

ECONOMIC COMMENTARY

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YOUR WEEKLY ECONOMIC UPDATE

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AN UPDATE ON THE RAND

Until recently, the rand has remained resilient against the United States (US) dollar. But during the past couple of weeks, the pressure has simply been too much for the rand to bear, causing it to depreciate to levels around R17.00. In the past, the rand's demise was primarily driven by bad local politics, which led to bad policies, which, ultimately, led to negative sentiment. Everything that led up to, and including, Nenegate was a good example of this. But this time, the rand's depreciation has more to do with an increasingly strong dollar.

Following its historic pattern, the dollar has been gaining considerable momentum against most other currencies, as the US central bank, the Federal Reserve (Fed), has been increasing interest rates at a much more rapid pace than most other countries have been able to. Not even the South African Reserve Bank's (SARB's) in-step increases have been able to do much to prevent the deterioration of the rand. Some analysts even expect the SARB to continue increasing interest rates by another 2% in 2022: I think that is a bit unnecessary and, as we have seen, it will not do a lot for inflation or the rand. Therefore, plan for another 2%, but expect at least another 1%.

Everything, it seems, is favouring the dollar, which has placed the rand between a rock and a hard place. On the one hand, if the US economy does well, the markets will expect the Fed to continue to increase interest rates at a more rapid pace. This happened on Friday when the US Department of Labour reported that the US economy added 372 000 new jobs in June, beating expectations by nearly 100 000, and keeping the unemployment rate at near full employment, namely 3.6%. In these instances, the US economy will continue to offer better returns and, therefore, drain liquidity from the rest of the world.

On the other hand, if markets fear that the Fed, and other developed country central banks, will overshoot and push the global economy into a recession, then investors will reduce their riskier investments in emerging markets and run to safe havens. Because the US offers better risk-adjusted returns, investors end up piling into the US dollar, which, once again, supports the dollar at the cost of emerging market currencies, like the rand. But during recessions countries also demand less of our goods, which puts pressure on our capital account, which ends up weighing the rand down. Excluding the COVID-19 slump, the previous two recessions in 2001 and 2008/2009 knocked as much as 13% off the rand's value. Some analysts, therefore, expect another 12% downside to the rand if a global recession materialises. We believe that, even if this does occur, and the rand depreciates another 12%, that the rand should then remain strong for at least some years after the recession, as markets recover and the transition towards emerging markets solidifies.

What this means for investors is that, during the next 6 to 12 months, the rand, like most other currencies, will face an uphill battle against the US dollar, and during this time ZAR/USD movements will remain volatile. We can easily expect swings around 5% a week. We might even see moves like these happen on specific days. As long-term investors, and considering the data that we now have, we would still recommend that our clients buy below R16.00, but levels closer to R15.50 would be better. But, of course, this will also depend on how the markets will react. It is pointless to wait too long to win 5% to 8% on the currency but then to miss out on +10% market growth. Entry points are important but trying to time the market usually hurts clients a lot more in the long term. We are, therefore, advising our clients to wait for at least R16.00, and from there to start deploying their cash strategically. Please speak to us, your trusted financial partner.

