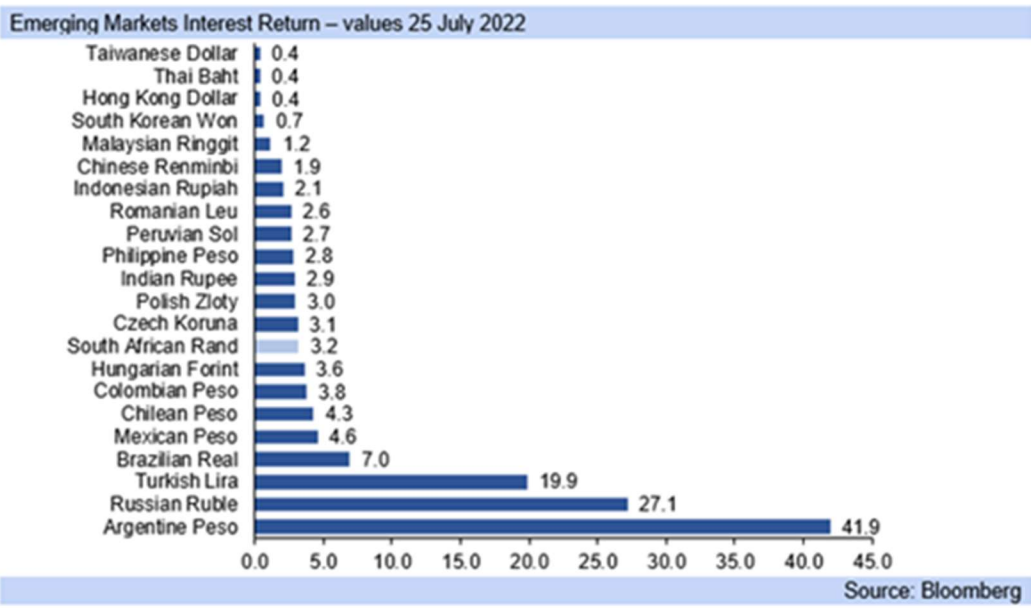




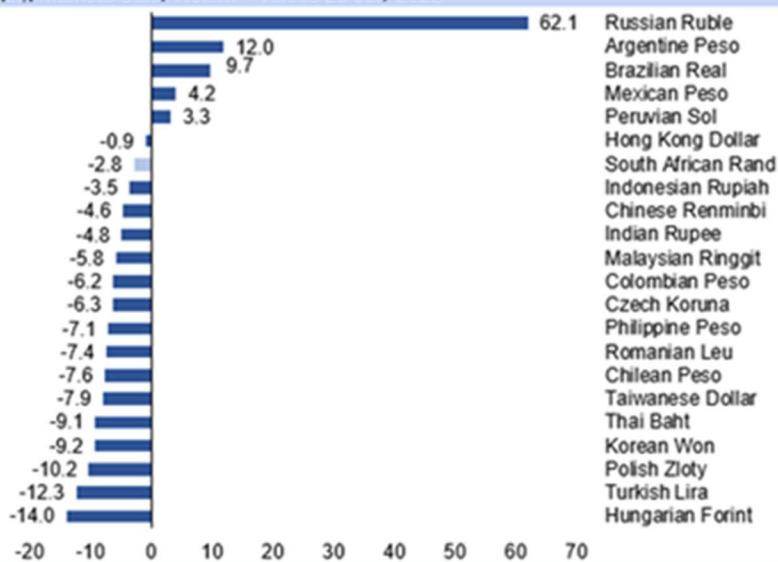
SA Economics

Monday 25 July 2022

Rand note: the mild weakness of the US dollar, along with last week's substantial SA interest rate hike, sees the rand gain



Emerging Markets Carry Return – values 25 July 2022

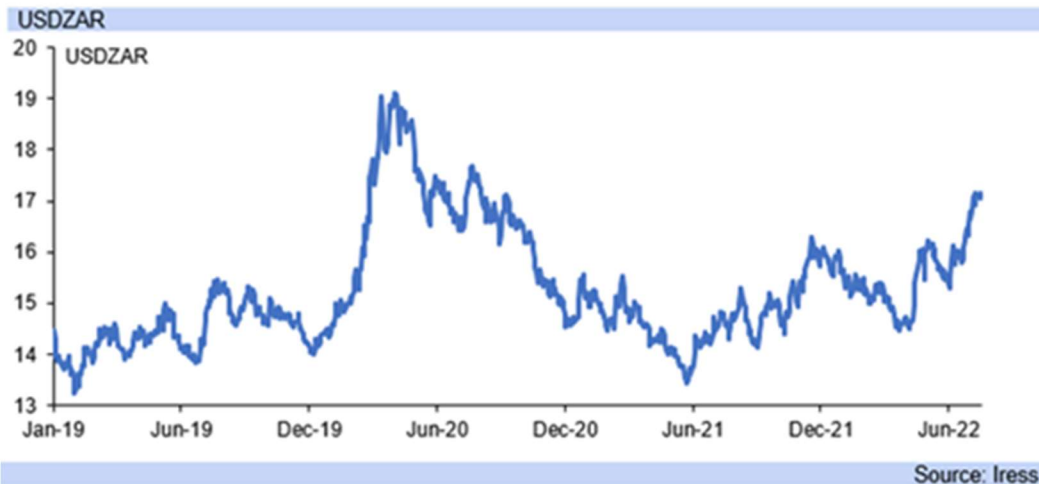


Source: Bloomberg

Economist's commodity indices



Source: IRESS, Economist



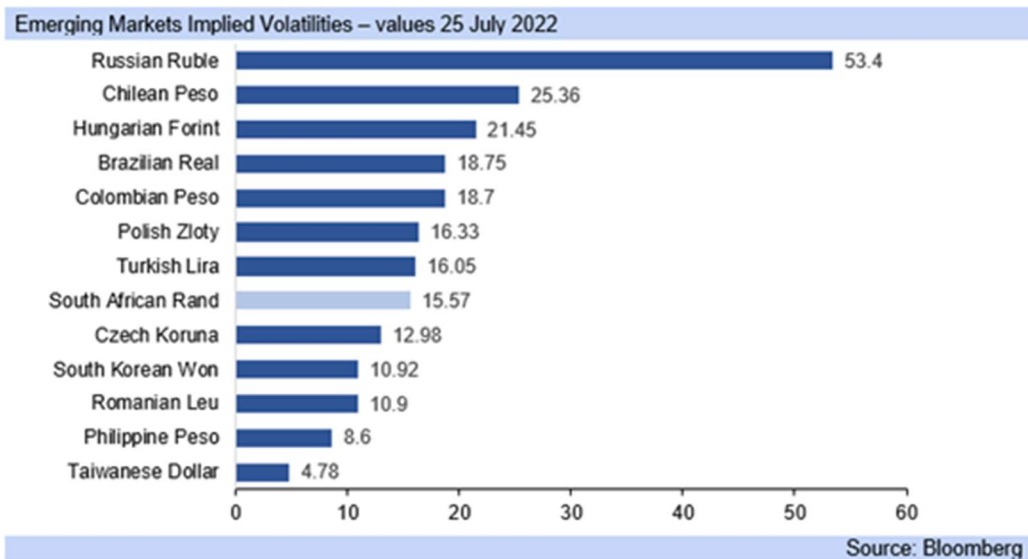
	Expected Case: Exchange Rate forecasts											
	2022				2023				2024			
	Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.23	Q4.23	Q1.24	Q2.24	Q3.24	Q4.24
USD/ZAR	15.21	15.59	16.60	15.80	15.60	16.00	16.40	15.90	15.70	16.20	16.70	16.20
GBP/ZAR	20.40	19.59	20.25	19.12	19.03	20.00	20.83	20.35	20.41	21.55	22.55	22.36
EUR/ZAR	17.07	16.60	17.76	17.22	17.32	18.08	18.70	18.29	18.53	19.44	20.54	20.25
ZAR/JPY	7.65	8.33	8.13	8.48	8.40	8.06	7.74	7.92	7.83	7.28	6.89	6.79
CHFZAR	16.47	16.15	17.47	16.81	16.77	17.39	18.02	17.47	17.25	17.80	18.35	17.80
AUDZAR	11.02	11.14	11.79	11.38	11.54	12.00	12.46	12.40	12.25	12.64	13.03	12.64
GBP/USD	1.34	1.26	1.22	1.21	1.22	1.25	1.27	1.28	1.30	1.33	1.35	1.38
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	130	135	134	131	129	127	126	123	118	115	110

Note: averages, Source: Investec, Iress

- The rand has strengthened to R16.71/USD, from R17.26/USD last week, with SA's 75bp hike matching June's FOMC's move, and the MPC's very hawkish tone of bolstering expectations that the SARB will not let SA's interest rate differential with the US narrow severely.
- The FRA curve did not fully factor in a 75bp hike at last week's MPC meeting, and as a consequence the rand has had room to strengthen significantly as markets digested the information from the meeting, and in particular the very hawkish tone of the SARB.
- Markets will continue digesting the MPC outcome this week, and the domestic currency has room to strengthen even further, although much will depend on the signals coming out from the US, with the latter likely to have a strong impact for the rand.
- SA's FRA (Forward Rate Agreement) curve currently anticipates that the SARB will only hike the repo rate by 50bp in September, while the November meeting is expected to deliver a 50bp hike but with a greater chance of 75bp.
- The FOMC meets this week and is expected to deliver a 75bp hike on the 27th July, which is fully factored in by the Fed Funds Futures. However, this will take the US lift in the cycle to 2.25%, while SA is at 2.00% currently, as SA saw a 75bp not 100bp hike last week.
- The differential between SA and US interest rates will consequently risk narrowing at the end of this week, causing some pressure on the rand. The US dollar has weakened somewhat ahead of the FOMC meeting, now at 1.02 dollars to the euro from parity earlier in the month.

- Risk aversion has subsided slightly, allowing the US dollar to lose some ground, with markets having pulled back somewhat, as recent US data showed some slightly better outcomes on the activity and inflation front than expected, although the pull back is relatively small.
- The US's strongly positive empire state building manufacturing survey on general business conditions for June (released 15th July) cheered markets (a negative outturn was expected, and the University of Michigan reading, and US retail sales were also market positive.
- As the rand is largely determined by international events, particularly those taking place in the US, the better than expected US data recently has allowed safe haven flows to calm somewhat, and the advancing US dollar to pull back.

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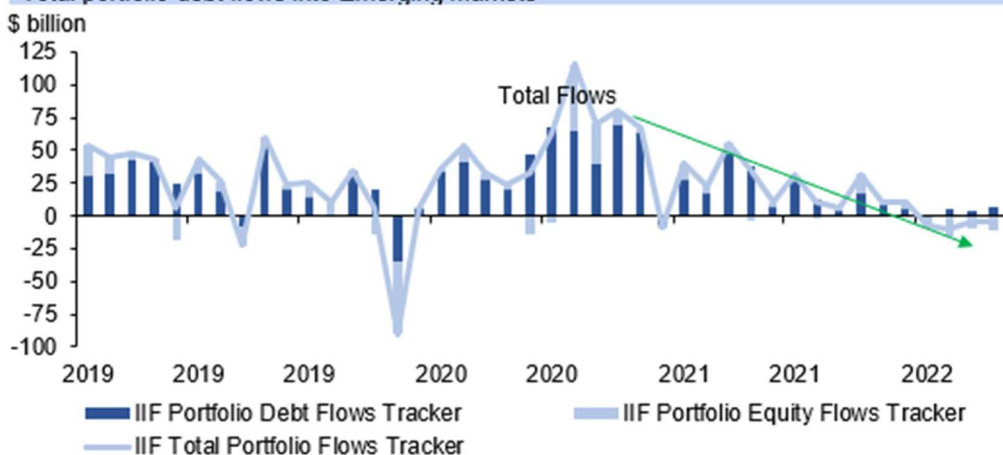


Emerging Markets currency depreciation (-) %, appreciation (+) %



Source: Bloomberg

Total portfolio debt flows into Emerging Markets



Source: IIF



- The rand has seen less volatility in 2022 than other key emerging market currencies, in the middle of the pack on SA's interest rate return, and the implied volatilities, running alongside the USD index, while against the EUR and GBP it has been relatively more stable.
- Risk aversion is still elevated however, despite having subsided somewhat since the middle of the month, and there is likely to be further market volatility this quarter, which will impact emerging market currencies, and so the rand.
- In particular, SA's interest rate hikes are not expected to keep up with (nor exceed) the moves in US interest rates initially, and consequently the rand is at risk of some further weakness this quarter, and in particular of some volatility.
- Foreigners remain net sellers of SA government bonds this quarter so far (Bloomberg JSE settled data for foreigner purchase, sales of SA bonds) at -R11.5bn. Foreigners also sold-off -R11.5bn of SA equities (net of purchases) in Q3.22 to date (Iress).

- The second, and particularly third, quarters of the year are usually weak periods for the rand, as trade thins in risk assets, including EM currencies and portfolio assets as the July/August months of peak northern hemisphere summer sees senior (risk-taking) traders on vacation.
- While the MPC meetings, at about two month intervals, are out of sync with those of the FOMC which tend to occur every six weeks, the MPC can hike between meetings, and if the differential between SA and US interest rates becomes significantly narrowed it may do so.
- Should the Fed deliver a 100bp hike this week (not expected), the rand will likely weaken, while a smaller move (50bp) could see rand strength, although the most likely outcome is the 75bp lift in the fed funds rate that the markets anticipate.
- The SARB has shown more concern about the recent rand weakness than it has tended to do historically, and will likely worry if the domestic currency tracks towards R18.00/USD, and so could deliver an inter meeting repo rate adjustment higher.
- The risk of recession has not disappeared however, and rapid rand strength back to R14.00/USD this quarter is unlikely, instead we have weakened our forecast modestly, as the risks to the global economy are likely to be seen to persist in H2.22 and over 2023.

Economic Scenarios: note updated forecasts									
		Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.23	Q4.23
Extreme Up case	USD/Rand (average)	15.21	15.59	14.00	13.80	13.70	13.60	13.40	13.30
	Repo rate (end rate)	4.25	4.75	4.00	3.75	3.75	3.75	3.50	3.50
1%	SA economic growth rises to 3–5%, then 5-7%. Good governance, growth-creating reforms (structural constraints eradicated), strong property rights, no nationalisation or expropriation without compensation. High business confidence and fixed investment growth, substantial FDI, fiscal consolidation drives debt to low ratios of 2000s. Very subdued domestic inflation on extreme rand strength, very favourable weather conditions. Strong global growth, risk-on, commodity boom. Rapid upgrades of credit ratings. Strong transition away from fossil fuel usage, a quick transition to renewable energy.								
Up case	USD/Rand (average)	15.21	15.59	15.00	14.90	14.90	14.70	14.60	14.50
	Repo rate (end rate)	4.25	4.75	4.50	4.25	4.00	4.00	4.25	4.25
1%	Economic growth of 3%, rising confidence and investment levels, structural constraints eroded, global growth strong, global financial markets risk-on. No nationalisation or expropriation without compensation. Low domestic inflation on favourable weather and global conditions, rand strength, lower state-controlled price inflation on increased private privatisation. Positive outlooks on credit ratings turn into upgrades fiscal consolidation, debt projections fall substantially. Substantial transition to renewable energy away from fossil fuel usage, comprehensive measures to alleviate climate change impact on economy.								
Base case	USD/Rand (average)	15.21	15.59	16.60	15.80	15.60	16.00	16.40	15.90
	Repo rate (end rate)	4.25	4.75	5.50	6.50	6.50	6.50	6.50	6.50
50%	Economic growth modest but lifts towards 3.0% y/y over five years on sufficient domestic policy support measures, global financial market risk sentiment is neutral to positive. South Africa in the BB credit rating category bracket as fiscal consolidation (debt to GDP stabilisation) occurs leading to some positive outlooks. The rand sees mild weakness and inflation is impacted by the course of weather patterns via food price inflation. Little expropriation without compensation occurs and has no negative effect on economy, no nationalisation. A modest transition to renewable energy and slow move away from fossil fuel usage occurs and measures to alleviate the impact of climate change on the economy are modestly implemented. The Russian/Ukraine conflict eases and does not exacerbate.								
Lite (domestic) Down case	USD/Rand (average)	15.21	15.59	16.90	17.00	17.50	17.60	17.50	17.70
	Repo rate (end rate)	4.25	4.75	5.75	6.75	6.75	7.25	7.75	8.25
39%	The international environment (incl. risk sentiment) is that of the base case. South Africa fails to see debt projections stabilise, falls into single B (local and foreign currency) credit ratings from all three agencies. Recession occurs. Business confidence depressed, significant load shedding, weak investment growth, civil and political unrest. High inflation on unfavorable weather conditions, marked rand weakness. Little transition to renewable energy or measures to alleviate the impact of climate change. Very limited expropriation of private sector property without compensation, with some negative impact on the economy. Substantial fiscal consolidation ultimately occurs, preventing ratings falling into the C grades.								
Severe down case	USD/Rand (average)	15.21	15.59	17.50	18.00	18.30	18.50	18.60	19.00
	Repo rate (end rate)	4.25	4.75	6.00	7.00	7.50	8.00	8.50	9.00
9%	Lengthy global recession, global financial crisis – insufficient monetary and other support domestically and internationally. Limited expropriation of private property without compensation with a marked negative economic impact. Very high inflation on very adverse weather conditions, severe rand weakness. SA rated single B from all three key agencies, downgrades eventually into CCC grade, increased risk of default. Government borrows from increasingly wider sources, sinks deeper into a debt trap, widespread, severe services load shedding, severe civil and political unrest. SA economy in depression. Failure to transition to renewable energy and to sufficient measures to alleviate the impact of climate change on the economy.								
Note: Event risk begins Q3.22. Source: Investec									

Severe Down Case: Exchange Rate forecasts												
	2022				2023				2024			
	Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.23	Q4.23	Q1.24	Q2.24	Q3.24	Q4.24
USD/ZAR	15.21	15.59	17.50	18.00	18.30	18.50	18.60	19.00	19.30	19.40	19.30	19.30
GBP/ZAR	20.40	19.59	21.35	21.78	22.33	23.13	23.62	24.32	25.09	25.80	26.06	26.63
EUR/ZAR	17.07	16.60	18.73	19.62	20.31	20.91	21.20	21.85	22.77	23.28	23.74	24.13
ZAR/JPY	7.65	8.33	7.71	7.44	7.16	6.97	6.83	6.63	6.37	6.08	5.96	5.70
CHF/ZAR	16.47	16.15	18.42	19.15	19.68	20.11	20.44	20.88	21.21	21.32	21.21	21.21
AUD/ZAR	11.02	11.14	12.43	12.96	13.54	13.88	14.14	14.82	15.05	15.13	15.05	15.05
GBP/USD	1.34	1.26	1.22	1.21	1.22	1.25	1.27	1.28	1.30	1.33	1.35	1.38
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	130	135	134	131	129	127	126	123	118	115	110
Note: averages, Source: Investec, Iress												

Lite Down Case: Exchange Rate forecasts												
	2022				2023				2024			
	Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.23	Q4.23	Q1.24	Q2.24	Q3.24	Q4.24
USD/ZAR	15.21	15.59	16.90	17.00	17.50	17.60	17.50	17.70	18.00	17.80	17.60	17.70
GBP/ZAR	20.40	19.59	20.62	20.57	21.35	22.00	22.23	22.66	23.40	23.67	23.76	24.43
EUR/ZAR	17.07	16.60	18.08	18.53	19.43	19.89	19.95	20.36	21.24	21.36	21.65	22.13
ZAR/JPY	7.65	8.33	7.99	7.88	7.49	7.33	7.26	7.12	6.83	6.63	6.53	6.21
CHFZAR	16.47	16.15	17.79	18.09	18.82	19.13	19.23	19.45	19.78	19.56	19.34	19.45
AUDZAR	11.02	11.14	12.00	12.24	12.95	13.20	13.30	13.81	14.04	13.88	13.73	13.81
GBP/USD	1.34	1.26	1.22	1.21	1.22	1.25	1.27	1.28	1.30	1.33	1.35	1.38
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	130	135	134	131	129	127	126	123	118	115	110

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	Q4.23	Q1.24	Q2.24	Q3.24	Q4.24
USD/ZAR	15.21	15.59	15.00	14.90	14.90	14.70	14.60	14.50	14.90	15.00	14.50	14.50
GBP/ZAR	20.40	19.59	18.30	18.03	18.18	18.38	18.54	18.56	19.37	19.95	19.58	20.01
EUR/ZAR	17.07	16.60	16.05	16.24	16.54	16.61	16.64	16.68	17.58	18.00	17.84	18.13
ZAR/JPY	7.65	8.33	9.00	8.99	8.79	8.78	8.70	8.69	8.26	7.87	7.93	7.59
CHFZAR	16.47	16.15	15.79	15.85	16.02	15.98	16.04	15.93	16.37	16.48	15.93	15.93
AUDZAR	11.02	11.14	10.65	10.73	11.03	11.03	11.10	11.31	11.62	11.70	11.31	11.31
GBP/USD	1.34	1.26	1.22	1.21	1.22	1.25	1.27	1.28	1.30	1.33	1.35	1.38
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	130	135	134	131	129	127	126	123	118	115	110

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	Q4.23	Q1.24	Q2.24	Q3.24	Q4.24
USD/ZAR	15.21	15.59	14.00	13.80	13.70	13.60	13.40	13.30	13.10	13.10	12.90	12.80
GBP/ZAR	20.40	19.59	17.08	16.70	16.71	17.00	17.02	17.02	17.03	17.42	17.42	17.66
EUR/ZAR	17.07	16.60	14.98	15.04	15.21	15.37	15.28	15.30	15.46	15.72	15.87	16.00
ZAR/JPY	7.65	8.33	9.64	9.71	9.56	9.49	9.48	9.47	9.39	9.01	8.91	8.59
CHFZAR	16.47	16.15	14.74	14.68	14.73	14.78	14.73	14.62	14.40	14.40	14.18	14.07
AUDZAR	11.02	11.14	9.94	9.94	10.14	10.20	10.18	10.37	10.22	10.22	10.06	9.98
GBP/USD	1.34	1.26	1.22	1.21	1.22	1.25	1.27	1.28	1.30	1.33	1.35	1.38
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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