Seed Market Overview

30 September 2019

Local Market

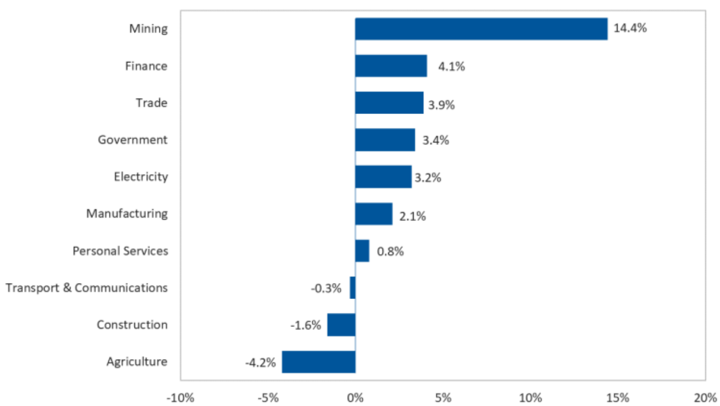
September was a volatile month for the local market. The local equity market was rapidly out of the blocks and the FTSE/JSE All Share Index was up 5.3% mid-month. However, trade war concerns again began to weigh on the market, reversing most of the early month gains. The Index ended the month moderately positive, gaining only 0.2% for the month. The dismal end to the month completed a miserable quarter for the local market, losing 4.6% over the quarter. The year-to-date gain stood at 7.1%, which is 5.1% lower than at the end of the second quarter.

Financial and retail shares propped up the market in September, as resources and industrials ended in the red. Losses during the quarter were broad based with resources, industrials, and financials all ending lower. There was no respite for listed property over the quarter, with the FTSE/JSE SA Listed Property Index down 4.4%. Like the equity index which was positive in September, the listed property index rose 0.3% during the month. The All Bond Index rose 0.5% in September, ending the quarter 0.7% up with benchmark bond yields moderately up in line with global bond yields.

The South African Reserve Bank (SARB) kept the interest rate flat at the Monetary Policy Committee meeting in September. The latest quarterly bulletin released by the SARB in September highlighted that the prime reason for the recovery in economic activity in the second quarter was due to the absence of the severe power disruptions that hampered output during the first quarter. Real GDP advanced 3.1% annualised in the second quarter, having declined by a similar magnitude during the first quarter. Mining, Finance, Trade, Government and Manufacturing contributed, while Agriculture and Construction detracted as illustrated in **Chart 1** (below).

Economic fundamentals, however, remain weak. The current account of the balance of payments widened by R 60.5bn to R 204.1bn from R 143.5bn. As a ratio of gross domestic product (GDP), the current account deficit deteriorated to 4.0% in the second quarter. South Africa's trade balance switched from a surplus of R 41.9bn in the first quarter of 2019, to a deficit of R 27.2bn in the second quarter. South Africa's terms of trade (including gold) deteriorated in the second quarter of 2019 as the rand price of imports increased more than that of exports. The unemployment rate increased to 29% and the government's reform agenda cannot come soon enough to turn around the economy.

Chart 1: Industry Growth in 2019-Q2 compared to 2019-Q1 (seasonally adjusted & annualised)



Source: Stats SA (30 September 2019)

Global Market

Geopolitics and Central Banks continued to dominate market headlines in September. Global Central Banks continued to support the markets with both the US Federal Reserve (Fed) and the European Central Banks (ECB) cutting interest rates in September. For the ECB, it was the second consecutive cut, while the United States' 0.25% cut was widely expected by market participants. The ECB further moved yields into negative territory despite the interest rate cut, but pledged to restart quantitative easing and will buy € 20bn worth of bonds a month from November.

The trade conflict between the US and China continued to dominate the headlines. The month started on a positive note, with China and the US announcing a resumption in talks scheduled for October. With US economic data releases showing positive numbers easing recession fears, the market rallied. The S&P 500 gained 1.8% and the MSCI World Index gained 2.1%, as developed markets again outperformed emerging markets with the MSCI Emerging Market Index up 1.9%. The MSCI World Index accumulated a gain of 0.5% over the quarter, while the MSCI Emerging Market Index lost 4.2%.

Early month optimism soon eroded towards the end of the month with tweets from US President Donald Trump suggesting restriction of access to US capital markets for Chinese firms. Trump found himself facing threats of impeachment over whistle-blower revelations that he pressured his Ukrainian counterpart to investigate political rival, Joe Biden. As political noise escalated in the US, the UK did not move any closer to a resolution regarding its breakaway from the European Union. The Prime Minister, Boris Johnson, suffered a defeat in court on his suspension of parliament, as the likelihood of an agreement on a Brexit deal became more and more unlikely.

As geopolitical tension and growth fears continued to escalate, investors piled into gold, the traditional *"defensive asset"*. Global gold-backed ETF holdings hit record highs, increasing by 13.4% to date this year. In September, global gold-backed ETF's and similar products held $ 3.9bn of net inflows across all regions, increasing their collective gold holdings by 75 tonnes to 2,808 tonnes (the highest levels of all time). Holdings surpassed late 2012 levels, at which time the gold price was near $ 1,700/ounce. Global gold-backed ETF flows for the third quarter are illustrated in **Table 1** (below).

Table 1: 2019-Q3 Global Gold ETF Net Flows

Flows by Region	Total AUM (bn)	Change tonnes	Flows ($ mn)	Flows (% AUM)
North America	69	183	8 879	13%
Europe	59	52	2 918	5%
Asia	4	14	687	17%
Other	2	4	193	12%
Total Net Flow	134	253	12 676	9%

Top 5 ETF Flows	Country	Change tonnes	Flows ($ mn)	Flows (% AUM)
SPDR Gold Shares	United States	127	6 122	17%
iShares Gold Trust	United States	48	2 291	17%
iShares Physical Gold ETC	United Kingdom	17	798	14%
Huaan Yifu Gold ETF	China	7	349	43%
Invesco Physical Gold ETC	United Kingdom	6	304	5%

Source: World Gold Council (30 September 2019)

Asset Class (ZAR)	MTD	YTD	1 Year	3 Years	5 Years	10 Years
Local Equity	0.2%	7.1%	1.9%	5.1%	5.3%	11.5%
Local Property	0.3%	1.3%	-2.7%	-3.5%	3.2%	11.2%
Local Bonds	0.5%	8.4%	11.4%	8.9%	8.3%	8.8%
Local Cash	0.5%	5.0%	6.6%	6.7%	6.5%	6.0%
Global Equity	2.0%	22.5%	8.6%	13.3%	13.1%	16.1%
Global Property	2.5%	28.8%	23.4%	9.9%	15.1%	18.8%
Global Bonds	-1.5%	12.3%	16.5%	4.6%	8.3%	9.3%
Global Cash	0.0%	7.4%	9.8%	5.1%	7.2%	7.9%

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Seed Local Review

Equity

The JSE All Share Index gained only 0.2% in September, bringing the YTD return to 7.1%. With gold and platinum prices down for the month, Resources (-1.1%) closed in the red, while Industrials (-0.8%) fared only slightly better. After lagging for the YTD, Financials (+3.5%) outperformed this month, thanks to strong earnings numbers reported by Banks and Insurers. The Capped Swix index has pulled back 5.1% over the last three months, while earnings have grown by 2.5%. Our models indicate that there is still reasonable value on offer, and we maintain our equity allocations at levels close to benchmark.

Property

The SA Property Index gained 0.3% in September, and both 1 year and 3 year returns remain in negative territory. Counters with global exposure outperformed this month, despite the retail environment in the UK (to which most of these counters are exposed), looking very negative. Local counters continue to struggle on the back of SA's poor economic growth prospects and oversupply in some sectors. The SAPY offers an attractive 1 year forward yield of 9.7%, but there is a significant risk that expected distributions or growth thereon may not materialise.

Bonds

The ALBI returned 0.5% and has been the top performing local asset class over 1, 3 and 5 years. The benchmark R186 yield followed global yields higher this month, and the risk premium component remains elevated. This signals ongoing concern around Emerging Markets in general, and SA's low growth rate and fiscal state specifically. Our valuation model indicates that bonds remain slightly expensive and, practically, we continue to take duration risk in the Property sector in our funds.

Cash

Annual inflation increased to 4.3% after last month's downside surprise, with higher food prices the main driver. The SARB kept the repo rate unchanged at 6.5% following the MPC's September meeting, despite SA's weak growth outlook for the rest of the year. Cash currently delivers a very attractive 2.5% real yield. We appreciate the optionality in cash, but recognise that several other asset classes currently offer more value. As a result, we remain neutral.

Seed Global Review

Currency

The rand started the month on the front foot and strengthened from R 15.19/$ to just below R 14.60/$ by mid-month. However, geopolitical concerns came to the fore during the rest of September, and the rand retraced most of its gains to close only slightly stronger at R 15.14/$. The trade-weighted USD remains strong, and as a counter-cyclical currency is supported by weak global growth. At month end, the ZAR was 7% undervalued against the trade weighted basket of currencies on a purchasing power parity basis. Significantly, the ZAR was 30% undervalued versus the USD using the same methodology.

Equity

Global equity markets reversed August's fortunes and posted gains, despite volatility introduced by the ongoing trade war. The MSCI ACWI returned 2.1%, while the markets of India and Brazil lifted the MSCI EM index to 1.9%. Globally, the Consumption and Services sectors are healthy, but still vulnerable to a drop in consumer confidence. Central banks globally seem to shift towards even easier policy, which should support growth in the short term. Recession risks are on the rise looking further out. We maintain a benchmark weight in global equity and continue to favour allocation to high quality stocks.

Fixed Income

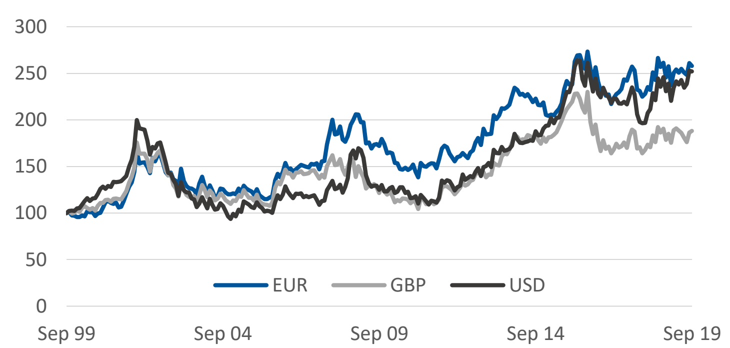
The US 10-year treasury bond yield increased to 1.68% from last month's 1.5%, reflecting recent positive surprises from US economic data. BCA Research opines that yields should rise from this point in line with GDP forecasts, given that underlying US inflation is on the rise. Given a very resilient US economy, the Fed can only afford to cut rates once more, not twice as the market anticipates.

Alternative

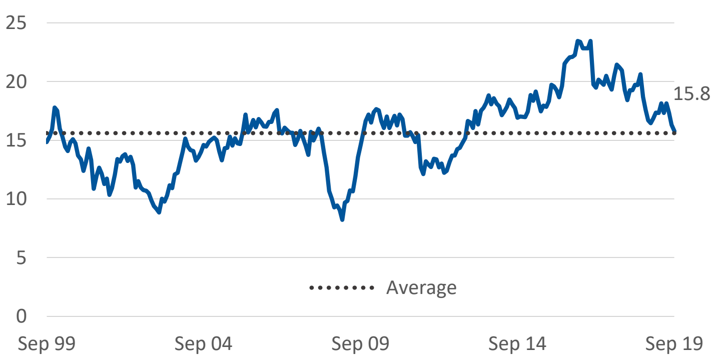
Other asset classes that can be considered include structured notes, private equity, direct real estate, commodities, and hedge funds and can provide investors with uncorrelated returns. However, as interest rates are slowly but surely rising, these alternative investments do become less attractive. These assets can still perform a useful role in multi asset portfolios as they help provide more consistent returns.

ZAR vs USD

Currencies vs ZAR (rebased to 100)



ALSI PE Ratio



SA Government 10 Year Bond Yield