sasfin beyond a bank

The Daily Market

13 January 2022

USD-ZAR	15,3118/15,3158	**GBP-ZAR**	20,9869/21,0109
GBP-USD	1,3713/1,3764	**AUD-USD**	0,7289/0,729
GOLD	$1825,42	**DJI**	44573,00
EUR-ZAR	17,5205/17,528	**EUR-USD**	1,1443/1,1444
USD-JPY	114,56/114,59	**R 186**	7,905%
BRENT	$84,5	**3m JIBAR**	3,892

Events (GMT)

-	SA	Switch Bond Auction		
O/N	JN	M3 money stock y/y	Dec	3,60%
06:00	JN	Machine tool orders y/y	Dec P	64,00%
13:30	US	PPI final demand y/y	Dec	9,60%

Factors on the radar

US Earnings

What happened?	The next major event that could determine broader risk appetite will be the earnings reports that will be released in the coming weeks
Relevance	Although inflation is running hot, companies are performing well and set to impress
Importance	4/5 (economy, markets)
Analysis	The market is positioned for strong earnings that will ease concerns that the global economy is struggling. Companies are managing to navigate a difficult climate and produce strong results

PM Johnson

What happened?	UK PM Boris Johnson is under intense pressure to resign after he was caught attending a party gathering at his official residence during lockdown
Relevance	One might expect the opposition to call for his resignation, but now some conservatives are too
Importance	5/5 (politics)
Analysis	His apology and defence have left most unimpressed. It will now take 54 of the 360 conservatives to call for a vote of no confidence to the party's 1922 committee for his to trigger

Fedspeak

What happened?	It would appear that the central theme permeating the Fed is that of a rate hike in March this year with San Fran Fed President Daly singing out March for a hike
Relevance	Daly is yet another that joins the growing number of FOMC members that could call for a hike
Importance	4/5 (economy, markets)
Analysis	With inflation running so hot, the economy headed for full employment and the Federal government still looking to spend more, the Fed's hand to remove accommodation

Today's Talking Point

Oil Update

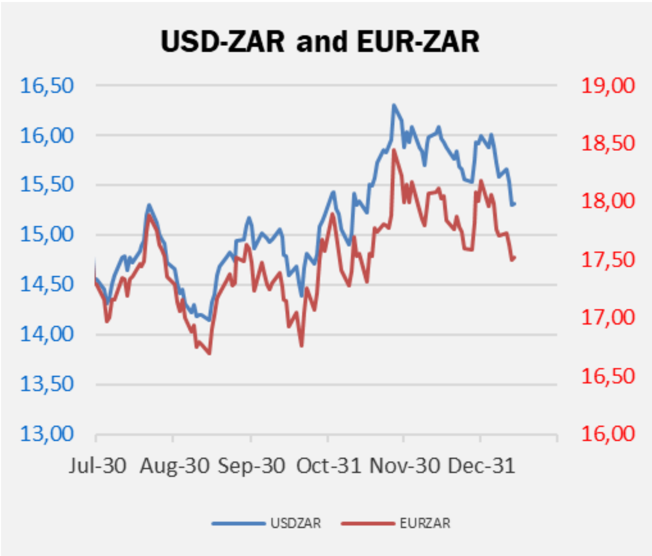
Analysis: Oil prices are steady this morning after continuing with their new year rally yesterday. The front-month Brent contract tested the $85 per barrel mark yesterday, supported by a weaker USD and a tightening market. The contract failed to sustain the break above this key level but we could see the bulls try once again in the sessions ahead. Demand has been more resilient than what many expected as we kicked off the new year, while concerns remain over supplies as many OPEC+ members are struggling to reach their output quotas already, even though another 400k barrel per day increase is likely to be announced at the start of the February. Technical indicators, however, are starting to flash some warning signs to suggest that the near term rally may have gone too far. The 14-day RSI has reached the overbought threshold for the first time since October, while in the US, options volumes surged for March put spreads on WTI, indicating increased demand to hedge against the downside. On balance, therefore, we may see oil prices eke out more gains in the near term, but it is starting to seem that the commodity may be close to topping out.

Rand Update

The USD's correction deepened on Wednesday, with the trade-weighted dollar index sliding to early-November lows even after Stateside CPI data came in at levels last seen in 1982. The data showed inflation amounted to 7% at the end of 2021, matching consensus expectations and therefore not coming as a major shock to the market. While 7% is unlikely the peak of this inflation episode, price growth is expected to moderate through 2022 as supply-chain bottlenecks ease, especially if the world begins to transition to a more sustainable way of living with COVID-19 as opposed to trying to eradicate it completely.

Accordingly, Fed rhetoric of late has pointed to a relatively less forcible approach to reducing monetary stimulus in the months ahead than investors were positioned for. There was so much in the way of policy divergence priced into the greenback after the December meeting minutes released last week mentioned the prospect of quantitative tightening, which rendered it extremely vulnerable to any information challenging that view. It is thus not surprising that the USD has corrected lower this week after Fed Chairman Powell and Fed Governor Brainard suggested the central bank would be cautious in its monetary tightening approach, and that it would maintain a strong focus on economic growth.

Naturally, the ZAR has capitalised on the USD's correction, adding another 1.65% to this week's rally as it closed yesterday's session at R15.3000/$. This was the first time the ZAR closed below the R15.50000/$ mark since mid-November, and also marked a strong improvement from the R16.0000/$ handle it was battling against just last week. The local unit has benefited significantly from the USD's retreat, both directly, and indirectly through the rise in commodity prices. As investors position for a Fed tightening cycle that may be less damaging to global economic growth than previously anticipated, the outlook for commodities has improved.



Bond Update

As reflected in Forward Rate Agreements (FRAs), rate hike expectations compressed with some vigour yesterday. The 21x24 contract, delivering in 21 months and ultimately covering 2-years out dipped down to 278bp worth of rate hike risk, now down 31bp from Monday's close. The move followed recent comments from Fed Chairman Powell favouring a measured approach to the Fed policy outlook, which has raised question marks over whether the SARB will be pressed to tighten as advertised.

The appreciation of the ZAR would have been a primary driver as relative USD overvaluation and ZAR undervaluation has resulted in downside pressure on the USD-ZAR, reducing the risk of import inflation. A moderation in Fed rate guidance also reduces the risk of ZAR weakness in coming quarters. Purchasing Power Parity calculations put the ZAR's 'fair value' around R14-R15/USD, with the R14.50 mid-point of that range some 5.5% lower than current spot levels. Reversion towards this fundamental value will constrain domestic inflation risk and stifle imported inflation. This, coupled with a weak growth outlook in many of SA's key sectors, also suggests that the central bank will be hard-pressed to maintain aggressive rate hikes through 2022 without stoking recessionary forces in the real economy.

Considering the effect of policy tightening on property affordability illustrates the point. When assuming limited wage growth over the next year or two, this would represent a significant decrease in bond affordability at a time when unemployment rates are very high and wage growth been negative in real terms even at the level of government.

S Forex

sasfin.com

29 Scott Street, Waverley, 2090
PO Box 95104, Grant Park, 2051 | +27 11 809 7500

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www.etmanalytics.com