



SA Economics

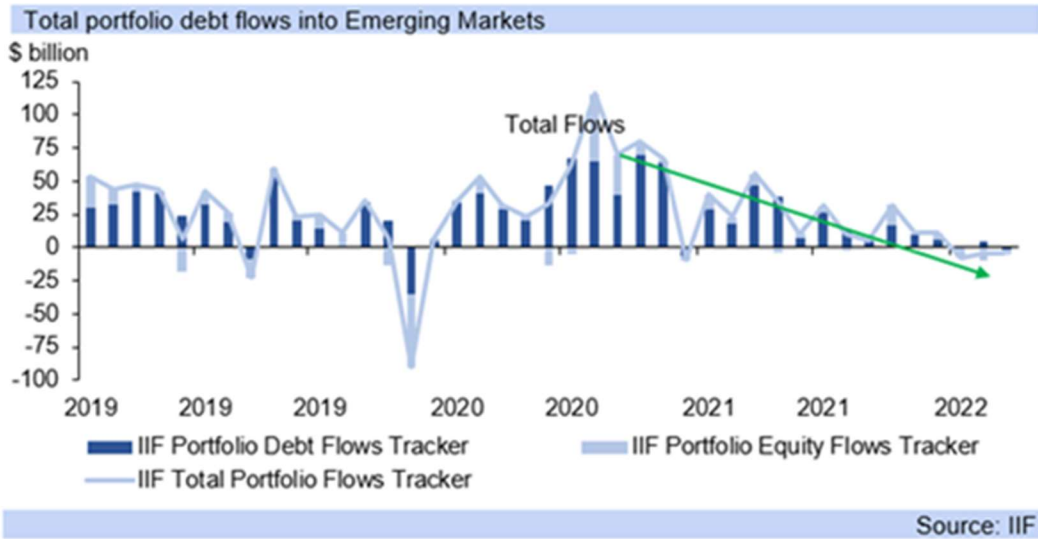
Monday 27 June 2022

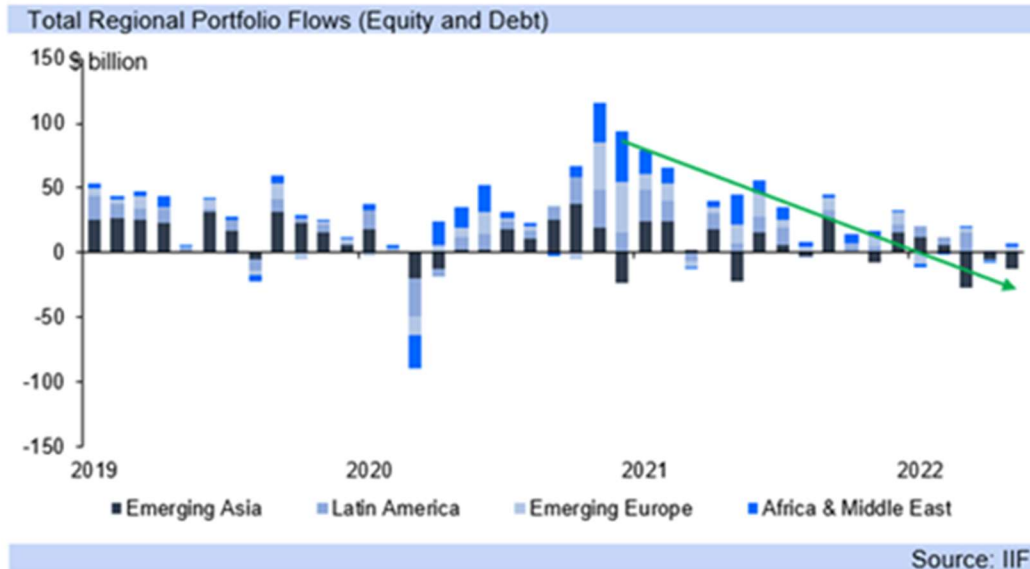
Rand note: rand runs towards forecasts for Q2.22 and Q3.22, but retains high risk of greater weakness

Economic Scenarios: note updated forecasts, scenarios

		Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.23	Q4.23
Extreme Up case 1%	USD/Rand (average)	15.21	14.00	13.80	13.70	13.60	13.40	13.30	13.10
	Repo rate (end rate)	4.25	4.75	4.00	3.75	3.75	3.75	3.50	3.50
	SA economic growth rises to 3–5%, then 5–7%. Good governance, growth-creating reforms (structural constraints overcome), 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 4%	USD/Rand (average)	15.21	14.50	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
	Quickening economic growth, rising confidence and investment levels, structural constraints eroded, global growth strong, global financial markets risk-on. Positive outlooks on credit ratings turn into upgrades fiscal consolidation, debt projections fall substantially. No nationalisation or expropriation without compensation. Low domestic inflation on favourable weather conditions, rand strength, reduction in state-controlled price inflation on increased private privatisation. Substantial transition to renewable energy away from fossil fuel usage, comprehensive measures to alleviate climate change impact on economy.								
Base case 50%	USD/Rand (average)	15.21	15.60	15.80	15.40	15.20	15.60	16.00	15.50
	Repo rate (end rate)	4.25	4.75	5.50	5.75	6.00	6.00	6.25	6.25
	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 39%	USD/Rand (average)	15.21	16.00	16.65	16.90	17.00	17.50	17.60	17.50
	Repo rate (end rate)	4.25	4.75	5.75	6.25	6.75	7.25	7.75	8.25
	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 6%	USD/Rand (average)	15.21	16.80	17.50	18.00	18.50	19.00	19.75	20.50
	Repo rate (end rate)	4.25	4.75	6.00	6.75	7.50	8.00	8.50	9.00
	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





Expected Case: Exchange Rate forecasts

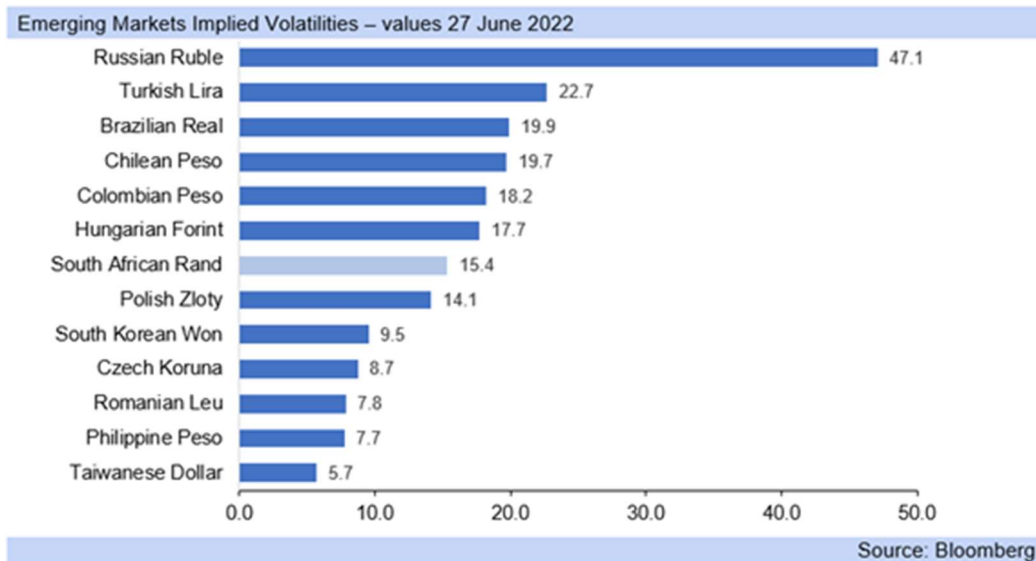
	2022				2023				2024			
	Q1.22	Q2.22	Q3.22	Q4.22	Q1.23	Q2.23	Q3.23	Q4.22	Q1.24	Q2.24	Q3.24	Q4.24
USD/ZAR	15.21	15.60	15.80	15.40	15.21	15.60	15.80	15.40	15.21	15.60	15.80	15.40
GBP/ZAR	20.40	19.64	19.99	19.87	20.40	19.64	19.99	19.87	20.40	19.64	19.99	19.87
EUR/ZAR	17.07	16.57	16.91	16.79	17.07	16.57	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

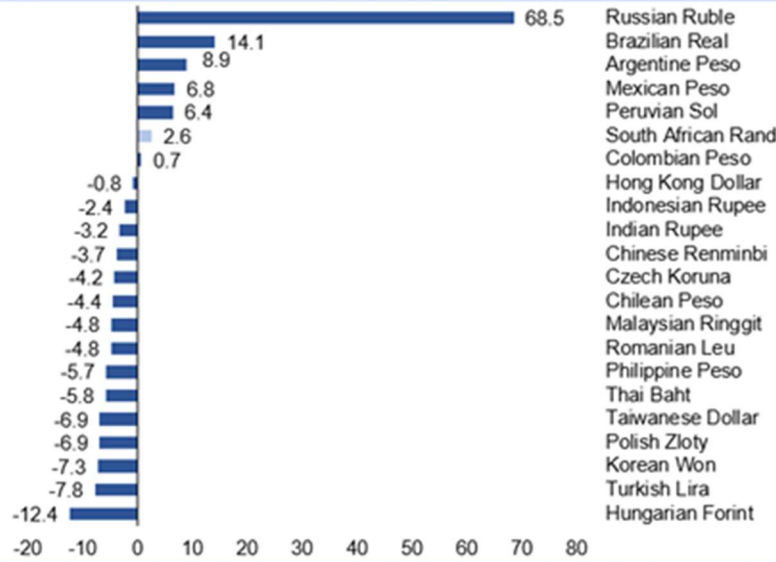
- With the rand averaging R15.59/USD so far this quarter, and only four readings left, the domestic currency is likely to attain its forecast (average) rate for Q2.22, while it is now tracking towards R15.80/USD, its Q3.22 forecast.
- However, Q3.22 is still at risk of marked volatility, despite some recent strength in the rand. While the domestic currency reached R15.77/USD today, before being rebuffed back towards R15.90/USD, it has yet to sustainably breach the R15.80/USD resistance level.
- The rand has gained from its geographical distance from the Russian/Ukraine conflict, and from Europe in general, as well as from portfolio disinvestment from China, with China seen as aligned with Russia, and having increased imports of Russian energy commodities.
- China has led EM non-resident portfolio outflows since the Russian/Ukraine war, while overall foreigners have been net disinvestors from EM portfolio assets, as higher interest rates (particularly in the US) and high inflation globally has driven recession fears and risk aversion.
- By the end of May, there was some evidence that the outflows had lessened, but investor sentiment has been volatile, and the volatility is likely to continue for emerging markets this quarter and next; and increased risk of US recession will heighten this.

- While the US monetary policy committee has been very positive about the strength of the US economy, it is increasingly believed that a marked slowdown, and weakness in the labour market is needed to bring inflation sustainably back to the FOMC's goal of around 2.0%.
- The Fed has yet to show notable concerns on the strength of the labour market and US economy, but markets are a lot less sanguine, which has driven risk aversion sentiment and so the weakness in risk assets, particularly those of EMs' and their currencies.
- Signs of an extensive slowing in the US economy are likely in H2.22, which should limit US interest rate hikes, while the global economy is also expected to slow, causing interest rate hike expectations to likely be scaled back in other key advanced economies too.
- While initially positive for the rand, which would likely see further weakness if the US continued to deliver large interest rate hikes this year and next, the domestic currency will also remain volatile, and at risk of particular weakness on global recession.

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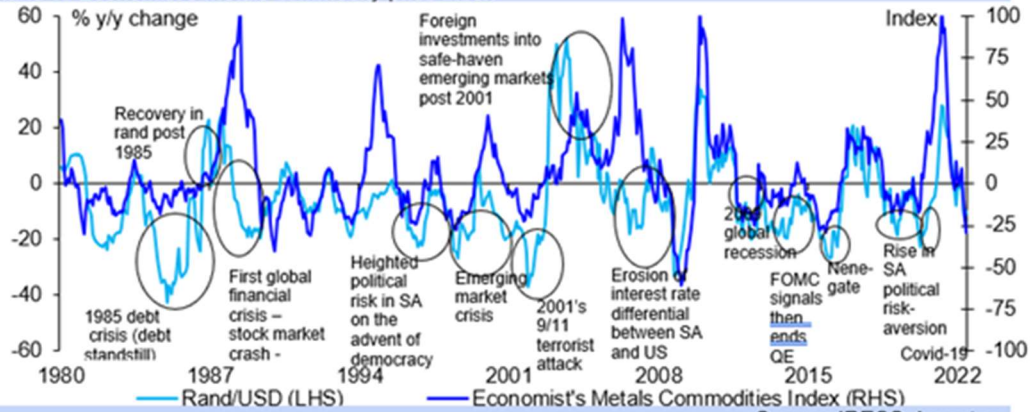


Emerging Markets Carry Return – values 27 June 2022

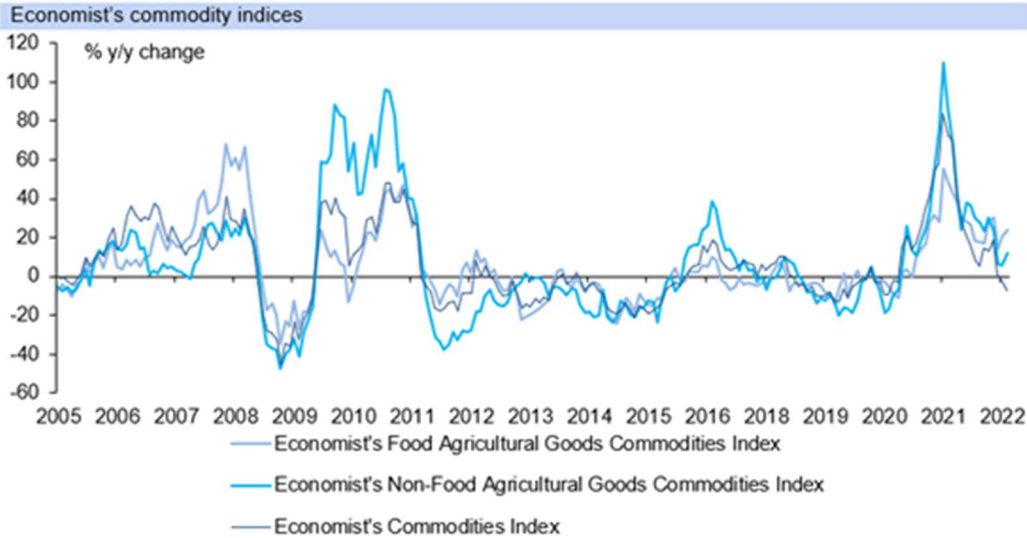


Source: Bloomberg

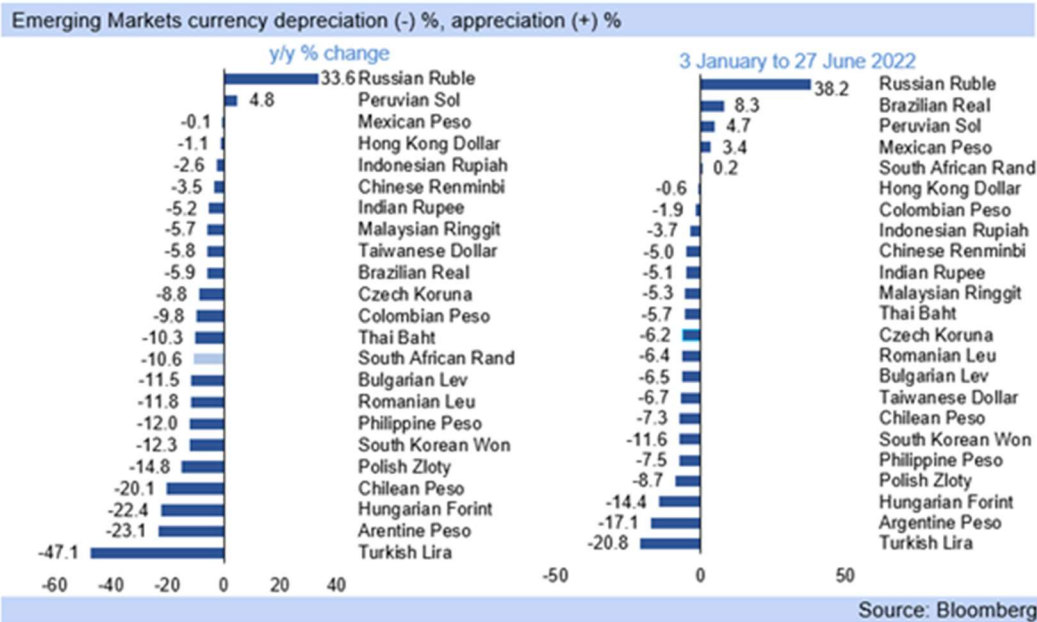
Rand vs Economist's metals commodity price index



Source: IRESS, Investec



Source: IRESS, Economist



- With the Russian/Ukraine war showing no signs of drawing to a close, and instead sanctions intensifying further against Russia from the West, high inflation, and weaker global growth is still the most likely characterisation for this year.
- The G7 group of key economies, US, UK, Canada, France, Germany, Japan, Italy (and so the EU in general), have agreed to “align and expand targeted sanctions to further restrict Russia’s access to key industrial inputs, services and technologies”.
- Food supply remains a concern globally. The G7 has now agreed that Russians deemed responsible for war crimes against the Ukraine, and those increasing “global food insecurity” by “stealing and exporting Ukrainian grain” would be targeted individually with sanctions.

- Nato has said it expects that Russia could pause its offensive in H2.22 to redeploy troops and refresh supplies and forces, but continue its onslaught into next year and beyond. The G7 is also discussing a cap on the oil price for Russia and sanctions on gold exports.
- With a lengthy war in the Ukraine of many years expected by Nato, the US will find it hard to collapse its inflation on the impact on food and fuel prices, and will likely either need to live with higher inflation or a substantially weaker jobs market which may necessitate recession.
- However, the FOMC is unlikely to wittingly drive the US into a severe recession, even a substantial slowdown in growth is likely to cool its appetite for severe interest rate hikes, although a technical recession of couple of quarters contraction may be unavoidable.
- Increasing the burden of sanctions on Russia increases the strain on economic activity globally, but the G7 are likely to continue to heavily support Russia this year and next, while Russia itself is now not expected to back out of its invasion of the Ukraine any time soon.
- The rand appears to have consolidated around R15.90/USD today, and could see further near term strength, but longer-term the domestic currency is at risk of material weakness as the global economy slows, if not falling into outright recession, which will exacerbate risk-off.
- In SA, high inflation aids the run-down of nominal debt, if accompanied by robust nominal inflation led GDP, with lower fiscal debt and deficits, both actual and projected, positive for the domestic currency. However, well above inflation wage demands seek to eat up the gains.

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
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

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

Long-term trend of the rand



Source: 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
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