

The rand - range bound!

Bond sell-offs, poor US and SA data, UK elections and chaos surrounding the future of Greece is what the rand had to deal with in May (we won't even mention load shedding). Despite the drama, the local unit managed to stay range bound to the Dollar. Trading in between 11.77/\$ and 12.20/\$, the rand failed to break these key levels on several occasions. The local unit played passenger (more like a rollercoaster) to the EUR/USD pair following its break south of the key 1.10 level. In this edition, we unpack the bond sell-off and get the low down on what is happening in the US.



USD/ZAR June 2015

Day to day - we recap the month so you don't have to

01 May - South African markets take a breather to celebrate Workers' Day.

03 May - Floyd "Money" Mayweather retains his unbeaten streak with a win over Manny Pacquiao.

04 May - Local vehicle sales and manufacturing data fall short of expectations, suggesting the latter could be affected by electricity shortages.

05 May - Poor US trade balance figures help the rand trade back below 12/\$.

07 May - No surprise as the Conservative Party win the UK elections.

08 May - A drop in EUR/USD sends the rand packing as the local unit tests the 12.20/\$ level.

11 May - US and EU inflation data hits the mark as the rand remains under pressure.

12 May - The local unit breaks 19/£, its weakest level in 6 years!

14 May - Markets bet on a US interest hike by the end of 2015, the news helps the rand strengthen to 11.80/\$

20 May - The collapse in EUR/USD means the rand is now trading at more 'normal' levels to the Euro.

21 May - SARB Governor Lesetja Kganyago announces that interest

rates will remain unchanged for now.

25 May - The continent celebrates Africa Day, as global markets see the EUR/USD pair drop below the key 1.10 level.

26 May - SA Q1 GDP (1.3%) and Unemployment rate (26.4%) leaves the country in the dark (kind of like Eskom). The latter reaching an embarrassing 12-year high.

27 May - It's chaos, as FIFA officials are arrested for suspected bribery and corruption.

Honourable mentions - what to look out for

- Whether or not Greece will be able to make the IMF payment
- Possible strengthening of the US economy in the 2nd quarter
- Winter load shedding? Will it be lights out for SA?

Did you know - the rand

South Africa ranks 41st out of 192 countries in the Economist's "Biggest Exporters" Index.

Did you know - Currencies Direct

We apply for foreign investment tax clearance certificates on your behalf. If you would like to take out more than your R1 Million discretionary allowance, we do the application at no additional cost. Call us to find out more.



Forex jargon – know what you’re talking about

- **Support level**

A price that might act as a floor. (i.e. the floor in a trading range of 11.77/\$ and 12.20/\$ would be 11.77/\$)

- **Resistance level**

A price that might act as a ceiling. The opposite of support.

- **Technical**

Short for technical analysis, the process by which past price patterns are studied for clues as to the direction of future price movements.

Bonds - whisky tango foxtrot

What are bonds? Don't worry, you're not alone!

In plain English a bond is:

A form of debt (i.e. like a loan) in which an investor loans money to an entity (usually corporate or government) which borrows the money for a certain period of time at a fixed or variable interest rate.

Simple!

Bonds are one of the most popular investment options for large global funds. They (especially government bonds) are seen as less risky investments (their risk is determined by our friends at the credit rating agencies: Fitch, Moody's and S&P - yes, that's why these guys actually matter!) and are important parking lots for trillions of dollar.

That's cool, but how do they affect the rand?

Believe it or not South Africa is a very popular destination for global funds in the US, UK and Europe to invest their money (this is due to the relatively high returns on SA bonds). To purchase South African bonds, these funds need... yes,

rand! And the most basic principle of economics tells us that if demand for a product increases, its price will go up. In this case, the product is our rand. Make sense?



How big an impact do bonds have on the rand?

Big... we're talking billions of rands daily. South Africa's bond market is one of the most liquid in the world with daily flows averaging R25bn. 26% of the market was foreign owned in 2013. So we're talking about potential flows of R6.5bn daily! It doesn't take a rocket scientist to work out the potential

impact on the rand.

So that's it, now you know why bonds matter.

South African Reserve Bank (SARB) - pre-emptive vs reactive

May saw the SARB keep interest rates at 5.75%, but the devil was in the detail as Governor Lesetja Kganyago laid the ground work for imminent rate hikes.

So why raise interest rates?

The thinking is as follows: When the US Fed finally begins to hike interest rates, it would lead to a flight of capital back to the US (i.e. investors will take money out of their SA investments and return the funds to the US). Why would they do this? As the US raise interest rates and returns on investments rise, they gradually become a more attractive destination for investors.

If emerging markets, SA included, have not raised their own interest proportionately, the fear is that a flight of money back to the US could cause severe currency depreciation for emerging markets.

What can the SARB do?

Despite the SARB only being mandated to control inflation, not the rand, the thinking is that any depreciation in the rand would lead to inflationary pressure. To prevent this, SARB Governor Kganyago has stated his intent to begin an interest rate hiking cycle.

The idea:

Raise interest rates before the US Fed and maintain SA's position as a favourable investment destination. Will it work? It will be a tough sell with growth in SA struggling to hit 2% in 2015.

Is it the right move?

Let's get technical

USD/ZAR



This month saw the USD/ZAR breach this years 11.79/\$ support level (purple line) only to bounce off the long term trend line and continue straight through the top of the descending triangle pattern. The latter coincides with the release of positive US data and the hint of a possible interest rate hike later this year. If the US economy continues to strengthen, the USD/ZAR long term upward trend looks to stay intact.

GBP/ZAR



The GBP/ZAR broke through the top of the symmetrical triangle pattern we saw forming last month. This confirms that this years upward trending trading range is still in play. Look out for price reversals once the trend lines are hit.

EUR/ZAR



EUR/ZAR is still trading in consolidation for the year but we saw a small breach of the 13.49/€ resistance level which came to nothing. The upward trend that started in April seems to be holding true as we saw the trend line come in to play at the end of May. If the trend continues to hold a proper break through the 13.49/€ level could see the rand weaken and break 14.00/€.

US Economy - hit or miss

The US economy got off to a questionable start in Q1 growing by -0.7% (well shy of the 1% forecast and miles off the 2.2% growth seen in Q4 of 2014). However, recent positive economic data may well be looking to turn this around. One must bear in mind that the US was in a similar slowdown this time last year and bounced back quite nicely during the year.

Reasons for the slump in Q1.

The following factors might be to blame for the low growth in the first quarter:

- **A harsh Winter:** America experienced unusually cold weather over Q1 which likely made the population stay indoors and save their cash or head overseas on holiday and spend their money abroad. This saw consumer spending barely rise.
- **Slow down in shipping:** Dock worker strikes on the west coast saw a decrease in US exports/imports and prevented manufacturers from receiving inventory on time, which in turn slowed down production.
- **A strong dollar:** The strong dollar made US products too expensive for the rest of the world, which decreased the number of exports and saw corporate profits drop.

The Q2 turn around.

The 2nd quarter of the year saw the US unemployment rate near a 7 year low at 5.4%, dropping from 10% in 2010. This coupled with a 2.2% increase in wages and job creation across all industries, suggests that the labour market is moving in the right direction but is still not fully recovered. Inflation has its part to play too. It has been on the rise for the 3rd consecutive month this year, signalling the US is stabilising and an interest rate hike by the Fed may be possible some time this year.

So where could things be heading?

If the strong US data keeps on coming this won't be good for the rand and we could see it surpass its all time weakest level at 12.77/\$. There is no need for panic stations just yet, as although the recent Q2 data has been positive, it is still disappointing in terms of what was seen in late 2014.

Currencies Direct presents: the crystal ball

Disclaimer: Folks, if we really had a crystal ball we'd be sitting on a tropical island sipping cocktails while we count our millions. This is just a fun opinion piece for us to try our hand at putting together a few scenarios for the month ahead, nothing more, nothing less.

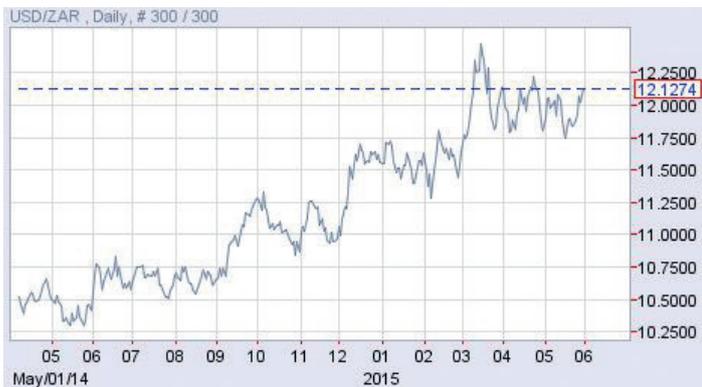
Dollar rally kicks into gear

A smashing start to the month with US jobs numbers setting the tone for serious USD strength. Janet Yellen mentions that Q1 was a temporary glitch in what is suppose to be a phenomenal 2015 for the USD. Inflation follows suit as markets bring forward a US interest rate hike with the rand saying hello to 12.50/\$.

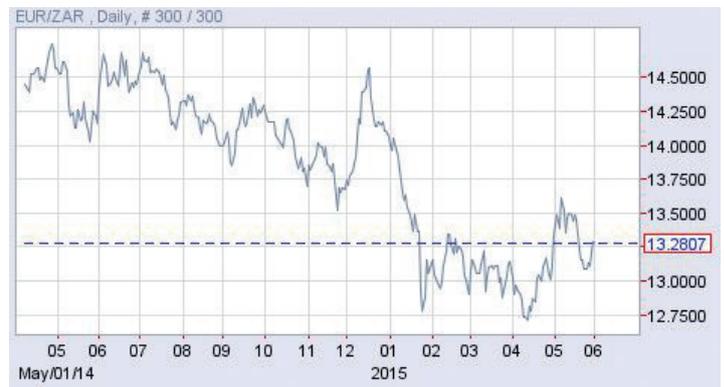
The technical corner

Technically we're in for rand weakness against the USD, with a test of the 12.50/\$ level not impossible. Look for 12.50/\$ before any rand recovery. The rand looks set to test the 13.49/€ again and may attempt a run at 14/€ if it can break 13.49/€. Against the Sterling the rand looks set to test the 19/£, as a weaker trend looks like it's here to stay.

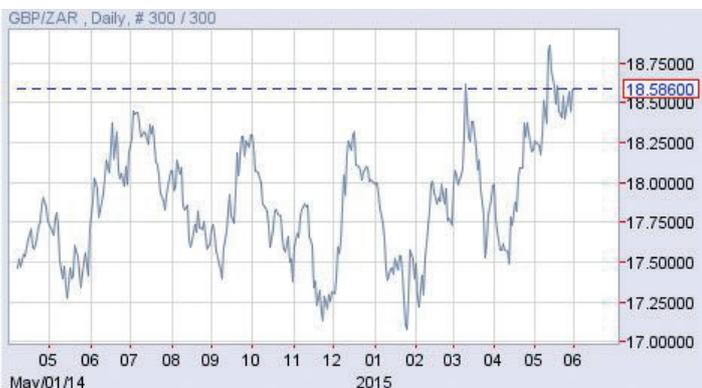
ZAR YEARLY vs THE MAJORS



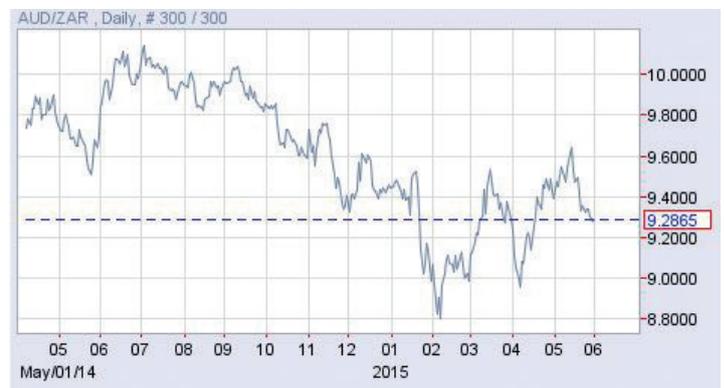
ZAR vs USD



ZAR vs EUR



ZAR vs GBP



ZAR vs AUD

ZAR May highlights

Currency	Open	High	Low	% Change
USD/ZAR	11.8924	12.2067	11.7002	-2.35%
EUR/ZAR	13.3424	13.7958	12.9464	0.5%
GBP/ZAR	18.2420	19.047	18.075	-2.2%

Economic calendar - what to look out for in June

Event	Date	Previous	Forecast	Our 2 cents
US Nonfarm payrolls and Unemployment rate	05-Jun	223k and 5.4%	227k and 5.4%	The labour market in the US is doing well, will it continue to improve?
US Interest rate decision	17-Jun	0.25%	0.25%	The press conference following the announcement will be what markets will be eyeing
SA Current Account	18-Jun	R-198 Billion	R-246.1 Billion	We might be in for a surprise
US Inflation rate	18-Jun	1.80%	1.63%	This could bring expectation for a rate hike forward
SA Trade Balance	30-Jun	R-2.5 Billion	R-5.4 Billion	2 consecutive months of beating expectations, will it be 3 in a row?