ECONOMIC REPORT

by Glacier Research

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REVIEW PERIOD: SEPTEMBER 2017

SUMMARY

Global equity markets have moved beyond the geopolitical tensions between the US and North Korea to end the month in positive territory. Both global bonds and equity were positive in ZAR terms as the rand weakened against the US dollar for the month of September. Markets drew strength from the positive economic data indicating a healthy global economy and were dominated by the chance of major corporate tax cuts in the US. On the monetary policy front in Europe, no changes were made by the European Central Bank (ECB). However, investors have shifted their focus to the ECB's meeting in October. Market participants expect the ECB to shed some light on its policy outlook and to start making formal announcements regarding its future asset purchases.

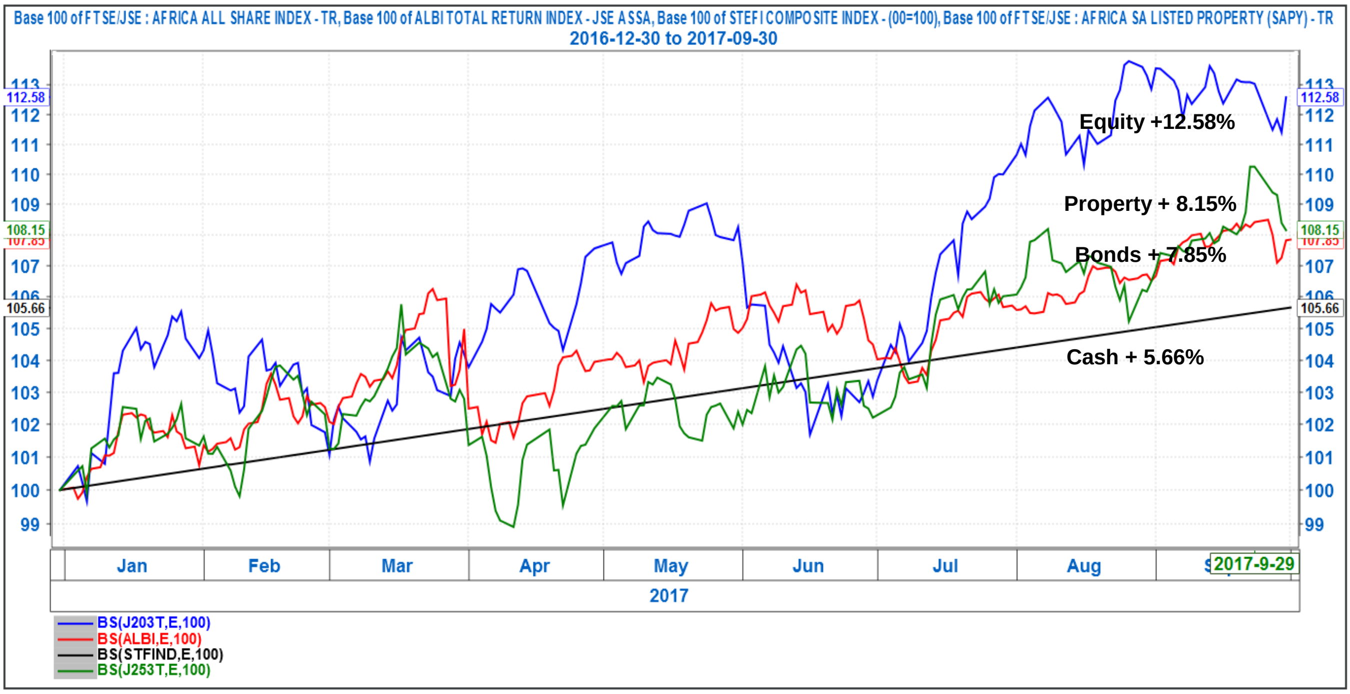
In Germany, Angela Merkel won a fourth term as German chancellor in a victory that reflected fading support for the two main political parties. Meanwhile, markets in Japan rallied after Prime Minister Shinzo Abe called a snap general election for 22 October. For the first month this year emerging market equities underperformed developed market equities, although year-to-date they still remain comfortably ahead. The main drag on performance during September came from the Europe, the Middle East and Africa, with Greece and Turkey leading the losses.

Locally, the month of September revealed further weakness in the South African economy and risk asset returns were relatively weak across the board. The JSE All Share Index delivered a negative performance, shedding 0.87% for the month, with industrials (-2.37%) being the main detractor. The positive contribution seen by resources over the last few months came to a halt in September as bulk metals and minerals prices plunged in September. SA government bonds gained overall in September on the back of large foreign net inflows and also risk-off trade by local and foreign investors in SA listed equity. SA government bonds have been a significant recipient of inflows due to the "global search for yield" phenomenon over the year, with foreign investors now owning more than 50% of SA government bonds. On the economic front, SA remains vulnerable and weak despite SA GDP growth in Q2 2017 surprising on the upside and despite the trade balance continuing to show strong surpluses on a monthly basis. Subsequently, inflation crept up again in September, prompting the SARB to leave

the repo rate at 6.75% and the prime rate at 10.25%. Markets were expecting a 25bps cut. However, policymakers left the door open for further loosening in November, saying it would be appropriate to reassess the data and the balance of risks at the next meeting.

Developed market equities (+2.24% in USD, +6.22% in ZAR and -1.80% in GBP) outperformed emerging market equities for the first time this year in September (-0.40% in USD, +3.47% in ZAR and -4.34% in GBP). On a global equity-style basis using the MSCI World style indices, value was the top performing style, returning (+3.02% in USD, +7.03% in ZAR and -1.05% in GBP), followed by momentum (+2.56% in USD, +6.54% in ZAR and -1.50% in GBP), quality (+1.88% in USD, +5.84% in ZAR and -2.15% in GBP) and then growth (+1.49% in USD, +5.44% in ZAR and -2.52% in GBP). Developed market property gave up 0.33% in USD terms, while local investors would have experienced a higher return of +3.54% due to the rand weakening against the US dollar (+4.16%).

Meanwhile, global bonds underperformed global equities, returning -0.90% in USD (-4.82% in GBP and +2.95% in ZAR). Locally, the ALSI turned in a weak performance, surrendering 0.87% in ZAR terms (-4.58% in USD and -8.36% in GBP). Year-to-date, the ALSI has returned 12.58%. The market was supported by consumer goods (+3.28%) and SA listed property (+1.19%). Meanwhile, technology (-7.66%), telecommunications (-5.95%), financials (-2.38%), industrials (-2.37%), general retailers (-2.27%) and resources (-0.98%) dragged the market lower. Fixed-interest returns were strong relative to local equities, with the ALBI adding 1.11%. Preference shares gained 0.62%, while inflation-linked bonds gained 0.98%. The longer end of the yield curve (over 12 years) was the best-performing fixed-interest asset class in September, returning 1.38%, followed by the middle end (7-12 years) which added 0.79%. The short end of the yield curve (3-7 years) was the worst performer, returning 0.51%. Furthermore, cash underperformed bonds, but outperformed equities in September, returning 0.59%.



Source: I-Net October 2017

LOCAL OVERVIEW

Consumer inflation in South Africa increased 5.1% year-on-year in September 2017, higher than 4.8% in the previous month. However, the figures came in above market expectations of 4.9%, mainly boosted by higher prices for housing, transport and miscellaneous goods and services. Prices rose faster for housing and utilities (4.9% compared to 4.5% in August), mainly boosted by the cost of actual rentals for housing (5.7% compared to 5%) and that of the owners' equivalent rent (5.4% compared to 4.9%); transport (5.6% compared to 3.9%), due to higher cost of fuel (12.2% compared to 5.7%) and private transport operation (10.2% compared to 5.2%); miscellaneous goods and services (7.6% compared to 7.5%); alcoholic beverages and tobacco (4.7% compared to 4.3%); household contents and equipment (2.1% compared to 2%); and health (7.2% compared to 7%).

Meanwhile, inflation eased for food and non-alcoholic beverages (5.5% compared to 5.7% in August); clothing and footwear (2.3% compared to 2.8%); recreation and culture (2.2% compared to 2.4%); and restaurants and hotels (3.4% compared to 4.2%). Inflation for communication continued to fall (-1.4% compared to -1.3% in August). On a monthly basis, consumer prices rose to 0.5%, beating expectations of 0.3%.

	Apr'17	May'17	June'17	July'17	Aug'17	Sep'17
CPI (y/y)	**5.3%**	**5.4%**	**5.1%**	**4.6%**	**4.8%**	**5.1%**
PPI (y/y)	**4.6%**	**4.8%**	**4%**	**3.6%**	**4.2%**	**-**

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

South Africa's trade surplus decreased to R5.94 billion in August 2017 from an upwardly revised R9.33 billion surplus in July, but beating market expectations of a R3.2 billion surplus. Exports increased 11%, while imports advanced at a faster 16.3%. Considering the January to August period, exports increased 5.8% and imports decreased 2.1%, shifting the country's trade balance into a R43.5 billion surplus from a R13.7 billion gap in the same period of 2016. Exports increased to R103.4 billion in August from R93.1 billion, led by higher shipments of mineral products (21%); precious metals and stones (20%); base metals (12%); machinery and electronics (12%) while those of vehicles and transport equipment fell 17%.

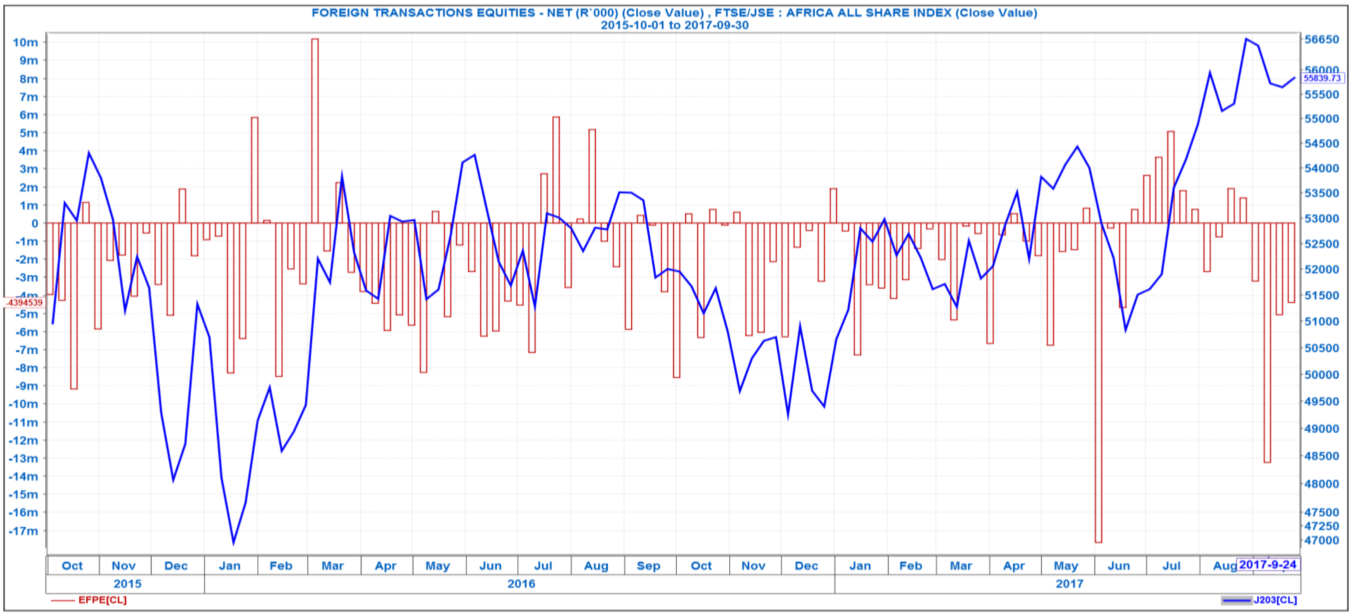
Major destinations for sales were China (9.9%); the US (8.1%); Germany (6.8%); Japan (4.7%) and Botswana (4.6%). Imports advanced to R97.4 billion from R83.8 billion, due to higher purchases of mineral products (65%); prepared foodstuffs (36%); textiles (27%); original equipment components (29%) and machinery and electronics (11%). Imports came mostly from China (21.3% of total imports); Germany (14.1%); the US (7.8%); India (5.6%) and Saudi Arabia (5.2%).

	30 September 2015	30 September 2016	30 September 2017
USD/ZAR	**13.82**	**13.72**	**13.55**
GBP/ZAR	**20.93**	**17.59**	**18.02**
EUR/ZAR	**15.46**	**15.42**	**16.01**

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

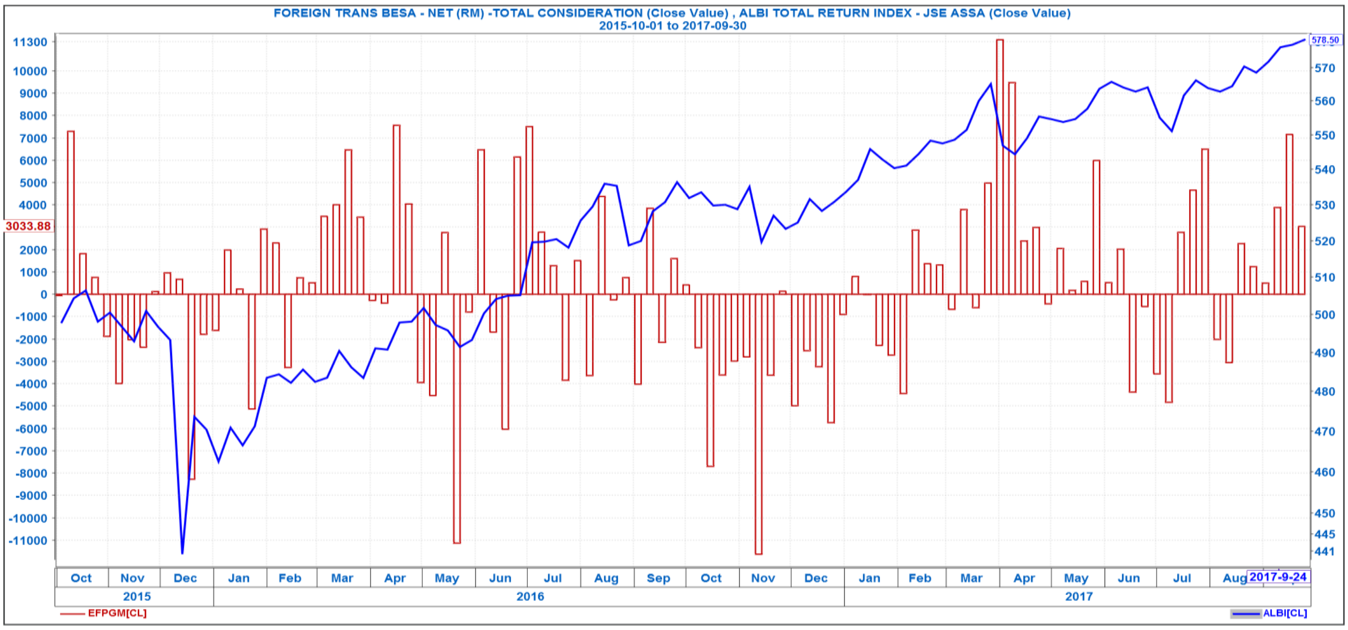
Locally, the ALSI was down 0.87% in rand terms. US foreigners invested in SA equities would have fared exceedingly worse with a return of -4.83% in USD, as the rand weakened (+4.16%) considerably against the US dollar in September. Industrials led the declines of the ALSI dropping 2.37% over the month. Financials followed suit dropping 1.93% in September. Resources ended its stellar run over the last few months, declining 1.07%, as prices of base metals and minerals tanked over the month. However, Brent crude oil bucked the trend, rising 7.43%. By market-cap, small-cap stocks (+0.08%) marginally led the gains, but the Top40 shed 0.39%, while mid-cap stocks ended the month torridly, returning -5.10%.

Consumer goods (+3.28%) was the best performing sub-sector over the month of September. This was followed by consumer services, down 0.86%, and basic materials off by 1.07%. Technology (-7.66%) was the worst-performing sub-sector, followed by telecommunication, returning -5.95%. The gold mining sub-sector dipped 7.48% over the month, as the price of gold fell 3.31%. This was largely driven by 'global synchronized growth' rhetoric spurring on positive market sentiment and general risk-on trade in global equities. Major resource counters in the Top40 had a difficult month under lower commodity prices, with Anglo Gold Ashanti dropping 3.31%, BHP Billiton falling 3.37% and Impala Platinum plummeting 22.89%. However, rand-hedge stocks in the Top40, such as Bidcorp (+2.86%), British American Tobacco (+4.82%) and Richemont (+6.17%) contributed to performance, with the rand weakening significantly against the US dollar and other global peer currencies. SA equities were sold off heavily by foreigners in September, as they were net sellers of R27 billion worth of equities. Year-to-date, they are also net sellers of R88.86 billion worth of SA equities.



Source: I-Net October 2017

Local fixed-income markets saw positive returns over the month as the ALBI (+1.11%) marginally underperformed property (+1.19%) but managed to outperform cash (+0.59%) and also preference shares (+0.62%). The longer end (12yr+) of the yield curve was the best-performing interest-bearing asset class, returning 1.38%, followed by inflation-linked bonds (+0.98%) and 7 to 12-year bonds (+0.79%). The 3 to 7-year section of the yield curve was the worst performer, returning +0.51% over the month. Year-to-date, however, the 3 to 7-year period still has been the best performer (+9.11%) followed by the 7 to 12-year period (+8.88%), while the 3 to 7-year (+10.26%) was the best performer over the past 12 months. SA listed property (a hybrid asset class) had a strong positive performance over the month returning 1.19% and is the second best-performing SA asset class year-to-date (+8.15%), following equities.



Source: I-Net October 2017

During September, foreigners returned to being net buyers of R17.84 billion worth of SA bonds. Year-to-date, the SA bond market has experienced a net foreign inflow of R56.52 billion. In a global fixed-income context, global bonds performed negatively as the Barclays Global Aggregate Bond Index (-0.90%) and the Citigroup World Government Bond Index (-1.20%) both closed lower in USD terms. However, they closed positively in ZAR due to rand weakness (+2.95% and +2.64% respectively). In September, SA's currency weakened against major peers. The rand depreciated heavily against the British pound sterling (+7.22%), the US dollar (+4.16%) and against the euro (+3.43%).

GLOBAL OVERVIEW

The US equity market ended September in positive territory, marking its sixth straight monthly gain and the longest winning streak since May 2013. The markets were propelled by the Republicans, unveiling a tax reform proposal aimed at lowering the corporate tax rate from 35% to 20%. Hopes remain that the US tax reform will aid economic growth. The Federal Reserve gave an optimistic take on the economic outlook for the US and warned that they should be wary of raising interest rates too gradually. The trade balance deficit in the US narrowed to $42.4 billion in August from a $43.6 billion gap in July. Core inflation in the US came in at 1.70% in August, the same as in the previous three months. Meanwhile, the Federal Reserve left its interest rate unchanged in the band between 1.00% and 1.25% during its September meeting, as widely expected. The US economy expanded by an annualised 3.10% quarter-on-quarter in Q2 from a 1.2% growth in the previous quarter. Energy-related stocks overtook technology stocks as the lead sector in September as the price of Brent crude oil rebounded. The technology sector had offered the hope of secular growth regardless of the underlying economy, which led the market higher in recent months. In corporate news, Toys “R” Us filed for bankruptcy protection in the US and Canada as it attempts to restructure its debts.

The broader Bloomberg commodities index closed 0.15% lower for the month of September. The Bloomberg WTI crude oil index advanced 7.82%, while the Bloomberg natural gas index gave up 2.98%. The Bloomberg precious metals index closed 3.34% lower, with gold, nickel, platinum and silver weakening 2.75%, 11.23%, 8.57% and 5.04% respectively.

On a total-return basis, the global energy sector was the top-performing sector for the month of September returning +10.40% in USD, +6.10% in GBP and +14.70% in ZAR. This was followed by the financial services sector which returned +5.10% in USD, +0.90% in GBP and +9.20% in ZAR. The top-performing sector over a one-year period was the financial services sector, returning +35.00% in USD, +30.70% in GBP and +32.60% in ZAR. The worst-performing global sector in September was the communications services sector returning -2.60% in USD, -6.50% in GBP and +1.20% in ZAR. Furthermore, the energy sector remains the worst-performing global sector for the second consecutive month over a one-year period, losing -0.80% in USD, -3.90% in GBP and -2.60% in ZAR.

In rand terms, developed market equities (+6.22%) outperformed emerging market equities (+3.47%) for the first time this year in September. In USD, the MSCI World added 2.24% and the MSCI Emerging Markets Index gave up 0.40% for the month. Developed market property weakened by 0.33% in USD, outperforming bonds, which surrendered 0.90% in USD. Developed markets indices in ZAR terms were positive across the board for the month of September due to rand weakness. The rand weakened against the US dollar (+4.16%), the Australian dollar (+3.61%), the pound sterling (+7.22%) and the euro (+3.43%).

The DAX (+9.22% in ZAR, +5.81% in USD and +1.62% in GBP), the Euro STOXX 50 (+8.62% in ZAR, +4.56% in USD and +0.42% in GBP), the CAC 40 (+8.37% in ZAR, +4.32% in USD and +0.19% in GBP), the FTSE 100 (+7.44% in ZAR, +3.42% in USD and -0.67% in GBP), the Canadian TSX (+7.41% in ZAR, +3.39% in USD and -0.70% in GBP), the Dow Jones (+6.13% in ZAR, +2.16% in USD and -1.88% in GBP) and the S&P 500 (+6.03% in ZAR, +2.06% in USD and -1.98% in GBP) were all higher in ZAR terms for the month.

In emerging markets, China’s Shanghai Composite Index lost 0.20% in its base currency (+2.96% in ZAR, -0.89% in USD and -4.81% in GBP), the Brazilian Bovespa Equity Index advanced 4.88% in its base currency (+8.38% in ZAR, +4.33% in USD and +0.20% in GBP) and the Indian Nifty gave up 1.30% in its base currency (+0.34% in ZAR, -3.41% in USD and -7.23% in GBP). The Argentina Merval Index surged 10.55% in its base currency (+14.80% in ZAR, +10.51% in USD and +6.13% in GBP) and the Nigerian All Share Index lost 0.18% in its base currency (+3.55% in ZAR, -0.32% in USD and -4.27% in GBP). The US dollar strengthened against the euro (-1.28%), but weakened against the British pound (+3.72%).

Spot Rates	30 September 2015	30 September 2016	30 September 2017
EUR/USD	**1.12**	**1.12**	**1.17**
GBP/USD	**1.51**	**1.30**	**1.34**
USD/JPY	**119.93**	**101.32**	**112.94**

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