Sygnals

April 2021

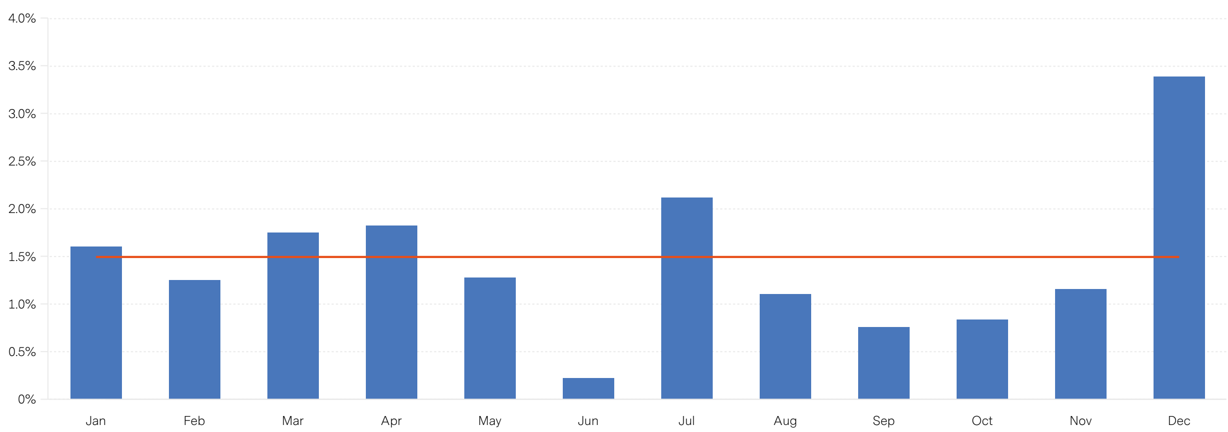
The Monthly Bulletin by Sygnia

Market review

After another solid return in April, should we heed the old adage, “Sell in May and go away”? Believed to be an old English saying, the phrase originally stated: “Sell in May and go away and come on back on St Leger’s Day”. Traders would leave the city of London in the hot summer months and return for the St Leger Derby in mid-September. Today, it is used to refer to the historically weaker performance of equities during the middle of the year.

In South Africa, over the last 60 years, the six months from October to April has shown an average return of 1.8% vs an average return of 1% for the following “wintery” six months. So, while on a relative basis the saying is true, a return of 1% per month is still better than what we have seen in other asset classes. 2021 is likely to experience a slowdown mid-year as the two key drivers of growth rebalance. China is reducing fiscal stimulus to switch the economy to domestic consumption demand and the US is balancing stimulus with additional taxes. While the year should end on a better footing, we anticipate higher volatility over the next six months. Excess money supply has turned down and further market gains require earnings growth to outweigh valuation contraction due to higher interest rates.

Chart 1: SA Equity monthly average returns over 60 years
Source: Bloomberg



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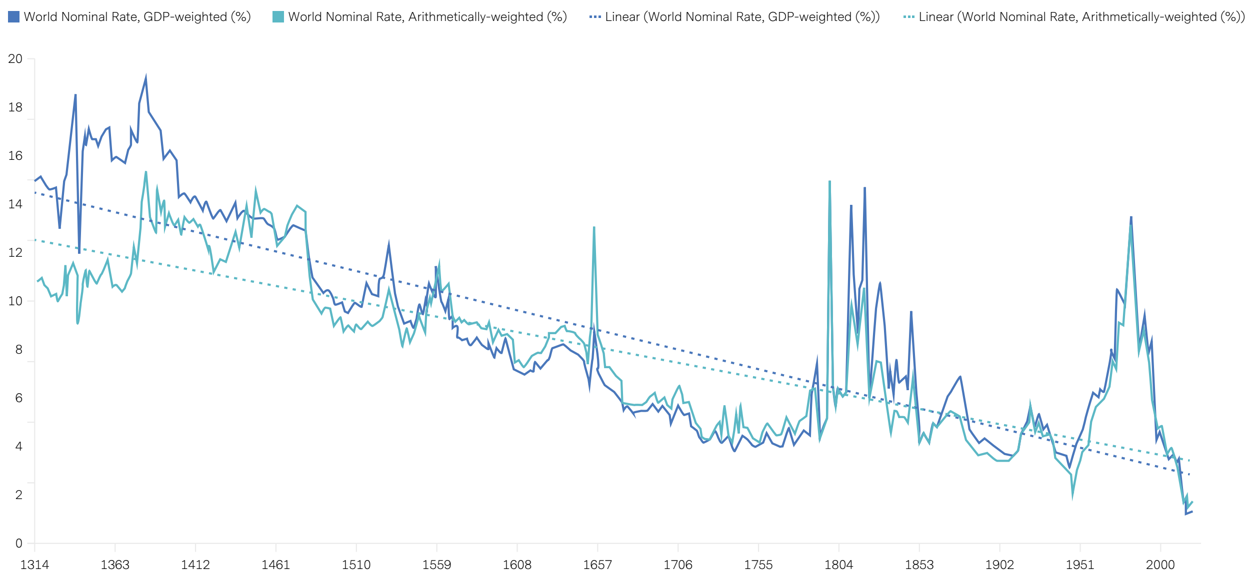
Global – You cannot spend yourself out of low growth

The US government budget deficit for March was $660bn, a record high for the month and three times South Africa's total national debt. With such high levels of additional money being spent and the US likely to keep interest rates artificially low, there is a concern that inflation will spike. It is true that in the short-term inflation will rise, keeping the dollar weak, however, this debt will need to be paid for by higher taxes at some point in the future. You cannot spend yourself out of low growth - Japan is proof of that.

An increase in debt has a diminishing return. In the US, during the Reagan era, GDP increased by 88c for every additional dollar of government debt. It now increases by just 35 cents for every additional dollar of government debt. In Japan, every Yen of debt adds just 20 cents to GDP. This tells us that despite huge amounts of stimulus, in the medium-term growth will remain low, inflation anchored and developed market bonds lower still. The 700-year trend of declining interest rates is unlikely to continue as the zero point offers resistance, but we will stay close to the lows. With record high levels of government debt, the global economy cannot handle much higher interest rates.

Chart 2: Global interest rates at 700-year lows

Source: Goldman Sachs

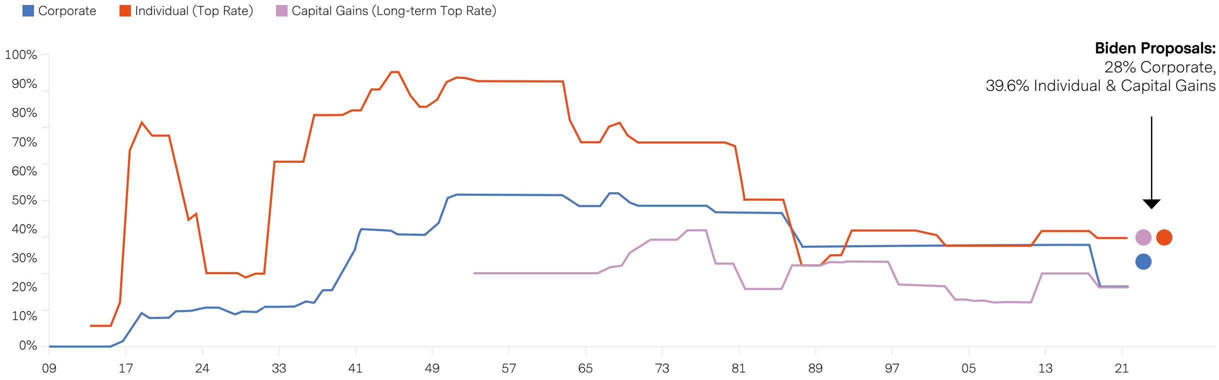


US – More taxes and regulation ahead

President Joe Biden's first 100 days delivered the strongest post-election equity rally in the last 75 years, due to record fiscal stimulus. However, the policies are no longer so clearly positive with tax increases required for $2.25tn infrastructure stimulus. Next year's US earnings are likely to be lower despite the fiscal stimulus as higher taxes take effect. Joe is now proposing doubling the capital gains tax rate for wealthy individuals to 39.6% to help pay for the $1.8tn American Families Plan, a raft of social spending to address inequality. We're also likely to see increased regulations going forward. Apple and Google's parent Alphabet once again faced antitrust scrutiny from lawmakers. Both taxes and regulations will be a headwind for US markets. Fortunately, monetary policy remains supportive. At the recent IMF meeting, chairman of the Fed, Jerome Powell said he is more concerned about rising Covid cases than inflation. And the Fed last week chose to hold interest rates steady, continuing its easy money policy.

Chart 3: Capital gains tax rates reach record highs

Source: JP Morgan



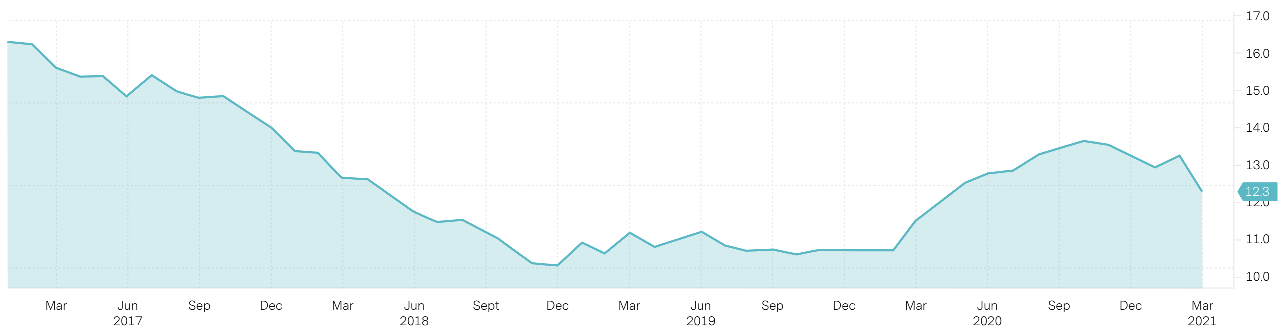
China - Launch of Sygnia Itrix MSCI Emerging Markets 50 ETF

After the successful launch of the Sygnia Itrix S&P Global 1200 ESG ETF, we are excited to be launching the Sygnia Itrix MSCI Emerging Markets 50 ETF on the 14th of May. Emerging markets have struggled over the last decade due to a lower allocation to Tech, a strong US dollar and lack of domestic reforms. China remains the cornerstone of any emerging market (EM) investment. When it comes to domestic reform, the Chinese 14th Five Year Plan (2021-2025) is set to enhance intellectual rights protections, and create a market-oriented, law-based, and internationalised business environment. In addition, government is firmly clamping down on mismanagement of State-Owned-Enterprises (SOEs). The head of China Huarong Asset Management, majority-owned by the Ministry of Finance, was recently found guilty of financial crimes. He was sentenced to a death penalty and executed within weeks.

Tech allocations and US dollar should no longer be headwinds to EM. China is cleaning up its tech sector, imposing wide ranging restrictions on the financial divisions of 13 companies and fining Alibaba $2.8 billion in March for behaving like a monopoly. And China is investing heavily into R&D to ensure it becomes the world's technology leader. However, the slow roll-out of vaccines in emerging markets remains a short-term concern. Once again China leads EM here. Not only is the Covid case load low, but China's growth remains strong. Retail sales beat expectations expanding 34.2%. Total social financing eased further in March, which is a good indicator that the government remains focused on supporting reforms and the new economy at the expense of overall growth and is comfortable to withdraw fixed asset investment support.

Chart 4: China all-system financing aggregate slows in March

Source: Bloomberg



SA – Vaccine rollout halted

Within South Africa we all await a step up and improvement in the reform agenda to boost growth. But it is likely to be a long wait. ANC secretary general Ace Magashule's deadline to step aside from his position in the party has passed and nothing has changed. The latest Ratings Afrika Municipal Financial Sustainability Index (MFSI) shows that municipalities have been collecting only R18 of every R100 invoiced. Allegations of corruption have emerged over the Risk Mitigation Independent Power Producer Programme, with Gwede Mantashe's wife a possible beneficiary of the Karpowership Tender. President Cyril Ramaphosa acknowledged that despite drawing numerous lines in the sand, corruption has not ceased and there are many factions within the ANC, some of which are carrying certain economic interests…

South Africa has restarted the Johnson & Johnson vaccines rollout. As at the 30th of April, only 307 591 vaccines had been administered.

Fortunately, despite itself, South Africa is benefiting from the weak dollar as it drives up commodity prices and luckily has avoided a 3rd wave so far. But reforms are needed to make us competitive even within the EM space.

Key take-aways

After the tumultuous rollercoaster of 2020, the prospect of some volatility in the next six months does not seem quite as daunting as it may have pre-2020. Globally, interest rates are at an all-time low going back 700 years and increases do not appear likely any time soon. In the United States, eyebrows are being raised over Joe's proposal to hike the corporate tax rate from 21% to 28% but corporate tax has previously been higher, climbing to as much as 52.8% in 1968 and 1969. All eyes are set on emerging markets which are set up for a comeback, led by China which has had an impressive recovery in recent months.

To conclude with the words of Warren Buffet: "Look at market fluctuations as your friend rather than your enemy. Profit from folly rather than participate in it."

Key indicators

		1 mo.	*3 mos.*	*6 mos.*	*1 yr.*	*2 yrs.*	*3 yrs.*	*5 yrs.*	*10 yrs.*
J203T	**FTSE/JSE All Share Index**	1.0%	8.6%	31.6%	36.4%	10.3%	8.1%	8.0%	10.7%
J200T	**FTSE/JSE Top 40 Index**	0.6%	8.0%	30.7%	35.1%	11.4%	9.2%	8.8%	10.8%
J210T	**FTSE/JSE Resources 10 Index**	2.9%	16.6%	48.7%	59.8%	27.5%	27.1%	20.8%	5.5%
J211T	**FTSE/JSE Industrials 25 index**	-1.4%	2.2%	18.0%	23.0%	10.1%	6.1%	6.2%	14.4%
J212T	**FTSE/JSE Financials 15 Index**	1.7%	7.3%	33.0%	23.4%	-11.3%	-7.4%	0.0%	8.6%
J403T	**FTSE/JSE SWIX Index**	-0.3%	7.6%	27.1%	32.4%	6.3%	4.8%	5.7%	10.3%
J433T	**FTSE/JSE Capped SWIX Index**	0.8%	10.1%	32.2%	36.2%	5.7%	3.2%	4.2%	-
J303T	**FTSE/JSE CAPI Index**	1.6%	10.0%	34.4%	38.7%	10.4%	7.4%	7.4%	10.6%
J253T	**FTSE/JSE SA Listed Property Index**	11.7%	22.8%	58.7%	40.3%	-12.9%	-11.8%	-7.4%	5.2%
ALBI	**JSE All Bond Composite Index**	1.9%	-0.6%	5.9%	14.7%	7.1%	6.4%	8.7%	8.2%
STeFI	**STeFI Index**	0.3%	0.9%	1.8%	4.3%	5.7%	6.2%	6.7%	6.3%
	MSCI World Index in SA Rands	2.8%	6.9%	15.3%	14.8%	18.9%	20.0%	14.5%	19.0%
	Rand/US Dollar Exchange Rate	-1.8%	-3.6%	-10.7%	-21.0%	0.7%	5.2%	0.4%	8.3%
	Rand/Euro Exchange Rate	0.6%	-4.5%	-7.7%	-13.2%	4.3%	5.1%	1.4%	6.0%
	Headline CPI	0.7%	1.7%	2.1%	3.2%	3.7%	4.0%	4.4%	5.0%
	PPI	1.3%	2.8%	3.4%	5.2%	4.3%	4.9%	4.7%	5.5%