The outlook for the Rand during the remainder of 2022

The Rand held-up well against the US Dollar in the first half of 2022, supported by high commodity prices, but has depreciated by almost 6% against the Dollar in the past 10 days. This is due to a combination of factors, including further Dollar strength, and declining commodity prices, but also increased concerns about the impact of electricity outages on the performance of the South African economy.

At R16.75/$ the Rand appears relatively weak, but a range of factors need to be evaluated in order to gauge the likely direction of the currency during the remainder of 2022. These include the strength of international metal and mineral prices, changes in domestic and international interest rates and the overall performance of the South African economy.

Commodity prices
During the first quarter of 2022 the Rand benefitted significantly from higher commodity prices. However, more recently a wide range of metal and mineral prices have softened considerably, largely as a result of increased concerns about a sharp slowdown in global growth. This has resulted in renewed Rand weakness.

Unfortunately, concerns about global growth are expected to intensify given further rate hikes. This will tend to further undermine that Rand performance through reduced export revenue and some deterioration in the country's trade balance.

South Africa's economic performance
The South African economy is expected to lose further momentum over the next six months, hurt by a combination of weak consumer confidence, higher fuel and food prices, persistent electricity outages, slowing export revenue, and higher interest rates. Fortunately, South Africa is not alone. Most emerging economies are also expected to experience a slowdown in economic activity. Consequently, South Africa's economic performance should, perhaps, not be viewed as a big downside risk for the Rand, especially at current levels.

Global and domestic interest rates
The United States is very likely to continue to hike interest rates during the remainder of 2022 and into early 2023. This, together with the recent increase in global risk aversion will tend to further support the Dollar. It also means that most emerging markets that are heavily reliant on attracting foreign capital, such as South Africa, will be under pressure to also continue to increase interest rates, or risk further currency weakness.

Fortunately, the South African Reserve Bank is determined to get South Africa's inflation back inside the target and seems willing to increase interest rates further despite the likely social and political backlash. This would suggest that while the ongoing strength of the Dollar is not good for the Rand's performance, this pressure will be partially offset by higher domestic interest rates.

SA political developments
Political tension in the country is clearly on the rise and is likely to intensify as we approach the ANC's elective conference later in the year. While increased political news is unhelpful at the best of times, most foreign investors view these types of developments as 'normal' within an emerging market context. Consequently, unless the political news is highly likely to lead to the replacement of President Ramaphosa, it is not expected to a have a very meaningful and direct impact on the performance of the Rand.

Overall
Taking these factors into account, it is evident that the current environment is net negative for the Rand. However, the rand is already undervalued and appears to have priced-in many of the concerns outlined above. This would suggest that some short-term improvement in the Rand /Dollar exchange rate is entirely feasible. Equally, however, although the Rand appears relatively weak, there is little evidence to suggest that the currency will strengthen on a sustained basis during the remainder of 2022.

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