ECONOMIC REPORT

by Glacier Research

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REVIEW PERIOD: JULY 2018

DOMESTIC OVERVIEW

Headwinds are blowing against the South African economy as the turbulent economic and market environment continues to prevail. The domestic landscape has precipitated a risk-off environment wherein investors are tending to exhibit biasness towards safer and more conservative assets as these asset classes are delivering attractive returns relative to more aggressive asset classes. In the month of July, bonds and cash were the leading performers, while equity and property detracted.

Domestic Highlights in July 2018

- SARB MPC meeting
- IMF growth forecast
- FNB/BER Consumer Confidence Index
- BRICS Heads of State Summit

SARB MPC meeting

The South African Reserve Bank (SARB) monetary policy committee (MPC) meeting decided to keep the repo rate unchanged at 6.5%, in line with market expectations. The SARB continued to indicate that the balance of risks to the domestic inflation outlook are now to the upside as a result of oil prices, electricity prices, escalating global trade tensions and weakening domestic currency. Inflation is projected to average 4.8% in 2018, and is expected to reach 5.6% in 2019 before it declines to 5.4% in 2020.

IMF growth forecast

The International Monetary Fund (IMF) released its July 2018 World Economic Outlook report and has kept global growth expectations for 2018 and 2019 unchanged at 3.9%. The report further highlighted the uneven growth prospects (incited by rising oil prices, higher US bond yields, and global trade tensions) among emerging market economies in which South Africa was included. The IMF kept South Africa's GDP growth forecast unchanged for both 2018 and 2019 at 1.5% and 1.7% respectively.

FNB/BER Consumer Confidence

The FNB/BER Consumer Confidence Index eased marginally to 22 from a record high of 26 in the first quarter of 2018, despite a weak business confidence, weakening economy, escalating fuel prices and weakening currency. Caution has been raised by economists regarding the sentiment not translating into actual spending as other indicators seem to show a consumer that is jittery about the economy.

BRICS Heads of State Summit

After securing a minimum investment commitment of $10 billion from the Saudi Arabian government, South African President, Cyril Ramaphosa, hosted all heads of states of the BRICS bloc countries (Brazil, Russia, India, China and South Africa) in a summit and ended up securing another commitment of $14.7 billion from China. The Chinese granted a $2.5 billion loan to the ailing power utility firm, Eskom, and a $300 million loan to logistics utility firm, Transnet. These transactions come after a $100 billion target of new investments into South Africa, set by President Ramaphosa.

South Africa: Economy

The scourge of rising fuel prices remained prevalent in the month of July as the Department of Energy announced a 23 cents per litre hike in the petrol price. SA inflation surprised the market, rising to 4.6% in June from 4.4% in May, and below market expectations. The uptick was mainly due to rising fuel prices. Stats SA released retail sales data for May 2018.

According to the data released, retail sales were up by 1% in May from a decline of 1.1% in April. SA manufacturing production rose by 1.5%, after having declined by a revised 0.5% in April. The SA economy remains in a precarious situation as the euphoria around President Ramaphosa is fading and the country is facing domestic challenges that could (if not averted) bring about a technical recession in the next economic growth figures.

	Feb'18	Mar'18	Apr'18	May'18	June'18	July'18
CPI (y/y)	**4.0%**	**3.8%**	**4.5%**	**4.4%**	**4.6%**	**5.1%**
PPI (y/y)	**4.2%**	**3.7%**	**4.4%**	**4.6%**	**5.9%**	**-**

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

	31 July 2016	31 July 2017	31 July 2018
USD/ZAR	**13.84**	**13.17**	**13.27**
GBP/ZAR	**18.27**	**17.38**	**17.42**
EUR/ZAR	**15.50**	**15.56**	**15.51**

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

South Africa: Markets

SA bonds led the gains in July, delivering returns of 2.2% after surrendering for the past couple of months as bond sales by foreigners decelerated. Cash was the second best performing asset class in July, delivering a sluggish 0.61%. Local property continued to deliver disappointing performance for the month, returning -0.50%, followed by local equities which surrendered 0.25%.

In terms of market capitalisation, the Top 40 delivered lacklustre performance, returning -0.33%. SA mid-caps added 0.54% for the month, while SA small-caps surrendered the most, losing 1.74%. Foreigners were net buyers of R6.8 billion worth of SA bonds, and net sellers of R4.2 billion worth of SA equities. In terms of sectors, Financials (+4.66%) took the crown as the leading performing sector for the month followed by muted gains from Consumer goods (+0.97%). Industrials (+0.45%) and General Retailers (+0.41%) advanced slightly, while Resources (-1.4%), SA Industrials (-1.99%) and Consumer Services (-5.14%) weakened.

LOCAL RETURNS IN ZAR

2017	May 2018	June 2018	July 2018	Year-to-date
SA TOP 40 23.07%	SA CASH 0.59%	SA TOP 40 3.62%	SA BONDS 2.42%	SA BONDS 6.48%
SA EQUITY 20.95%	SA BONDS -1.95%	SA EQUITY 2.78%	SA CASH 0.61%	SA CASH 4.15%
SA PROPERTY 17.15%	SA SMALL CAPS -2.44%	SA CASH 0.55%	SA MID CAPS 0.53%	SA TOP 40 -0.85%
SA BONDS 10.24%	SA TOP 40 -3.06%	SA BONDS -1.17%	SA EQUITY -0.25%	SA EQUITY -1.95%
SA CASH 7.56%	SA EQUITY -3.48%	SA MID CAPS -2.14%	SA TOP 40 -0.33%	SA SMALL CAPS -7.36%
SA MID CAPS 7.36%	SA PROPERTY -5.92%	SA SMALL CAPS -3.31%	SA PROPERTY -0.50%	SA MID CAPS -10.05%
SA SMALL CAPS 2.95%	SA MID CAPS -8.37%	SA PROPERTY -3.45%	SA SMALL CAPS -1.74%	SA PROPERTY -21.76%

LOCAL SECTOR RETURNS IN ZAR				
2017	May 2018	June 2018	July 2018	Year-to-date
CONSUMER SERVICES 52.66%	RESOURCES 4.01%	CONSUMER SERVICES 9.37%	FINANCIALS 4.66%	RESOURCES 13.43%
SA INDUSTRIALS 22.50%	CONSUMER SERVICES -3.87%	RESOURCES 5.96%	CONSUMER GOODS 0.97%	CONSUMER GOODS -3.09%
FINANCIALS 20.61%	CONSUMER GOODS -4.26%	SA INDUSTRIALS 4.18%	INDUSTRIALS 0.45%	FINANCIALS -5.14%
GENERAL RETAILERS 19.00%	SA INDUSTRIALS -5.14%	CONSUMER GOODS 1.72%	GENERAL RETAILERS 0.41%	CONSUMER SERVICES -6.19%
RESOURCES 17.90%	FINANCIALS -6.26%	INDUSTRIALS -2.52%	RESOURCES -1.40%	SA INDUSTRIALS -6.25%
INDUSTRIALS 14.73%	INDUSTRIALS -10.20%	FINANCIALS -2.88%	SA INDUSTRIALS -1.99%	INDUSTRIALS -10.50%
CONSUMER GOODS -1.12%	GENERAL RETAILERS -12.65%	GENERAL RETAILERS -6.85%	CONSUMER SERVICES -5.14%	GENERAL RETAILERS -11.72%

GLOBAL OVERVIEW

The global equity markets ended the month of July in positive territory, spurred by healthy second quarter economic growth and relief over the unexpected agreement reached by the US and the EU on resolving trade tensions. In addition, trade progress included reports of efforts by the US and China to also come to an agreement. However, optimism was tempered when US Mega-cap technology stocks saw their share prices fall after reporting their latest earnings. Twitter shadowed Facebook in conveying disappointing results (and a fall in user numbers) and Intel said a new key chip technology wouldn't be available until late next year. Facebook suffered the biggest one-day loss of market value in US history, dropping almost US$120bn.

Netflix suffered as its quarterly earnings revealed disappointing viewer growth. The tech sector was one of the weakest performers over the month with concerns that the market had grown narrow and was over-dependent on the dominant internet companies for their growth. Technology company growth rates are considered relatively resilient to escalating trade tensions and it is worth mentioning that without the inclusion of technology stocks the US equity market would be down for the year. The industrials sector was the strongest performing sector over the month, driven not only by trade optimism but by many companies reporting beating earnings forecasts. Both Global Bonds and Global Equity were negative in ZAR terms as the rand strengthened against the US dollar for the month.

United States

The US economy continued to report above-trend economic data and markets responded to a number of strong company earnings' reports. Consumers remain confident about the future and are spending at a fast rate. Retail sales grew 6.6% year on year for the month of June. This is the fastest pace of spending growth since 2012. The strength of the labour market is certainly playing a role in boosting household sentiment. 213,000 nonfarm jobs were created in June but because 601,000 people joined the labour market in the same month, the unemployment rate rose to 4%. The US economy recorded its strongest pace of GDP growth since 2014 at 4.1%. Inflation rose to 2.9% in June, well above the Federal Reserve's (Fed's) target.

Eurozone

European equity markets ended the month of July in positive territory, posting solid gains as the second quarter earnings season proved to be reasonably strong. All sectors delivered positive returns with relative strength coming from healthcare, financials, energy and telecoms, while consumer staples, information technology and real estate were the relative laggards over the month. Trade wars eased towards the end of the month, as an agreement was reached between the European Union and the US to work together to reduce tariffs related to non-auto industrial goods.

The European Central Bank's (ECB's) Monetary Policy Committee meeting in July was uneventful. All key interest rates remained unchanged and the ECB reiterated its intention to end quantitative easing by the end of the year but hold interest rates at their current levels at least through the summer of 2019.

United Kingdom

UK equity markets rose during July, a month plagued by Brexit headlines, mixed economic data and continued sterling weakness. July saw the publication of the Government's Chequers plan, where Theresa May assembled her cabinet to try to agree a common position for her to commence the formal negotiations on the UK's future relationship with the European Union (EU). As a result two cabinet members, David Davis and Boris Johnson, tendered their resignations as they did not support the plan.

Weaker-than-expected retail sales data released for the previous month added to downward pressure on sterling, as the World Cup and extended hot weather kept consumers at home. In addition, the UK Government distributed the largest public sector pay rise in more than a decade, as the 1% cap on pay increases was lifted for teachers, soldiers, police and prison officers, as well as for NHS doctors and dentists.

Spot Rates	31 July 2016	31 July 2017	31 July 2018
EUR/USD	1.11	1.11	1.16
GBP/USD	1.32	1.31	1.31
USD/JPY	102.06	110.36	111.88

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

Emerging Markets

Emerging markets registered positive returns in July, underperforming their developed market counterparts. This was largely supported by encouraging macroeconomic data and upbeat corporate earnings.

GLOBAL RETURNS IN ZAR

2017	May 2018	June 2018	July 2018	Year-to-date
MSCI EM 24.28%	S&P 500 3.90%	GLOBAL PROPERTY 10.75%	EURO STOXX 50 -0.46%	S&P 500 12.65%
EURO STOXX 50 12.50%	GLOBAL PROPERTY 3.75%	S&P 500 8.89%	S&P 500 -0.88%	MSCI WORLD 9.58%
FTSE 100 10.95%	MSCI WORLD 2.09%	MSCI WORLD 8.17%	MSCI WORLD -1.45%	GLOBAL PROPERTY 7.82%
MSCI WORLD 10.81%	FTSE 100 0.75%	EURO STOXX 50 8.03%	MSCI EM -2.33%	EURO STOXX 50 6.10%
S&P 500 10.29%	GLOBAL BONDS 0.68%	GLOBAL BONDS 7.74%	GLOBAL PROPERTY -3.53%	FTSE 100 5.90%
SHANGHAI STOCK EXCHANGE 4.78%	SHANGHAI STOCK EXCHANGE 0.68%	FTSE 100 7.13%	FTSE 100 -3.61%	GLOBAL BONDS 4.09%
GLOBAL PROPERTY -0.98%	MSCI EM -2.14%	MSCI EM 3.73%	GLOBAL BONDS -4.59%	MSCI EM 0.93%
GLOBAL BONDS -2.78%	EURO STOXX 50 -4.45%	SHANGHAI STOCK EXCHANGE -4.05%	SHANGHAI STOCK EXCHANGE -5.84%	SHANGHAI STOCK EXCHANGE -12.50%