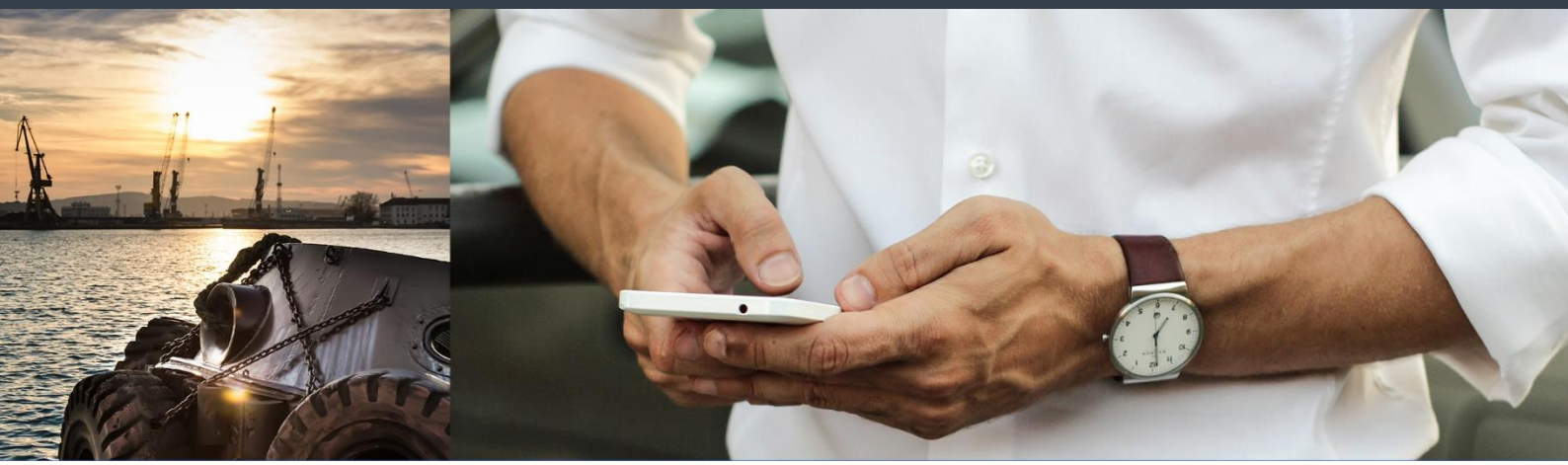
ECONOMIC REPORT

by Glacier Research

glacier by Sanlam



26 August 2021

Review period: July 2021

Introduction

In the month of July, local equity markets rebounded handsomely from losses of the previous month, thanks to strong recovery in the resources sector as commodity prices remain supportive. The rand continued to weaken with the social unrest being a contributor. On the economic front, social unrest that broke out in KwaZulu Natal and Gauteng took the spotlight and will have dampening ramifications for the country's path to economic recovery. On the global side, the spread of the COVID-19 Delta variant unsettled cyclical areas of the market with bond yields retreating to levels last seen in February this year while the ECB tweaked its policy guidance on inflation. Talks of the Fed tapering off its bond purchases are starting to make their way into market sentiment. The Chinese regulatory crackdown of the private education and tech sectors led to a sharp sell-off in emerging market equities.

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Domestic Highlights

- Fiscal intervention package
- SARB interest rate decision

Fiscal intervention package

Following the social unrest that took place in the aftermath of the imprisonment of former President Jacob Zuma, the National Treasury unveiled a relief package to the tune of R38.8 billion. The relief package is aimed at financially supporting households impacted by the COVID-19 pandemic and businesses affected by the destruction of property and the disruption of business operations that emanated from the unrest. The relief package will reportedly be funded through the Treasury's existing funding framework and the reprioritisation of existing departmental budgets. Budgetary reprioritisation will unlock R2.65 billion while the remaining R36 billion will be funded through the R100 billion windfall from the mining sector as opposed to issuing new debt. The breakdown of the relief package spending is as follows:

- R26.7 billion will fund the R350-a-month COVID-19 social grant that was reintroduced until March 2022.
- R2.3 billion will fund the support of uninsured businesses that suffered losses as a result of the social unrest.
- R3.9 billion will be allocated to the South African Special Risks Insurance Association (SASRIA) to assist with business claims emanating from the social unrest. These are estimated to be close to R50 billion in total.
- R950 million will be allocated to the security cluster (the police and the army) in order to stabilise areas affected by the social unrest.

SARB interest rate decision

In its July meeting, the SARB left interest rates unchanged at 3.5% in a unanimous decision, citing some fiscal improvements over commodity price tailwinds and an accommodative global macro policy backdrop. However, it also raised important issues relating to the negative impact of the recent unrest on investor confidence and recovery. The slow pace of vaccination uptake and peaking of the COVID-19 third wave were also highlighted as weighing negatively on the path to recovery. The SARB currently expects growth to be 4.1% in 2021 before sliding to 2.3% in 2022 and 2.4% in 2023. The headline consumer price inflation forecast was revised slightly higher to 4.3% in 2021 before easing to 4.2% in 2022 and stabilising at 4.5% in 2023. Higher food and petrol prices are key drivers. Overall risks to short-term inflation are assessed to be on the upside. The SARB's Quarterly Projection Model is pointing to a 25 basis points increase in the fourth quarter of 2021 and right through 2022.

SA economy

Elevated commodity prices have presented handsome tailwinds and windfalls for the fiscus such that a trade surplus has been persisting and helping to stabilise the country's finances as growth is starting to come through. However, the recent unrest has interrupted this momentum as funding that could have been potentially used to finance growth initiatives has now been used to finance the cost of the unrest. Prolonged lockdowns and slower vaccination rates also weigh negatively on economic recovery. Economic activity in July has seen a substantial

slowdown as the manufacturing PMI fell from 57.4 in June to 43.5 in July. Business activity and new sales orders were the biggest contributors to the downfall, reflecting the effects of tighter lockdown measures that were put in place.

	Feb'21	Mar'21	Apr'21	May'21	Jun'21	Jul'21
CPI (y/y)	2.9%	3.2%	4.4%	5.2%	4.9%	4.6%
PPI (y/y)	4.0%	5.2%	6.7%	7.4%	7.7%	-

Sources: Trading Economics

	31 July 2019	31 July 2020	31 July 2021
USD/ZAR	14.34	17.06	14.62
GBP/ZAR	17.44	22.34	20.31
EUR/ZAR	15.88	20.11	17.34

Source: IRESS

SA markets

Local equity markets ended the month higher, rebounding from the June sell-off as the resource sector made a strong recovery after the sharp losses recorded in June. The All Share was up 4.18% for the month with large caps delivering a gain of 2.56% while mid-caps turned in a gain of 2.79%. Small caps, however, bucked the trend to end the month 1.12% lower. Meanwhile, property (-0.40%) gave up some of the gains it recorded in June. On the fixed income side, bonds closed 0.83% higher with the belly of the curve, i.e. 3-7 year and 7-12-year maturities, driving most of the returns. The 12 year+ area was marginally up 0.55% while the seven- to 12-year area gained 1.11%. On the front-end of the curve, the one- to three-year area gained 0.94% while cash was up 0.33%. Inflation-linked bonds regained some ground, adding 0.22% along with preference shares which gained 0.73%.

Foreigners were net sellers of R28.17 billion worth of SA equities and net sellers of R8.08 billion worth of SA bonds.

LOCAL RETURNS IN ZAR				
2020	May 2021	June 2021	July 2021	Year-to-date
SA TOP 40 9.97%	SA MID CAPS 6.16%	SA PROPERTY 3.02%	SA TOP 40 4.53%	SA SMALL CAPS 29.46%
SA BONDS 8.65%	SA BONDS 3.73%	SA BONDS 1.09%	SA EQUITY 4.18%	SA PROPERTY 19.62%
SA EQUITY 7.00%	SA SMALL CAPS 3.33%	SA CASH 0.31%	SA MID CAPS 2.79%	SA MID CAPS 19.07%
SA CASH 5.39%	SA EQUITY 1.56%	SA SMALL CAPS -1.00%	SA BONDS 0.83%	SA EQUITY 17.93%
SA SMALL CAPS -0.28%	SA TOP 40 1.14%	SA EQUITY -2.43%	SA CASH 0.32%	SA TOP 40 17.33%
SA MID CAPS -14.37%	SA CASH 0.31%	SA TOP 40 -2.56%	SA PROPERTY -0.40%	SA BONDS 5.86%
SA PROPERTY -35.53%	SA PROPERTY -3.23%	SA MID CAPS -2.58%	SA SMALL CAPS -1.12%	SA CASH 2.16%

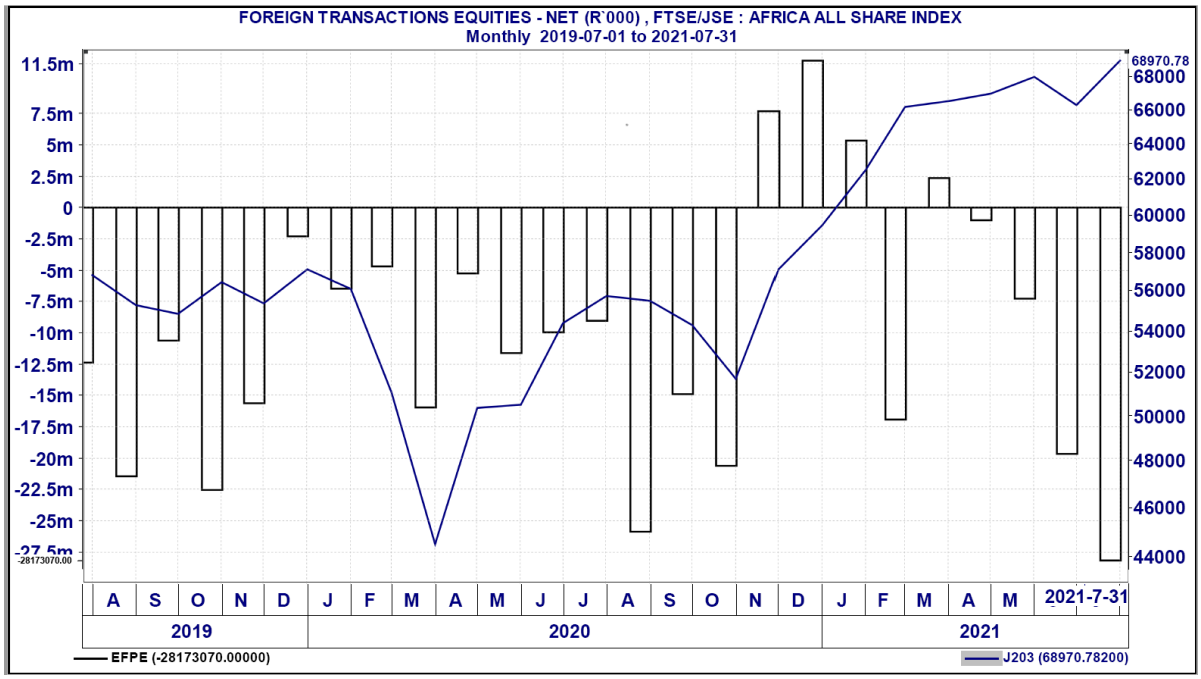
Source: Morningstar & Glacier Research

In terms of sectors, resources were the leading contributor, advancing 11.67% followed by industrials which were up 5.90% while SA industrials gained 0.94%. Financials were the laggards for the month, losing 1.21%.

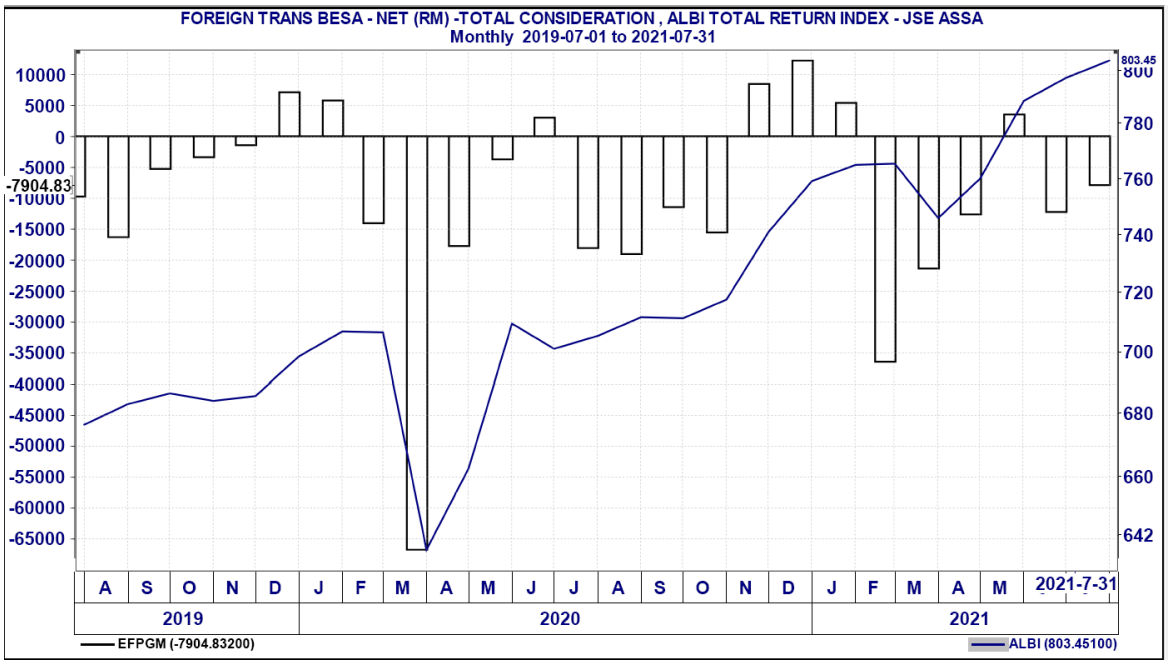
LOCAL SECTOR RETURNS IN ZAR

2020	May 2021	June 2021	July 2021	Year-to-date
RESOURCES 21.20%	CONSUMER SERVICES 12.04%	CONSUMER SERVICES 3.30%	RESOURCES 11.67%	CONSUMER SERVICES 42.67%
CONSUMER GOODS 13.31%	FINANCIALS 9.30%	GENERAL RETAILERS 1.86%	CONSUMER SERVICES 6.33%	GENERAL RETAILERS 39.54%
SA INDUSTRIALS 12.00%	CONSUMER GOODS 4.14%	CONSUMER GOODS 1.20%	INDUSTRIALS 5.90%	INDUSTRIALS 26.68%
CONSUMER SERVICES -8.80%	INDUSTRIALS 2.62%	SA INDUSTRIALS 0.38%	CONSUMER GOODS 1.13%	RESOURCES 25.98%
GENERAL RETAILERS -15.39%	SA INDUSTRIALS 1.59%	INDUSTRIALS -0.19%	SA INDUSTRIALS 0.94%	SA INDUSTRIALS 14.89%

Source: Morningstar & Glacier Research



Source: IRESS July 2021



Source: IRESS July 2021

Global markets

Global equity markets continued their recovery, supported by substantial stimulus, savings, and a pick-up in vaccinations. However, markets were constrained by concerns that the spread of the more contagious Delta variant of COVID-19 may slow down the pace of recovery. In addition, actual inflation risks remain heightened, but estimates continue to suggest upward pressure is transitory. As a result, global equity markets ended the month of July higher. Most equity sectors experienced positive returns with the S&P 500, MSCI World AC and MSCI Developed Market returning +2.27%, +0.59% and +1.72%, respectively, in dollar terms. From a sector perspective, sectors were mostly positive, with real estate, healthcare and utilities leading the pack.

Energy and financial services were the laggards during the month. The price of Brent crude oil increased from US$74.62 to close at US$75.41 a barrel, as demand grew faster than supply and vaccinations are expected to alleviate the impact of a resurgence in COVID-19 infections across the world. The US 10-year treasury yields dropped by 25 bps, falling to 1.22%, with the decline helping growth stocks to outperform value stocks. On a global equity style basis using the MSCI World style indices, quality was the top-performing style (+3.55%), followed by growth (+2.94%), momentum (+1.65%) and lastly value, delivering 0.61% in dollar terms. Both global equity and global bonds were positive during the month.

United States

US equity markets performed positively during the month, on the back of steady progress from the vaccine rollout and easing restrictions on activity. As a result, the S&P 500 gained 2.27% (18.0% YTD) outperforming the NASDAQ which was up 1.16% (14.3% YTD) in dollar terms. On the macroeconomic front, the US Manufacturing Purchasing Managers' Index (PMI) increased to 63.4 in July from 62.6 in June. The change points to record growth in factory activity, supported by stronger expansion in output and new orders, with the latter increasing at the second-fastest pace ever. Unprecedented supplier shortages and delays continued to exert upward pressure on input costs and deadlock firms' ability to process incoming new work. The US Services PMI fell to 59.9 in July from 64.8 in June.

The reading pointed to a further slowdown in service sector growth from May's record high, amid labour shortages and difficulties acquiring stock. New business rose the least for five months, with some firms noting customer hesitancy amid significant hikes in selling prices. The US unemployment rate dropped to 5.4% in July from 5.9% in the previous month. The number of unemployed people declined by 782 000 to 8.7 million, while employment levels fell by 18 000 to 151.60 million. However, the jobless rate remains above the pre-pandemic levels as the recovery from the COVID-19 shock showed signs of slowing. The annual inflation rate in the US remained at 5.4% in July of 2021, reflecting the low base effect caused by the COVID-19 crisis, the re-opening of the economy and continued supply constraints. US GDP grew 6.5% q/q annualised in the second quarter, which was less than the 8.5% expected. Consumption was the largest driver and expanded 11.8% versus 11.4% previously.

Eurozone

European equity markets advanced during the month, on positive acceleration in the rate of vaccinations and continued the pickup in economic activities across the region. As a result, the Euro Stoxx finished 0.46% higher in euro terms. During the month, the main event in the region was that the ECB strengthened its forward guidance on interest rates in line with the new policy strategy. The inflation aim was adjusted to a more symmetric 2% target (versus the previous target of “below, but close to 2%”) while housing costs will also be incorporated into the calculation of inflation over time.

On the macroeconomic front, the Eurozone Manufacturing PMI fell to 62.8 in July from 63.4 in June. The reading pointed to slower growth, linked to the worsening supply lines and shortages of inputs, although new orders remain elevated. Nevertheless, the sector has now recorded successive months of expansion since July 2020, with the latest reading only slightly below June’s survey record high. In addition, employment levels rose the most since inception, amid a considerable increase in backlogs of work. The Eurozone Services PMI rose to 59.8 in July from 58.3 in the previous month. The latest reading points to the steepest pace of expansion in the service sector since June 2006, due to the easing of COVID-19 restrictions.

United Kingdom

UK equity markets were in negative territory during the month, on the back of a new wave of COVID-19 cases. However, currently 58% of the population is fully vaccinated, which is expected to limit the impact on restrictions vs previous waves. As a result, the FTSE 100 finished -0.07% lower in pound terms. On the data front, the Purchasing Manager’s Index fell to 60.4 in July from 63.9 in June. The reading points to the softest pace of expansion in the manufacturing sector since March, reflecting weaker rates of output and new order growth during the latest survey period. Manufacturers reported strong demand from both domestic and export clients, with shortages of materials and other critical components the main factor holding back production volumes.

The UK Services PMI dropped to 59.6 in July from 62.4 in the previous month. The latest reading indicates the weakest pace of recovery since March, due in part to COVID isolation rules and other restrictions due to the pandemic. There were also reports that the end of the stamp duty holiday had led to softer demand for services related to residential property transactions. New business growth eased to a five-month low, even as new export orders increased at the fastest pace since June 2018, while the pace of job creation remained strong.

Spot Rates	31 July 2019	31 July 2020	31 July 2021
EUR/USD	1.11	1.18	1.87
GBP/USD	1.22	1.31	1.39
USD/JPY	108.76	105.88	109.69

Source: IRESS

Emerging markets and Asia

Emerging markets delivered negatively during the month, underperforming their developed market counterparts. The MSCI EM index returned -7.04%, while the MSCI Developed World delivered 1.72% in dollar terms. Emerging markets were dragged lower by a correction in Chinese markets as regulatory concerns escalated.

GLOBAL RETURNS IN ZAR				
2020	May 2021	June 2021	July 2021	2021 - YTD
SHANGHAI STOCK EXCHANGE 33.42%	SHANGHAI STOCK EXCHANGE 0.83%	S&P 500 6.50%	GLOBAL PROPERTY 7.09%	GLOBAL PROPERTY 21.34%
S&P 500 24.37%	EURO STOXX 50 -1.74%	MSCI WORLD 5.62%	S&P 500 4.88%	S&P 500 17.51%
MSCI EM 24.27%	FTSE 100 -1.86%	GLOBAL PROPERTY 5.16%	MSCI WORLD 4.29%	MSCI WORLD 14.60%
MSCI WORLD 21.75%	MSCI EM -3.24%	MSCI EM 4.25%	GLOBAL BONDS 3.81%	EURO STOXX 50 12.83%
GLOBAL BONDS 14.70%	GLOBAL PROPERTY -3.77%	GLOBAL BONDS 3.15%	FTSE 100 3.18%	FTSE 100 12.42%
EURO STOXX 50 10.83%	MSCI WORLD -4.07%	EURO STOXX 50 1.64%	EURO STOXX 50 3.18%	MSCI EM -0.19%
GLOBAL PROPERTY -3.27%	GLOBAL BONDS -4.54%	FTSE 100 1.55%	SHANGHAI STOCK EXCHANGE -3.61%	GLOBAL BONDS -2.32%
FTSE 100 -4.13%	S&P 500 -4.77%	SHANGHAI STOCK EXCHANGE 0.62%	MSCI EM -4.44%	SHANGHAI STOCK EXCHANGE -3.73%

Source: Morningstar & Glacier Research