

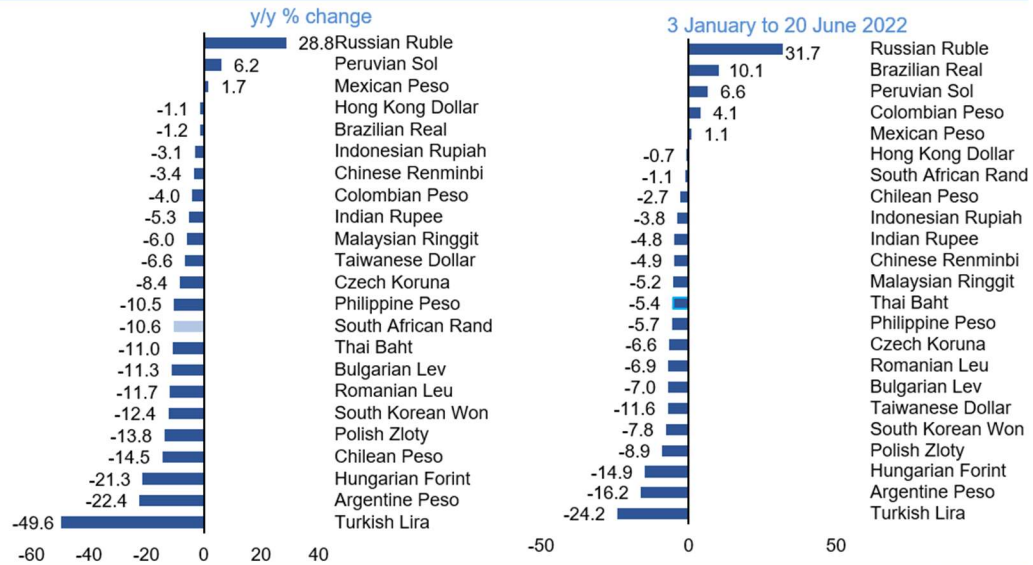


SA Economics

Monday 20 June 2022

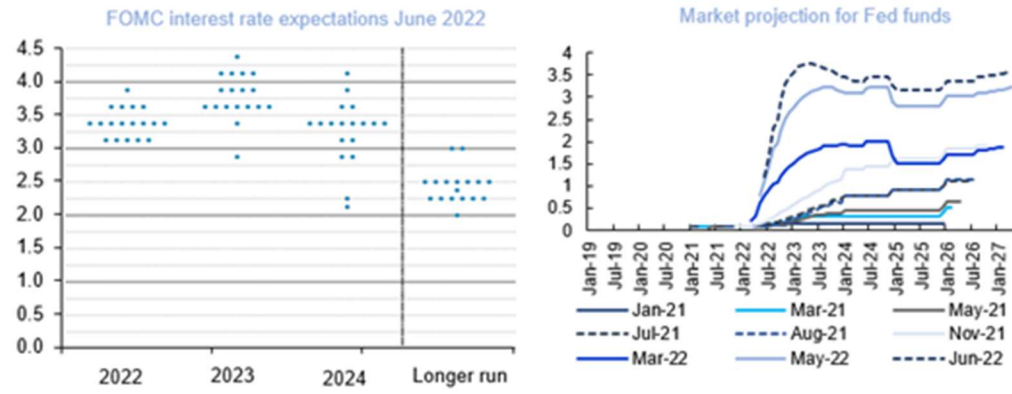
Rand note: the rand is still on track to average R15.60/USD in Q2.22, but H2.22 is at risk from the deteriorating global environment

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



Source: Bloomberg

US interest rate projections



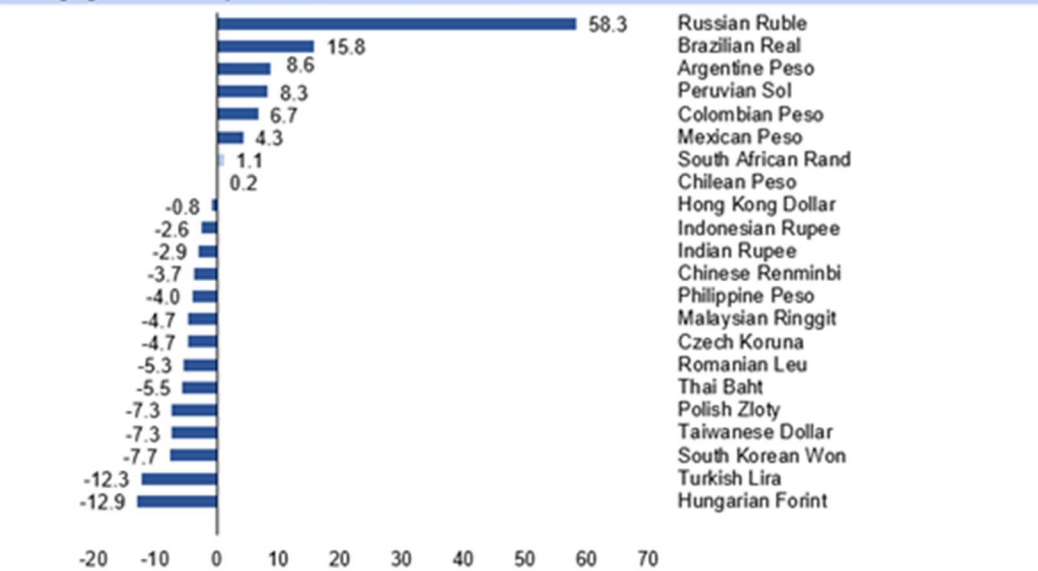
Source: FOMC, Bloomberg

Fed Fund Futures implied rates – 20th June 2022

Meeting	#Hikes/Cuts	% Hike/Cut	Implied Rate Δ	Implied Rate	A.R.M
07/27/2022	+2.847	+284.7%	+0.712	2.307	0.250
09/21/2022	+5.279	+243.2%	+1.320	2.915	0.250
11/02/2022	+7.005	+172.5%	+1.751	3.347	0.250
12/14/2022	+8.047	+104.3%	+2.012	3.608	0.250
02/01/2023	+8.597	+55.0%	+2.149	3.745	0.250

Source: Bloomberg

Emerging Markets Carry Return – values 20 June 2022



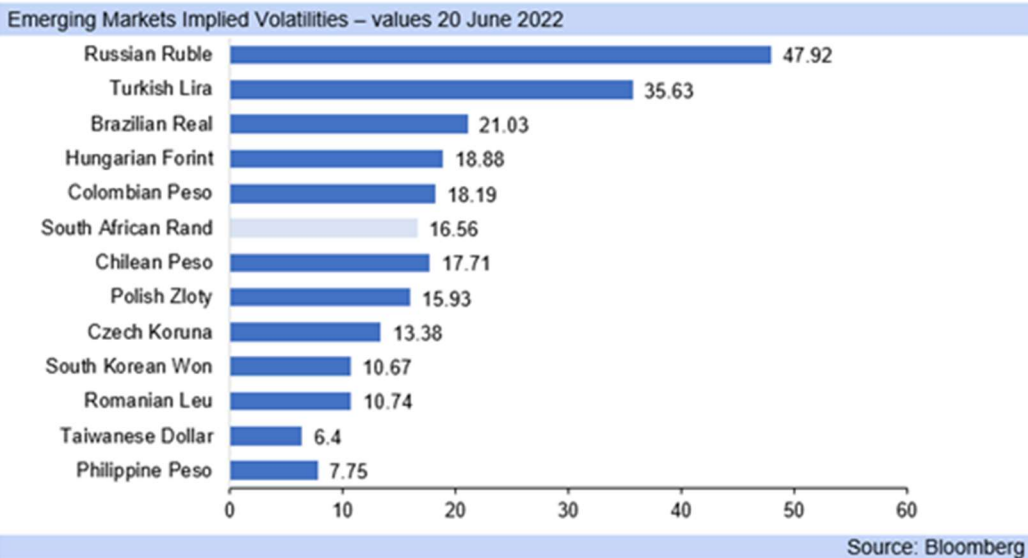
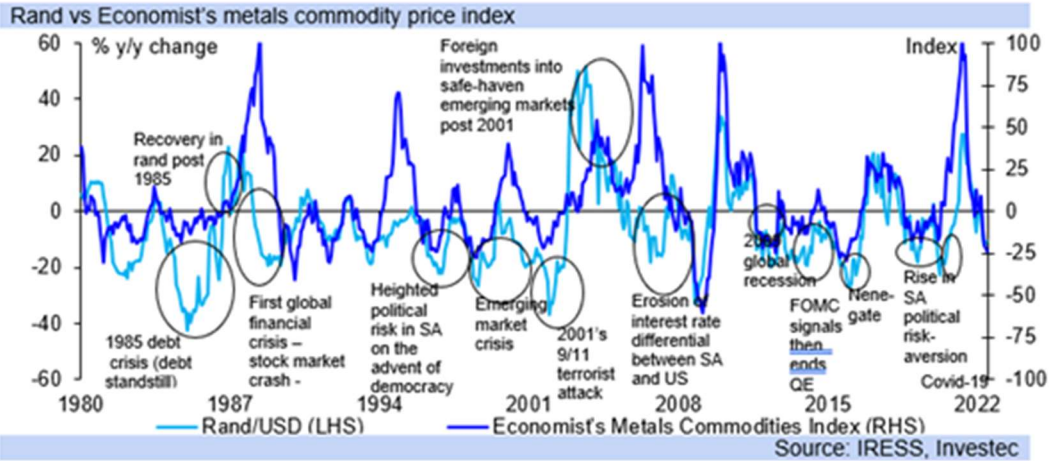
Source: Bloomberg

Expected Case: Exchange Rate forecasts												
	2022				2023				2024			
	Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.23	Q4.22	Q1.24	Q2.24	Q3.24	Q4.24
USD/ZAR	15.21	15.60	15.80	15.40	15.21	15.60	15.80	15.40	15.21	15.60	15.80	15.40
GBP/ZAR	20.40	19.64	19.99	19.87	20.40	19.64	19.99	19.87	20.40	19.64	19.99	19.87
EUR/ZAR	17.07	16.57	16.91	16.79	17.07	16.57	16.91	16.79	17.07	16.57	16.91	16.79
ZAR/JPY	7.65	8.17	7.94	8.05	7.65	8.17	7.94	8.05	7.65	8.17	7.94	8.05
CHF/ZAR	16.47	16.07	16.26	15.84	16.47	16.07	16.26	15.84	16.47	16.07	16.26	15.84
AUD/ZAR	11.02	11.18	11.61	11.63	11.02	11.18	11.61	11.63	11.02	11.18	11.61	11.63
GBP/USD	1.34	1.26	1.27	1.29	1.32	1.35	1.36	1.37	1.40	1.43	1.45	1.46
EUR/USD	1.12	1.06	1.07	1.09	1.11	1.13	1.14	1.15	1.18	1.20	1.23	1.25
USD/JPY	116	127	126	124	122	121	120	120	118	115	110	107

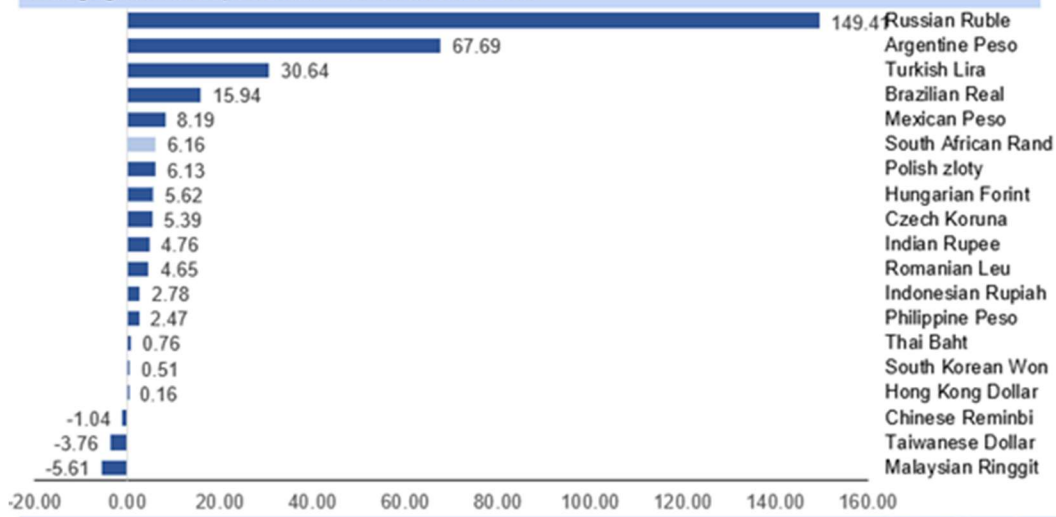
Note: averages, Source: Investec, Iress

- With US CPI inflation surprising markets on the upside recently, Thursday's 75bp hike was built into expectations for the Fed's fund rate, and the rand saw little sustained reaction, still around R16.00/USD, and on track to average R15.60/USD this quarter.
- The US interest rate move reinforces the likelihood of a 50bp, instead of a 25bp, hike by the SARB in July, although SA's FRA curve is now factoring in a larger hike (so far 66bp have been built in as the markets start to lean towards 75bp at SA's next MPC).
- Currently, we continue to expect a 50bp lift in SA's repo rate from the MPC in July, with the SARB likely to follow the direction, but not necessarily the exact moves of the FOMC, which has hiked in consecutive 25bp, 50bp and 75bp tranches so far this year.
- The FOMC warns that "the current picture is plain to see: The labor market is extremely tight, and inflation is much too high", "(i)t is essential that we bring inflation down if we are to have a sustained period of strong labor market conditions that benefit all."
- The Fed noted that in May "there was a broad sense ... that a ... (50bp) change should be considered at ... (June's) meeting ... (but) inflation has again surprised to the upside, ... inflation expectations have risen, and projections for inflation this year have been revised up".
- Then Fed funds implied rate for the July FOMC meeting is now just above 70bp in the financial markets, with the very hawkish commentary from the Fed aligned towards further large rate hikes, with the dot plot showing another 175bp in US rate hikes in H2.22.
- Failure for US inflation to turn the corner and begin sustainably subsiding would further add to pressure on US interest rates, driving further financial market risk-off, with a mild US recession over the turn of this year only currently seen as a risk.
- The FOMC worries that a wage-price spiral is developing, stating "(t)he labor market has remained extremely tight, with the unemployment rate near a 50- year low, job vacancies at historical highs, and wage growth elevated", while lowering its GDP projections.
- The Fed is expected to continue to move aggressively this year to stamp out high inflation, and will not be adverse to causing weakness in the labour market, and in the US economy, to break the upwards shift in US wage increases, with further rand weakness the risk.

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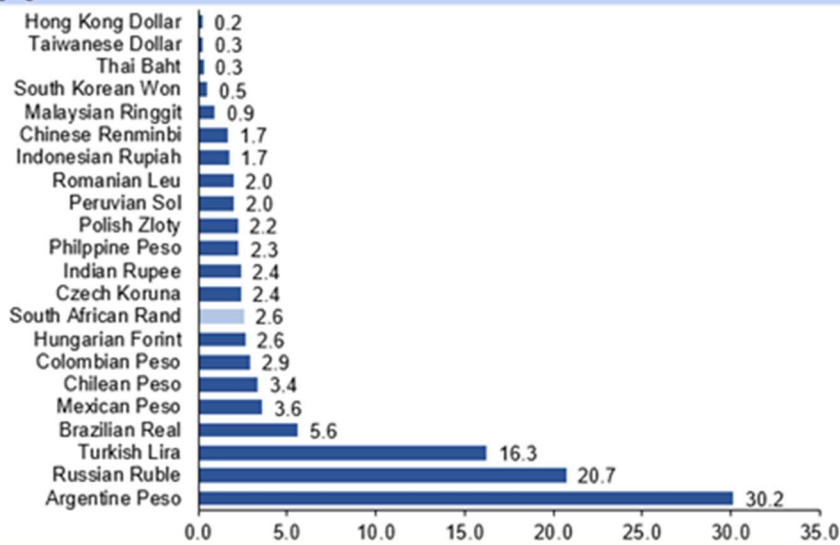


Emerging Markets Implied Rates – values 20 June 2022

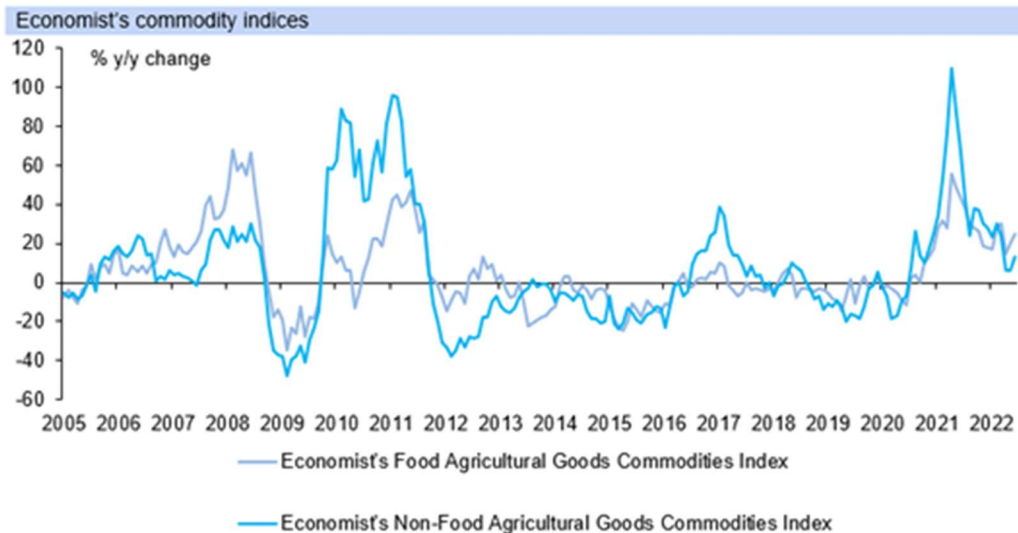


Source: Bloomberg

Emerging Markets Interest Return – values 20 June 2022



Source: Bloomberg



Source: IRESS, Economist

- The rand is currently expected to average R15.80/USD in Q3.22, but the Ukrainian President, Zelensky, has warned of the Russian invasion intensifying, and NATO is now warning that the war could last for years, providing no end in sight for related price pressures.
- NATO Secretary-General Jens Stoltenberg is reported to have said "(w)e must not weaken in our support of Ukraine, even if the costs are high -- not only in terms of military support but also because of rising energy and food prices", "we must be prepared for this to last for years."
- Russia is targeting Mykolaiv, strategic to Ukraine's main port, Odessa, on the Black Sea, after having blockaded its ports. Romania is now exporting grain for the Ukraine, which is reported to have 20million tones to clear before its new harvest comes in.
- The port of Constanta, the fastest cereal clearing Port in the EU, and the Ukraine is sending grain to it by land or along the Danube River by barge, while Romania is increasing its capacity to rapidly unload the Ukrainian barges, which should be ready by the end of June.
- President Zelensky warns "there may be a physical shortage of products in dozens of countries around the world. Millions of people may starve if the Russian blockade of the Black Sea continues," with agricultural prices likely to feel further pressure.
- Sanctions against Russia are likely to persist for longer than anticipated, further supporting high agricultural and energy commodity prices. Russia and the Ukraine account for a third of the world's wheat and two thirds of sunflower production.
- Export volumes of Ukrainian grain are reported to have dropped by 80% since the Russian/Ukraine war began. Food price pressures are not expected to collapse in the near term, while input costs are risking too, and not just from elevated fertilizer prices.
- Inflation has surprised global (and local) financial markets on the upside this year, and the Fed notes inflation surprises, and related jumps in inflation expectations and wages as its key concern, not US economic growth, which is likely to weaken in H2.22.

- The risk is that the US economy slows more quickly than its policy makers and markets anticipate, with a recession, and not necessarily a mild one, spooking markets as stagflation worsens on obdurate supply side price pressures, weakening the rand.

Economic Scenarios: note up case rises		Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.23	Q4.23
Extreme	USD/Rand (average)	15.21	14.00	13.80	13.70	13.60	13.40	13.30	13.10
Up case	Repo rate (end rate)	4.25	4.00	4.00	3.75	3.75	3.75	3.50	3.50
1%	Impact of Covid-19 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 other EW or nationalisation. High business confidence and fixed investment growth, substantial FDI, strong fiscal consolidation (state debt falls back to low ratios of 2000s). Very subdued domestic inflation on extreme rand strength, rapid capacity expansion and very favourable weather conditions. Strong global growth, commodity boom. Stabilisation of credit ratings, then upgrades.								
Up case	USD/Rand (average)	15.21	14.50	15.00	14.90	14.90	14.70	14.60	14.50
4%	Repo rate (end rate)	4.25	4.00	4.00	4.00	4.00	4.00	4.25	4.25
	Quick rebound from Covid-19 pandemic, rising confidence and investment levels - structural problems eroded. No further credit rating downgrades, become positive on fiscal consolidation (debt projections fall substantially). Global risk-on, global demand quickly returns to trend growth. Very limited impact of expropriation without compensation) to abandoned, labour tenants' and government land (individuals are new owners and receive title deeds) does not have a negative effect on economy - no nationalisation. Low domestic inflation on favourable weather conditions, rand strength reduction in state-controlled price inflation on increased private privatisation.								
Base case	USD/Rand (average)	15.21	15.60	15.80	15.40	15.20	15.60	16.00	15.50
50%	Repo rate (end rate)	4.25	4.75	5.50	5.50	5.75	5.75	6.00	6.00
	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 neutral to positive. 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 fiscal consolidation (debt to GDP stabilisation) occurs. Civil and political unrest wanes. Inflation impacted by normal course of weather patterns via food price inflation and rand, with modest transition to renewable energy and slow move away from fossil fuel usage, measures to alleviate impact of climate change on economy are modestly implemented.								
Lite	USD/Rand (average)	15.21	16.00	16.65	16.90	17.00	17.50	17.60	17.50
(domestic)	Repo rate (end rate)	4.25	5.00	5.75	5.75	6.00	6.00	6.25	6.50
Down case	The international environment (incl. 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. Very limited expropriation of private commercial sector property without compensation, with some negative impact on the economy. Business confidence depressed, marked rand weakness and higher inflation (adverse weather), significant load shedding and weak investment growth. Substantial fiscal consolidation ultimately occurs, preventing ratings falling into the C grades.								
39%									
Severe down case	USD/Rand (average)	15.21	16.80	17.50	18.00	18.50	18.70	19.20	19.55
6%	Repo rate (end rate)	4.25	5.25	6.00	6.25	6.50	7.00	7.50	7.75
	Lengthy global recession, global financial crisis – insufficient monetary and other policy supports to growth domestically and internationally. Depression in SA, severe rand weakness, very high inflation (very adverse weather). A somewhat wider level of nationalisation of private sector commercial property. SA rated single B from all three key agencies, with further rating downgrades eventually into CCC grade and the risk of moving towards default. Government borrows from increasingly wider sources as it sinks deeper into a debt trap), eventually include widespread civil unrest, services strike action and strike action.								

Note: Event risk begins Q222. Source: Investec

Lite Down Case: Exchange Rate forecasts												
	2022				2023				2024			
	Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.23	Q4.22	Q1.24	Q2.24	Q3.24	Q4.24
USD/ZAR	15.21	16.00	16.65	16.90	17.00	17.50	17.60	17.50	17.20	17.00	16.80	17.00
GBP/ZAR	20.40	20.14	21.06	21.80	22.36	23.54	23.94	23.89	24.08	24.31	24.36	24.82
EUR/ZAR	17.07	17.00	17.82	18.42	18.87	19.78	20.06	20.04	20.30	20.40	20.66	21.25
ZAR/JPY	7.65	7.97	7.54	7.34	7.18	6.89	6.82	6.86	6.86	6.76	6.55	6.29
CHFZAR	16.47	16.48	17.13	17.38	17.55	18.14	18.24	18.22	18.49	18.68	18.46	18.68
AUDZAR	11.02	11.47	12.24	12.76	13.09	13.83	14.08	14.00	13.42	13.26	13.10	13.26
GBP/USD	1.34	1.26	1.27	1.29	1.32	1.35	1.36	1.37	1.40	1.43	1.45	1.46
EUR/USD	1.12	1.06	1.07	1.09	1.11	1.13	1.14	1.15	1.18	1.20	1.23	1.25
USD/JPY	116	127	126	124	122	121	120	120	118	115	110	107

Note: averages, Source: Investec, Iress

Up Case: Exchange Rate forecasts												
	2022				2023				2024			
	Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.23	Q4.22	Q1.24	Q2.24	Q3.24	Q4.24
USD/ZAR	15.21	14.50	15.00	14.90	14.90	14.70	14.60	14.50	14.50	14.40	14.40	14.30
GBP/ZAR	20.40	18.25	18.98	19.22	19.59	19.77	19.86	19.79	20.30	20.59	20.88	20.88
EUR/ZAR	17.07	15.40	16.05	16.24	16.54	16.61	16.64	16.60	17.11	17.28	17.71	17.88
ZAR/JPY	7.65	8.79	8.37	8.32	8.19	8.20	8.22	8.28	8.14	7.99	7.64	7.48
CHFZAR	16.47	14.93	15.43	15.32	15.38	15.24	15.13	15.09	15.59	15.82	15.82	15.71
AUDZAR	11.02	10.39	11.03	11.25	11.47	11.61	11.68	11.60	11.31	11.23	11.23	11.15
GBP/USD	1.34	1.26	1.27	1.29	1.32	1.35	1.36	1.37	1.40	1.43	1.45	1.46
EUR/USD	1.12	1.06	1.07	1.09	1.11	1.13	1.14	1.15	1.18	1.20	1.23	1.25
USD/JPY	116	127	126	124	122	121	120	120	118	115	110	107

Note averages, Source: Investec, Iress

Extreme Up Case: Exchange Rate forecasts												
	2022				2023				2024			
	Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.23	Q4.22	Q1.24	Q2.24	Q3.24	Q4.24
USD/ZAR	15.21	14.00	13.80	13.70	13.60	13.40	13.30	13.10	12.90	12.80	12.60	12.30
GBP/ZAR	20.40	17.62	17.46	17.67	17.88	18.02	18.09	17.88	18.06	18.30	18.27	17.96
EUR/ZAR	17.07	14.87	14.77	14.93	15.10	15.14	15.16	15.00	15.22	15.36	15.50	15.38
ZAR/JPY	7.65	9.10	9.09	9.05	8.97	8.99	9.02	9.16	9.15	8.98	8.73	8.70
CHFZAR	16.47	14.42	14.20	14.09	14.04	13.89	13.78	13.64	13.87	14.07	13.85	13.52
AUDZAR	11.02	10.03	10.14	10.34	10.47	10.59	10.64	10.48	10.06	9.98	9.83	9.59
GBP/USD	1.34	1.26	1.27	1.29	1.32	1.35	1.36	1.37	1.40	1.43	1.45	1.46
EUR/USD	1.12	1.06	1.07	1.09	1.11	1.13	1.14	1.15	1.18	1.20	1.23	1.25
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Note: averages, Source: Investec, Iress

Severe Down Case: Exchange Rate forecasts												
	2022				2023				2024			
	Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.23	Q4.22	Q1.24	Q2.24	Q3.24	Q4.24
USD/ZAR	15.21	16.80	17.50	18.00	18.50	18.70	19.20	19.55	19.70	19.90	20.20	20.40
GBP/ZAR	20.40	21.15	22.14	23.22	24.33	25.15	26.11	26.69	27.58	28.46	29.29	29.78
EUR/ZAR	17.07	17.85	18.73	19.62	20.54	21.13	21.89	22.38	23.25	23.88	24.85	25.50
ZAR/JPY	7.65	7.59	7.17	6.89	6.59	6.44	6.25	6.14	5.99	5.78	5.45	5.25
CHFZAR	16.47	17.30	18.00	18.51	19.10	19.39	19.90	20.35	21.18	21.87	22.20	22.42
AUDZAR	11.02	12.04	12.86	13.59	14.25	14.77	15.36	15.64	15.37	15.52	15.76	15.91
GBP/USD	1.34	1.26	1.27	1.29	1.32	1.35	1.36	1.37	1.40	1.43	1.45	1.46
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