sasfin beyond a bank

The Daily Market

22 June 2022

USD-ZAR	15.9894/15.9985	GBP-ZAR	19.5494/19.5734
GBP-USD	1.2228/1.2282	AUD-USD	0.6911/0.6913
GOLD	$1825.23	DJI	44733,00
EUR-ZAR	16.7707/16.784	EUR-USD	1.0488/1.0492
USD-JPY	136.25/136.28	R 186	8.675%
BRENT	$110.81	3m JIBAR	4,942

Events (GMT)

08:00	SA	CPI y/y	May	6,1%	5,9%
06:00	JN	Machine tool orders y/y	May F		23,7%
06:00	GB	CPI y/y	May	9,1%	9,00%
11:00	US	MBA mortgage applications	Jun 17		6,6%
13:30	US	Powell Delivers Semi-Annual Testimony Before Senate Panel			
14:00	EZ	Consumer confidence	Jun P	-20,5%	-21,1%

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

Powell Testimony

What happened?	Potentially the major event for the week for global markets will be Powell's testimony before the Senate today and the House FSC tomorrow
Relevance	A commitment to containing inflation this week will support market bets of more aggressive tightening
Importance	4/5 (monetary policy)
Analysis	The testimony will be focused on the Fed's inflation fight with questions likely on how the central bank got its inflation projections so wrong initially and how policy is impacting the economy

China Economic Support

What happened?	Officials in China have intensified their calls for more economic support, greater infrastructure spending, and new pro-growth fiscal policies
Relevance	China is adding to global growth fears, so policy support will help to alleviate recession concerns
Importance	3/5 (economics / fiscal policy)
Analysis	Recent data has pointed to a weaker growth outlook, but China has the policy space to boost spending and provide other support measures to prop up the economy in the months ahead

Today's Talking Point

CPI Y/Y: May

Expected: 6.2%

Prior: 5.9%

Analysis: CPI was unchanged in April; however, expectations are for an acceleration to have occurred in May, due to the impact of elevated oil and food prices globally. CPI is expected to have increased to 6.2%, which is above the SARB's target range of 3-6%. If we see this occur, it could force the SARB to consider hiking interest rates more aggressively, especially after the recent move by the Fed. The main components which are likely to have led to the increase CPI for May are transportation prices, fuels, electricity, as well as oils and fats, which have seen prices surge globally. Core inflation, which excludes the price of food, non-alcoholic beverages, and fuel and energy, is also expected to have increased last month, however it is expected to have remained below the target midpoint of 4.5%, which indicates that inflation is mainly being driven by these external factors as local demand remains quite weak.

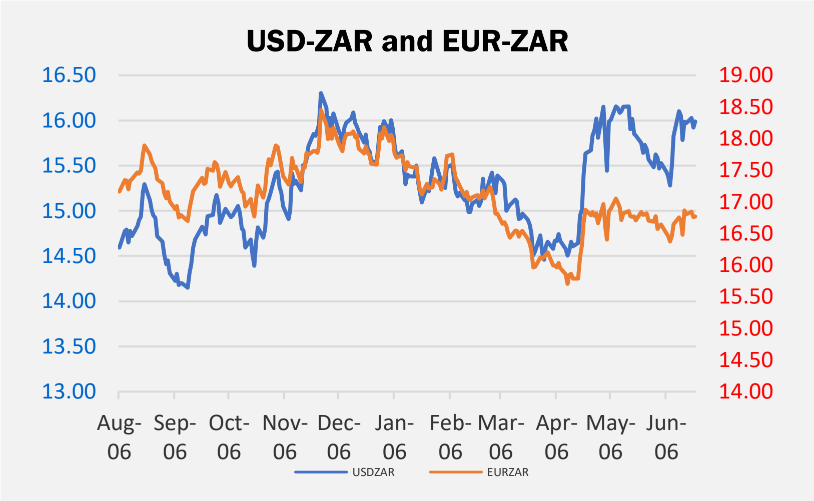
Rand Update

The ZAR had the wind at its back on Tuesday, appreciating 0.90% against a broadly-weaker USD amid a tentative improvement in market sentiment. Investors should be cautious of reading too much into this, however, as there is still significant uncertainty over the global economic outlook and how aggressively the likes of the US Federal Reserve and other major central banks will need to tighten monetary conditions to ease inflationary pressures.

Against this backdrop, Fed Chairman Powell's testimony in Congress today and tomorrow will attract plenty of attention. Powell may provide a more detailed explanation for the outsized 75bp rate hike implemented a week ago, and also issue additional forward guidance for the upcoming policy meetings through the rest of the year.

As things stand, the Fed looks set to front-load its rate hike cycle with more big rate hikes in the months ahead, until there are material signs that inflation expectations and core inflation are declining. Thereafter, it may begin to discuss a flatter rate-hike trajectory to try and avoid a so-called "hard landing" for the economy. However, in the meantime, the Fed's hawkish outlook will likely keep the USD supported, while emerging-market currencies may remain under pressure for a while longer.

Locally, the CPI reading today will hold focus, CPI was unchanged in April; however, expectations are for an acceleration to have occurred in May, due to the impact of elevated oil and food prices globally. CPI is expected to have increased to 6.2%, which is above the SARB's target range of 3-6%. If we see this occur, it could force the SARB to consider hiking interest rates more aggressively, especially after the recent move by the Fed. The main components which are likely to have led to the increase CPI for May are transportation prices, fuels, electricity, as well as oils and fats, which have seen prices surge globally. Core inflation, which excludes the price of food, non-alcoholic beverages, and fuel and energy, is also expected to have increased last month, however it is expected to have remained below the target midpoint of 4.5%, which indicates that inflation is mainly being driven by these external factors as local demand remains quite weak.



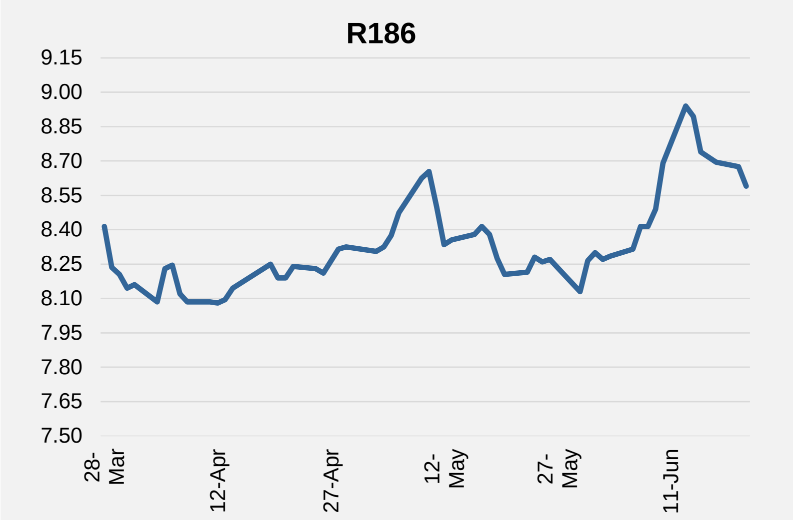
Bond Update

CPI data will hold market focus today and could have implications for the SARB rate outlook. Recall that the outlook for fuel inflation remains towards the upside, while investors will be monitoring the data for evidence of second-round effects. Core CPI has been accelerating marginally but remains soft amid tepid consumer affordability. However, it is also expected to have increased last month, but still remain below the target midpoint of 4.5%, which indicates that these external factors are mainly driving inflation as local demand remains quite weak.

Offshore, the focus will sit with Fed Chairman Powell who is set to testify to lawmakers. This is often market-moving as the Fed chairman is forced to justify his position on rates in detail.

In looking at the bond market, note that the vanilla bond auction was stronger than last week, with total bids rising to R8.75bn from R8.67bn last week and bond yields tightening. While the R2035 and R2040 were also auctioned last week, the duration of the slate was lengthened this time with the R2048 auctioned instead of the R2040. The R2048 was clearly unloved in generating a bid-cover ratio of just 1.72x, marking the lowest demand level in records dating back to 2020. The slight pick-up in aggregate bids to R8.750bn mark the third-lowest this year; below the year-to-date average of R10.807bn.

High yields and low demand in the long end suggest that the market remains concerned with fiscal risk, which tends to be priced into the long end. Interestingly, this is taking place against the backdrop of a doubling in corporate bond issuance in 2022 relative to last year. Bloomberg reports that the corporate bond market has issued R131bn year-to-date, which suggests that issuance to the market will exceed its prior annual record of R137bn just six months into the year.



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