

SA Economics

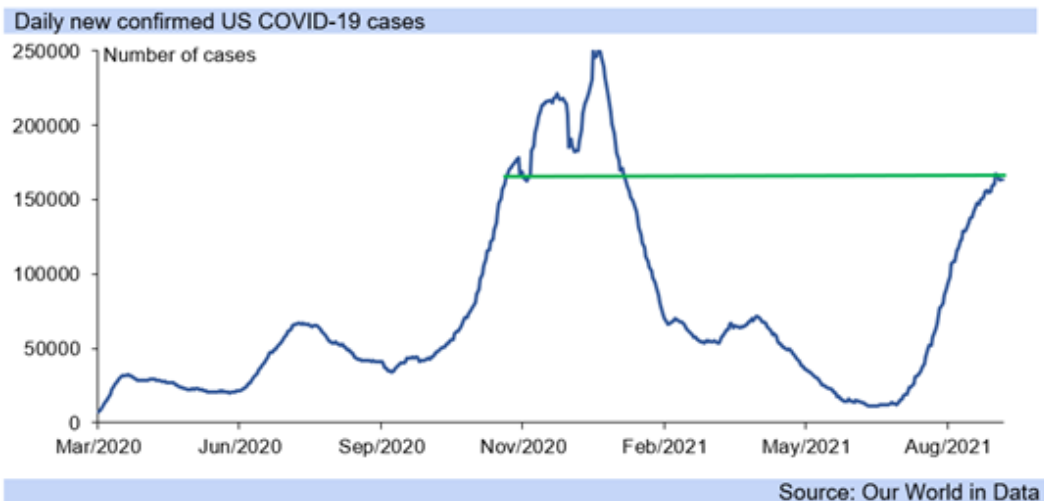


Monday 6 September 2021

Rand note: the rand strengthens towards R14.00/USD, at R14.25/USD today, as the growing COVID-19 third wave in the US continues to negatively impact its economic data, potentially reducing the speed of tapering

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



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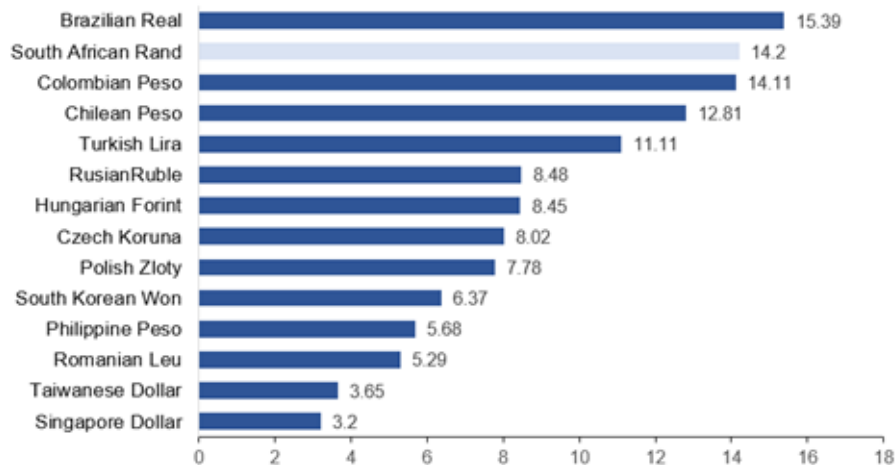


United States daily confirmed COVID-19 deaths, seven day rolling average



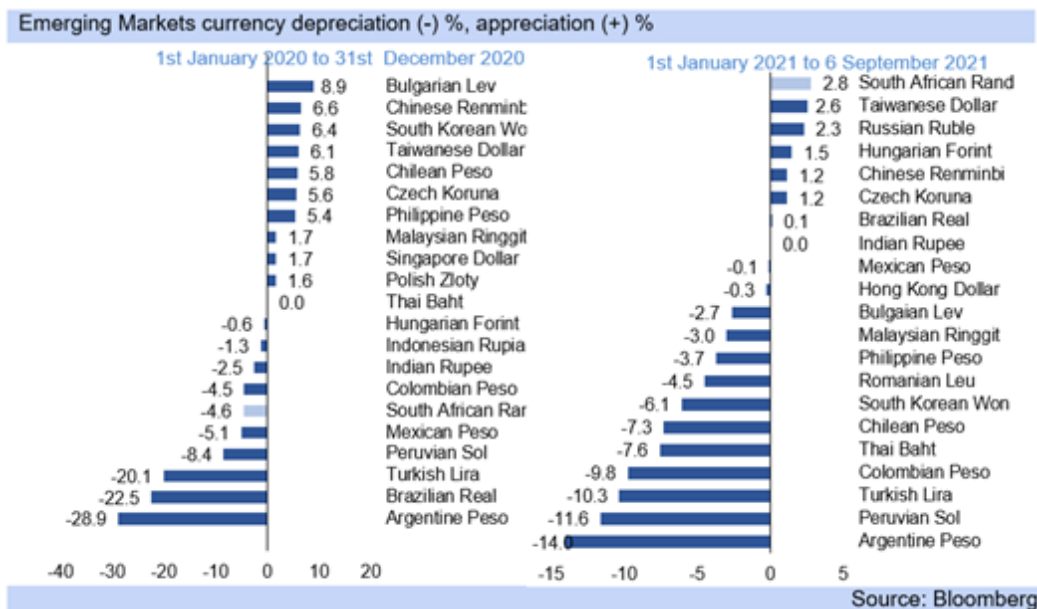
Source: Our World in Data

Emerging Markets Implied Volatilities – values as at 6 September 2021



Source: Bloomberg

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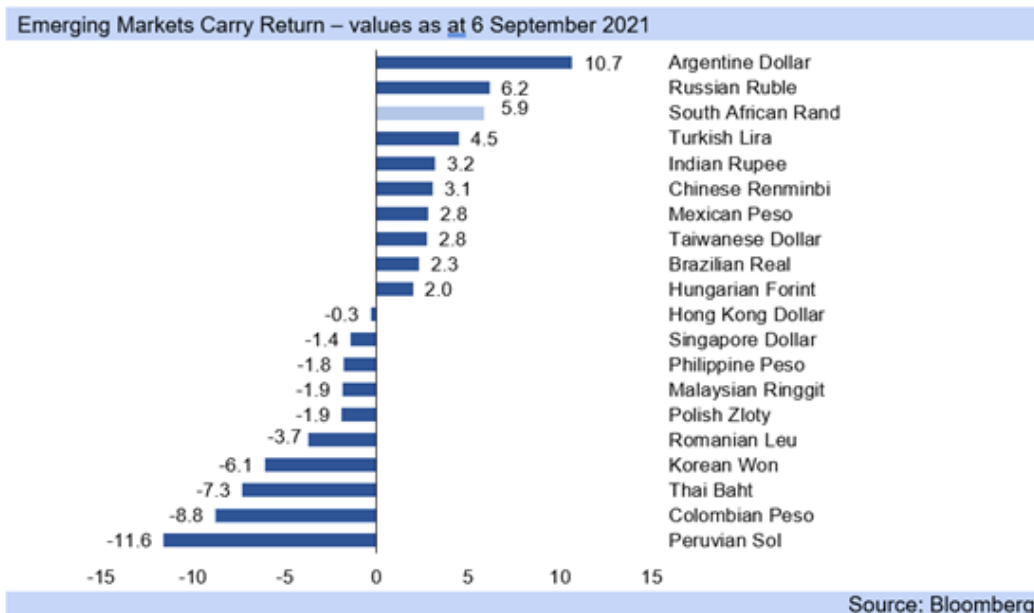
- The US continues to see a marked rise in its third wave of COVID-19 infections which is having a negative impact on consumer sentiment as well as market expectations for the rapidity of QE tapering, which previously was strongly anticipated for November even.
- The Fed Chair's comments on a dovish tapering process are increasingly being heard by the markets, after his Jackson Hole address, as key economic data readings continue to show a propensity to disappoint on the downside while the third wave builds.
- Deaths too are surging across the US as the delta variant spreads rapidly, with just over half of the population vaccinated, and hard-line anti vaxxers persisting in still significant numbers, while Dr Fauci highlights a number of new variants of interest have emerged.
- New variants of interest include mu, which has been identified to have some similar characteristics as the delta variant, but the mu variant possibly may be able to surpass certain antibodies and so some vaccines. It has been found in around forty countries so far.
- A variant of interest has the potential to do more harm than the strain it mutated from, with four others also of interest, eta, iota, kappa and lambda. The spread of delta through the US has already negatively impacted confidence measures, with worries over its growth outlook.
- A tightening of lockdown restrictions is still not widely expected, in the face of strong anti-lockdown sentiment in the US. The Fed is likely to remain in no hurry to cause substantial QE reduction given the uncertainty, with its dovish approach having sparked some risk taking.
- In particular, the Fed watches financial market sentiment, and if this starts to flag and turn significantly negative, it could also add to the FOMC's caution in reducing QE. The third wave of deaths and cases has not yet peaked, and risks worsening substantially.

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- The seven-day rolling average of new US COVID-19 deaths is seven times higher than at the start of the third wave and still growing on the rapid rise in COVID-19 underway. There is evidence of some weakening in some areas of the US economy as COVID-19 cases climb.
- The rand currently averages R14.64/USD and is on track to average R14.55/USD for the quarter, if not slightly stronger, as the rand continues to attempt to pull towards R14.00/USD. US economic data releases will continue to remain key.

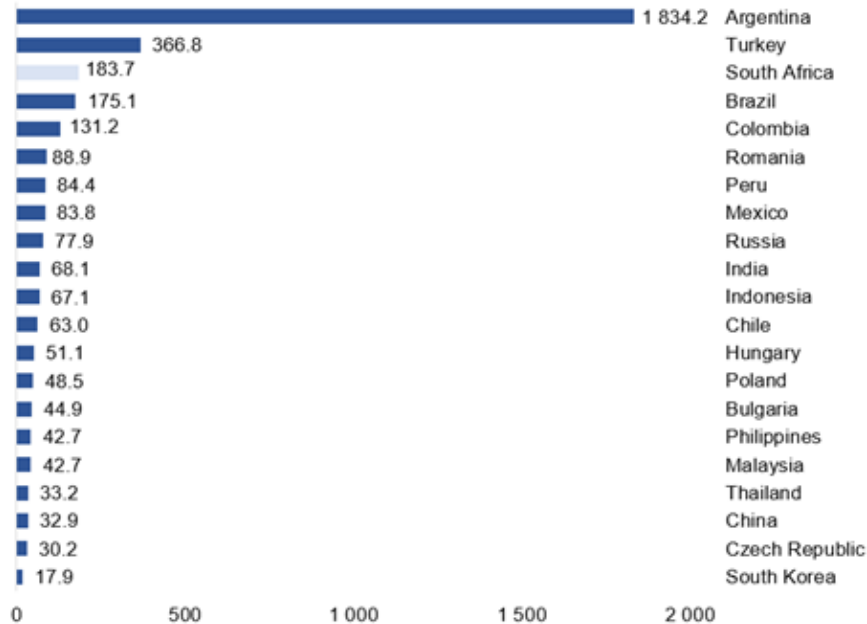
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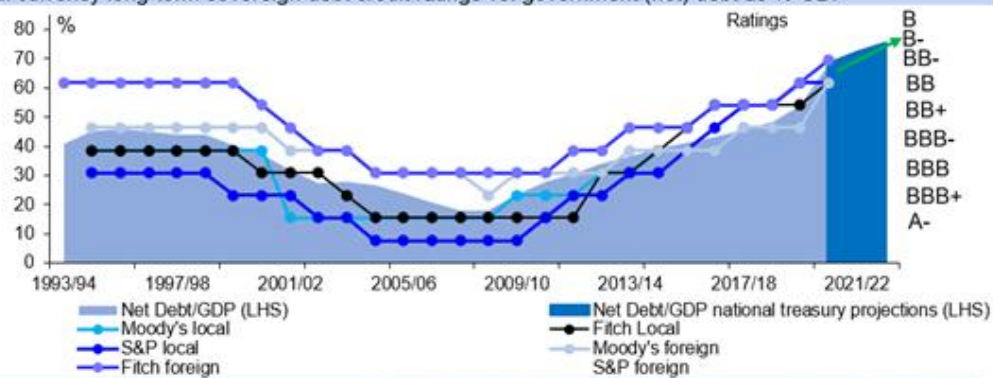


Emerging Markets CDS Spreads – values as at 6 September 2021



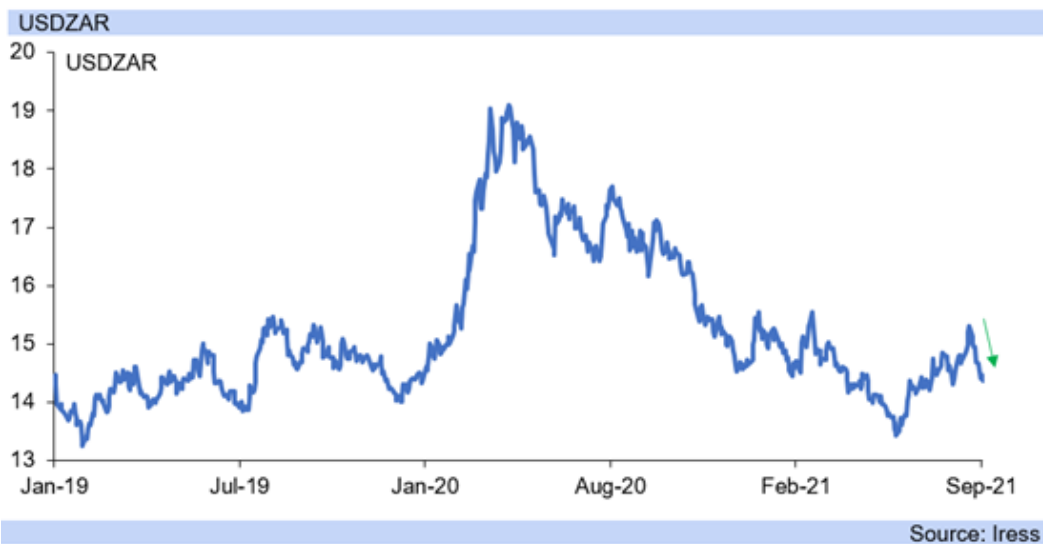
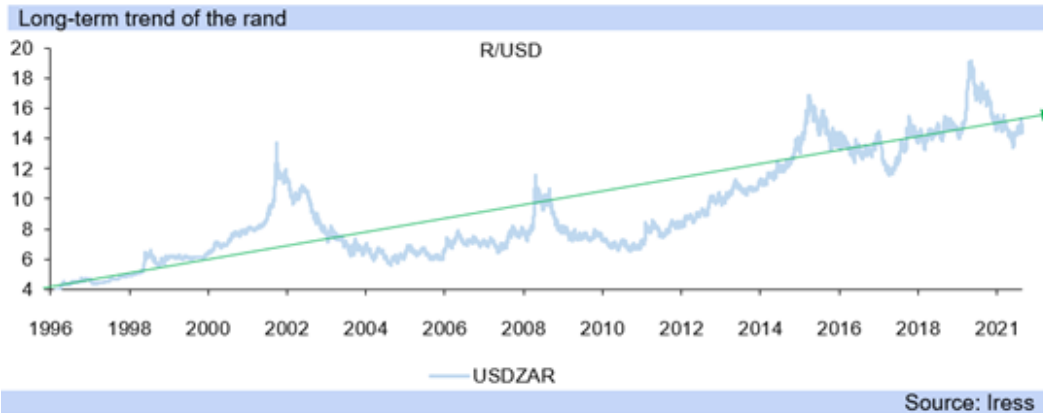
Source: Bloomberg

Local currency long-term sovereign debt credit ratings vs. government (net) debt as % GDP



Source: Credit rating agencies, National treasury, Bloomberg

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- Domestically, with the courts requiring the municipal elections to go ahead around the end of October, start of November, what is traditionally a calm period for the rand, when the rand typically sees some strength, could instead be one of higher volatility.
- This would particularly be the case if electioneering got very heated, with already a reported pro-Zuma march in Durban this weekend at the student level and dispersed by the police, and some of the mobilisers arrested.
- Coming after the destructive unrest in July, these events negatively impact sentiment, and have the potential to do so much more severely, as electioneering political parties, particularly the radical ones do not worry over negatively affecting business and investor confidence.

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- September is typically a period for global financial markets where risk-off can subside, and while some churn is evident, risk-taking can start to pick up, and further dovish comments from the Fed would support this.
- However, SA also sees the MTBPS in early November, and with the damage to the fiscus from the lockdown restrictions on economic activity, along with the additional spending after the riots, and ongoing aid to SOEs, the land bank etc. risk to fiscal consolidation remains.
- There is also ratings risks as well, with the agencies due to review SA's ratings post the MTBPS and two of the three key agencies still have SA on a negative outlook. For many reasons, the rand would face headwinds in convincingly piercing R14.00/USD.
- Instead, the domestic currency is likely to remain above R14.00/USD for the remainder of this year, unless the FOMC becomes very clear in communicating that QE tapering is unlikely this year, and even early next year, and that it will then be very gradual.
- Absent this, and with other EM currencies tightening interest rates, the rand will be at risk of weakness next year. The long-term trend of the rand is also one of weakness, with weak growth, lack of substantial fiscal consolidation and structural reforms key issues.
- If the SARB hikes interest rates by more than expected this will support the domestic currency, but it will continue to remain volatile, with SA seeing little to materially boost economic growth, such as change in mining legislation to heavily support exploration.

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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	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). Strong global growth, commodity boom. Stabilisation of credit ratings, then credit rating upgrades.								
Up case 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. 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.								
Base case 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– sufficient global and domestic monetary and other policy supports to growth and financial markets occur and risk sentiment stabilises then improves. 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.								
Lite (domestic) Down case 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. 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. 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	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). 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. 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
CHF/ZAR	16.52	15.51	16.45	16.90	17.50	18.12	18.46	18.63	19.23	19.34	19.23	18.90
AUD/ZAR	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
CHF/ZAR	16.52	15.51	14.87	14.72	14.55	14.59	14.42	14.24	14.07	13.85	13.79	13.52
AUD/ZAR	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

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
CHF/ZAR	16.52	15.51	14.65	14.39	14.22	14.04	13.98	13.91	13.74	13.52	13.35	13.19
AUD/ZAR	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
CHFZAR	16.52	15.51	16.99	17.88	18.59	19.05	19.66	20.27	20.55	21.10	21.48	21.65
AUDZAR	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
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												