Seed Market Overview

29 February 2020

seed investments

Local Market

February was one of the toughest months for equity markets since the global financial crisis of 2008. Local equities fell 9% as markets retreated sharply, as seen in **Chart 1** (below). Local property had a distressing month falling 15.7%, while bonds benefited from defensive properties and recorded a 0% return for February.

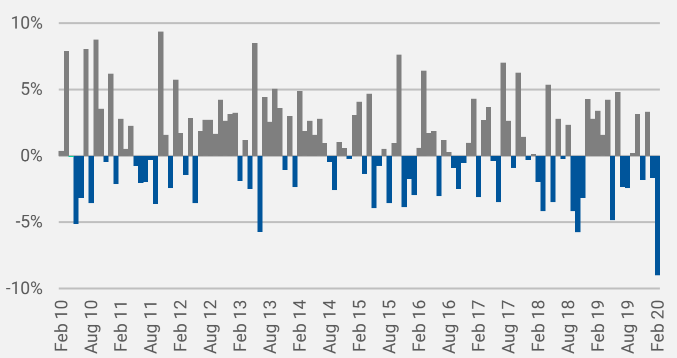
Fears about the economic impact of the Corona Virus escalated in February. For South Africa, it is a potential pandemic that the nation could hardly afford. Eskom is facing operational, financial and structural issues, while the country is experiencing sub-par economic growth. As a result, sentiment in SA's manufacturing index fell to the lowest level in a decade and ABSA's Purchasing Managers' Index fell to the lowest level since August 2009.

President Cyril Ramaphosa delivered the State of the Nation Address (SONA) mid-February. The President admitted that public finances in SA are in a dire state and he acknowledged that recent bouts of power cuts have had a crippling effect on the economy. The President also announced the government's decision to establish a sovereign wealth fund, ensuring that South Africans could share the nation's wealth from natural resources. He said that the government was going ahead with plans to establish a state bank.

The 2020/21 budget speech, as delivered by Minister of Finance Tito Mboweni towards the end of February, was well received by market commentators. Taxes (income and VAT) did not increase, showing that government is thinking differently. While the speech sounded good in theory, the proof will be in the pudding as the nation still faces many challenges. More good news is that restrictions on taking money offshore have been loosened and private investment is expected to improve in 2020, growing at 2.1% (compared to 1.5% in 2019). Mr. Mboweni also addressed the cost of public sector wages and has proposed reducing the public sector compensation bill by R160 billion over 3 years.

Moody's is expected to announce a review assessment of SA in March. Although many may argue that a downgrade looks certain, good news is that regardless of what the rating agency decides, it seems the market has adjusted to the reality of a potential downgrade.

Chart 1 : JSE / FTSE All Share Monthly Returns Over 10 Years



Source : Morningstar (29 February 2020)

Global Market

Global markets suffered in February under Corona Virus fears, as the virus spread significantly beyond China. Investors worldwide grew increasingly fearful of the impact of the outbreak on the global economy and as such, the markets. For the month, developed markets were down 8.5% and emerging markets were down 5.3%.

Stocks plummeted and the volatility index on the US Stock market more than doubled, making cash the only steady asset class for the month. Stocks that were most affected were European oil stocks, airlines, cruise lines and some luxury goods makers.

Although there could be a rebound in equity markets in the coming months as the Corona Virus threat fades, the upcoming US presidential election in November might give equity markets an excuse to sell-off even further.

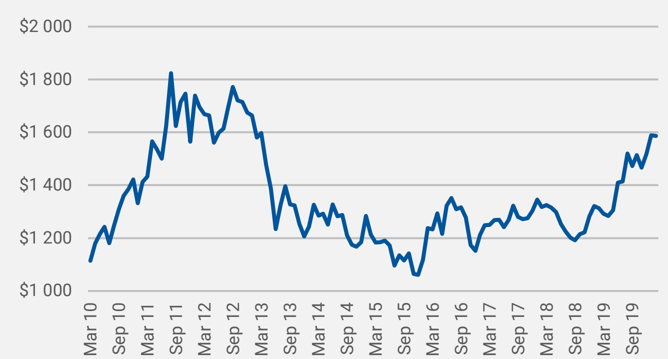
There are some signs that Chinese activity is on the mend, thanks mainly to drastic measures taken by the Chinese authorities. Chinese government estimates that around 60% of the work force has resumed and live traffic statistics from TomTom show that by the end of February, road congestion in Shanghai was back to 50% of its normal level.

February saw US 10-year bond yield drop to record lows, ending the month at 1.2% as the Corona Virus angst sparked demand for US debt at the expense of riskier assets. BCA opines that the market has priced in at least three US Federal reserve rate cuts by year-end.

The US Dollar firmed against most emerging market currencies. Being a safe-haven currency, the dollar has benefitted from the rush to safety in February. Investors have also been chasing gold for the past few weeks. Towards the end of February, the precious metal was trading at its highest level since April 2013, as seen in **Chart 2** (below).

Both gold and the US dollar have been rising at the same time, which historically reflects periods of market stress.

Chart 2 : Gold Spot US Dollar Price over 10-Years



Source : Investing.com (29 February 2020)

Asset Class (ZAR)	MTD	YTD	1 Year	3 Years	5 Years	10 Years
Local Equity	-9.0%	-10.5%	-5.7%	3.1%	2.2%	9.9%
Local Property	-15.7%	-18.3%	-19.1%	-10.4%	-4.8%	8.0%
Local Bonds	0.0%	1.1%	8.9%	9.1%	7.2%	8.7%
Local Cash	0.5%	1.0%	6.6%	6.7%	6.6%	5.9%
Global Equity	-3.6%	2.3%	16.2%	13.7%	12.1%	16.2%
Global Property	-3.8%	4.4%	16.3%	11.9%	10.8%	18.0%
Global Bonds	6.2%	15.9%	21.7%	11.2%	9.3%	10.0%
Global Cash	5.0%	12.8%	14.4%	8.3%	7.5%	8.2%

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Local Review

Equity

The JSE All Share Index delivered a negative return of -9.0%, making February the Index's worst month in 11 years. Resources (-11.6%) bore the brunt of this month's sell-off, while Financials (-9.5%) and Industrials (-7.0%) also struggled. Mondi PLC (0.4%) was the only stock on the JSE Top 40 Index that managed to post a positive return for the month. On average, the companies in the Top 40 Index were 27% below their respective 12-month highs at month end. Our models indicate that there is still reasonable value on offer and we therefore maintain our equity allocations at levels close to benchmark.

Property

The SA Property Index lost a further 15.7% in February, bringing the year-to-date return down to -18.3%. This was the worst monthly performance that the index has experienced since it was introduced in 2004. Due to low property inflation, the sector is likely to remain under pressure. We therefore maintain a neutral ranking on the asset class.

Bonds

The JSE All Bond Index performed relatively well and posted a return of 0.0% this month. Over a 5-year period, the bonds sector has been the best performing local asset class, delivering 7.2% per annum. The benchmark R186 yield increased slightly to 8.1% at month end, and the risk premium component remains close to 15-year highs. The 2020 Budget indicated that the National Treasury will issue bonds more evenly across the yield curve. Our valuation model indicates that bonds are fairly valued, and the high yield in real terms is looking attractive compared to other asset classes.

Cash

Annual inflation increased further to 4.5%, the highest rate since June 2019. This increase was mainly due to higher prices of transport, housing and utilities, alcoholic beverages and tobacco, as well as health. Cash currently delivers a 2.0% real yield. We appreciate the optionality in cash, but recognise that several other asset classes have higher expected real returns at the moment.

Global Review

Currency

The ZAR headed for a near-four-year low in February as the nation continues to experience power outages and weak economic growth. The South African Rand suffers added pressure from concerns over the impending credit downgrade by Moody's rating agency. ZAR closed the month at R 15.66/$ from a starting point of R 15.00/$. At month end, the ZAR was 9% undervalued against the trade weighted basket of currencies on a purchasing power parity basis. Significantly, the ZAR was 33% undervalued versus the USD using the same methodology.

Equity

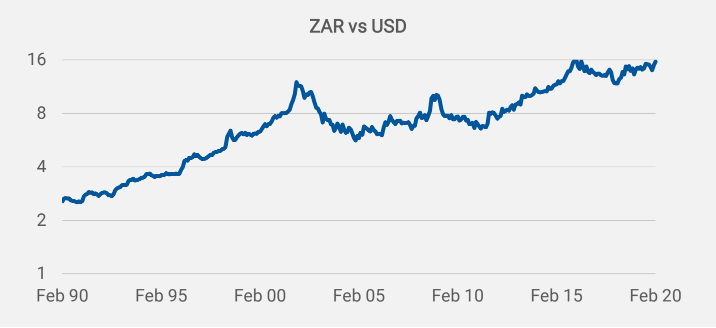
February saw a large global market decline, with the MSCI All Country World Index returning -8.1%. The S&P500 ended the month down 8.2% after it hit an all time high mid-February, making it the fastest correction for the S&P500 on record. Emerging Markets held up relative to developed markets and the MSCI Emerging Markets Index delivered -5.3%. Although global equities remain under heavy selling pressure, the market continues to shift towards more cyclical sectors. We therefore maintain our global equity ranking to overweight, and continue to favour allocation to high quality stocks.

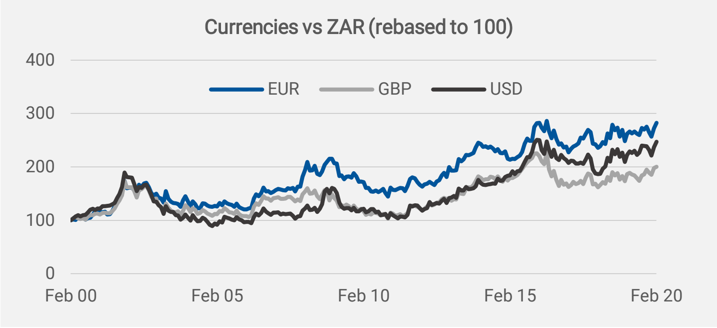
Fixed Income

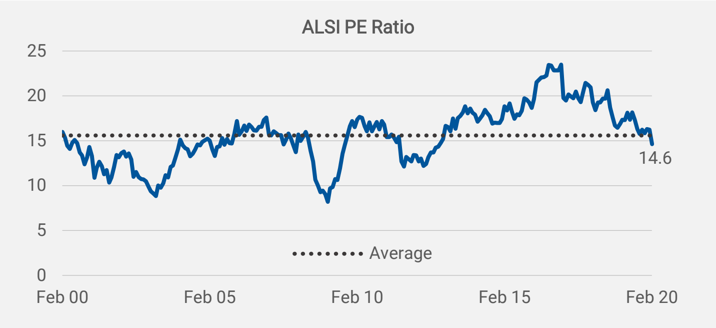
The US 10-year treasury bond yield decreased drastically to 1.2% towards the end of February. This drop in the 10-year yield to a record low is a reflection of global demand for the safety that US sovereign debt offers. BCA Research expects yields to be significantly higher in 12 months, as history shows that Treasury yields jump sharply once viral outbreaks end.

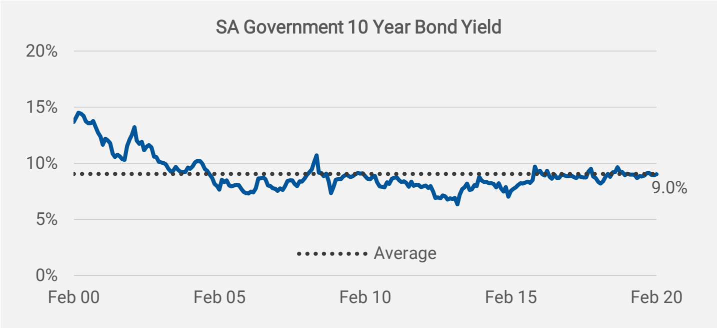
Alternative

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.









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