

# SA Economics



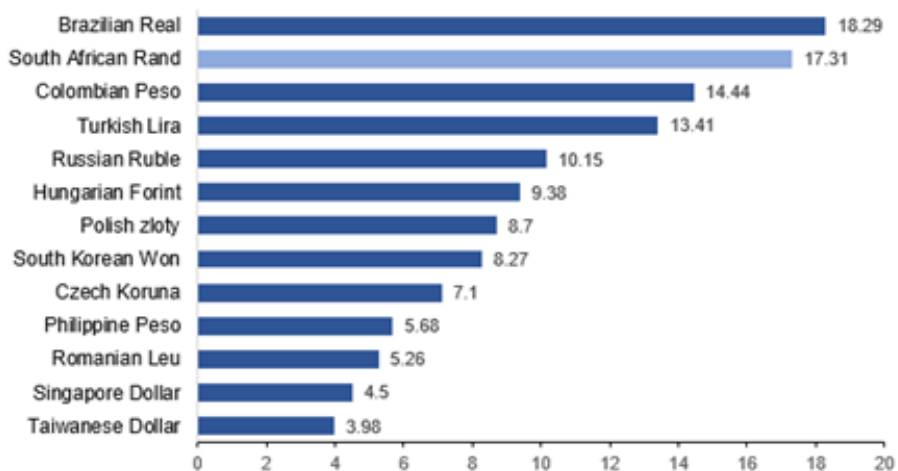
Monday 20 September 2021

Rand note: the volatile domestic currency turns again, as markets fret about the FOMC meeting this week, fearing tapering may begin even as early as September while SA bond yields have also weakened

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	14.96	14.13	14.55	14.45	14.45	14.85	15.15	14.75	14.55	14.95	15.35	14.85
GBP/ZAR	20.63	19.75	19.87	20.00	20.66	21.53	22.42	22.34	21.53	21.68	21.95	21.24
EUR/ZAR	18.03	17.03	17.36	17.48	17.70	18.27	18.86	18.59	18.19	18.69	19.19	18.56
ZAR/JPY	7.09	7.75	7.52	7.40	7.27	7.00	6.86	7.05	7.22	7.16	6.97	7.21
CHF/ZAR	16.52	15.51	15.79	15.75	15.80	16.16	16.55	16.16	15.99	16.43	16.87	16.32
AUD/ZAR	11.56	10.88	11.06	11.34	11.56	11.88	12.12	11.80	11.35	11.66	11.97	11.58
GBP/USD	1.38	1.40	1.37	1.38	1.43	1.45	1.48	1.51	1.48	1.45	1.43	1.43
EUR/USD	1.21	1.21	1.19	1.21	1.23	1.23	1.25	1.26	1.25	1.25	1.25	1.25
USD/JPY	106	109	109	107	105	104	104	104	106	107	107	107

Note: averages, Source: Investec, Iress

Emerging Markets Implied Volatilities – values 20 September 2021

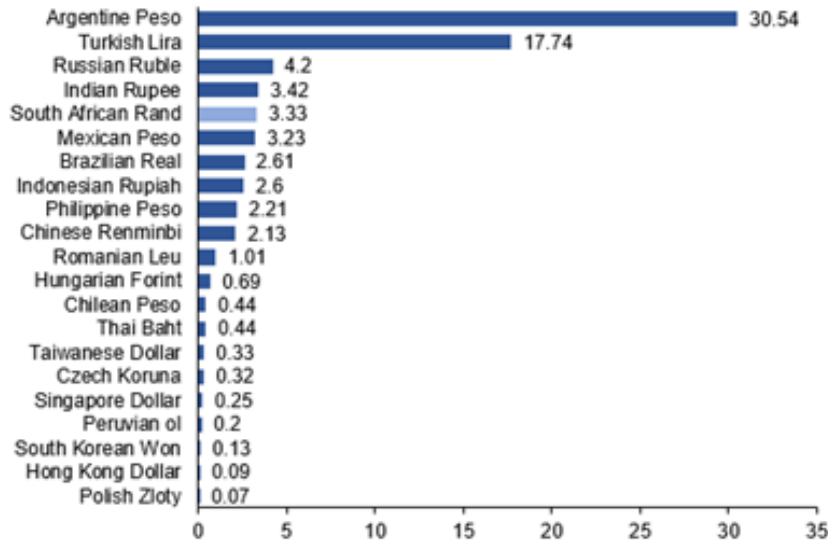


Source: Bloomberg

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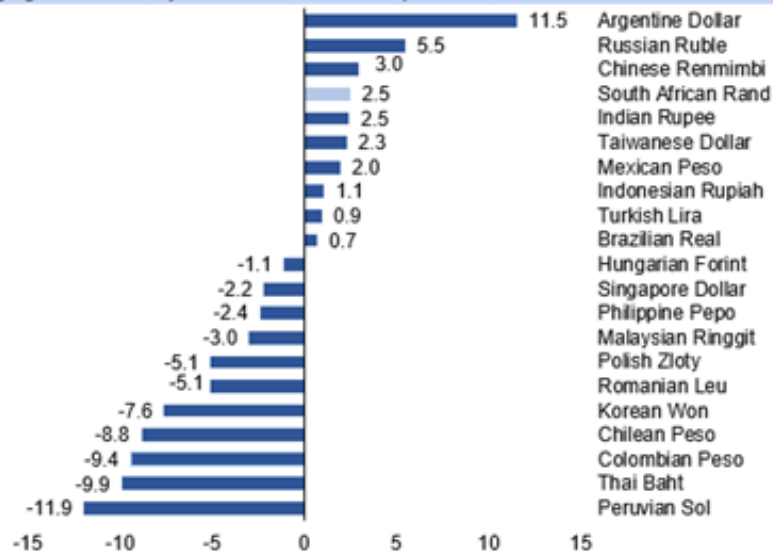


Emerging Markets Interest Return – values 20 September 2021



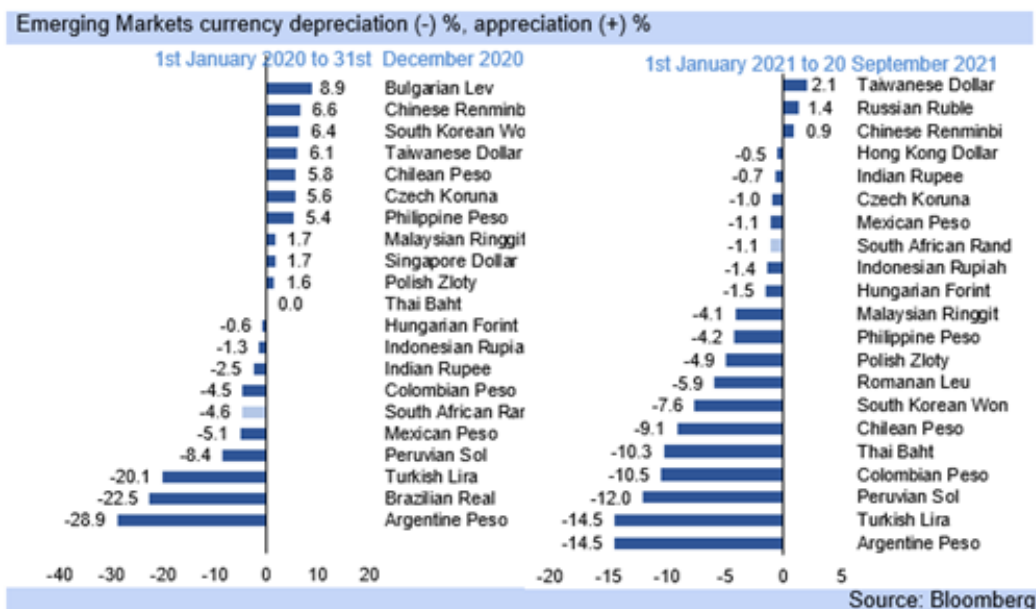
Source: Bloomberg

Emerging Markets Carry Return – values 20 September 2021



Source: Bloomberg

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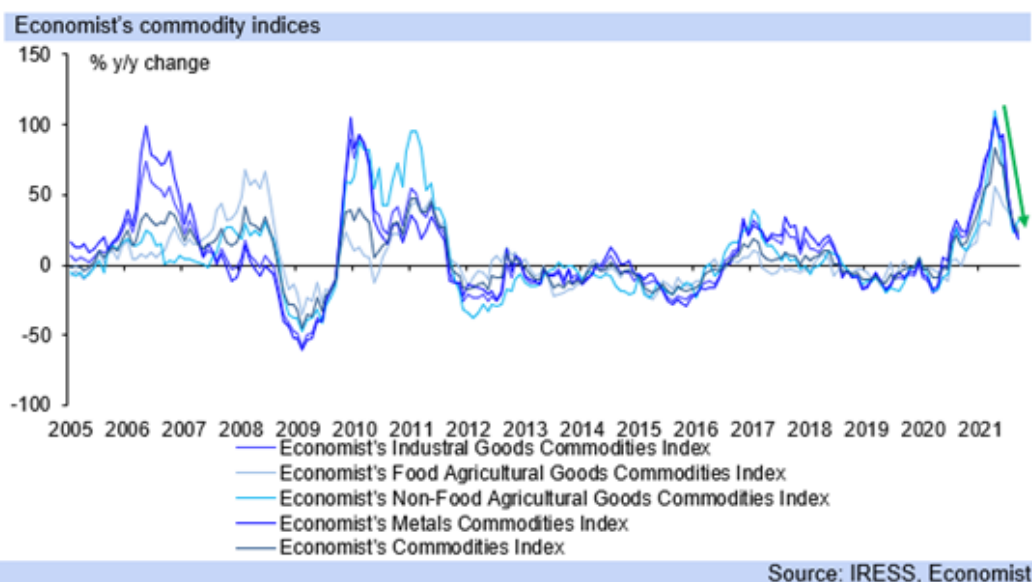
- The US is facing two days of monetary policy discussions, culminating in potential guidance on future tapering of QE. While markets don't necessarily expect QE tapering to begin in September, there is very high sensitivity to any indication of when it will start.
- Reaching R14.86/USD this morning, the domestic currency has pulled back to R14.73/USD, with the rise in risk aversion negatively affecting commodity prices as well, causing a double whammy for the rand.
- September's FOMC meeting will also deliver projection materials on the Fed's updated inflation and economic growth forecast, and interest rate expectations, while markets will also seek any indication of a more hawkish tone.
- In particular, the Fed's dot plot (interest rate expectations) chart caused concern in June when it revealed expectations of a quickening trajectory, as FOMC members brought forward rate hike forecasts to two increases in 2023. No further change would support markets.
- In June, markets reacted negatively to the quickening in FOMC members' forecast rate hike trajectory, and the rand weakened from R13.68/USD to R14.10/USD, although Governor Powell warned against reading too much into the dot plot, at the time.
- The Fed Chair also highlighted in June the continuation of its asset purchases and interest rates near zero for the foreseeable future in order to "ensure monetary policy would deliver powerful support to the economy until the recovery was complete."
- In July, Jerome Powell reiterated this, adding that "(t)he pace of the recovery in economic activity and employment has moderated in recent months, with weakness concentrated in the sectors most adversely affected by the pandemic."

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- The US third wave continues to build, and has affected growth and employment. Deaths from COVID-19 continue to rise in the US, while those hospitalised in ICU are near the same high rates of the second wave.
- Global financial market sentiment, and the rand, would be further weakened from current levels if the Fed says this week that it would (as opposed to may) be appropriate to start reducing asset purchases this year.

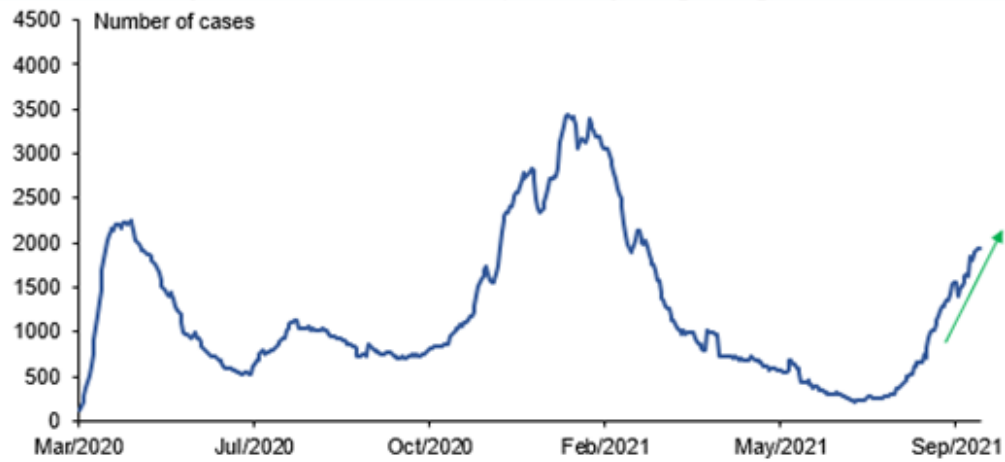
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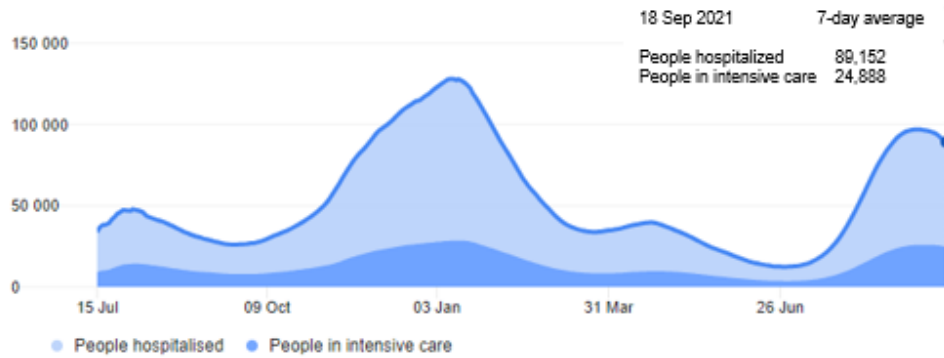


United States daily confirmed COVID-19 deaths, seven day rolling average



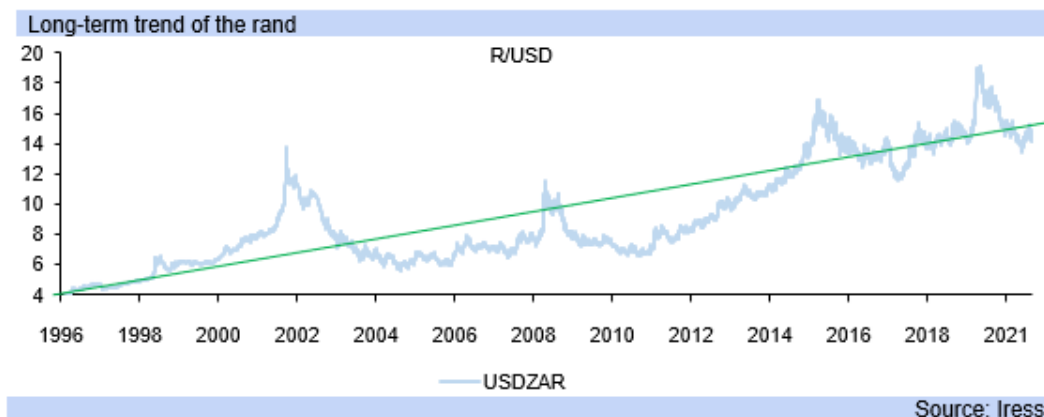
Source: Our World in Data

United States - Hospitalisations



Source: Our World in data

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- Markets believe the Fed could begin tapering in November or December (Investec expects December), with September seen as too soon for any reductions in the current pace of asset purchases.
- A repetition of the Fed's view that "if the economy evolved broadly as anticipated, it could be appropriate to start reducing the pace of asset purchases this year", is expected, but will not bring enough calm to current risk off to see the rand pierce R14.00/USD this month.
- US economic data has been mixed, indicating both growing uncertainties as its third wave of COVID-19 infections and deaths build while the most recent key jobs numbers disappointed, but some lift occurred in retail sales and U Michigan sentiment, exceeding expectations.
- On 27<sup>th</sup> August the Fed said, compared to at the time of the July FOMC meeting, that "(t)he intervening month has brought more progress in the form of a strong employment report for July, but also the further spread of the Delta variant".
- "We will be carefully assessing incoming data and the evolving risks. Even after our asset purchases end, our elevated holdings of longer-term securities will continue to support accommodative financial conditions."
- However, the tone turned hawkish as Fed Chair Powell specified that his "view is that the "substantial further progress" test has been met for inflation. There has also been clear progress toward maximum employment."
- QE tapering this year in the US would place upwards pressure on EM interest rates, and emerging market economies which do not hike their interest rates as others do would risk seeing their currencies weaken potentially.
- The rand has already weakened from R13.40/USD in June, to R14.82/USD on Friday on QE tapering fears, and much will depend on the Fed's concerns about the US's third wave. The rand currently averages R14.59/USD for the quarter to date.



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- Looking forward, the rand will be at risk in Q4.21, and it may no longer achieve the R14.45/USD expectation for the quarter average if this week's FOMC outcome remains supportive of near term tapering.

Economic Scenarios: note interest rate hikes pushed out in expected case									
		Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22
<b>Extreme Up case</b> 1%	USD/Rand (average)	14.96	14.13	13.50	13.20	13.00	12.90	12.80	12.70
	Repo rate (end rate)	3.50	3.50	3.25	3.25	3.25	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)	14.96	14.13	13.70	13.50	13.30	13.40	13.20	13.00
	Repo rate (end rate)	3.50	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)	14.96	14.13	14.55	14.35	14.45	14.85	15.15	14.75
	Repo rate (end rate)	3.50	3.50	3.50	3.50	3.50	3.50	3.75	3.75
	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 (domestic) Down case</b> 43%	USD/Rand (average)	14.96	14.13	15.15	15.50	16.00	16.65	16.90	17.00
	Repo rate (end rate)	3.50	3.50	3.75	3.75	4.00	4.00	4.25	4.25
	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 down case</b> 6%	USD/Rand (average)	14.96	14.13	15.65	16.40	17.00	17.50	18.00	18.50
	Repo rate (end rate)	3.50	3.50	4.00	4.00	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 Q3.21. Source: Investec

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Life 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	14.96	14.13	15.15	15.50	16.00	16.65	16.90	17.00	17.50	17.60	17.50	17.20
GBP/ZAR	20.63	19.75	20.69	21.46	22.88	24.14	25.01	25.75	25.90	25.52	25.03	24.60
EUR/ZAR	18.03	17.03	18.07	18.76	19.60	20.48	21.04	21.42	21.88	22.00	21.88	21.50
ZAR/JPY	7.09	7.75	7.23	6.90	6.56	6.25	6.15	6.12	6.00	6.08	6.11	6.22
CHFZAR	16.52	15.51	16.45	16.90	17.50	18.12	18.46	18.63	19.23	19.34	19.23	18.90
AUDZAR	11.56	10.88	11.52	12.17	12.80	13.32	13.52	13.60	13.65	13.73	13.65	13.42
GBP/USD	1.38	1.40	1.37	1.38	1.43	1.45	1.48	1.51	1.48	1.45	1.43	1.43
EUR/USD	1.21	1.21	1.19	1.21	1.23	1.23	1.25	1.26	1.25	1.25	1.25	1.25
USD/JPY	106	109	109	107	105	104	104	104	106	107	107	107

Note: averages, Source: Investec, Iress

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	14.96	14.13	13.70	13.50	13.30	13.40	13.20	13.00	12.80	12.60	12.55	12.30
GBP/ZAR	20.63	19.75	18.71	18.69	19.02	19.43	19.54	19.69	18.94	18.27	17.95	17.59
EUR/ZAR	18.03	17.03	16.34	16.34	16.29	16.48	16.43	16.38	16.00	15.75	15.69	15.38
ZAR/JPY	7.09	7.75	7.99	7.93	7.89	7.76	7.88	8.00	8.20	8.49	8.53	8.70
CHFZAR	16.52	15.51	14.87	14.72	14.55	14.59	14.42	14.24	14.07	13.85	13.79	13.52
AUDZAR	11.56	10.88	10.42	10.60	10.64	10.72	10.56	10.40	9.98	9.83	9.79	9.59
GBP/USD	1.38	1.40	1.37	1.38	1.43	1.45	1.48	1.51	1.48	1.45	1.43	1.43
EUR/USD	1.21	1.21	1.19	1.21	1.23	1.23	1.25	1.26	1.25	1.25	1.25	1.25
USD/JPY	106	109	109	107	105	104	104	104	106	107	107	107

Note averages, Source: Investec, Iress

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	14.96	14.13	13.50	13.20	13.00	12.90	12.80	12.70	12.50	12.30	12.15	12.00
GBP/ZAR	20.63	19.75	18.43	18.27	18.59	18.70	18.94	19.24	18.50	17.84	17.37	17.16
EUR/ZAR	18.03	17.03	16.11	15.97	15.93	15.87	15.94	16.00	15.63	15.38	15.19	15.00
ZAR/JPY	7.09	7.75	8.11	8.11	8.08	8.06	8.13	8.19	8.40	8.70	8.81	8.92
CHFZAR	16.52	15.51	14.65	14.39	14.22	14.04	13.98	13.91	13.74	13.52	13.35	13.19
AUDZAR	11.56	10.88	10.27	10.36	10.40	10.32	10.24	10.16	9.75	9.59	9.48	9.36
GBP/USD	1.38	1.40	1.37	1.38	1.43	1.45	1.48	1.51	1.48	1.45	1.43	1.43
EUR/USD	1.21	1.21	1.19	1.21	1.23	1.23	1.25	1.26	1.25	1.25	1.25	1.25
USD/JPY	106	109	109	107	105	104	104	104	106	107	107	107

Note: averages, Source: Investec, Iress



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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	14.96	14.13	15.65	16.40	17.00	17.50	18.00	18.50	18.70	19.20	19.55	19.70
GBP/ZAR	20.63	19.75	21.37	22.70	24.31	25.37	26.64	28.02	27.68	27.84	27.96	28.17
EUR/ZAR	18.03	17.03	18.67	19.84	20.83	21.53	22.41	23.31	23.38	24.00	24.44	24.63
ZAR/JPY	7.09	7.75	7.00	6.52	6.18	5.94	5.78	5.62	5.61	5.57	5.47	5.43
CHF/ZAR	16.52	15.51	16.99	17.88	18.59	19.05	19.66	20.27	20.55	21.10	21.48	21.65
AUD/ZAR	11.56	10.88	11.90	12.87	13.60	14.00	14.40	14.80	14.59	14.98	15.25	15.37
GBP/USD	1.38	1.40	1.37	1.38	1.43	1.45	1.48	1.51	1.48	1.45	1.43	1.43
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