Source: Investec, Iress

**Severe Down Case: Exchange Rates 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 |
| USDZAR | 15.38 | 22.00 | 24.00 | 21.00 | 20.00 | 19.00 | 18.00 | 16.50 | 16.80 | 17.50 | 18.00 | 17.00 |
| GBPZAR | 19.64 | 27.17 | 29.66 | 26.31 | 25.43 | 24.30 | 23.37 | 22.00 | 22.51 | 23.63 | 24.48 | 23.29 |
| EURZAR | 16.95 | 23.84 | 25.80 | 22.89 | 22.00 | 20.90 | 19.98 | 18.48 | 18.98 | 19.95 | 20.70 | 19.72 |
| ZARJPY | 7.12  | 4.91  | 4.54  | 5.24  | 5.45  | 5.66  | 5.89  | 6.33  | 6.31  | 6.06  | 5.89  | 6.24  |
| CHFZAR | 15.89 | 22.61 | 24.45 | 21.39 | 20.28 | 19.09 | 18.08 | 16.57 | 16.80 | 17.50 | 18.00 | 17.00 |
| AUDZAR | 10.09 | 13.17 | 14.22 | 12.81 | 12.60 | 12.26 | 11.97 | 11.39 | 11.76 | 12.25 | 12.78 | 12.07 |

Note: averages, Source: Investec, Iress

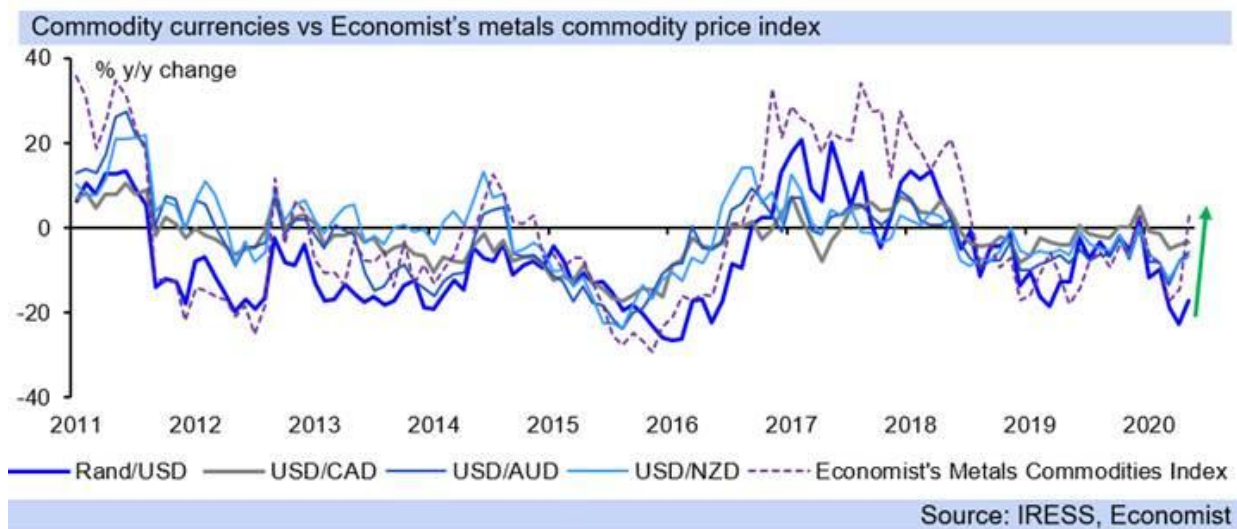
**Economic Scenarios: note updated forecasts**

|   |   | Q1.20 | Q2.20 | Q3.20 | Q4.20 | Q1.21 | Q2.21 | Q3.21 | Q4.21 |
|---|---|-------|-------|-------|-------|-------|-------|-------|-------|
| <b>Extreme Up case</b><br>1%            | USD/Rand (average)  | 15.38 | 15.00 | 14.00 | 13.00 | 12.00 | 11.00 | 10.00 | 9.00  |
|   | Repo rate (end rate)  | 5.25  | 3.50  | 3.50  | 3.50  | 3.50  | 3.50  | 3.50  | 3.50  |
|   | 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><br>4%                    | USD/Rand (average)  | 15.38 | 16.00 | 15.00 | 14.00 | 13.50 | 12.00 | 11.50 | 11.00 |
|   | Repo rate (end rate)  | 5.25  | 3.75  | 3.75  | 3.75  | 3.75  | 3.75  | 3.75  | 3.75  |
|   | 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><br>43%                 | USD/Rand (average)  | 15.38 | 18.00 | 17.50 | 16.50 | 15.75 | 15.50 | 15.50 | 15.00 |
|   | Repo rate (end rate)  | 5.25  | 3.75  | 3.75  | 3.75  | 4.00  | 4.25  | 4.50  | 4.50  |
|   | Temporary sharp global slowdown and global financial turmoil from Covid-19 pandemic (severe currency depreciation, low interest rates) - <b>eventually sufficient global and domestic monetary and other policy supports to growth and financial markets occur and risk sentiment stabilises.</b> South Africa exits recession in Q3.20. Market unfriendly policies like expropriation of private sector property put on hold in the crisis. <b>SA remains BB+ rating from Moody's - government debt projections stabilise.</b>   |       |       |       |       |       |       |       |       |
| <b>Lite (domestic) Down case</b><br>42% | USD/Rand (average)  | 15.38 | 19.50 | 22.00 | 20.00 | 18.50 | 17.00 | 16.50 | 16.00 |
|   | Repo rate (end rate)  | 5.25  | 4.25  | 4.25  | 4.50  | 4.75  | 4.75  | 4.75  | 5.00  |
|   | The international risk sentiment environment is that of the base case. <b>South Africa continues to fail to see its debt projections stabilise and loses its BB+ rating from Moody's and falls towards B ratings from all three rating agencies.</b> More severe recession in SA over 2020 than in the expected case. Expropriation of some private commercial sector property without compensation, with some negative impact on the economy. Business confidence depressed even further, significant rand weakness, significant load shedding and weak investment growth until substantial fiscal repair ultimately effected.   |       |       |       |       |       |       |       |       |
| <b>Severe down case</b><br>10%          | USD/Rand (average)  | 15.38 | 22.00 | 24.00 | 21.00 | 20.00 | 19.00 | 18.00 | 16.50 |
|   | Repo rate (end rate)  | 5.25  | 4.50  | 4.75  | 5.00  | 5.50  | 6.00  | 6.50  | 7.00  |
|   | Lengthy global recession on impact of Covid-19 - 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 occurring into C grade 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. |       |       |       |       |       |       |       |       |

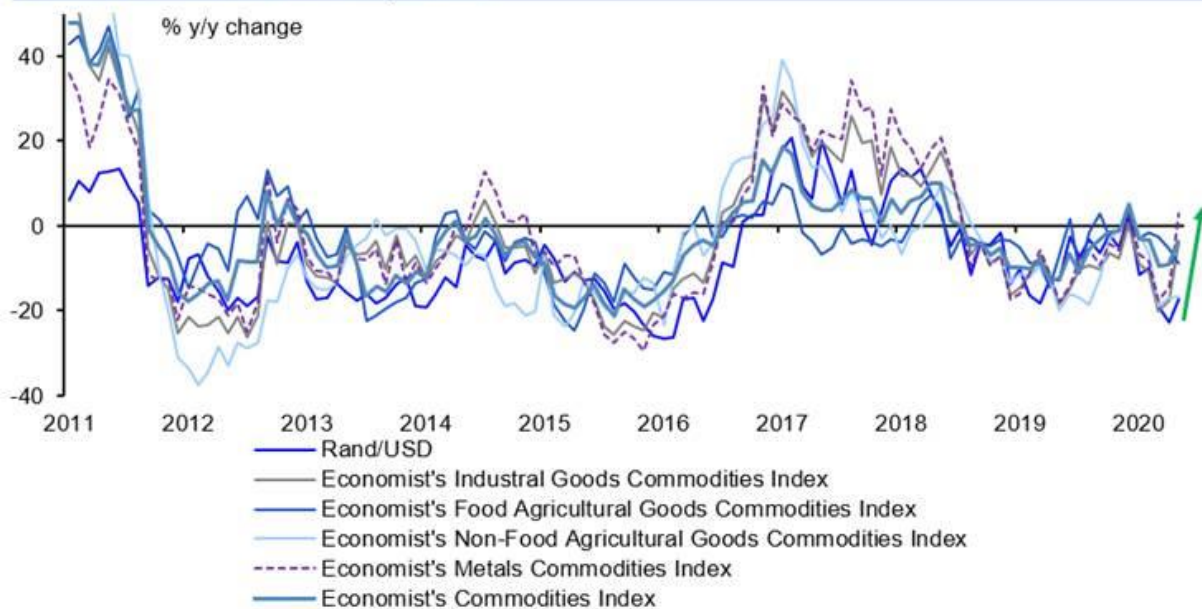
**Note: Event risk begins Q2.20. Source: Investec**

- The rand has strengthened to R17.52/USD, R19.10/EUR and R21.35/GBP this month, leading emerging market currencies, along with the Mexican peso, in recovery, but still below its pre-crisis level of R16.26/USD, R17.83/EUR and R19.82/GBP in mid-March. The global market sentiment lift driving the rand is still prone to risks however.
- Both China and Germany are seen to show some early indications of recovery potentially beginning, i.e. that economic activity has bottomed at very low levels and is likely in the process of improving. Countries ahead in the easing of restrictions are seeing some optimism on their future outlooks, but a deep severe recession globally will not be avoided.

- With these two countries key importers of SA's exports, the rand has also seen some benefit from rising sentiment as a commodity currency. Metals prices have lifted by 12.4% on the month, and by 3.0% y/y (Economist Metal's Commodity Index), also driving the domestic currency stronger.
- Industrial commodity prices have also lifted on the month, by 9.3%, with food commodity prices up 2.0% m/m, assisting the overall commodities' price index in a 6.3% lift compared to in April (all Economist data). With the price lift in metals' commodities leading the pack the rand has benefitted from this source.
- So too, South Africa's imminent move to level three lockdown on 1<sup>st</sup> June, which is currently reported as allowing mining to scale up to 100% employment, but with restrictions and not full clarity yet, has added to market optimism, as has SA's planned general move to level 3 in June.
- Indeed, level 3 is now reported as all economic activity is permitted in South Africa, with a few exceptions where the risk of transmission is high. All public transport, subject to some restrictions, as well as limited domestic air travel for work purposes is also reported to be allowed. Virtually all retail activity will be permitted, with stringent health protocols.
- However, getting back to full operation of the economy will be another matter. The severe interruptions to supply chains, along with the huge loss in incomes, plunge in the circulation of money and high levels of unemployment have damaged both supply and demand, while level 3 still has a number of restrictions to the smooth functioning of the economy.
- Indeed, before the Covid-19 lockdown in South Africa there were many impediments to the smooth functioning of the economy, and Eskom indicates that various units of Medupi will experience outages in a number of remaining months of this year, which will likely contribute to limiting the ability for economic recovery.
- Globally, early optimism in economic recovery, particularly the marked lift in metals prices, is likely to be very vulnerable to a switch in sentiment, and the recent support for the rand from this source will be at risk. Commodity currencies are exhibiting less weakness in May so far on a year ago, versus in April, but are still very weak versus a year ago.

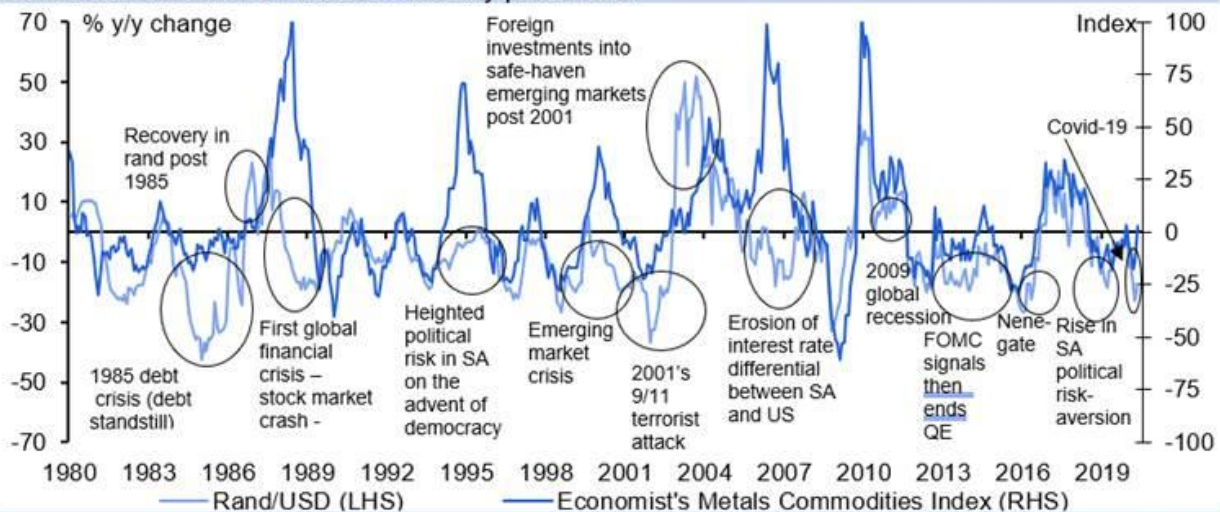


### Rand vs Economist's commodity indices



Source: IRESS, Economist

### Rand vs Economist's metals commodity price index



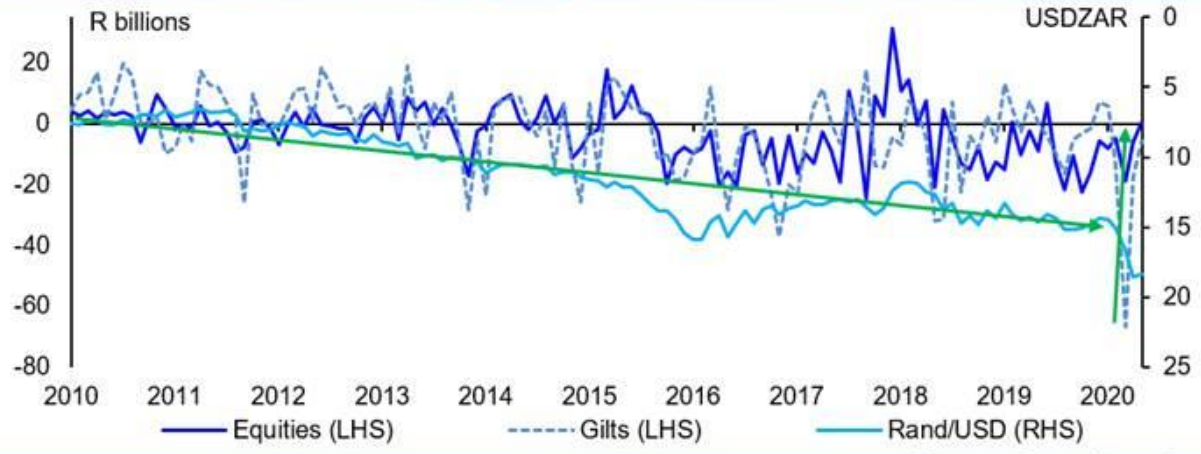
Source: IRESS, Investec

- While the rand has seen new historic weak points, on a level basis of R19.35/USD, R20.92/EUR and R23.72/GBP, the depreciation in the domestic currency on an annual basis has not been as marked as occurred either in South Africa's 1985 debt (standstill) crisis or in 2001's 9/11 terrorist attack.
- The weakness in the rand has even been less than that which occurred following Nene-gate, and that experienced in the emerging market crisis in 1998. The bounce back in the domestic currency that has been underway since the last few days of April has likely not run its course, but will also likely see various interruptions.
- Foreigners showed increased appetite for South African portfolio assets last week, purchasing R1.3bn in equities on a net of sales basis at the end of last week, and buying R2.1bn worth of SA government bonds on Friday, net of sales, as global financial market sentiment's increasingly risk-on bent benefited SA's portfolio flows.

- To date, the rand averages R18.49/USD this quarter, and if it averages R17.50/USD for the remainder of the quarter, it will come out at R18.15/USD, slightly weaker than our forecast. The domestic currency is likely to see further strength this year, moving towards R16.00/USD by year end, with the potential to strengthen further into 2021.
- The high levels of QE globally, which are not expected to be unwound this year, or necessarily next year either, will contribute to EM currencies' strength, while global recovery, which is already being anticipated by markets, will assist with supporting commodity currencies.
- However, the high sensitivity of EM currencies to financial market risk aversion will place the rand in continual jeopardy from shifts in market sentiment, continuing to keep the domestic currency highly susceptible to volatility, while also seeing an ongoing downward trend overall due to South Africa's higher inflation rates than its key trading partners.
- Furthermore, the weak fundamentals of the South African economy, particularly government finances, still weak governance in municipalities and in other public areas including utilities (even though many are in the process of being resolved), will also have a negative impact on the domestic currency until they are resolved.
- Furthermore, South Africa's ease of doing business was suppressed and declining before the lockdown, reflecting the little that had been done to ease the regulatory burden, and the mining industry has suffered from many impediments to robust growth. The lockdown will have exacerbated the declining nature of the industry.
- Other emerging market countries with weakened economic fundamentals, such as Brazil, Turkey, Russia, Argentina and Indonesia have seen marked currency depreciation over the past decade or so, and this is also reflected in the widened CDS of these countries, reflecting the risks, and so repair markets believe needs to be done.



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



Source: Iress, Investec

## Summary of alert levels

### Alert level 4

Extreme precautions to limit community transmission and outbreaks, while allowing some activity to resume.

### Alert Level 3

Strict precautions to keep transmission low, and additional measures to contain outbreaks in hotspots.

### SECTORS PERMITTED

All essential services, plus a limited number of sectors with a low rate of transmission and high economic or social value.

All economic activity is permitted, with a few exceptions where the risk of transmission is high.

### RETAIL PERMITTED

(including stores, eCommerce and informal traders)

All essential goods, as well as educational books, stationery, office supplies, IT equipment (including computers and mobile phones), children's clothing, winter goods such as clothing, bedding and heaters, and textiles required to produce masks.

All retail permitted, with strict health protocols in place.

Alcohol will be sold under strict conditions and on specified days.

Restaurants and fast food outlets may open for delivery only.

### MOVEMENT

You must remain at home except to go to work, do shopping where necessary, or seek medical care.

You must remain at home, except to travel to work, purchase goods, seek medical care or attend schools and universities when these reopen.

No inter-provincial movement of people, except to return to usual place of residence, for transportation of goods and exceptional circumstances (e.g. funerals).

Additional restrictions on movement apply in hotspot areas.

Curfew in place between 8pm and 5am, except for essential workers.

There is no curfew on the movement of people.

Walking, jogging and cycling permitted between 6am and 9am, but not in groups.

Exercise permitted at any time during the day, but not in groups.

### GATHERINGS

All public gatherings are prohibited.

All public gatherings are prohibited.

### TRANSPORT

Passenger rail, bus services, taxi services, e-hailing and private motor vehicles may operate subject to directions.

All public transport may operate subject to directions, as well as limited domestic air travel for work purposes.

### EDUCATION

Directions issued by the Minister of Basic Education and Minister of Higher Education, Science and Innovation.

Source: The Presidency



