Caveat Newsletter March 2020

South Africa

Economy

The South African economy decreased by -1.4% in the fourth quarter of 2019 after a contraction of -0.8% (revised) in the third quarter of 2019. After two quarters of consecutive negative growth in GDP, the South African economy finds itself in a technical recession.

The South African economy grew by 0.2% in 2019 which is the lowest growth rate since 2009 when the economy decreased by -1.5%. Agriculture was reportedly the main contributor to the decrease in 2019 growth, followed by construction, mining and manufacturing. The main positive contributors to 2019 growth was finance and government spending.

The poor performance of the South African economy also led to 2019 business confidence levels decreasing to the worst level since 1985 when global sanctions hit South Africa.

Business climate in South Africa is largely dependent on domestic economic performance however, policy certainty is also important. This can be reflected as the domestic economy is not finding traction with numerous problems being faced by state owned enterprises which is dragging an already weak economy further down.

ESKOM

President Cyril Ramaphosa said in an interview, on the third of March 2020, that he is in fact open to the idea of selling a part of Eskom's power stations to private companies. The president stated that such a move will help communities in those towns where the power stations are located further adding that privatising certain parts of Eskom would in fact lead to job creation.

Eskom's split into generation, transmission and distribution means that the transmission facility will remain state-owned, but the generation facility could be improved if it were privatised. The silver lining with such a transition is that independent power producers would in effect be selling electricity to Eskom which would allow for competitive competition to be added to the Eskom model. From a electricity supply point of view there should be increased stability when there are more producers of electricity.

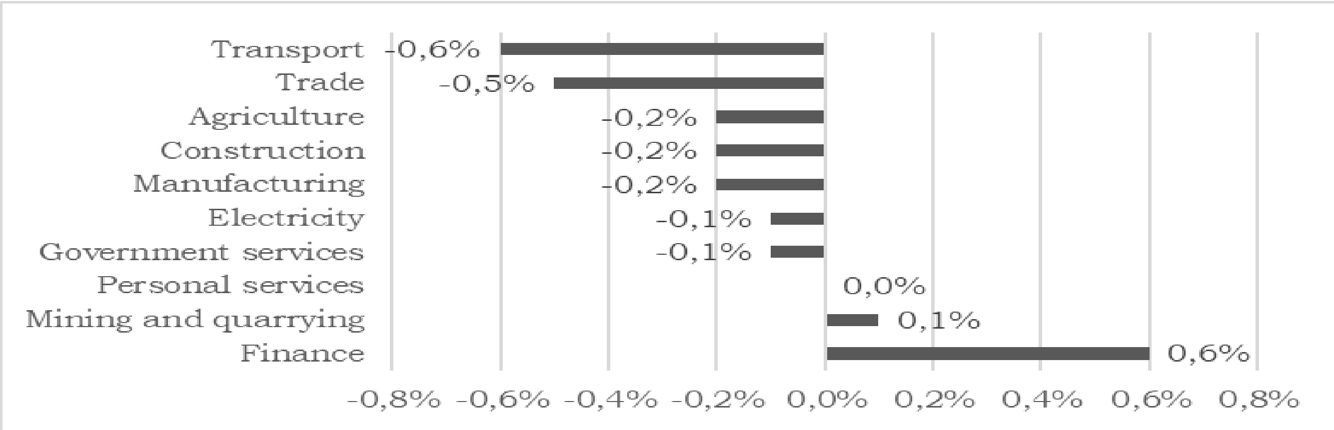
Coming back to Eskom's R450bn worth of Debt. Pension funds would be used to help and decrease Eskom's debt load. Although such an act might sound devastating, for pension funds to invest in a restructured Eskom would be different from just using pension funds to repay debt of a sinking company.

Key economic indicators

GROSS DOMESTIC PRODUCT (GDP) – Measured by production Q4: 2019 (-1.4% QoQ)

South Africa's GDP (measured by production) increased y 3.1% during the fourth quarter of 2019. The overall decrease in the GDP growth rate is attributable to the following industries:

Growth Rates: % change quarter-on-quarter (seasonally adjusted and annualised)

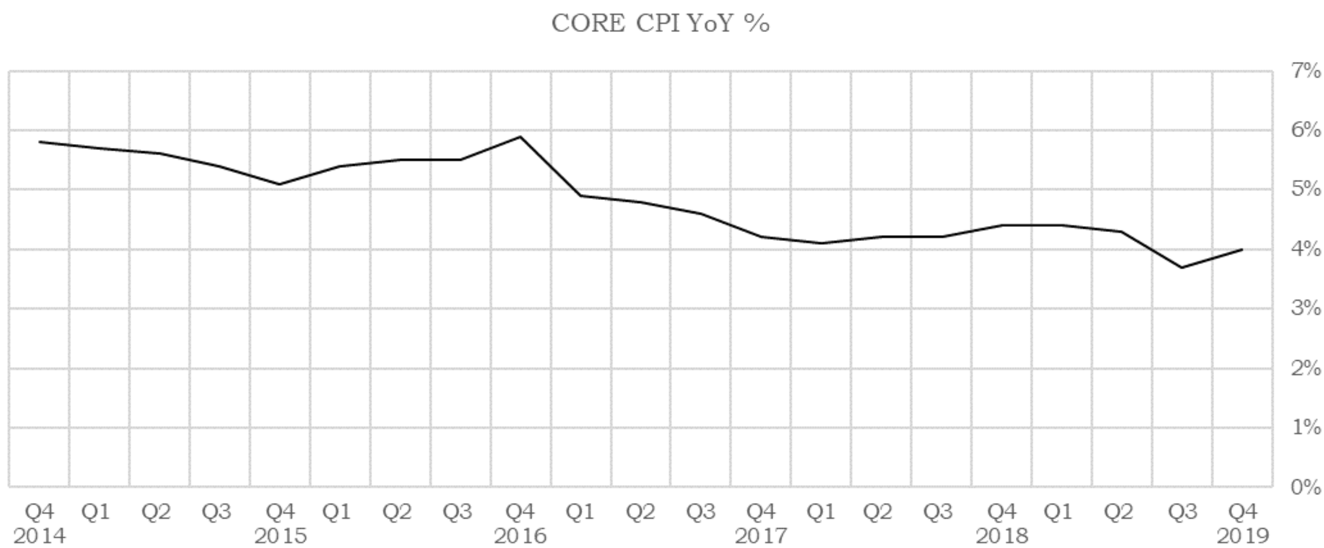


The worst blackouts in South Africa's history during the December 2019 period severely affected seven out of the ten major industries. The transport, storage and communication industry decreased by 7.2% which contributed -0.6% to GDP growth reportedly due to decreased economic activity for land and air transport.

On the other hand, the finance, real estate and business services industry increased by 2.7% which contributed to 0.6% to GDP growth.

Source: Statistics SA

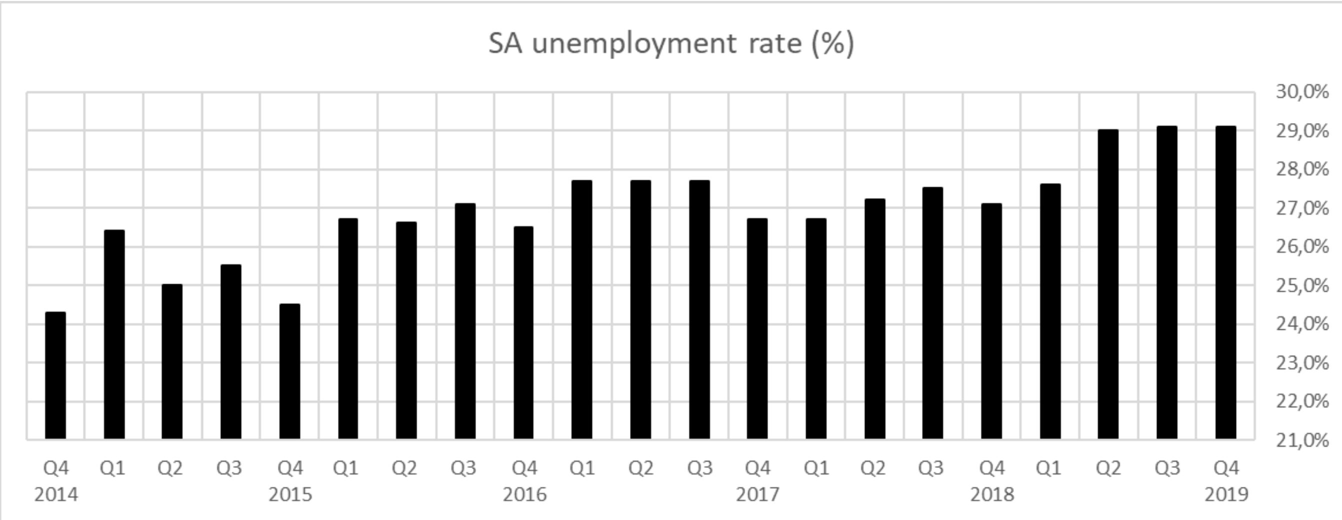
CONSUMER PRICE INDEX (CORE CPI) Q4: 2019 (4% YoY)



Looking back at 2019, average inflation was 4.1% which is lower than the average inflation rates recorded for 2018 (4.7%) and 2017 (5.3%). Given a series of policy rate decreases during 2019, overall inflation levels remain within the 3% - 6% inflation target range. After a further 25 basis points decrease during January 2020, the Monetary Policy Comity (MPC) reported that their improving inflation forecasts opens further space for additional monetary policy easing. Current inflation data suggests that a further rate cut could be expected going forward during 2020.

Source: Statistics SA

UNEMPLOYMENT RATE (29.1%) Q4 2019



Data from the Quarterly Labour Force Survey published by Stats SA shows that South Africa's unemployment rate has remained constant for the last two quarters of 2019.

Apart from being the country with the fourth highest unemployment rate out of 182 countries tracked by Trading Economics, the National Development Plan (NDP) aimed for an unemployment rate of 14% by 2020. Despite accommodative policies set by the South African MPC to stimulate the economy and employment, the structural norms of the South African government remain the main drawdown on critical issues that South Africa has faced for several years.

Source: Statistics SA, Trading Economics

SACCI SOUTH AFRICA BUSINESS CONFIDENCE INDEX (BCI – 93.1)

The current Business Confidence Index (BCI) indicates that the potential of the South African economy is decreasing, meaning that positive corrections must be made to the economy in an appropriate manner. Global economic conditions would not accommodate a highly export driven country such as South Africa. Thus, the global competitiveness of South Africa is being diminished by prolonged structural implications such as BEE, unsupportive labour laws and the current crisis faced by various Stated owned enterprises.

Source: Bloomberg

SOUTH AFRICA: KEY RATES

	2015	2016	2017	2018	2019	2020
Repo Rate (%)	5,75	7,00	7,00	6,50	6,50	6,25%
Prime Rate (%)	9,25	10,50	10,50	10,00	10,00	9,75%
3-Month Deposit rate (%)	6,40	7,60	7,15	7,10	6,78	6,52%

Coronavirus fears has global economies tightening as seen with early 2020 global GDP figures. Central Banks around the globe are moving towards more accommodative policies to help stabilize the effects of the coronavirus. South Africa, having weak domestic growth would likely follow suit during the rest of 2020 to stabilize the effect of the coronavirus on global demand for domestic goods and to help spur domestic spending activities.

Source: SARB

SOUTH AFRICA: EQUITY MARKETS

	Close (ZAR)	YTD	1 Year Return	52-week range
FTSE/JSE Africa ALSI	53 023,86	-7,16%	-1,69%	50 875,08 - 59 544,80
Satrix Swix	1 023	-5,02%	-2,84%	955.00 - 1 180.00
FTSE/JSE Africa Top 40	47 666,56	-6,35%	-0,68%	45 4615,99 - 53 234,09

Source: Bloomberg

Global Economy

G10 COUNTRIES' EXCHANGE RATES

Ticker	Mar '20	YTD	52-week range
EUR/USD	1,1115	-0,50%	1,0778 - 1,448
GBP/USD	1,2813	-3,54%	1,1959 - 1,3514
USD/JPY	107,27	-1,23%	104,46 - 112,4
AUD/USD	0,6610	-5,88%	0,6434 - 0,7206
NZD/USD	0,6287	-6,57%	0,6180 - 0,6939
USD/CAD	1,3375	2,80%	1,2952 - 1,3565
USD/CHF	0,9567	-0,87%	0,9516 - 1,0237
USD/NOK	9,2749	5,37%	8,4112 - 9,4956
USD/SEK	9,5035	1,42%	9,1014 - 9,9648
Ticker	**Mar '20**	**YTD**	**52-week range**
USD/ZAR	15,3498	9,96%	13,8140 - 15,8641
GBP/ZAR	19,6527	6,15%	17,1564 - 20,3204
EUR/ZAR	17,0551	8,05%	15,4240 - 17,5174

The USD has strengthened against most fiat currencies leading after coronavirus fears as demand for safe haven currencies (such as the USD) has increased significantly over the first part of 2020. During times of global uncertainty, the USD strengthens due to the "safe haven sticker" attached to it.

Source: Bloomberg

Commodities

	Gold ($/oz) Mar '20	Brent Crude Oil ($/barrel) Mar '20
Price	1 640,10	$ 52,43
52-week range	1266,35 - 1689,31	58,40 - 70,25
YTD	8,47%	-19,21%

Source: Bloomberg

BRENT CRUDE OIL

From the start of 2020 oil prices have decreased significantly off the back of coronavirus fears. The decrease in oil prices were further amplified after many countries halted production and global transport being decreased by roughly 25% since the outbreak of the coronavirus.

OPEC+ countries have gathered in March to prevent oil prices from further weakening given a weakening demand. Supply cuts of 1.5mn barrels per day have been decided upon by the participating nations which could stabilise oil prices in the short term.

The problem with such a supply cut relates to the same scenario where central banks across the globe are reducing interest rates to stabilise their economies from the overall decrease in demand. It could be problematic to fully incorporate the effects of the coronavirus as there are at least 3-month lags in various economic indicators which are used to aid policy decision-making. On the other side, how could one fully price in a coronavirus, in the sense that supply cuts from oil producers and policy rate decreases by central banks might not be enough to help the global economy fight against the coronavirus. In a sense there could be worse to come if the coronavirus is not contained.

GOLD

Gold has seen a difficult start to 2020 with strong gains from January going to major losses during February. The volatility has various aspects attached to it. Firstly, the coronavirus uncertainty sent gold prices running as investors feared the impact that the coronavirus might have on the global economy. Secondly the sell-off came shortly after various companies around the world have lowered their earnings forecast due to production cuts and supply constraints with the coronavirus worsening during February.

It might seem strange that gold and global indices moved in the same direction during intraday trading. However, given the sharp sell-off on global indices during the end of February, many traders had to close gold positions in order to meet margin requirements after the indices sell-off.

The question is, what is next for gold? One should always remember that safe-haven securities appreciate during times of uncertainty and as long as the coronavirus uncertainty remains, we might see gold reaching even new highs for 2020. However, if a cure for the coronavirus is found, markets might adjust rapidly given the tough run it had up until now. Thus, the demand for safe-haven securities will decrease, causing a decrease in the prices of the safe-havens.

This means that gold prices might decrease if a cure for the coronavirus is found, however, given global economic growth before the coronavirus, gold still remains an attractive asset class in tough economic conditions.

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Sources:

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