ECONOMIC REPORT

by Glacier Research

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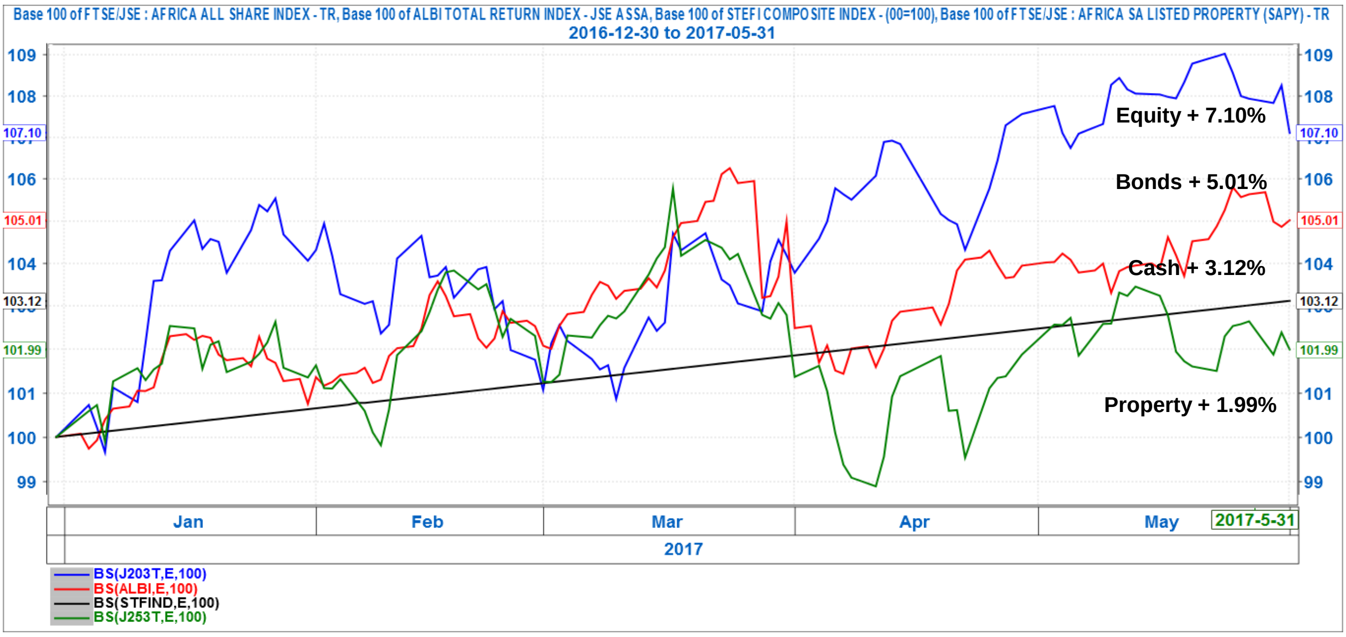
REVIEW PERIOD: MAY 2017

SUMMARY

Politics dominated the headlines in May, with elections in France, Iran and South Korea, as well as renewed political controversy in the United States and Brazil weighing on investor sentiment. France kicked off the presidential elections which took place in May with Emmanuel Macron securing a larger-than-expected victory over Marine le Pen and South Korea electing Moon Jae-In as their President months after their former President was impeached and removed from office. Meanwhile, Iran re-elected President Hassan Rouhani. Global equities and global bonds in US dollar terms continued their upward trend in May, as strong company earnings growth supported optimism in the global economy. However, in ZAR, both global bonds and global equities turned in a negative performance as the rand strengthened against the US dollar (-2.14%). The S&P 500 earnings season wrapped up with robust earnings growth across all sectors. More than three-quarters of US companies beat analyst revenue expectations, implying a higher earnings trend in the US market. The technology sector enjoyed solid earnings growth in particular, with tech giants Facebook, Apple, Amazon, Netflix and Google rallying hard. European equity markets continued their advance in May as the victory of pro-Europe centrist Emmanuel Macron resolved uncertainty about the outlook. Eurozone economic data continues to show signs of further improvement. In the UK, the FTSE 100 reached a record high, which was supported by a weakening pound. Furthermore, emerging market equities outperformed developed market equities once again, which marks the fifth successive month of outperformance. Asia was the strongest performing region, with South Korea leading the gains driven by robust Q1 earnings and receding leadership and political concerns. China turned in a strong performance, despite being downgraded by Moody's. In contrast, Brazil underperformed as political risk increased following corruption allegations against their President Michel Temer.

Locally, the JSE All Share index was marginally down (-0.42%) for the month, with resources (-4.1%) and financials (-1.35%) weighing down the index. SA Industrials, however, returned 1.42% over the month, supported by solid performances from most rand hedge counters as the local currency came under pressure. The month of May was marred by political upheavals with the controversial re-appointment of Brian Molefe as the CEO of embattled state-owned enterprise, ESKOM, a move which sparked fury amongst opposition parties of the ANC who approached the court to declare the notion illegal. Even senior members within the ANC's own ranks questioned the rationale of the enterprise's board and the minister. The move clearly seemed politically motivated as it was described as incoherent and contradictory. In addition to this debacle, President Jacob Zuma survived yet another challenge to his leadership at a meeting of the ANC's National Executive Committee (NEC).This, despite breaking news of leaked email correspondence by employees of the Gupta family, seemingly revealing the extent of the family's influence over the President, various past and sitting ministers and the top management of state-owned enterprises. As a result of the burden of political corruption, the risk of a downgrade to SA's local-currency rating by rating agencies remains high. On an economic front, mining production rose by 14.7% q/q but manufacturing production declined by 3.6%, wholesale sales dropped by 14.6%, retail sales fell by 4.4% and bank loans also shrunk marginally over the first quarter. However, new vehicle sales managed annualised growth off a low base of 35.1% after adjusting for seasonal factors. Analyst forecasts for SA GDP growth remain unchanged at 0.7% for 2017, 1.3% for 2018 and 1.9% for 2019. The Reserve Bank revised its growth forecast for 2017, 2018 and 2019 downwards to 1%, 1.5% and 1.7% respectively from 1.2%, 1.7% and 2% previously.

Developed market equities (+1.78% in USD, -0.40% in ZAR and +2% in GBP) underperformed emerging market equities (+2.80% in USD, +0.60% in ZAR and +3.10% in GBP) for the fifth successive month in May 2017. Developed market property gained 0.58% in USD terms, while local investors would have experienced a negative return (-1.58%) due to the rand strengthening against the US dollar (-2.14%). Meanwhile, global bonds underperformed global equities, adding 1.55% in USD and 1.77% in GBP, while losing 0.63% in ZAR. Locally, the ALSI surrendered 0.42% (+1.76% in USD and +1.29% in GBP) for the month of May. The market was dragged lower by Retailers (-8.56%), Resources (-4.11%), Financials (-1.35%) and Industrials (-0.04%). Meanwhile, SA Industrials, which includes dual-listed companies (+1.42%) and the SA Listed Property Sector (+0.11%) contributed positively to performance. Fixed interest returns were strong relative to local equities and cash with the ALBI returning 1.03% for the month supported by continuous foreign inflows. Preference shares turned in a stellar performance, returning 1.87%, while Inflation-linked bonds gave up a meagre -0.08%. The middle end of the yield curve (seven-12 years) was the best performing fixed interest asset class in May, returning 1.43%, followed by the three-seven years part of the yield curve which added 1.10%. The shorter end of the yield curve (one-three years) was the worst performer, returning +0.72%. Cash underperformed the ALBI but outperformed the ALSI in May, returning +0.63%.



Source: I-Net - 1 June 2017

LOCAL OVERVIEW

South Africa's annual headline inflation increased by 5.30% y/y in April, showing a strong deceleration from 6.10% in March and beating market expectations on the downside and reaching its lowest rate since December 2015, primarily due to slowing food and transport inflation. Prices rose at a slower pace for food and non-alcoholic beverages (6.7% from 8.7% in March); miscellaneous goods and services (7.3% from 7.5%); transport (4.6% from 7.7%); alcoholic beverages and tobacco (2.9% from 3.2%); household contents (2.8% from 3.2%); recreation and culture (3.6% from 3.7%) and clothing and footwear (4% from 4.5%). In contrast, inflation was steady for housing and utilities (5.7%) and education (7%) and increased for restaurants and hotels (6.4% from 6.1%) and health (6.5% from 6.2%). On a monthly basis, consumer prices increased by 0.10%% after a 0.59% rise in the previous month. Consumer prices edged up 0.1%, below 0.6% in March and lower than expectations of 0.4%. The only upward contribution came from prices of miscellaneous goods and services (prices up 0.4%). In contrast, the cost of food and housing and utilities was flat and transport declined 0.3%.

	Dec'16	Jan'17	Feb'17	Mar'17	Apr'17	May'17
CPI (y/y)	**6.8%**	**6.6%**	**6.3%**	**6.1%**	**5.3%**	**-**
PPI (y/y)	**7.1%**	**5.9%**	**5.6%**	**5.2%**	**4.6%**	**-**

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

South Africa posted a trade surplus of R5.1 billion in April compared to a downwardly revised R11.3 billion surplus in March and slightly below market expectations of R5.5 billion. Exports fell 9.2% to R91.8 billion, due to lower sales of precious metals and stones, vehicles & transport equipment, machinery & electronics and chemicals.

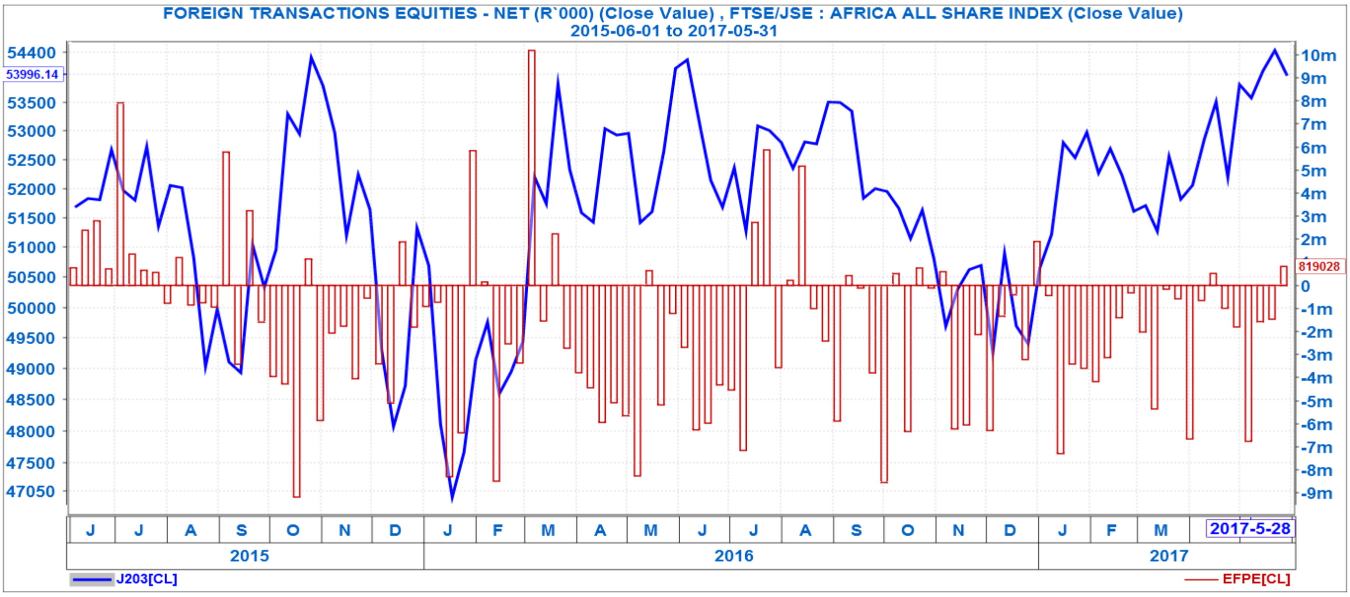
Imports went down 3.4% to R86.7 billion, driven by purchases of optical photographic products, original equipment components, vegetables, and chemicals. Major destinations for exports were China (9.4% of total exports), Germany (7.7%), the US (6.9%), India (5%) and Japan (4.5%). Imports came mainly from China (17.3% of total imports), Germany (10.5%), the US (6.3%), Saudi Arabia (5.9%) and India (5%).

	31 May 2015	31 May 2016	31 May 2017
USD/ZAR	12.15	15.69	13.07
GBP/ZAR	18.48	22.75	16.84
EUR/ZAR	13.35	17.49	14.70

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

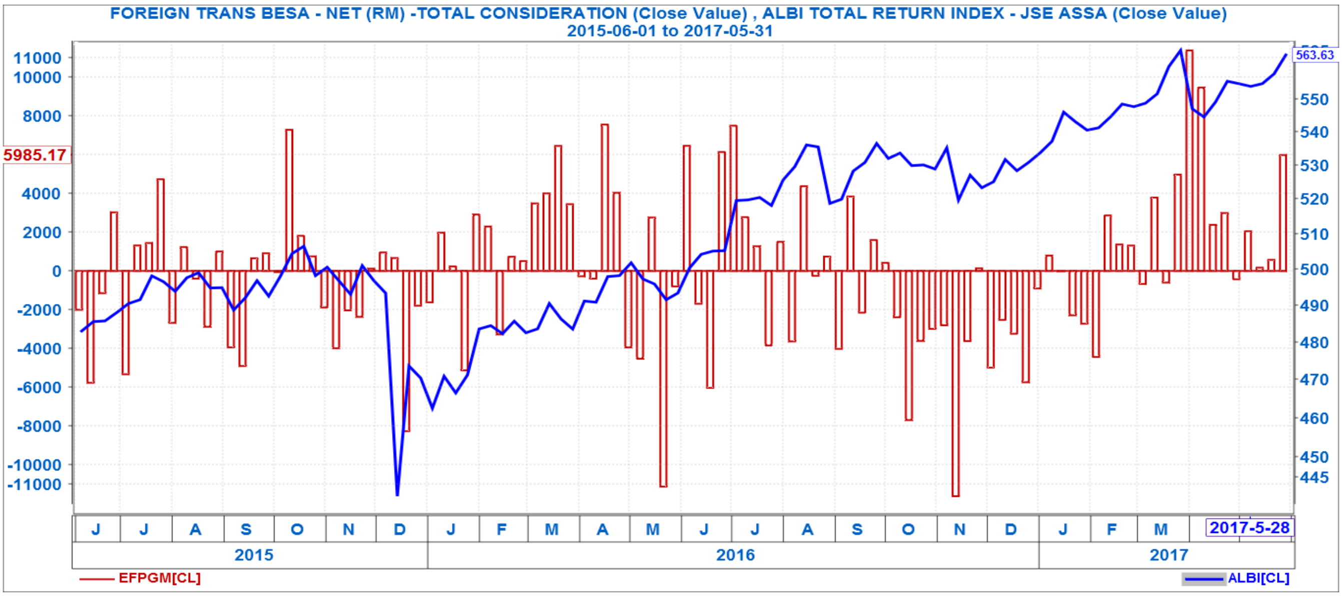
Locally, the ALSI was down -0.42% in rand terms. US foreigners invested in SA equities would have returned 1.76% in USD, helped by the rand appreciating by 2.14% against the US dollar in May. SA Industrials led the gains on the ALSI, advancing 1.42% in May, despite SA retailers (-8.56%) being hammered by the market over the month. Resources were the lowest returning sector, ending the month 4.11% lower, as precious metal demand dampened following the favourable French election outcome and base metals came under pressure over doubts on China's demand sustainability. The Financials index slipped 1.35%, as the country's big four banks all shed more than 1% over the month. By market-cap, the Top 40 index yet again led the gains, rising 0.21% as the rand weakened against major currencies. Small-cap stocks ended the month 2.59% lower and the Mid-cap index lost a notable 4.24% during May.

Consumer Services was yet again the top performing sub-sector for a fourth successive month, returning a solid 3.57% for the month. This was followed by Health Care, up 2.02%. Technology (-10.70%) was the worst performing sub-sector, followed by Basic Materials (-4.11%). The Gold Mining sub-sector shed a further 1.93% as the gold price stagnated over the month, rising only 0.05%. Sibanye Gold (-41.52%), Harmony Gold (-9.32%) and Anglo Gold Ashanti (-1.78%) led the Gold mining index lower, while Gold Fields (+6.06%) bucked the trend for the sub-sector. Under the large diversified miners, Anglo American PLC (-8.31), African Rainbow Minerals (-3.91%) and BHP Billiton (-0.88) performed poorly as they came under pressure on lower iron ore, copper and coal prices. Other notable mining company performances include Kumba Iron Ore (-9.77%), receding on substantially lower iron ore prices, and Impala Platinum (-14.39%) trending lower, while Lonmin (-33.44%) drove the platinum index firmly down. Rand-hedge stocks in the Top 40, such as Aspen Pharmacare (+7.13%), Naspers (+6.97%), British American Tobacco (+4.80%), Investec PLC (+3.75%) and Steinhoff (+2.79%) excelled, as the rand weakened against most major currencies over the month and were the best performing large-cap stocks. Anglo American Platinum (-15.50%) and Impala Platinum (-14.29%), were the worst performing large-cap stocks as resources performed poorly. The financials index experienced a weak month, ending 1.35% lower. The index was driven mainly by losses in major banking stocks in the Top 40 index, namely, Barclays (-5.44%), Old Mutual (-4.90%), Nedbank (-2.37%) and Standard Bank (+1.23%), while Capitec (+2.13%) bucked the trend and fared well over the month. SA equities were sold off again in May by foreigners as they were net sellers of R9 billion worth of equities. YTD they have sold R50.6 billion worth of SA equities.



Source: I-Net 1 June 2017

Local fixed income markets saw superior returns over the month relative to equities as the ALBI (+1.03%) outperformed cash (+0.63%), but underperformed Preference Shares (+1.87%). The seven-12 year end of the yield curve was the best performing interest-bearing asset class, returning 1.43%, followed by three-seven year bonds (+1.10%). The shorter end of the yield curve (one-three years) was the worst performer, returning +0.72%. Over the last three months the seven-12 year period was the best performer (+3.42%) followed by the three-seven year period (+3.29%), while the seven-12 year (+14.53%) was the best performer over the past 12 months. SA listed property (a hybrid asset class) had a consecutive dismal month, returning only 0.11% for May and 0.62% over two months.



Source: I-Net 1 June 2017

During May, foreigners were net buyers of R9.2 billion worth of bonds, despite foreign rating agencies having a negative outlook on SA. YTD the bond market has experienced a net foreign inflow of R39.4 billion. In a global fixed income context, emerging markets generally remain attractive and the current higher yields in the asset class provide at least some measure of diversification against rising interest rate risk globally. As a result countries such as SA have been a beneficiary of this market sentiment with foreign investors favouring its bonds. In May, SA's currency returns strengthened against major global peers. The rand appreciated against the US dollar (-2.14%), British pound sterling (-2.43%), Japanese yen (-1.50%), while it weakened more extensively versus the euro (+0.93%).

GLOBAL OVERVIEW

Both global equities and bonds in US dollar terms continued their upward trend in May as strong company earnings growth supported optimism in the global economy. Investors' unease over geopolitical events was apparent, particularly surrounding the political controversies in the US and Brazil. The month of May started on an upbeat note, after a strong US jobs data report showed that the US economy added on average 138 000 jobs in May, below a downwardly revised 174 000 jobs in the previous month. This was further supported by the US economy GDP number which came in above market expectations as well as the latest unemployment rate figure. The Federal Reserve kept its target range for its federal funds rate steady between 0.75% and 1% during its May meeting, which was in line with market expectations. The US economy expanded by an annualised 1.2% q/q for Q1 2017. Moreover, the unemployment rate in the US fell to 4.3% in May from 4.4% in the previous month, which is the lowest jobless rate since May 2001. By 15 May, the US equity market closed at a new record high after oil prices rallied on news that Russia was ready to join OPEC in extending its oil supply cuts with the hopes of reducing the current oil glut. However, this was short-lived as energy-related stocks were hit by a drop in oil prices later during the month as Libya increased its oil production. The US market retreated after President Donald Trump came under fire for dismissing former FBI director James Comey amid speculation that he was motivated by the FBI's probe into his electoral campaign ties to Russia.

The broader commodities index surrendered -0.35% in May, dragged lower by significantly weaker iron ore prices as well as Nickel and the price of Brent crude oil. The gold price rose marginally by 0.05%, as geopolitical tensions dissipated during the month of May. Investors were relieved by the French election victory of Emmanuel Macron. The platinum price added 0.11% in May, which was further boosted by improving industrial production in the Eurozone. Brent crude oil prices were trading above $56 per a barrel at one stage in May, but ended the month 2.19% lower. Furthermore, iron ore sank 17.12%, the third successive month of weakness as Chinese supplies, which were already elevated, hit record highs.

On a total return basis, the global technology sector was the top performing sector for the month of May returning 4.4% in USD, 4.7% in GBP and 2.9% in ZAR. This was followed by the utilities sector which returned 4.0% in USD, 4.3% in GBP and 2.5% in ZAR. Technology was the top performing sector over a one year period in USD (+34.5%), GBP (+51.7%) and ZAR (+12.8%). The worst performing global sector in May was the energy sector, returning -3.9% in USD, -3.7% in GBP and -5.3% in ZAR. Furthermore, the energy sector was also the worst performing global sector over a one year period returning -1.1% in USD, 11.5% in GBP and -17.1% in ZAR.

In rand terms, global developed market equities (-0.40%) underperformed emerging market equities (+0.60%) in May. In USD, the MSCI World added 1.78% and the MSCI Emerging Markets Index advanced 2.80% for the month. Developed market property added 0.58% in USD, underperforming bonds, which added 1.55% in USD. Developed markets indices in ZAR terms were mostly positive for the month of May, with the rand strengthening against the US dollar, the pound sterling, and the Australian dollar, but weakening against the euro. The DAX (+2.90% in ZAR, +5.16% in USD and +4.96% in GBP), the FTSE 100 (+1.85% in ZAR, +3.79% in USD and +4.92% in GBP), the CAC 40 (+1.25% in ZAR, +3.47% in USD and +4.15% in GBP), the Euro Stoxx (+0.79% in ZAR, +3% in USD and +4.51% in GBP) and the Nikkei (+0.68% in ZAR, +2.21% in USD and +3.41% in GBP) were the top performers for the month. Meanwhile, the ASX 200 (-6.04% in ZAR, -3.98% in USD and -2.99% in GBP), the Canadian TSX (-2.45% in ZAR, -0.19% in USD and +0.03% in GBP) and the S&P 500 (-1.01% in ZAR, +1.16% in USD and +1.55% in GBP) were the worst performers for the month. In emerging markets, China's Shanghai Composite index gave up 1.19% in its base currency (-1.73% in ZAR, +0.43% in USD and +0.34% in GBP) and the Indian Nifty 50 added 1.51% in its base currency (-0.67% in ZAR, +1.51% in USD and +3.33% in GBP), while the Brazilian Bovespa equity index surrendered 4.12% in its base currency (-6.06% in USD and -5.86% in GBP). The US dollar weakened against the euro (+3.15%) and strengthened against the British pound (-0.57%).

Spot Rates	31 May 2015	31 May 2016	31 May 2017
EUR/USD	1.10	1.11	1.12
GBP/USD	1.53	1.45	1.29
USD/JPY	124.13	110.74	110.86

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