sasfin beyond a bank

The Daily Market

24 November 2022

USD-ZAR	16,931/16,9441	**USD-JPY**	138,75/138,76
GBP-ZAR	20,4962/20,5202	**GOLD**	$1754,93
EUR-ZAR	1,0439/1,0443	**BRENT**	$85,09
GBP-USD	1,2106/1,2163	**DJI**	34 194,06
EUR-USD	1,0322/1,0326	**R 186**	8,67%
AUD-USD	0,6764/0,6765	**3m JIBAR**	6,683

Events (GMT)

Time	Country	Event	Month	Fc	Prior
-	SA	SARB Announce Interest Rate	24-Nov	7.00%	6.25%
09:30	SA	PPI	Oct		16.3%
09:00	GE	IFO Business Climate	Nov	85.0	84.3
09:00	GE	IFO Current Assessment	Nov	93.8	94.1
13:00	EC	ECB's Schnabel Speaks			
16:00	EC	ECB's Nagel Speaks			

Factors on the radar

Black Friday and Thanksgiving

What happened?	This week signals Black Friday, which also implies a long weekend in the US, with Thursday marking Thanksgiving
Relevance	Not only will Black Friday give insight into consumption, but liquidity will be thin
Importance	5/5 (markets, economy)
Analysis	This will ensure that investors are a little more cautious in their trading this week, which will be characterised by consolidation

BoE quantitative tightening

What happened?	The BoE laid out plans for selling some of the £19bn of long-dated and index-linked gilts that it bought last month to stabilise markets after the Truss budget
Relevance	BoE will be selling gilts Tue, Wed and Fris giving minimum prices before each sale
Importance	4/5 (monetary policy, fiscal policy)
Analysis	This will further drain liquidity from the system but unwind the support that was required after Kwasi Kwarteng announced his mini budget that spooked markets

German yield curve

What happened?	Germany’s yield curve has inverted to the deepest levels seen in over 14 years, signalling the high probability of a recession
Relevance	Europe’s largest economy will drag many other economies with it
Importance	4/5 (monetary policy, market)
Analysis	The ECB will be mindful of this and will try to keep monetary policy as accommodative as it can without disregarding inflationary pressures

Today's Talking Point

SARB Interest rate announcement

Expected: 7.00%

Prior: 6.25%

Analysis: A shifting Fed narrative appears to be driving some speculation of a compression in rate hike risk. However, when looking holistically at JIBAR and the 1x4 FRA, it should be noted that a 75bp rate hike could conceivably be delivered in November without affecting pricing. The outlook could more meaningfully shift in an environment where US data starts to underperform, yet the latest US retail sales data and comments from Fed members suggest that the Fed could still be pushed to tighten rates further. A US rate peak of 5-5.25% is being tabled, suggesting that at least another 125bp could be expected from the Fed. If so, this would keep some pressure on the SARB to keep hiking. However, SA's macro dynamics are not conducive to supporting higher rates, meaning that once pressure from external rates eases, the SARB will be able to slow its hikes.

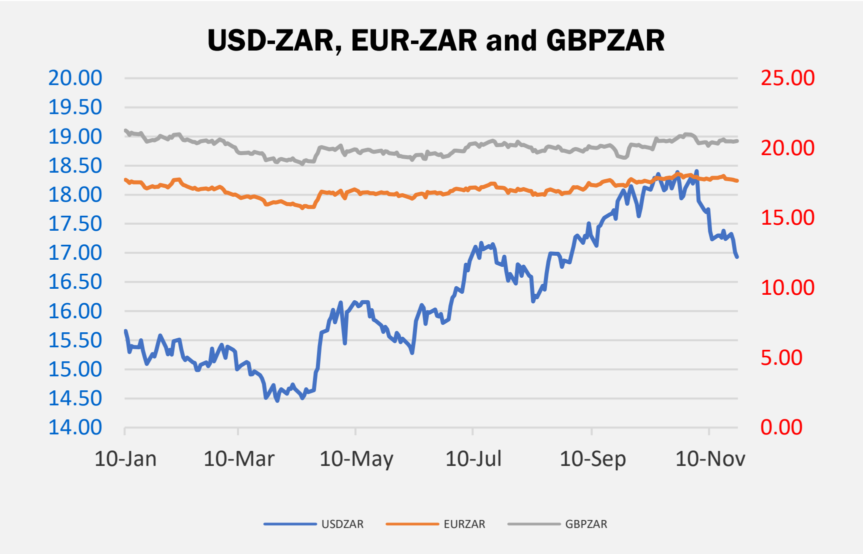
Rand Update

Yesterday's inflation data disappointed and raised overall expectations of today's interest rate decision. Unfortunately, the SARB had warned that the risks to inflation lay to the upside and yesterday's inflation data confirmed that. Although inflation has likely peaked, it may remain stubbornly buoyant initially before dropping off more sharply early in 2023. For now, it means that the SARB may consider another 75bp rate hike, perhaps the last such hike, using the stubbornly high inflation reading as its justification.

Conservative monetary policies have been rewarded by currency resilience and strength. Another 75bp hike today would likely support the ZAR and help it regain more lost ground. Equally important will be the tone that the SARB chooses to use. If hawkish, the ZAR might well extend its gains through the afternoon. If less hawkish than expected, then the USD-ZAR will likely consolidate.

However, while all the local developments are important, the depreciation in the USD will drive a broader FX market direction. As important as local events such as the MPC decision are, they will pale into insignificance if the USD weakens sharply. That is not to say that the SARB's efforts are meaningless, but rather that the bulk of direction on FX markets at the moment is driven by the performance of the USD, not local developments.

Heading into the US long weekend where there is unlikely to be good reason to back the USD unless Black Friday sales do something extraordinary, the ZAR is set to end the week on a much firmer footing. A quick assessment of the ETM ZSI suggests that a recovery back below 15.00/dlr is possible in the coming months, implying a long phase of protracted USD weakness. The window for exporters to take advantage is steadily closing.



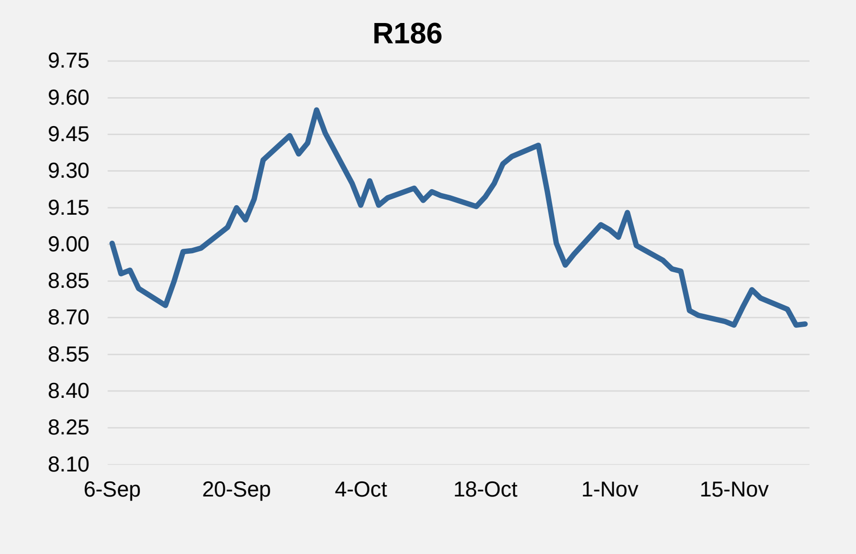
Bond Update

Against expectations for a further decline in headline CPI in October, the print increased to 7,6% y/y from 7,5% y/y in September. Although inflation ticked upwards in October, it is likely still peaking domestically. SA remains in a global inflationary cycle driven by the effects of the war, particularly on the food price front. The latest CPI outcome increases the likelihood that the SARB may raise interest rates by 75bp and not the 50bp we had expected. Households continue to face a cost-of-living crisis as elevated inflation and rising interest rates erode disposable incomes.

The primary driver of the increase in October was ongoing elevated food inflation at a decade-long high of 12,3% y/y in October. Although skyrocketing agricultural food commodity prices have fallen from post-war highs, food inflation domestically remains elevated. Hopefully, Russia rejoining the so-called grain deal allowing the safe passage of Ukrainian grain exports through the Black sea will alleviate some supply constraints. There was a further pick up in inflation of vehicles to 6,1% y/y in October from 5,8% y/y in September. Concerningly, second-round effects were still evident in the October numbers. Core inflation, which excludes volatile food and energy prices, rose further, to 5,0%y/y in October, from 4,7% y/y in September.

This stubbornly high result may lead the SARB to make another bold decision to contain inflation expectations and buy further insurance against inflation remaining stubbornly high for longer. The latest elevated reading may reflect the lagged weakness of the ZAR in recent months. However, ETM's ZAR inflation risk indicator confirms that peak inflation has passed, that the underlying momentum behind inflation has weakened, and that price pressures will moderate from here.

Furthermore, with the ZAR staging a strong recovery at the moment and expected to appreciate a lot further, one should not turn pessimistic on the outlook for domestic inflation. On the contrary, inflation is still likely to trend sharply lower in the months ahead and, by the middle of next year, be well within the 3-6% inflation target band. A combination of tighter monetary conditions, conservative fiscal policy, a much stronger ZAR, and high base factors will all help inflation lower and keep it lower.



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