ECONOMIC REPORT

by Glacier Research

27 February 2017

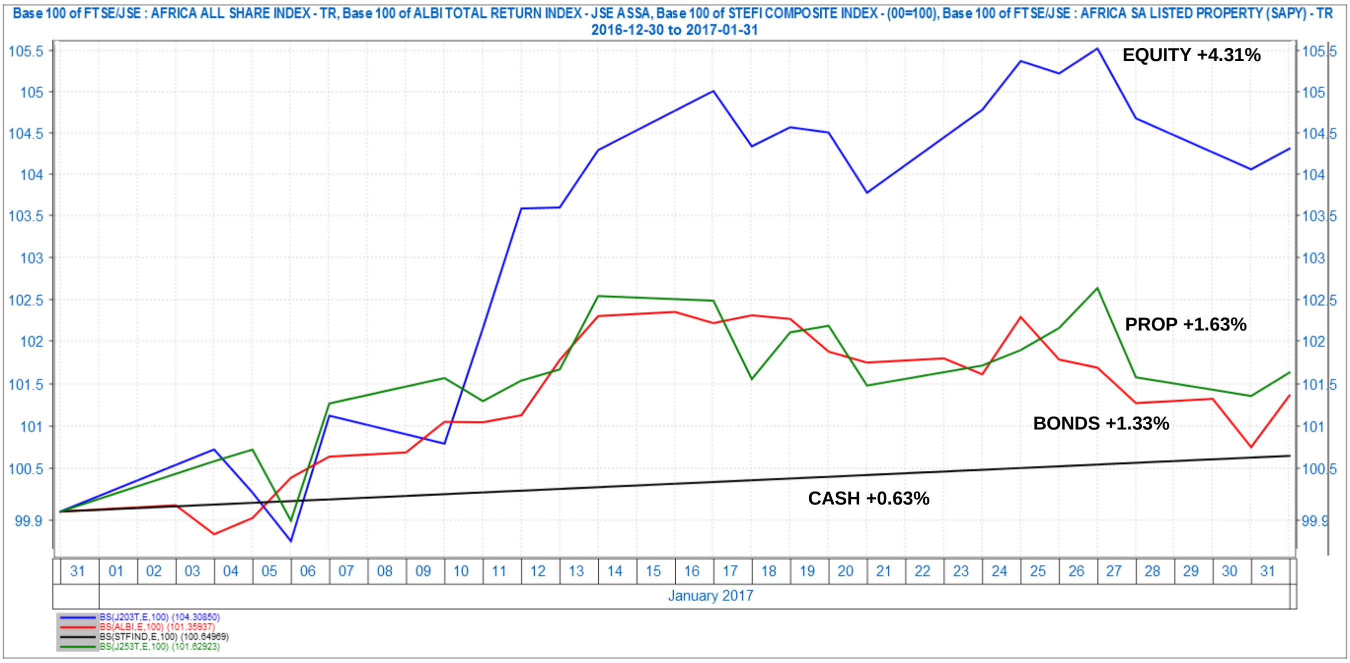
REVIEW PERIOD: JANUARY 2017

SUMMARY

The first month of 2017 can be characterised by political noise, with the inauguration of President Donald Trump and political headlines dominating the global arena. There have been a wide range of political flashpoints, from immigration to trade, however, the implications in the short term are still unknown. Despite the political noise, economic data has remained robust. The reflation theme, which was evident in the last two months of 2016 continued through January with equity markets rising, while global bonds declined in rand terms but rose in USD terms on rising expectations of improving global growth and inflation. US equities started the year on the front foot, with major indices hitting record highs despite uncertainty over the transition of a new administration. Investment clarity for UK investors is slowly improving, with Theresa May outlining her approach to leaving the EU and confirming that the UK will not look to retain access to the single market, but will seek a free trade agreement with the EU. The UK Supreme Court confirmed that Article 50 can only be activated by a parliamentary vote. The European Central Bank met in January, leaving its monetary policy and interest rate the same, which was widely expected. Emerging market equities bounced backed in January, with a tough end to 2016. The rebound was underpinned by the fall in the US dollar, combined with improving growth prospects on the back of higher commodity prices.

Locally, SA's equity market got off to a resoundingly good start in 2017 with the JSE All Share index returning an impressive 4.31% in rand terms. These gains were largely attributed to a rally in commodity prices in January which saw the resources index jump 10.74%. SA's fixed income market also saw positive momentum with steady gains over the month. Economic statistics for the final quarter of 2016 painted a picture of subdued and weak economic conditions, with mining and production both declining sharply over the quarter. As a result the SARB and the IMF are forecasting annual GDP growth of 0.4% and 0.3% respectively for 2016. On the political front the year so far has been relatively uneventful, which undoubtedly has boosted investor confidence and spurred risk-on trade. However, now the succession battle within the ANC caucus will receive much more public attention, with various bodies in the broader coalition declaring support to either Cyril Ramaphosa or Nkosazana Dlamini-Zuma. There is also speculation of an imminent cabinet reshuffle by President Zuma which may take various forms. This could possibly trigger another vicious cycle of plunging confidence and market volatility and place the country's already compromised 'investment' grade sovereign risk ratings under renewed threat. Other concerns which loom negatively over SA's economy is its rising inflation and stretched period of drought. Nonetheless, economic analysts believe that if the political climate remains relatively calm and global risks do not escalate, the domestic economy should fare moderately better in 2017. This may be helped by a turnaround in agriculture (if the drought recedes) and some recovery in mining and manufacturing (as global commodity prices drift higher).

Developed market equities (+2.35% in USD and +0.68% in ZAR) underperformed emerging market equities (+5.45% in USD and +3.73% in ZAR) in January 2017. Developed market property added 0.44% in USD terms, while local investors would have experienced a 1.20% loss due to the rand strengthening against the US dollar (-1.63%). Meanwhile, global bonds underperformed global equities, adding 1.13% in USD, while losing 0.52% in ZAR. Locally, the ALSI turned in a strong performance, returning 4.31% (+6.04% in USD) in the month of January, which is 1.63% above its entire year's performance for 2016. This stellar performance was largely due to the strong performance of Resources (+10.74%), SA Industrials – which includes dual-listed companies (+3.97%), Retailers (+2.64%) and the SA Listed Property Sector (+1.63%). Industrials led the laggards on the ALSI losing 2.26%, followed by Financials, which surrendered 0.66%. Fixed interest returns turned in a meagre performance relative to local equities with the ALBI returning 1.33%. Preference shares added 0.51% for the month. Over a one-year period, Property was the best performing asset class (+15.43%), followed by the ALBI, which delivered +11.82%. The longer end of the yield curve (12yrs+) was the best performing fixed interest asset class in January returning 1.43%, followed by the 7-12yr maturity fixed interest asset class which delivered +1.30%. The shorter end of the yield curve, 1-3yrs, was the worst performer returning +0.82%. Cash underperformed the ALBI and the ALSI in January, returning +0.63%.



Source: I-Net - 1 February 2017

LOCAL OVERVIEW

South Africa's annual headline inflation was recorded at January to 6.60% y/y, showing a slight reduction from 6.76% in December and below market expectations of a 6.70% increase. It was the highest inflation rate since February 2016 as costs increased at a faster pace for food and non-alcoholic beverages and housing and utilities. Year-on-year, costs increased less for: food and non-alcoholic beverages (11.4% from 11.7% in December 2016), alcoholic beverages and tobacco (3.5% from 5.5%), clothing and footwear (5.1% from 5.3%), recreation and culture (3.7% from 7.6%) and restaurants and hotels (6.2% from 7.1%). On a monthly basis, consumer prices went up 0.6% after a 0.4% gain a month earlier. Transport prices rebounded (+1.5% from -0.4% in December) and costs rose faster for food and non-alcoholic beverages (1.6% from 0.8%) and miscellaneous goods and services (0.8% from 0.1%). The South African Reserve Bank left its benchmark repo rate on hold at 7% at its January 2017 meeting, as widely expected, saying the near-term outlook for inflation has deteriorated and growth remains weak.

	Aug'16	Sep'16	Oct'16	Nov'16	Dec'16	Jan'17
CPI (y/y)	**5.9%**	**6.1%**	**6.4%**	**6.6%**	**6.8%**	**6.6%**
PPI (y/y)	**7.2%**	**6.6%**	**6.6%**	**6.9%**	**7.1%**	**5.9%**

Sources: SA Reserve Bank, Statistics SA, I-Net, BER, Trading Economics, MorningStar, Reuters

South Africa posted a trade surplus of R12.04 billion in December 2016, compared to an upwardly revised R1.68 billion deficit in November and well above market forecasts of a R6 billion surplus. Exports declined to R93 billion, mainly driven by lower sales of vehicles & transport equipment (-35%), machinery & electronics (-16%), precious metals & stones (-6%), base metals (-8%) and prepared foodstuff (-14%). By contrast, sales of vegetable products and mineral products rose 34% and 15% respectively. SA's major destinations for exports were China (11.5%), Germany (6.1%), the US (5.4%), Botswana (4.5%) and Japan (4.5%). Imports fell to R81 billion, as purchases declined for: machinery & electronics (-24%), equipment components (-53%), chemical products (-20%), base metals (-29%), textiles (-38%) and plastic & rubber (-30%). Meanwhile, mineral products imports rose 10%. Imports came mainly from China (16.9% of total imports), Germany (8.3%), Saudi Arabia (6.9%), the US (6.9%) and France (6.6%).

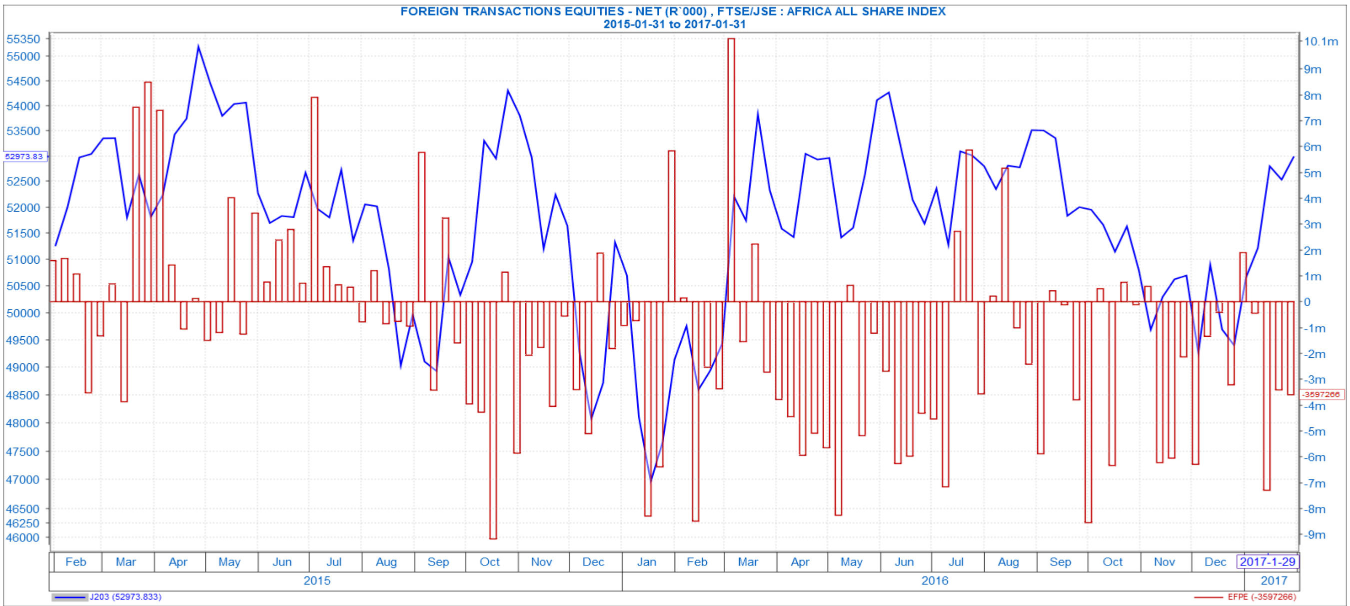
Considering the full year, the trade deficit in 2016 shrank to R2.92 billion compared to R52.18 billion in 2015, as exports went up 5.8% and imports grew at a much slower 1%.

	31 January 2015	**31 January 2016**	**31 January 2017**
USD/ZAR	**11.63**	**15.86**	**13.47**
GBP/ZAR	**17.47**	**22.61**	**16.95**
EUR/ZAR	**13.14**	**17.21**	**14.54**

Sources: SA Reserve Bank, Statistics SA, I-Net, BER, Trading Economics, MorningStar, Reuters

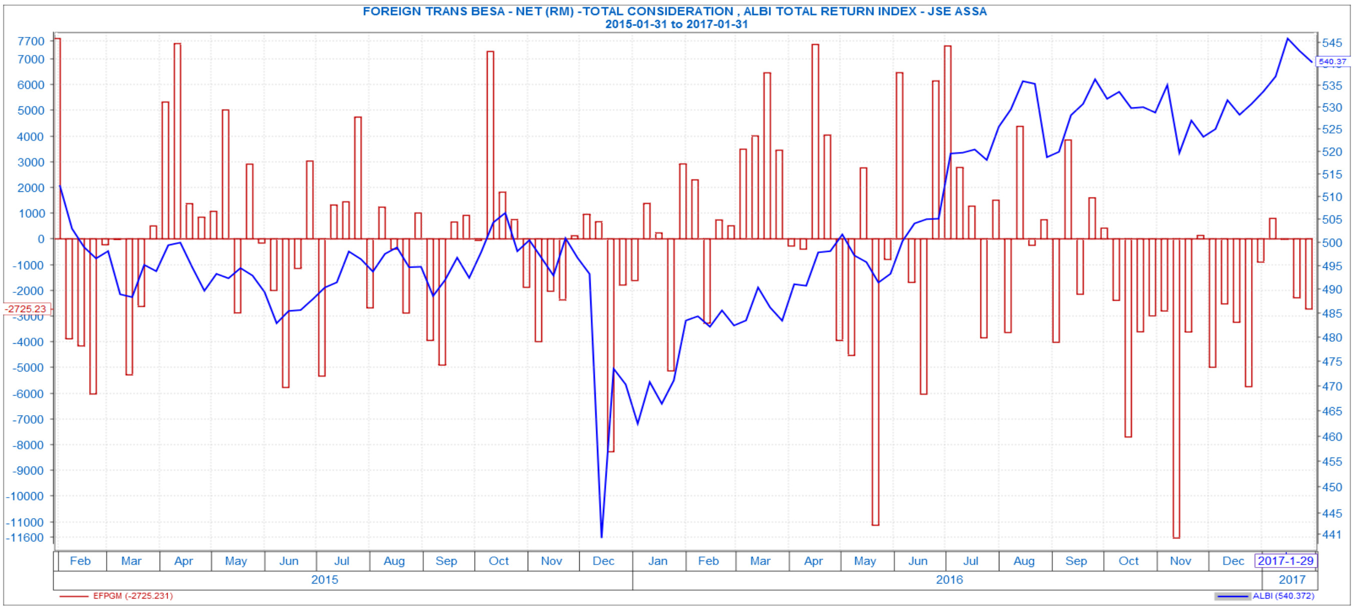
Locally, the ALSI was up a resounding 4.31% in rand terms. US foreigners invested in SA equities would have benefitted substantially as the ALSI returned 6.04% in USD as the rand strengthened against the US dollar in December. Resources led the gains on the ALSI, returning 10.74%, as commodity prices rallied in January. The Industrials index (excluding dual-listed companies) dragged on the gains of the ALSI, down 2.25%. A stark contrast to its December performance of 6.12% in ZAR. By market-cap, the Top 40 led the gains, rising 4.67% despite the rand strengthening against the US dollar. The rand, however, weakened against every other major currency in January. Small-cap stocks followed, increasing by 2.42%, Mid-caps returned 1.66% for the month.

Basic materials was the top performing sub-sector, returning a staggering 10.74% for the month. This was followed by Consumer Goods (+7.17%). Technology (-5.22%) was the worst performing sub-sector, followed by Telecommunication (-0.62%). The Gold Mining sub-sector bounced back in January returning 10.41% in January. Gold miners Sibanye Gold jumped 19.26%, Anglo Gold Ashanti surged by 11.34%, Harmony Gold added 7.23% and Gold Fields rose 5.92%. Other mining companies that performed exceptionally well were platinum miners, Anglo American Plat soaring 32.85%, Northam Platinum jumping 26.30% and Impala Platinum rising 25.04%. Trencor gained 31.40% and Kumba Iron Ore added 30.19%. Diversified miners such as Anglo American (+18.09%) and BHP Billiton (+11.87%) also had an excellent month, recovering from December's slump. Rand-hedge stocks in the Top 40, such as Naspers (+6.14%), British American Tobacco (+5.27%) and Compagnie Fin Richemont (+15.72%) gave sterling performances over the month as the rand weakened against the US dollar. Anglo American Plat (+32.85%), Anglo American (+18.09%), Compagnie Fin Richemont (+15.72%) and BHP Billiton (+11.87%) were the best performing large-cap stocks, while Brait (-9.78%), Steinhoff (-9.78%) and Capital & Counties Prop (-7.58%) were the worst performing large-caps. The financials index had a tough month dropping 0.66%. The index was dragged down major banking stocks in the Top 40 index, namely, Barclays Africa (-5.86%), Firstrand (-5.59%), Standard Bank (-5.16%) and Nedbank (-2.49%). SA equities were sold off again in January by foreigners. They were net sellers of R16.15 billion worth of equities in January signalling a continued decrease in investor confidence in SA equities.



Source: I-Net 1 February 2017

Local fixed income markets saw steady returns over the month, with the ALBI (+1.36%) outperforming cash (+0.63%), as well as Preference Shares (+0.51%) but lagging inflation linked bonds (+1.41%). The longer end of the yield curve (12yrs+), was the best performing interest-bearing asset class, returning 1.43%, followed by 7-12yr bonds (+1.30%). The shorter end of the yield curve (1-3yrs) was the worst performer, returning +0.82%. However, over a rolling three-month period it was the best performer (+1.74%) after cash (+1.88%). SA listed property (a hybrid asset class) had a positive month returning 1.63% and has returned 15.4% over a one year period.



Source: I-Net 1 February 2017

For the month, foreigners were net sellers of R6.51 billion worth of bonds. This suggests that foreign investors are continuing to re-allocate capital from emerging markets to developed markets in anticipation of higher inflation and interest rates in the US. In January, SA's currency returns were mixed against major global peers: It appreciated against the US dollar (-1.63%) and the Japanese yen (-0.26%) but depreciated against the euro (+0.68%) and the pound sterling (+1.51%).

GLOBAL OVERVIEW

Globally, the reflation theme which was evident towards the back-end of 2016 continued through January with equity markets rising, while bonds declined on rising expectations of improving global growth and inflation. The US dollar weakened against most major currencies following a suggestion by President Donald Trump that he favoured a weaker dollar. Global economic data, both sentiment surveys and hard data, continued to surprise to the upside, showing further gains and moving to levels consistent with improving global growth. The US earnings season got underway in January, with company results coming in above market expectations. The US economy advanced an annualised 1.9% q/q in Q4 of 2016, which was lower than the 3.5% expansion in the previous period. Nonfarm payrolls in the US increased by 227 000 in January 2017, following an upwardly revised increase of 157

000 in December 2016. Furthermore, the US trade deficit narrowed to $44.3 billion in December 2016 from a $45.7 billion gap a month earlier. Commodities rose during the month of January (+4.79%), despite the weakness in energy prices. Brent Crude oil was down 1.11% and Nickel weakened by 1.20%. Silver surged 10.23% and Platinum advanced 9.26%, while Iron ore and Gold added 5.67% and 5.22% respectively.

On a total return basis, both the global Basic materials sector and the Technology sector were the top performing sectors for the month returning 4.6% in USD, 2.7% in Pound Sterling (GBP) and 3.1% in ZAR. This was followed by the Consumer cyclicals sector which returned 3.6% in USD, 1.7% in GBP and 2.1% in ZAR. Basic materials was the top performing sector over a one year period in USD (+39.3%), GBP (+57.1%) and ZAR (+18.1%). The worst performing global sector in January was the Energy sector returning -3.1% in USD, -4.9% in GBP and -4.5% in ZAR. Furthermore, the Consumer defensive sector was the worst performing global sector over a one year period returning 7.9% in USD, +21.7% in GBP and -8.5% in ZAR.

In rand terms, global developed market equities (+0.68%) underperformed emerging market equities (+3.73%) in January. In USD, the MSCI Developed World Index added 2.35% and the MSCI Emerging Markets Index returned an impressive 5.45% for the month. Developed market property added 0.44% in USD whereas bonds fared better gaining 1.13% in USD. Looking at developed markets, the majority of global indices yielded positive returns for the month of January in rand terms. The NASDAQ (+2.60% ZAR and +4.30% USD), the Canadian TSX (+2.15% ZAR and +0.64% USD), the German DAX (+1.54% ZAR and +3.54% USD) and the FTSE 100 (+0.89% ZAR and +1.40% USD) were the top performers for the month. Meanwhile, the CAC 40 (-1.67% ZAR and +0.28% USD), the Euro Stoxx 50 (-1.15% ZAR and +0.80% USD) and the Dow Jones (-1.12% ZAR and +0.51% USD) were the worst performers for the month. In emerging markets, China's Shanghai Composite index added 1.79% in its base currency and rose 0.89% in ZAR, while the Brazilian Bovespa equity index returned an impressive 7.38% in its base currency. The US dollar weakened against both the euro (2.67%) and the British pound (2.03%).

Spot Rates	31 January 2015	31 January 2016	31 January 2017
USD/EUR	**1.13**	**1.03**	**1.08**
USD/GBP	**1.51**	**1.42**	**1.26**
Yen/USD	**117.45**	**121.11**	**112.78**

Sources: SA Reserve Bank, Statistics SA, I-Net, BER, Trading Economics, MorningStar, Reuters