ECONOMIC REPORT

by Glacier Research

28 September 2018

REVIEW PERIOD: AUGUST 2018

DOMESTIC OVERVIEW

The economic and market environment in South Africa remains challenged as investor anxiety prevails because of the volatility in emerging markets and the lack of clarity in the ruling party's land reform program. In the month of August, local equities and property were lead performers, while the more conservative asset classes delivered poor performance.

Domestic Highlights in August 2018

- Land Reform
- Rand Depreciation

Land Reform

Land reform has recently been the most topical subject in South Africa, attracting commentary from different internal and external stakeholders. Following its two-day Lekgotla, the African National Congress, pronounced that it will propose an amendment to South African constitution to enable land expropriation without compensation. This comes on the back of the ANC's December 2017 elective conference resolution to accelerate land reform in South Africa. While the land reform debate heightens, no detailed clarity was provided on the specifics of land expropriation. The ruling party remains uncertain about the implementation of the policy, if it is voted.

President Ramaphosa made attempts to allay investor fears by assuring the country that the land stance will not pose a negative effect on food security. He continued to assert that the proposed land reform policy will be implemented constitutionally in a manner that unlocks economic growth, and enables more productive participation of South Africans in the economy.

Rand Depreciation

The rand weakened sharply in month of August, following increased concerns about Turkey and the broader emerging markets. It recorded its worst month in 5 years, this was mainly driven by the sharp sell-off in the Turkish Lira, which was triggered by Turkey's political tensions with the United States coupled with Turkey's weakening economic fundamentals and the political interference of its central bank. Rand volatility was further exacerbated by the media frenzy on land reform. Year-to-date, the rand was recorded to have weakened by over 15% against the U.S dollar, while on the month of August it recorded a depreciation of 9.6%. The sharp weakening of the rand was driven by global, rather that local factors.

South Africa: Economy

SA inflation rose to 5.1% in July to ease at 4.9% in August, below market expectations of 5.2%. The slowdown was driven by prices of transport. SA unemployment rate rose by 0.5% to 27.2% in the second quarter of 2018, shedding 90 000 jobs. The number of discouraged workers jumped by 77 000 in the second quarter of 2018. In addition, youth unemployment rate, using the expanded definition of unemployment, is at 67.1%. The seasonally adjusted ABSA Purchasing Managers' Index (PMI) rose by 3.6 index points to 51.5 index points in July, from 27.9 index points in June. The SA economic fundamentals are weakening as land reform uncertainty and currency depreciation have been the source of investor concerns.

	Mar'18	Apr'18	May'18	June'18	July'18	Aug'18
CPI (y/y)	**3.8%**	**4.5%**	**4.4%**	**4.6%**	**5.1%**	**4.9%**
PPI (y/y)	**3.7%**	**4.4%**	**4.6%**	**5.9%**	**6.1%**	**6.3%**

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

	31 August 2016	31 August 2017	31 August 2018
USD/ZAR	**14.68**	**13.00**	**14.68**
GBP/ZAR	**19.30**	**16.81**	**19.02**
EUR/ZAR	**16.39**	**15.48**	**17.03**

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

South Africa: Markets

Equities returned 2.34% making them the best performing asset class for the month. After delivering disappointing performance for the past couple of months, SA property had good month in August, advancing 2.15%. Cash was the second worse performing asset class in August, delivering a sluggish 0.59%. SA bonds had a disappointing month, surrendering 1.87%. In terms of market capitalization, the Top 40 delivered the highest gains for the month, returning +2.42%. SA mid-caps added 1.48%, while SA small-caps strengthened by 1.23%. Foreigners were net seller of 22 billion worth of SA bonds, and net seller of R13 billion worth of SA equities.

In terms of sectors, Consumer goods (+6.8%) took the crown as the best performing sector for the month followed by gains from Resources (+5.59%). Industrials (+2.52%) and SA Industrials (+1.88%) advanced moderately, while General retailer (+1.44%), Consumer services (+1.39%) and Financials (-+0.22%) recorded muted gains.

LOCAL RETURNS IN ZAR

2017	June 2018	July 2018	August 2018	Year-to-date
SA TOP 40 23.07%	SA TOP 40 3.62%	SA BONDS 2.42%	SA TOP 40 2.42%	SA CASH 4.77%
SA EQUITY 20.95%	SA EQUITY 2.78%	SA CASH 0.61%	SA EQUITY 2.34%	SA BONDS 4.50%
SA PROPERTY 17.15%	SA CASH 0.55%	SA MID CAPS 0.53%	SA PROPERTY 2.15%	SA TOP 40 1.55%
SA BONDS 10.24%	SA BONDS -1.17%	SA EQUITY -0.25%	SA MID CAPS 1.48%	SA EQUITY 0.35%
SA CASH 7.56%	SA MID CAPS -2.14%	SA TOP 40 -0.33%	SA SMALL CAPS 1.23%	SA SMALL CAPS -6.22%
SA MID CAPS 7.36%	SA SMALL CAPS -3.31%	SA PROPERTY -0.50%	SA CASH 0.59%	SA MID CAPS -8.72%
SA SMALL CAPS 2.95%	SA PROPERTY -3.45%	SA SMALL CAPS -1.74%	SA BONDS -1.87%	SA PROPERTY -20.08%

LOCAL SECTOR RETURNS IN ZAR

2017	June 2018	July 2018	August 2018	Year-to-date
CONSUMER SERVICES 52.66%	CONSUMER SERVICES 9.37%	FINANCIALS 4.66%	CONSUMER GOODS 6.80%	RESOURCES 19.77%
SA INDUSTRIALS 22.50%	RESOURCES 5.96%	CONSUMER GOODS 0.97%	RESOURCES 5.59%	CONSUMER GOODS 3.50%
FINANCIALS 20.61%	SA INDUSTRIALS 4.18%	INDUSTRIALS 0.45%	INDUSTRIALS 2.52%	SA INDUSTRIALS -4.49%
GENERAL RETAILERS 19.00%	CONSUMER GOODS 1.72%	GENERAL RETAILERS 0.41%	SA INDUSTRIALS 1.88%	CONSUMER SERVICES -4.89%
RESOURCES 17.90%	INDUSTRIALS -2.52%	RESOURCES -1.40%	GENERAL RETAILERS 1.44%	FINANCIALS -4.89%
INDUSTRIALS 14.73%	FINANCIALS -2.88%	SA INDUSTRIALS -1.99%	CONSUMER SERVICES 1.39%	INDUSTRIALS -8.25%
CONSUMER GOODS -1.12%	GENERAL RETAILERS -6.85%	CONSUMER SERVICES -5.14%	FINANCIALS 0.26%	GENERAL RETAILERS -10.45%

GLOBAL OVERVIEW

The Global Equity Markets ended the month of August in positive territory, on the back of the reduction of risk to the global economy. In addition global markets reacted favourably to news of the development on trade announced by the US and Mexico and speculations that the Trump administration would continue to de-escalate global trade conflicts. Cyclical sectors linked to global growth performed the strongest over the month including technology and consumer discretionary.

The Faang stocks (Facebook, Amazon, Apple, Netflix and Google's parent company Alphabet) continued to dictate market performance. The total value of the five companies amounts to an astounding 19% of total US GDP. Apple became the first US firm to be valued at US$1 trillion, thanks to a mixture of robust iPhone sales and a vast capital returns programme running into hundreds of billion dollars. Shares of Amazon and Google-parent Alphabet rose after Morgan Stanley raised its price targets, which projects the future price level of a financial security through assumptions of future activity.

The energy sector was the weakest performer over the month, despite oil prices rallying more than 10% in the past two weeks. The oil price rose to a high of US$80 a barrel driven by Iran and the looming drop in supplies, with US sanctions tied to its nuclear programme set to be reintroduced in November. Both Global Bonds and Global Equity were positive in ZAR terms as the rand weakened against the US dollar for the month.

United States

The US equity market continued its record-setting run in August to reach fresh all-time highs and what many are dubbing as the longest bull-run in history. US consumer confidence surged to an 18-year high in August, well ahead of economists' expectations, as households remained upbeat on the jobs market. Consumer confidence and the overall economy are seen as important indicators of how freely consumers will spend, especially on big-ticket items such as cars, in coming months. Consumer spending accounts for 70% of economic activity in the US. The Federal Reserve (the Fed) looks set to continue raising rates in a gradual fashion. The policy rate was held steady in August but the minutes of the meeting, along with Jerome Powell's speech at Jackson Hole, indicates that the Fed is likely to continue to raise rates at a pace of 25 basis points per quarter.

Eurozone

European equity markets fell in August due to concerns over the Italian budget combined with contagion fears over the Turkish Lira weakness. Financials and telecoms bore the brunt of the sell-off, while technology demonstrated the only sector to hold on to positive territory over the month. The Eurozone Economic Surprise Index, which displays how economic data is developing relative to the consensus forecasts of market economists, has fluctuated back into positive territory, rebounding from its lows in May and in June. Manufacturing PMI (Purchasing Managers' Index) numbers showed a small increase, which is consistent with a strong economy and provides the European central bank with some assurance that they are right to be thinking about normalising monetary policy.

United Kingdom

UK equity markets sold off during the month, caused mainly by on-going trade tensions and speculation of their impact on sectors such as mining. The sterling ended the month weaker against the US dollar, despite a notable rally into month end. This was driven by dollar weakness and improved Brexit headlines. The Bank of England's Monetary Policy Committee (MPC) voted to increase the UK's base interest rate at its August meeting.

The market had widely anticipated the 0.25% rise, as it offers the MPC greater flexibility to cut back interest rates if thought necessary following the final deal negotiated for the UK's exit from the European Union. On the economic front, GDP growth for the second quarter came in at 1.5% on an annualised basis, which was in line with expectations but a bit lower than the BoE's forecasts. Inflation also came in a bit lower than the BoE's forecasts, with the consumer price index (CPI) and core CPI of 2.5% year on year and 1.9% year on year, respectively.

Spot Rates	31 August 2016	31 August 2017	31 August 2018
EUR/USD	1.11	1.18	1.16
GBP/USD	1.31	1.29	1.29
USD/JPY	103.33	110.07	111.04

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

Emerging Markets

Emerging markets registered negative returns in August, underperforming its developed market counterpart. This was largely due to trade war woes between the US and China escalating, rising interest rates and increased volatility in Argentina and Turkey.

GLOBAL RETURNS IN ZAR

2017	June 2018	July 2018	August 2018	Year-to-date
MSCI EM 24.28%	GLOBAL PROPERTY 10.75%	EURO STOXX 50 -0.46%	S&P 500 15.50%	S&P 500 30.11%
EURO STOXX 50 12.50%	S&P 500 8.89%	S&P 500 -0.88%	GLOBAL PROPERTY 13.60%	MSCI WORLD 24.09%
FTSE 100 10.95%	MSCI WORLD 8.17%	MSCI WORLD -1.45%	MSCI WORLD 13.24%	GLOBAL PROPERTY 22.48%
MSCI WORLD 10.81%	EURO STOXX 50 8.03%	MSCI EM -2.33%	GLOBAL BONDS 11.97%	GLOBAL BONDS 16.55%
S&P 500 10.29%	GLOBAL BONDS 7.74%	GLOBAL PROPERTY -3.53%	MSCI EM 8.83%	EURO STOXX 50 13.63%
SHANGHAI STOCK EXCHANGE 4.78%	FTSE 100 7.13%	FTSE 100 -3.61%	FTSE 100 7.18%	FTSE 100 13.51%
GLOBAL PROPERTY -0.98%	MSCI EM 3.73%	GLOBAL BONDS -4.59%	EURO STOXX 50 7.10%	MSCI EM 9.84%
GLOBAL BONDS -2.78%	SHANGHAI STOCK EXCHANGE -4.05%	SHANGHAI STOCK EXCHANGE -5.84%	SHANGHAI STOCK EXCHANGE 6.19%	SHANGHAI STOCK EXCHANGE -7.08%