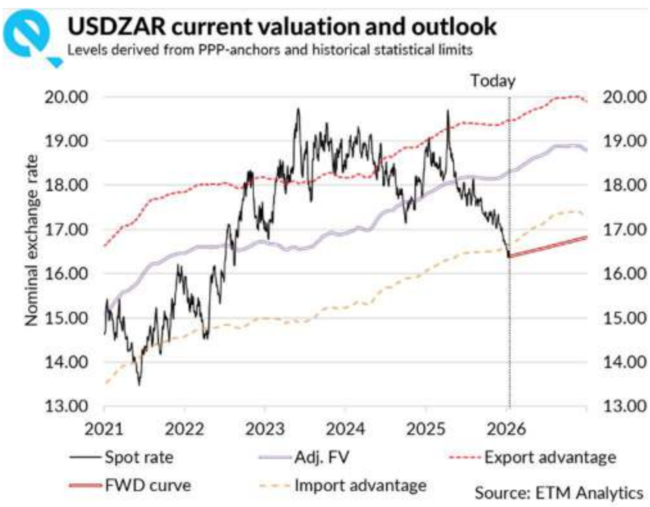
ZAR Service: FX positioning
January 2026

Summary of macroeconomic research views:

- **Currency:** At the start of 2025, the rand was under significant pressure, with investors wary of political instability and the potential collapse of the Government of National Unity, keeping USD/ZAR at elevated levels, but sentiment shifted decisively as the year unfolded. Confidence returned after the GNU survived the budget standoff and delivered a fiscally responsible budget, reinforced by South Africa's removal from the FATF greylist, a sovereign credit rating upgrade, and the adoption of a more credible 3% inflation target, while improving global risk appetite and strong commodity prices lifted South Africa's terms of trade. Together, these factors sparked a sustained and powerful rand rally that accelerated into late 2025 and early 2026. Although short-term volatility and occasional pullbacks have emerged, the underlying fundamentals point to a structurally stronger trading range. Despite valuation models suggesting the currency is overbought, positive sentiment and the prospect of another prudent budget support continued strength, keeping USD/ZAR stronger, with a push towards R16.00 possible.
- **Inflation:** Headline CPI remained stubbornly buoyant at 3.5% y/y in Nov vs the 3.6% y/y in Oct. Overall, SA's inflationary outlook remains subdued, albeit it above the 3% inflation target and should prompt the SARB to remain somewhat conservative.
- **Repo rate:** The SARB cut interest rates by 25bp in November. Although this was the first meeting under the newly formalised inflation-targeting framework, policymakers agreed that monetary conditions could be eased without jeopardising progress toward the new target. The SARB QPM model forecasts interest rates to average 6.19% by the end of 2026 and 5.99% by the end of 2027.
- **Government Finances:** South Africa's monthly budget deficit narrowed to -R14.9bn in November from -R35.8bn in October as a result of a R22.9bn increase in revenue, which outweighed a R2.1bn increase in expenditure. While the improved main budget numbers in 2025/26 are welcome, the government must leverage lower borrowing costs and the opportunity for policy reform to run a more balanced budget.
- **GDP Growth:** Q/q seasonally adjusted growth declined slightly from 0.9% in Q2 to 0.5% in Q3. Gross fixed capital formation (GFCF) saw a moderate improvement, driven largely by transport. Alongside the improvement in exports, one suspects that the impact of Operation Vulindlela on restructuring the transport sector is beginning to yield fruit. Nonetheless, growth remains fairly pedestrian overall, at around 1%, suggesting that further reforms are necessary to boost the economy.
- **Offshore conditions:** Global equity markets remain strong and continue to power through the wall of worry about valuations and a global cyclical downturn. With central banks responding by lowering interest rates and companies investing aggressively in AI infrastructure, the US economy appears to be bucking the downturn trend. Whether that remains the case will depend on whether the AI boom continues and how strongly monetary policy supports asset prices. Geopolitically, there are also numerous shifting developments, from Venezuela to Ukraine, Iran, Greenland, China, and Taiwan, but these are not yet boosting risk premia.

FX valuation indicators:



USD-ZAR: Since May 2025, the ZAR has posted an impressive performance, appreciating at an accelerated pace towards the end of 2025 and the start of 2026. While 2025 started in perilous fashion with investors fearing the collapse of the GNU and higher degrees of risk aversion, that all changed dramatically.

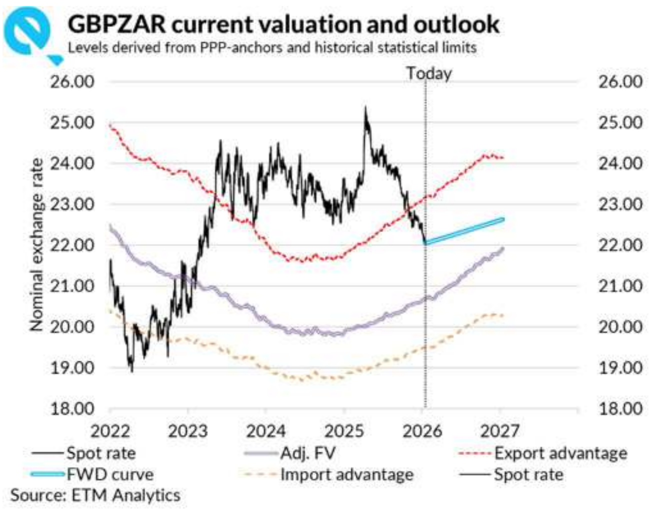
Five main events triggered this. The first was that the GNU survived the budget impasse. The second was the passing of a responsible budget, the third was removal off the FATF greylist, the fourth was a credit rating upgrade and the fifth was the adoption of a 3% inflation target. These come on top of improved market conditions that bolstered risk appetite and strong commodity prices, which raised SA's terms of trade.

The combination resulted in a sustained phase of ZAR appreciation and given all the factors above, the ZAR has entered a new phase where it can continue trading in a fundamentally stronger range.

EUR-ZAR: Against the USD, the EUR has held firm in a well-contained range at the stronger end of the valuation spectrum. In other words, the EUR has been able to hold on to its gains vs the USD despite all the difficulties the eurozone has faced, including the war in Ukraine, a slowing business cycle and deteriorating fiscal positions of the main economies within Europe.

Against this backdrop, the ZAR's recovery against the EUR has been a notable performance, although the accompanying chart shows that the ZAR remains in undervalued territory relative to the EUR. Gradually, it is heading back towards fair value, which would approach levels closer to 179.50 EUR, but that may take several more weeks to unfold.

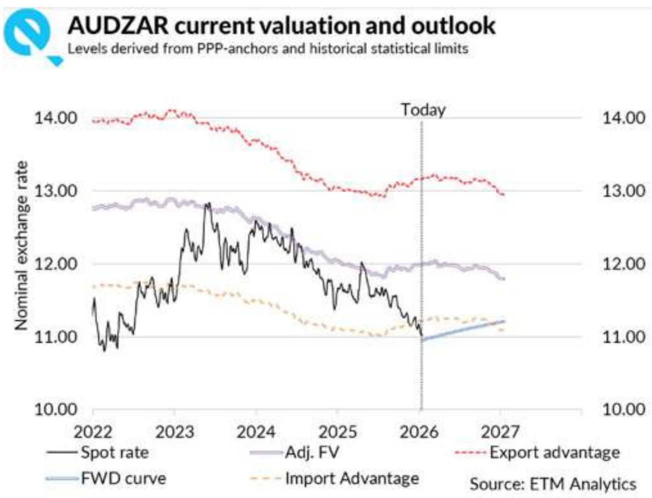
The conclusion is that the ZAR is currently appreciating in its own right, due to domestic fundamentals that appear to have improved significantly over the past six months, for the reasons listed above. That said, there is still room for the ZAR to appreciate further with the EUR, especially if the ECB cuts rates further.



GBP-ZAR: Although the ZAR has made a remarkable recovery since mid-2025, when the GBP-ZAR traded well above 25.00/GBP, the ZAR remains heavily undervalued against the GBP and holds the potential to extend its recovery significantly further.

Although a tighter fiscal policy is generally more supportive of an underlying currency, there is a point where tighter fiscal policy might undermine economic prospects to such a degree that it undermines in the investment thesis of that jurisdiction. In the case of the UK, unsustainable debt levels and the budget deficit needed to be addressed.

The Labour government has chosen to address this by raising the overall tax burden. GDP growth will likely falter, and the size of the government will choke out the private sector. It is likely that the BoE will be inclined to reduce rates further, possibly at a more rapid rate than in SA, as the business cycle continues to moderate and gradually erodes the GBP's carry potential. In ETM's carry attractiveness rankings, the GBP ranks poorly.

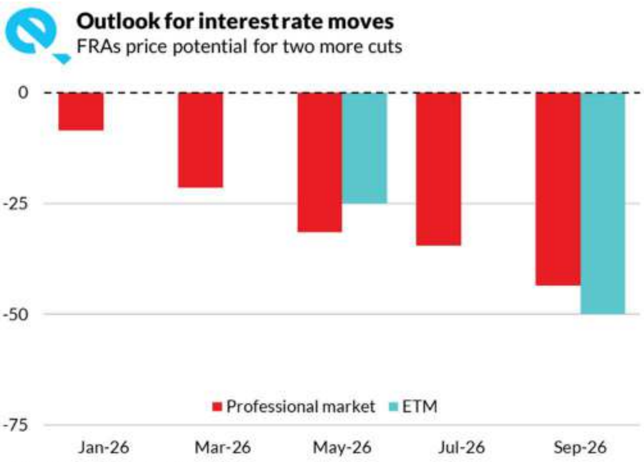


AUD-ZAR: Notwithstanding the positive prospects for the AUD over the next six months, the ZAR has continued to gain ground against the AUD and now finds itself in overbought territory. What is particularly interesting about the ZAR's appreciation against the AUD, is that it is appreciating against a fellow commodity currency that should also have benefited from the positive market environment now.

This offers further perspective on the ZAR's appreciation and suggests that the appreciation has less to do with market gyrations and more to do with a reduction in risk assessment concerning South Africa. There are many reasons for this, as mentioned above, but a significant shift in foreign assessments of SA is also reflected in the drop in bond yields, a neutral current account, and constructive future prospects.

There is a strong argument to be made for a sharp reset in the ZAR's trading range, and that what appears to be overbought in these charts, is simply part of the reset process.

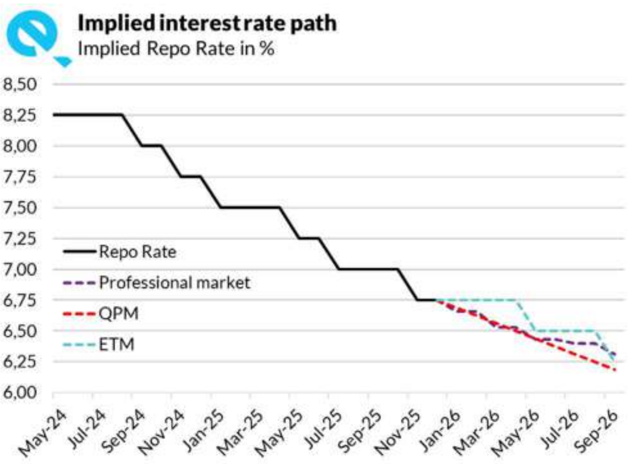
Interest rate indicators:



Source: Bloomberg, ETM Analytics

Recent movements in the FRA market suggest a cautiously improving outlook for South African interest rates. A firmer rand has helped shift the FRA curve slightly lower, reinforcing market expectations that the SARB could begin easing policy as early as March.

However, the anticipated pace of cuts remains slow and measured. While one cut is increasingly priced in for the near term, a second reduction is more likely only in the second half of the year, with the FRA curve implying roughly two 25bp cuts through 2026. This reflects a deliberately conservative approach, aimed at anchoring inflation expectations even as other global central banks move more decisively in response to economic weakness.



Source: SARB, Bloomberg, ETM Analytics

Recall that the SARB's November MPC decision to cut the repo rate by 25bp to 6.75% was widely expected and framed as consistent with a still-restrictive stance. Despite questions around alignment with a 3% inflation target, the central bank maintained that policy remains appropriately tight to secure price stability.

If the rand remains resilient and global market volatility is contained, inflation should stay subdued, giving the SARB scope for the one or two additional cuts priced in through 2026.

Even so, the outlook points to gradual easing rather than an aggressive cycle, with patience required as the SARB continues to work on firmly anchoring inflation expectations