

# SA Economics



Monday 25 October 2021

Rand note: rand trades around R14.70/USD, with some subsidence of risk-off in global financial markets but noise from the final run-up to local elections and negative Fitch commentary sees some weakness

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	14.64	14.70	14.55	14.75	15.00	14.80	14.65	15.05	15.45	14.95
GBP/ZAR	20.63	19.75	20.18	20.41	20.88	21.61	22.35	22.42	21.68	21.82	22.09	21.38
EUR/ZAR	18.03	17.03	17.26	17.40	17.53	18.00	18.60	18.50	18.31	18.81	19.31	18.69
ZAR/JPY	7.09	7.75	7.52	7.47	7.35	7.12	6.93	7.03	7.17	7.11	6.93	7.16
CHF/ZAR	16.52	15.51	15.95	15.79	15.65	15.92	16.32	16.09	16.10	16.54	16.98	16.43
AUD/ZAR	11.56	10.88	10.76	10.84	10.91	11.06	11.40	11.40	11.43	11.74	12.05	11.66
GBP/USD	1.38	1.40	1.38	1.39	1.43	1.46	1.49	1.51	1.48	1.45	1.43	1.43
EUR/USD	1.21	1.21	1.18	1.18	1.21	1.22	1.24	1.25	1.25	1.25	1.25	1.25
USD/JPY	106	109	110	110	107	105	104	104	105	107	107	107
Note: averages. Source: Investec, Iress												

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Economic Scenarios: note interest rate hikes pushed out in expected case

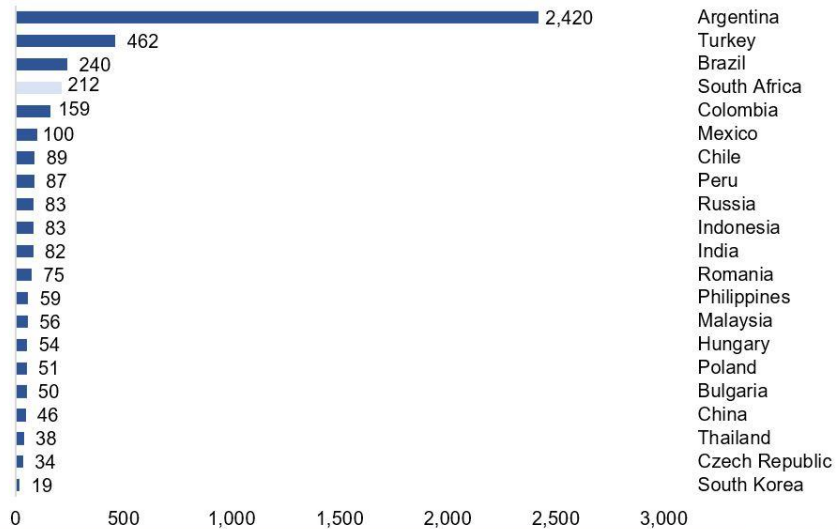
		Q1.21	Q2.21	Q3.21	Q4.21	Q1.22	Q2.22	Q3.22	Q4.22
Extreme Up case 1%	USD/Rand (average)	14.96	14.13	14.64	13.80	13.30	13.00	12.90	12.80
	Repo rate (end rate)	3.50	3.50	3.50	3.25	3.25	3.25	3.25	3.25
Impact of Covid-19 pandemic very rapidly resolved - economic growth of 3-5%, then 5-7% for SA. Good governance, 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). <i>Strong global growth, commodity boom. Stabilisation of credit ratings, then credit rating upgrades.</i>									
Up case 2%	USD/Rand (average)	14.96	14.13	14.64	14.00	13.50	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. <i>No further credit rating downgrades, rating outlooks move to stable and eventually positive, strong fiscal consolidation (government debt projections fall substantially).</i> 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.									
Base case 48%	USD/Rand (average)	14.96	14.13	14.64	14.70	14.55	14.75	15.00	14.80
	Repo rate (end rate)	3.50	3.50	3.50	3.50	3.75	4.00	4.00	4.25
Recovery from the sharp global economic slowdown by 2024 in real terms - <i>sufficient global and domestic monetary and other policy supports to growth and financial markets occur and risk sentiment stabilises then improves.</i> Expropriation of private sector property is limited and does not have a negative impact on the economy or on market sentiment. <i>SA remains in the BB category rating bracket for Moody's - fiscal consolidation (debt to GDP stabilisation) occurs.</i>									
Life (domestic) Down case 43%	USD/Rand (average)	14.96	14.13	14.64	15.50	16.00	16.65	16.90	17.00
	Repo rate (end rate)	3.50	3.50	3.50	3.75	4.00	4.25	4.50	4.75
The international environment (including risk sentiment) is that of the base case. <i>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.</i> 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.									
Severe down case 6%	USD/Rand (average)	14.96	14.13	14.64	16.00	16.80	17.50	18.00	18.50
	Repo rate (end rate)	3.50	3.50	3.50	4.00	4.50	4.75	5.00	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). <i>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.</i> 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 Q4.21. Source: Investec

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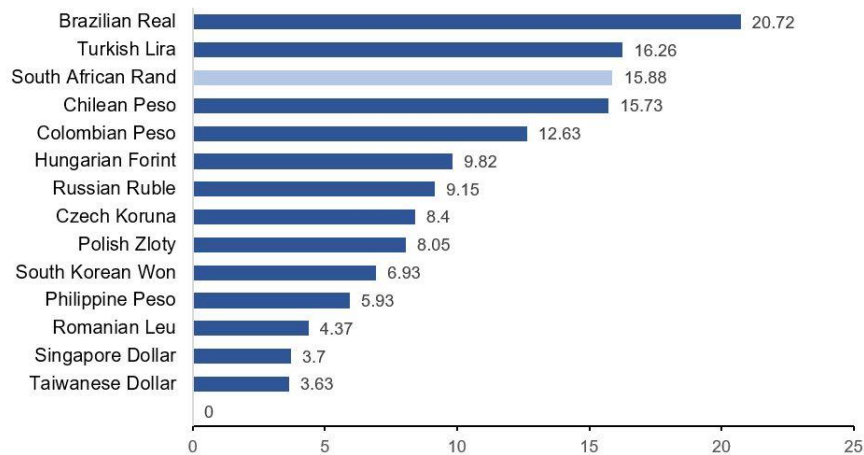


Emerging Markets CDS Spreads – values 25 October 2021



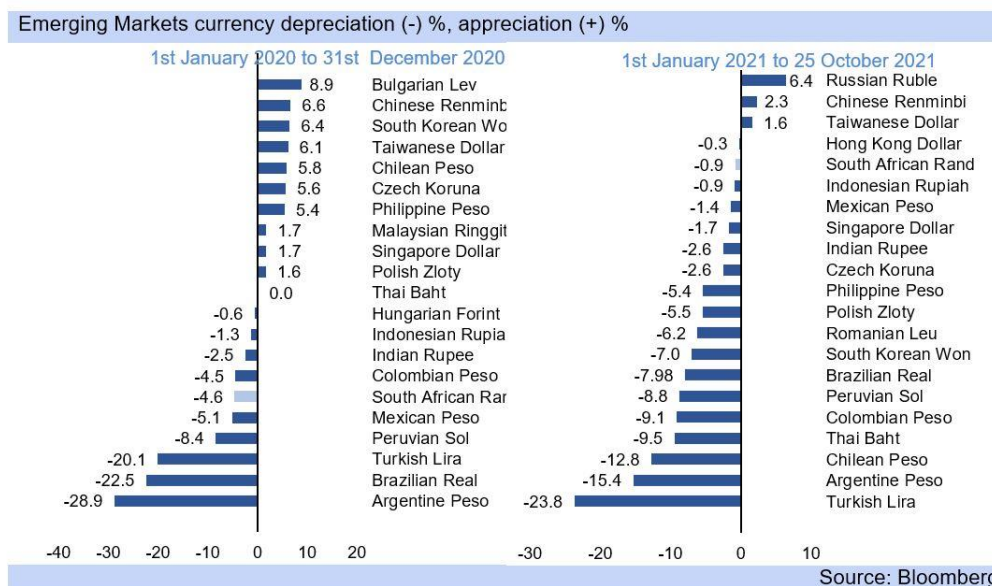
Source: Bloomberg

Emerging Markets Implied Volatilities – values 25 October 2021



Source: Bloomberg

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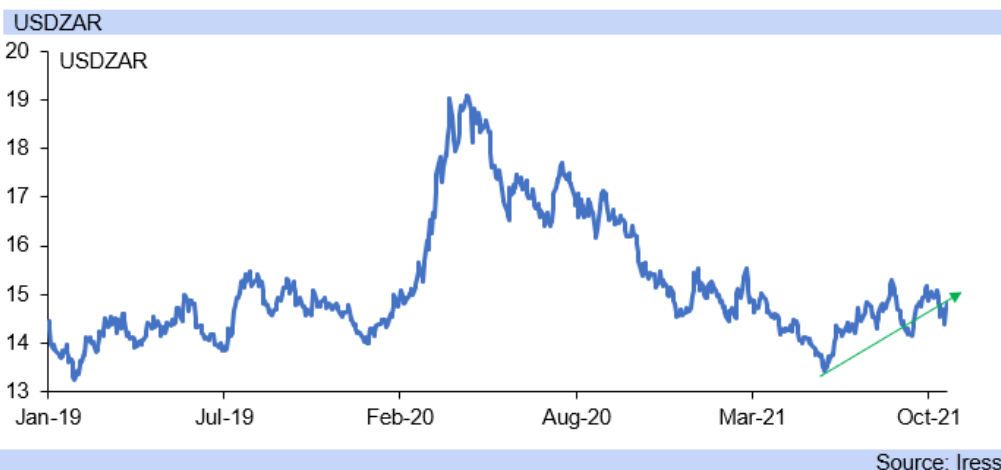
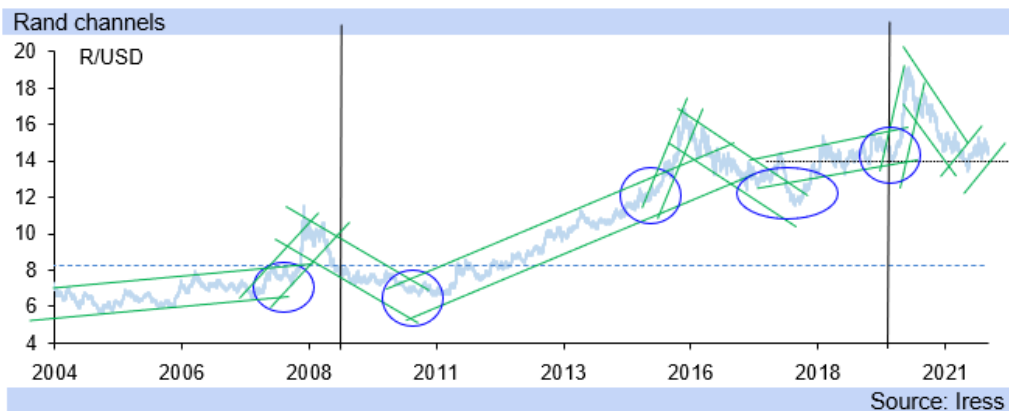
- South Africa's risk of credit rating downgrades remains relatively high (we continue to place it at 43%) as seen by ramp up in borrowings, while fractured politics pulling in different directions, exacerbating the difficulty government has in overcoming structural constraints.
- The ruling party has attempted to move quicker on structural reforms, but opposition to this from both inside and outside the party has seen little actually occur in moving the country into a freer market state needed to accelerate business dynamism, and so erode unemployment.
- While government has made some progress in improving the ease of doing business and has also made inroads into the repair and rebuilding of many SOE's and government institutions hollowed out by state capture, the enormous damage makes it a lengthy, ongoing task.
- Consequently, Fitch is reported to have said it expects South Africa to see weak gains in tackling the very high unemployment rate, particularly for youth, given the many structural constraints to job creation, including the poor educational system.
- Furthermore, "Fitch expects (South Africa's) unemployment rate to average 29.9% over our long-term forecast period to 2030, due to problems in the education system and labour market rigidities".
- It expected a deterioration in SA's fiscal situation, projecting "gross government debt to reach 82.9% of GDP by 2026, increasing from 69.4% of GDP in 2020," which it said would negatively affect the economy and lengthen the path to achieving investment-grade again.

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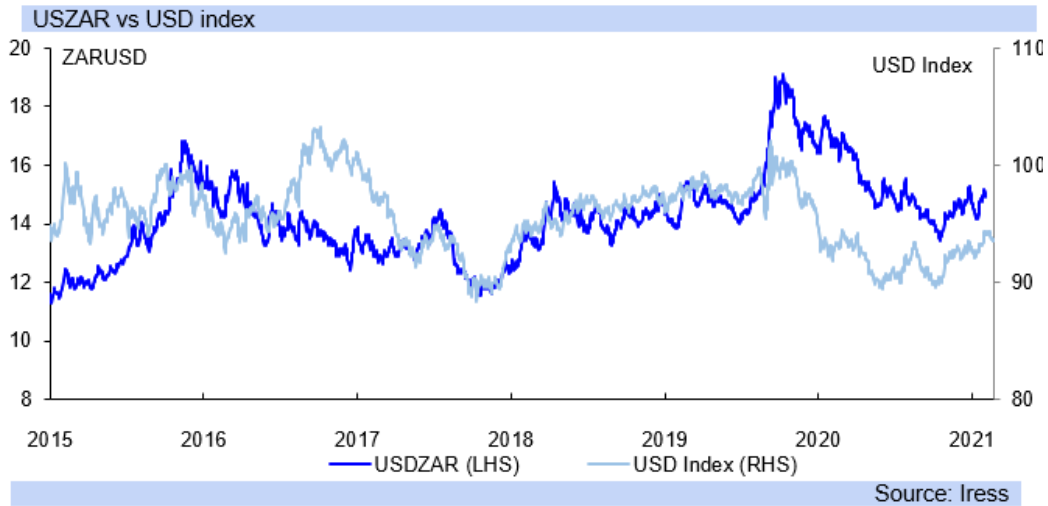
- Fitch adds that while it expects some progress, as government has allowed private power generators to provide more capacity, most of these additions would only begin in H2.22 which means the economy would continue to see power supply constraints in the interim.
- Consequently, Fitch expects GDP growth of 2.5% y/y for SA next year, after its rebound of 5.0% y/y this year, with a slowdown in global economic growth likely next year which would detract from SA's performance as well.
- The rand is facing headwinds this week, and currently averages R14.82/USD so far this month. However October often sees some churn for risk assets, with the rand having recorded a low of R14.35/USD and a high of R15.20/USD in the past three and almost a half weeks.

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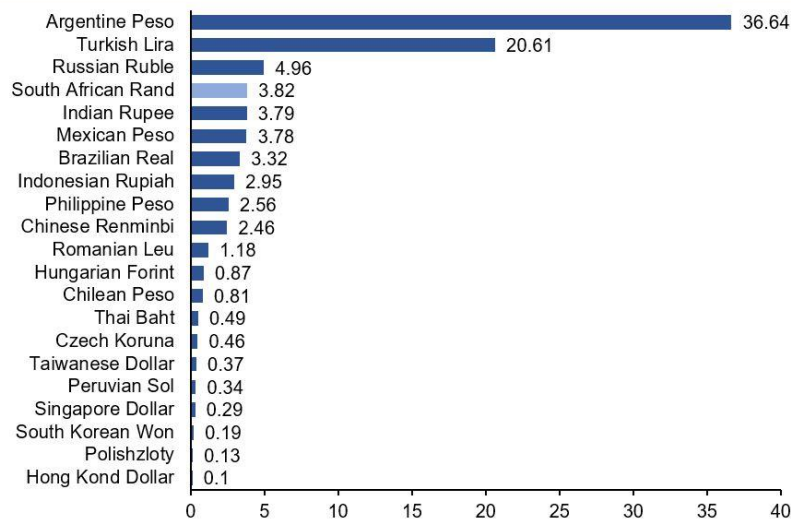




# SA Economics

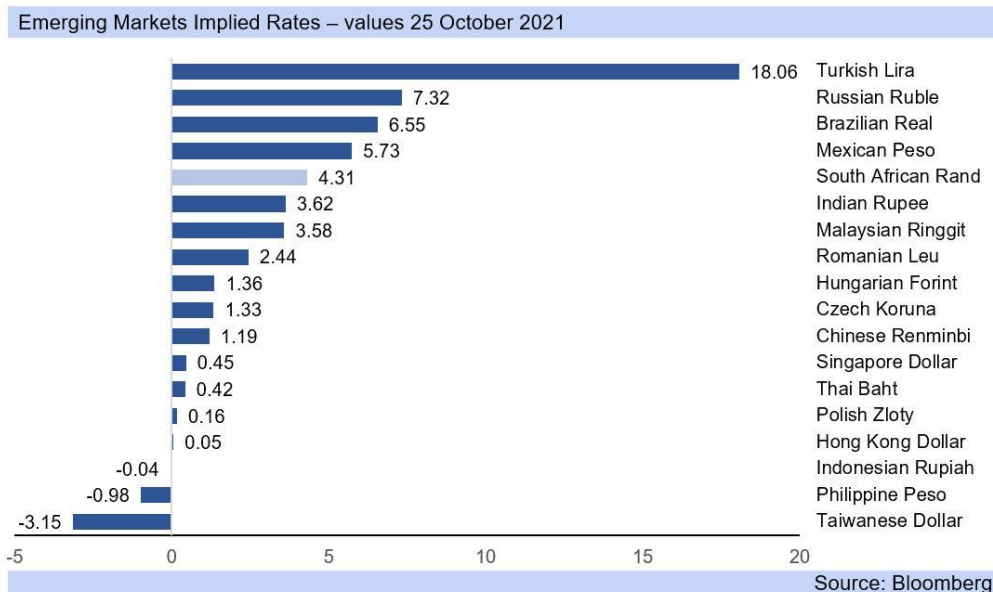


**Emerging Markets Interest Return – values 25 October 2021**



Source: Bloomberg

# SA Economics

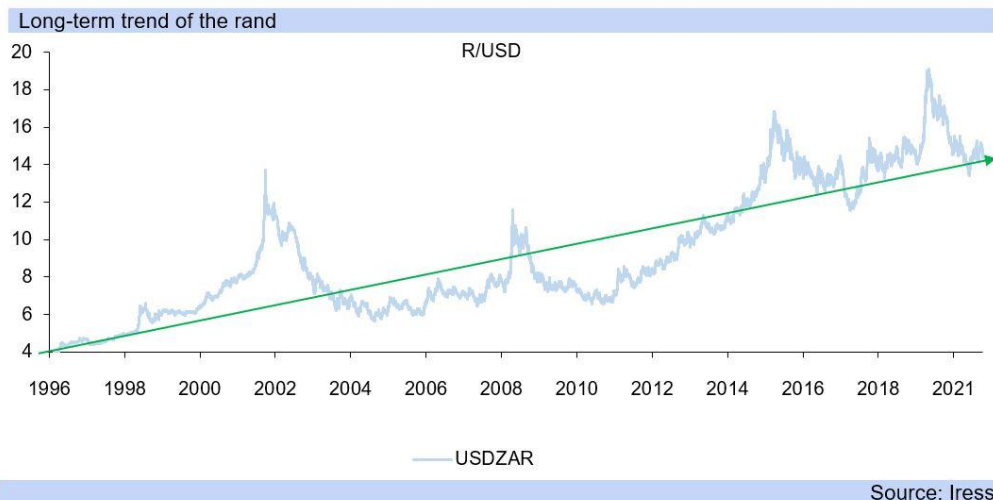


- Campaigning for SA's municipal elections is likely to be intense this week, but fade over the weekend as special voting begins on Saturday, and general voting on Monday 1st November. A recent poll shows the ANC is unlikely to obtain a majority in any of Gauteng's three metros.
- Such has been the waning support to the ANC since 2009, as the 'lost decade' saw economic growth fall and unemployment rise substantially. Zuma gained Presidency after Mbeki achieved a drop in unemployment to 21%, and exited in 2018 with unemployment at 27%.
- However, structural damage to the economy, such as the wholly insufficient electricity supply, saw unemployment continue to climb as the economy was constrained from achieving faster rates of growth, with the country's jobless rate reaching 29% in 2019, and 30% in Q1.21.
- Economic growth dropped to 0.1% qysa by Q1.20 (or 0.7% qysaa), from above 5.0% during the Mbeki period, and it is reported the ANC has now included ex-Presidents Mbeki and Motlanthe in its campaigning as voters identify unemployment as their biggest concern.
- However voter appetite is low, and a low turnout at the polls is expected. This has likely inspired politicians to intensify campaigning but risks a deterioration in business confidence if it becomes extreme, and specifically anti the private business sector and so anti job creation.
- Post elections, business confidence would be at risk too on a marked swing to the left/ to extreme left in the results, as left wing political parties are typically anti-private businesses, favouring increased state control and heavy regulations, which suppress business activity.

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- Globally, high oil prices continue to increase inflationary fears, with the Brent crude oil price today at US\$86/bbl, worrying financial markets and causing some risk off as the potential for a November tapering of QE is seen as a risk, now, increasing rand volatility.
- The run up to the November FOMC meeting on the 3<sup>rd</sup> will see close scrutiny, with the all important US core PCE deflator due out on Friday and GDP on Thursday, which markets' will gauge for a November or December taper, with worries on stagflation in particular.
- The rand is likely to remain highly volatile, heavily afflicted by events in global financial markets, but still tending towards R14.70/USD dollar this quarter, although US data outcomes this week may have the potential for a severe impact on the rand.



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	14.96	14.13	14.64	15.50	16.00	16.65	16.90	17.00	17.50	17.60	17.50	17.20
GBP/ZAR	20.63	19.75	20.18	21.52	22.96	24.39	25.18	25.75	25.90	25.52	25.03	24.60
EUR/ZAR	18.03	17.03	17.26	18.35	19.28	20.31	20.96	21.25	21.88	22.00	21.88	21.50
ZAR/JPY	7.09	7.75	7.52	7.08	6.69	6.31	6.15	6.12	6.00	6.08	6.11	6.22
CHF/ZAR	16.52	15.51	15.95	16.65	17.21	17.98	18.38	18.48	19.23	19.34	19.23	18.90
AUD/ZAR	11.56	10.88	10.76	11.43	12.00	12.49	12.84	13.09	13.65	13.73	13.65	13.42
GBP/USD	1.38	1.40	1.38	1.39	1.43	1.46	1.49	1.51	1.48	1.45	1.43	1.43
EUR/USD	1.21	1.21	1.18	1.18	1.21	1.22	1.24	1.25	1.25	1.25	1.25	1.25
USD/JPY	106	109	110	110	107	105	104	104	105	107	107	107

Note: averages, Source: Investec, Iress



# 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	14.96	14.13	14.64	14.00	13.50	13.40	13.20	13.00	12.80	12.60	12.55	12.30
GBP/ZAR	20.63	19.75	20.18	19.44	19.37	19.63	19.67	19.69	18.94	18.27	17.95	17.59
EUR/ZAR	18.03	17.03	17.26	16.58	16.27	16.35	16.37	16.25	16.00	15.75	15.69	15.38
ZAR/JPY	7.09	7.75	7.52	7.84	7.93	7.84	7.88	8.00	8.20	8.49	8.53	8.70
CHFZAR	16.52	15.51	15.95	15.04	14.52	14.47	14.36	14.13	14.07	13.85	13.79	13.52
AUDZAR	11.56	10.88	10.76	10.32	10.13	10.05	10.03	10.01	9.98	9.83	9.79	9.59
GBP/USD	1.38	1.40	1.38	1.39	1.43	1.46	1.49	1.51	1.48	1.45	1.43	1.43
EUR/USD	1.21	1.21	1.18	1.18	1.21	1.22	1.24	1.25	1.25	1.25	1.25	1.25
USD/JPY	106	109	110	110	107	105	104	104	105	107	107	107

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	14.96	14.13	14.64	16.00	16.80	17.50	18.00	18.50	18.70	19.20	19.55	19.70
GBP/ZAR	20.63	19.75	20.18	22.21	24.11	25.64	26.82	28.02	27.68	27.84	27.96	28.17
EUR/ZAR	18.03	17.03	17.26	18.94	20.24	21.35	22.32	23.13	23.38	24.00	24.44	24.63
ZAR/JPY	7.09	7.75	7.52	6.86	6.37	6.00	5.78	5.62	5.61	5.57	5.47	5.43
CHFZAR	16.52	15.51	15.95	17.19	18.08	18.89	19.58	20.11	20.55	21.10	21.48	21.65
AUDZAR	11.56	10.88	10.76	11.79	12.60	13.13	13.68	14.25	14.59	14.98	15.25	15.37
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EUR/USD	1.21	1.21	1.18	1.18	1.21	1.22	1.24	1.25	1.25	1.25	1.25	1.25
USD/JPY	106	109	110	110	107	105	104	104	105	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	14.64	13.80	13.30	13.00	12.90	12.80	12.70	12.50	12.30	12.15
GBP/ZAR	20.63	19.75	20.18	19.16	19.08	19.04	19.22	19.39	18.80	18.13	17.59	17.37
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CHFZAR	16.52	15.51	15.95	14.83	14.31	14.04	14.03	13.91	13.96	13.74	13.52	13.35
AUDZAR	11.56	10.88	10.76	10.17	9.98	9.75	9.80	9.86	9.91	9.75	9.59	9.48
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