Summary of macroeconomic research views:

- **Inflation:** Headline inflation eased by slightly less than expected in January to 3.5% y/y from 3.6%. The softer reading marks continued progress toward the SARB's 3% inflation target, validating the timing of its mandate shift. Looking ahead, inflation is likely to ease further in February. However, further out, much will depend on how long the Middle East war continues and whether ZAR deprecation is sustained or not.

- **Repo rate:** Given the latest developments in the Middle East, which have pushed oil and the ZAR upwards, it is possible that inflation could rise to 4% in March; the SARB will likely keep interest rates unchanged later this month.

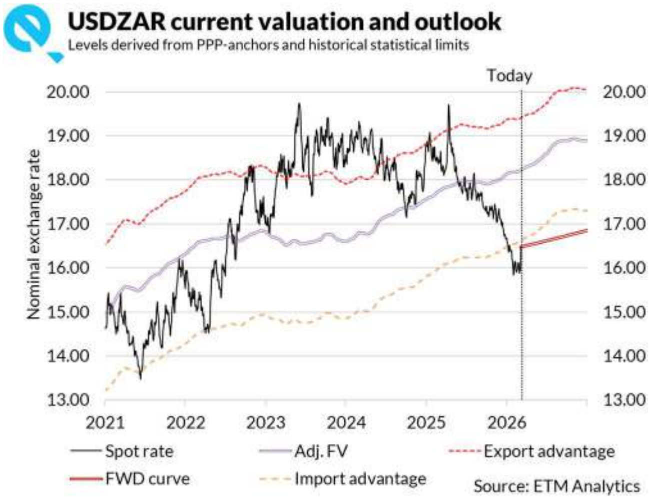
- **Government Finances:** While the ytd budget deficit has narrowed to -R312.6bn from -R347.8bn a year earlier, the gross borrowing requirement has worsened to -R444.7bn, largely due to heavy redemptions of maturing government debt. Stronger revenues offer fiscal relief, yet doubts remain over whether the government can sustain consolidation and rein in spending.

- **GDP Growth:** Q/Q seasonally adjusted growth declined slightly from 0.9% in Q2 to 0.5% in Q3. Gross fixed capital formation (GFCF) improved moderately, largely driven 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.

- **Currency:** The ZAR appreciated by 1.3% against the USD, 1.7% against the EUR and 2.9% against the GBP in February even as the geopolitical risk started rising into the month-end as the US built up its military presence in the Middle East. The ZAR gained following the tabling of the Budget. However, much of SA's fiscal relief depends on volatile, uncertain commodity prices. Into March, risk-off sentiment due to the war in the Middle East has led the ZAR to weaken along with other emerging market currencies. ZAR weakness will be tempered somewhat by the rise in gold prices driven by safe-haven demand, which will feed through into SA's terms of trade. However, a prolonged war has the potential to keep the ZAR under pressure. ETM's indicators suggest that the volatility the ZAR is currently experiencing could see the USD-ZAR spike significantly further and unwind most of the ZAR's appreciation over the past six months.

- **Offshore conditions:** Renewed uncertainty around Trump's tariff agenda intensified after the Supreme Court overturned his emergency tariffs. Trump then implemented a 15% tariff globally. Meanwhile, late-January FOMC minutes struck a hawkish note and signalled caution on further rate cuts, which underpinned the US dollar. That support has strengthened further as escalating geopolitical risks in the Middle East and the prospect of inflationary pressures from surging oil prices have fuelled a sharp rally in the US dollar. The conflict will keep uncertainty levels high and market volatility elevated.

FX valuation indicators:



USD-ZAR: The Middle East war has driven global risk-off sentiment. The ZAR has depreciated to levels of 16.68/$ at the time of writing, its weakest levels since the end of December 2025. While it has recovered somewhat, on a risk-adjusted basis, the degree of ZAR overvaluation against the USD has lessened (USD-ZAR undervalued).

Nonetheless, it remains at levels which importers should take advantage of. The model suggests that USD-ZAR fair value is more in line with levels north of R18/USD.

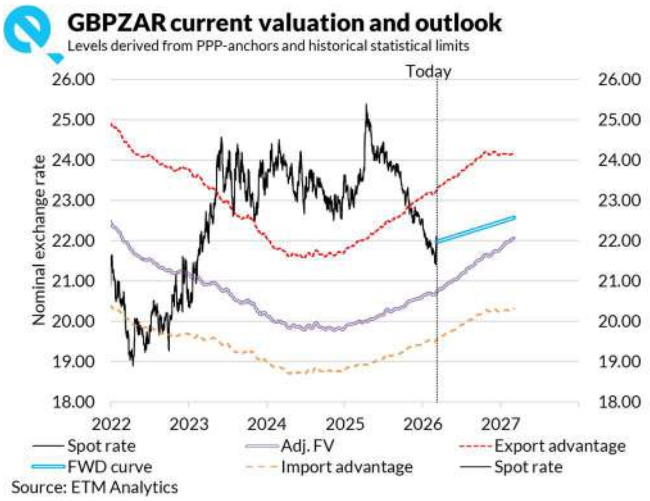
Much will hinge on the duration and intensity of the Middle East conflict, which has boosted the greenback on safe-haven demand and inflation risk from higher oil prices, pushing US Fed fund futures to move expectations of a July rate cut to September/October.

The effects of ZAR weakness and the rise in oil prices to almost $90/bbl (at time of writing) will be somewhat cushioned by buoyed gold prices on safe-haven demand, which will benefit SA's terms of trade. Valuations versus the USD were stretched, with heavy foreign buying and hedging activity suggesting the ZAR could face a sharp reversal if sentiment shifted or commodity prices fell. Therefore, the ZAR remains vulnerable to any developments in the Middle East that could further raise risk aversion.

EUR-ZAR: The EUR-ZAR's move from 21.00 in August to current levels around 19.00 has brought it to fair value, eliminating what was previously an opportunity for exporters. The ECB held its benchmark rate at 2%, but markets have started pricing some hike risk as concerns grow over sustained oil price increases if the Strait of Hormuz remains disrupted. This marks a notable shift for a central bank that recently finished cutting rates.

The SARB's rate sits at 6.75% with little to no further easing now priced in. However, this could shift back to around two full 25bp cuts should Middle East tensions ease and conditions return to normal. A quick resolution would likely push the pair lower and deeper into undervalued territory, favouring importers who wait. Prolonged conflict would reverse recent ZAR gains and benefit importers who hedge now.

On the whole, the fair value positioning creates uncertainty, with neither exporters nor importers facing clear value at current levels. The pair has shifted from a trending market into a situation where the Iran conflict will determine direction in the coming weeks.

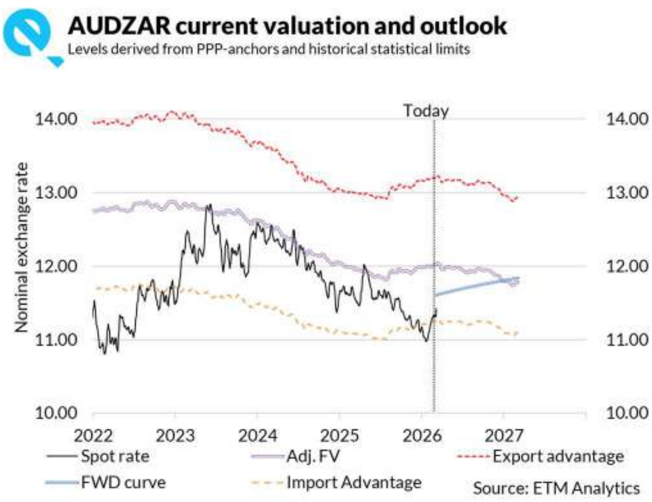


GBP-ZAR: The GBP-ZAR continues to trade above fair value despite falling from 25.00 in April to current levels around 22.00, maintaining some exporter value. The recent spike above 22.00 came from Middle East tensions, but the broader downtrend remains intact if the conflict resolves quickly.

In terms of carry, the BoE has held rates at 4%, with only one more rate cut priced for this year unless oil pressures fade. The SARB's 6.75% rate could see two further cuts if conditions normalise, but current pricing shows caution given ongoing uncertainty.

The pair's distance from fair value has narrowed considerably from the extreme overvaluation seen earlier in the year, limiting the attraction for exporters compared to previous months. With the cross hovering closer to fair value and direction tied to geopolitical developments beyond either central bank's control, exporters and importers face a wait-and-see environment.

Future direction depends more on how quickly stability returns to the Middle East than on domestic fundamentals from either the UK or South Africa.



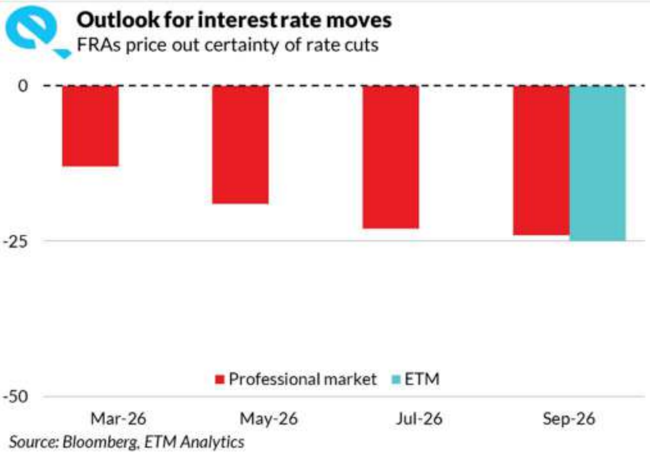
AUD-ZAR: The AUD-ZAR cross compressed through much of 2025, bottoming near key 11.000 support in January and leaving the cross deeply oversold. Since then, sentiment has turned and the AUD-ZAR has rebounded sharply, breaking above 11.6000 and clearing its 200DMA at 11.3670 as it moves back toward risk-adjusted fair value around 12.0000.

The rebound has been supported by diverging monetary policy expectations. The RBA has already begun tightening, delivering a hike at its February meeting, with cash rate futures pricing another 25bp increase as early as May, while the SARB is now expected to keep rates on hold, for now.

Even so, AUD-ZAR remains well below risk-adjusted fair value, leaving the ZAR strong relative to the AUD. Historically, such undervaluation has proven difficult to sustain and has typically preceded a move back toward fair value.

With the RBA entering a tightening cycle while the SARB outlook has turned much less certain, alongside a more fragile global backdrop and rising oil prices that threaten South Africa’s external balance, the balance of risks is beginning to shift. Against this backdrop, a gradual move in AUD-ZAR back toward fair value appears increasingly plausible.

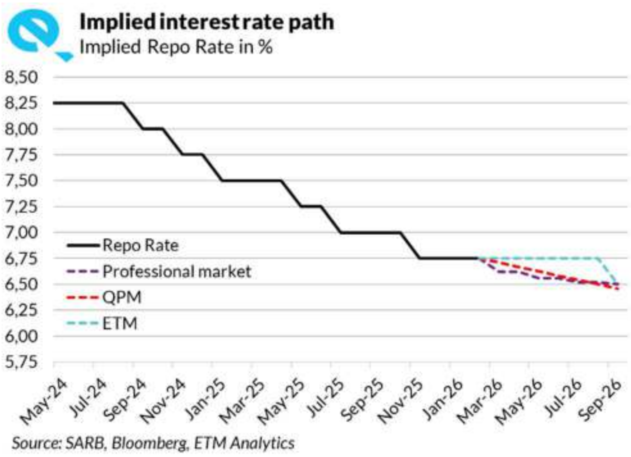
Interest rate indicators:



The conflict in the Middle East has prompted a major rethink of the market's expectations for further rate cuts from the SARB. Unsurprisingly, movement in the FRA market remains highly dependent on the ZAR's performance and current oil price dynamics.

The higher the oil price in ZAR, the lower the probability of a rate cut this year, and we have already seen a major repricing.

Not even the longer-dated FRAs fully price in a rate cut anymore, with the tenor covering the September MPC meeting pricing in just under 25bp of cuts. The 1x4 FRA, which covers this month's meeting, has just under 13bp of cuts priced in, which is likely to reduce further unless we get a strong ZAR recovery and a retreat in global oil prices.



If oil prices spike significantly further, FRA rates might even price in a rate hike. Whether the market tilts towards rate hikes again will depend on how protracted this war becomes. The longer the conflict continues without signs of de-escalation, the greater the risk of global stagflation, leaving central banks in a tricky position.

The current situation justifies the SARB's decision to keep interest rates unchanged in January, while vindicating the QPM's more cautious rate path ahead as the central bank aims to keep inflation expectations anchored around the 3% target.

Given the recent spike in oil and the expected inflation pressures that come with it, it is likely we will see another cautious decision this month, with the tone to shift even more toward the hawkish side to cement the view that the SARB is not afraid to act if needed to ensure its new inflation target is met.

Looking further out, if the situation stabilises, the SARB may resume easing depending on how the ZAR recovers and oil prices retreat. However, the situation remains extremely fluid at the moment, and the outlook for interest rates will likely be determined on a meeting-by-meeting basis as the situation is assessed at the time.

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