sasfin beyond a bank

# The Daily Market

21 June 2022

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|---|---|---|---|
| USD-ZAR | 16.0428/16.0578 | GBP-ZAR | 19.6661/19.6901 |
| GBP-USD | 1.2258/1.2312 | AUD-USD | 0.6952/0.6954 |
| GOLD | $1835.69 | DJI | 44732,00 |
| EUR-ZAR | 16.8734/16.886 | EUR-USD | 1.0514/1.0518 |
| USD-JPY | 135.05/135.08 | R 186 | 8.695% |
| BRENT | $114.94 | 3m JIBAR | 4,942 |

## Events (GMT)

| | | | | | |
|---|---|---|---|---|---|
| 07:00 | SA | Leading Indicator | Apr | | 128 |
| 09:00 | SA | Vanilla auction (R3,9bn R2035, R2040, R2048) | | | |
| 07:15 | UK | BOE's Huw Pill speaks | | | |
| 12:15 | UK | BOE's Tenreyro speaks | | | |
| 12:30 | US | Chicago Fed activity index | May | | 0,47 |
| 14:00 | US | Existing home sales | May | 5,4mn | 5,61mn |

## Factors on the radar

### PMIs

| | |
|---|---|
| **What happened?** | Global PMIs for June will be released later this week, potentially providing more signs that major economies are coming under some pressure |
| **Relevance** | Any signs that economies are slowing will keep risk assets under pressure |
| **Importance** | 4/5 (economics) |
| **Analysis** | Continued supply disruptions, high inputs costs, and weakening demand are all factors that can be highlighted in the PMIs and point to weaker growth dynamics ahead |

### Europe Corporate Distress

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|---|---|
| **What happened?** | Corporate distress in Europe is at two-year highs amid surging inflation and expectations for higher borrowing costs and tighter monetary conditions |
| **Relevance** | The cost of borrowing for highly leveraged companies will surge and create financial stability risks |
| **Importance** | 4/5 (corporate credit markets) |
| **Analysis** | Years of loose monetary policy created significant malinvestment as the cost of capital was so low. Now, the impact of that is going to be felt as companies will no longer be able to service their debt |

### Container Shortage

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|---|---|
| **What happened?** | Disruptions in major ports are still leaving a major shortage of shipping containers with Asian exporters likely to be the most affected |
| **Relevance** | Higher shipping costs and longer lead times are here to stay, a downside risk for global growth |
| **Importance** | 3/5 (inflation/ global trade) |
| **Analysis** | As China reopens and tries to make up for unfulfilled orders, demand for limited containers will spike, leading to higher costs which will keep elevated global inflation entrenched |

## Today's Talking Point

**Leading indicator: Apr**

**Expected:**

**Prior: 128.0**

**Analysis:** The SARB's leading indicator has been trending gradually higher this year, indicating that SA's economy has been holding up, as shown in the recent Q1 GDP numbers. However, external and local headwinds have made the recovery challenging and uncertain at times, with the outlook deteriorating as the weeks go by. In particular, supply chain disruptions stemming from the Russia-Ukraine conflict and China's zero-Covid related lockdowns, amongst idiosyncratic factors such as a lack of reforms, rolling blackouts and the KZN flooding have been major setbacks for a nascent growth cycle. With all of this in mind, it is difficult to see a continued improvement in the leading indicator, which would start to suggest that SA's economy is set to lose some momentum as the easy gains following the COVID plunge have now been made.

## Rand Update

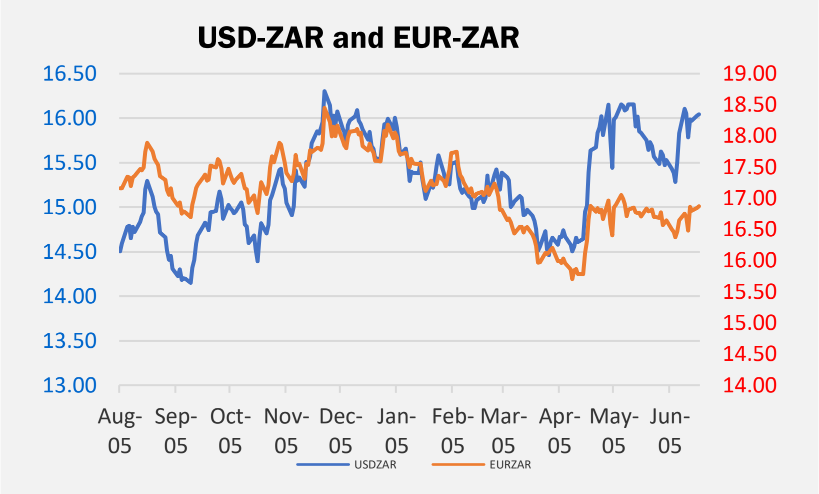
It was a slow start to the new week as a lack of market-moving data releases and thin liquidity conditions due to a US public holiday kept traders on the sidelines. For the most part, the USD-ZAR continued to consolidate around the 16.0000 handle, gaining only marginally as the return of rolling blackouts in South Africa weighed on the ZAR's relative attractiveness.

Ailing state utility Eskom announced the return of stage two load-shedding between 5pm and 10pm until Thursday due to an ongoing shortage of generation capacity. It noted that it had 5,232MW on planned maintenance, while another 14,202MW of capacity was unavailable due to breakdowns that may also keep the risk of load-shedding elevated in the weeks ahead.

The lack of stable electricity supply is just one of many well-documented growth headwinds that are preventing a stronger recovery despite the boost in economic activity after the post-COVID reopening. These countervailing economic forces are set to be reflected in today's release of the SARB's leading indicator for April, to which ZAR traders will be paying close attention given the implications of growth momentum for prospective SARB policymaking and SA's trade and current accounts.

With that in mind, note that data released by the Commodities Futures Trading Commission (CFTC) yesterday showed speculators in the market increased their long ZAR positions to a new record in the week of 14 June. This suggests traders are betting on a ZAR rebound from the recent Fed-induced selloff, with the ZAR looking increasingly oversold at levels north of R16.0000/$.

Of course, this bodes well for the ZAR and suggests exporters should take advantage of the current exchange rate while it is still available. Market agents seemingly expect SA's commodity exports to remain buoyant enough to offset improving import demand, and the SARB to keep up with the global rate-hike cycle. Moreover, with so much in the way of prospective Fed monetary tightening now priced into the USD, the balance of risks is tilted towards the downside for the greenback from here.

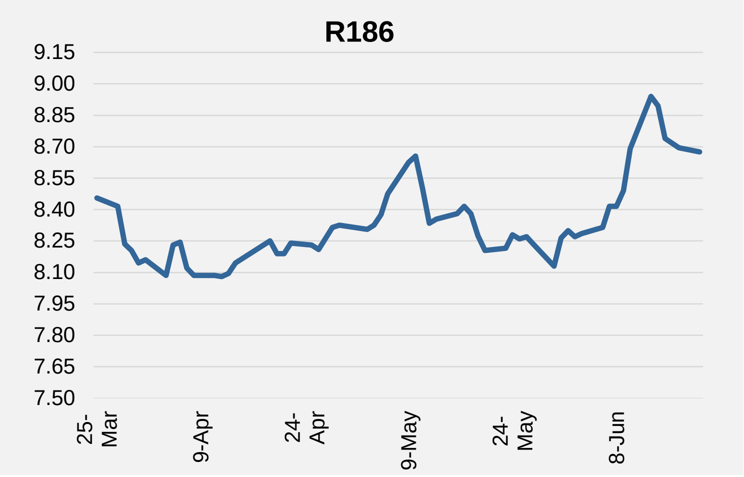



## Bond Update

There are signs in the market that speculators are positioning in favour of the ZAR. CFTC data that amalgamates market positioning at the Chicago Mercantile Exchange has highlighted a rise in speculative long-ZAR positions. This may ultimately reflect increased interest in ZAR assets, as economic theory suggests that the position would benefit from a cessation in US rate hike risk and a commensurate fall in the USD.

Domestic factors are unlikely to be the driver at this cycle stage, with investment weak and the trade balance narrowing in recent prints. That said, an outlook for continued rate hikes at the SARB would support the ZAR to benefit unhedged long-SAGB positions when priced in USD. US yields may be rising, but so is the risk of a US (and perhaps global) recession that would kick up some dust in high yield US debt markets. Keep an eye on comments from Fed's Mester today, which could affect market positioning at the margin. A US slowdown would amplify default risk in the US high yield debt category, while SA bonds are already priced with high risk in mind. The long end is still yielding well north of 11%. With the USD already highly overvalued on a PPP basis, it would be plausible to see a period of weaker USD spot prices despite rising yields, which would support local bonds.

The narrative of recovering SA growth could also be supported as eased COVID restrictions enable a semblance of normal in economic data. While the economy is still far from its pre-COVID trend, a recovery towards trend was clear in an above-consensus Q1 GDP outcome. This narrative may be strengthened today if the leading indicator for April continues to reflect economic recovery, although headwinds are certainly forming as the rate of annual growth in the indicator slows. The indicator trended gradually higher since bottoming out in October, indicating that SA's economy has been recovering. In year-on-year terms, the indicator rose 0.5% from 3% in February but is set to dip into negative y/y territory in April.

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