Sygnals

January 2020

Global Outlook

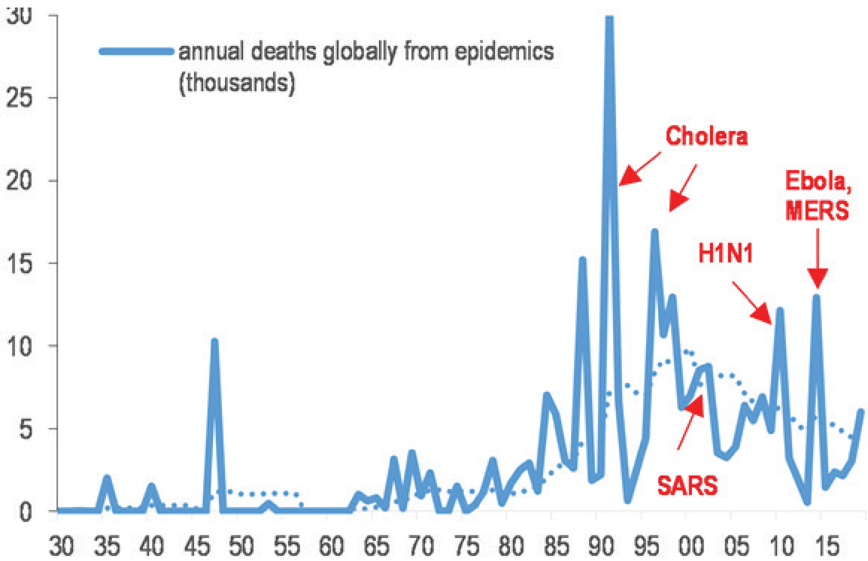
WHO declares global health emergency

January had a strong start thanks to a decent earnings season, improving macro data, a tsunami of liquidity and the signing of the US/China trade deal, which pushed global equities to all-time highs in January. However, the coronavirus brought this cyclical bounce to a sudden end.

Hundreds of people have already died as the coronavirus continues to spread, and the WHO has declared a global health emergency. Working against time, Chinese officials have announced multiple measures to contain the epidemic, which shows no immediate signs of abating. The economic impact is potentially devastating: economists have estimated that the 2003 SARS epidemic was responsible for a 1–2% dent in China's economic growth and a 0.5% dip across southeast Asia.

The big picture: Over the last twenty years, epidemics have been on the decline (see Chart 1), and the effect on markets will likely be limited should the hit to global growth be contained. However, rising daily mortality rate headlines have caused fear-induced knee-jerk reactions, and markets fell during the month, with oil down 17% from its intra-month peak. Longer term, we remain well positioned for cyclical bounce in global growth driven by looser monetary conditions and improved trade conditions. In the short term, we have reduced our EM overweight until further clarity is available.

Chart 1: Annual deaths globally from epidemics (thousands)
Source: JPMorgan



China: Phase one trade deal finally signed

The US and China signed phase one of a trade deal after 18 months of dispute, delivering some certainty to global markets. The agreement eases some sanctions on China and, in return, China has agreed to implement further structural reforms and significantly increase its purchases of US goods and services. The deal also contains stricter rules on intellectual property rights and a requirement for China to not manipulate its currency. Phase two negotiations will begin shortly but are only likely to be signed after the US elections in November of this year.

The big picture: China's economy grew 6.1% last year, its lowest pace of growth in nearly 30 years, but monthly industrial production and fixed asset investment beat market expectations again in December. The signing of the deal, although it does not remove tariffs, will help stimulate Chinese growth and supports the positive emerging market momentum. The coronavirus is likely to dent short-term growth numbers.

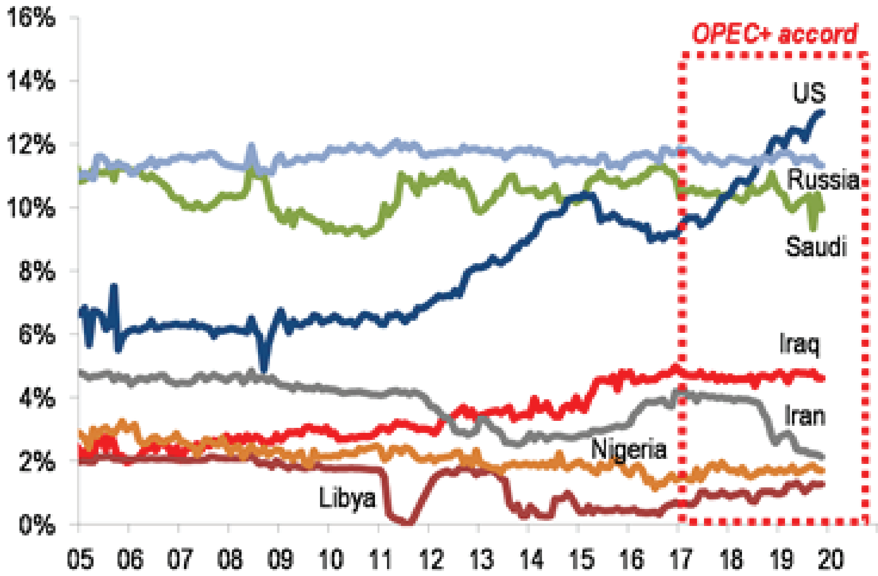
"All is well!"

The remains of a vehicle hit by missiles outside the Baghdad airport. The commander of Iran's powerful Revolutionary Guards Corps, Maj. Gen. Qasem Soleimani, was killed. (Credit: Iraqi Prime Minister Press Office, via Associated Press.)

The assassination of Major General Qasem Soleimani in an American drone strike ratcheted up tensions in a precariously unsettled region of the world. Iran retaliated by firing 22 missiles on two Iraqi bases hosting US troops; fortunately, the strikes resulted in no fatalities, and President Trump indicated that the US would not escalate the conflict further. Trump has backed down for now, but he is well aware that wars win elections: in 2011, he tweeted, "In order to get elected, @BarackObama will start a war with Iran." No wonder that hashtags #wagthedog and #WorldwarIII lit up Twitter after the strike.

The big picture: Judged against oil supply shocks of the past 50 years, the recent action was a non-event. Previous conflicts that cut oil output have generated massive spikes in oil prices, especially the two 1970s oil shocks. The current event resulted in only a 6% rise in crude oil. As a result of diversified production sources and less energy-intensive global demand, oil markets have become far less sensitive to geopolitics. The US is now the world's largest producer, and Iran is barely more significant than Nigeria (see Chart 2).

Chart 2: Global oil producers
Source: JP Morgan



US: Elections take centre stage

The US elections are fast approaching, scheduled for 3 November of this year. In the short term, the Democratic primary elections will be the most relevant for markets, and as the primaries unfold, we will have some indication as to who the Democratic presidential candidate will be. The Iowa vote on 3 February and the New Hampshire vote on 11 February have historically helped to identify the winners. At present, Iowa polls suggest a relatively equal probability for the top four candidates (see Chart 3), while national polls favour Biden and Sanders.

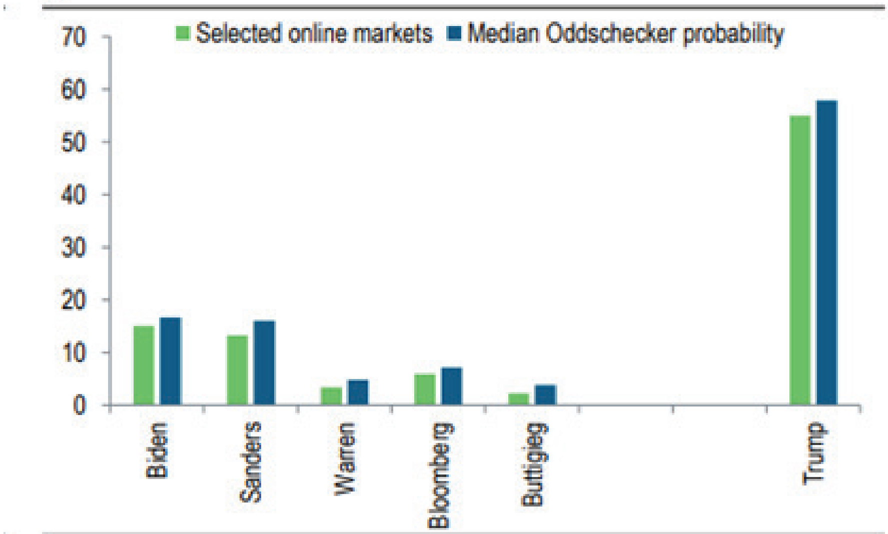
The big picture: Bloomberg and Biden are viewed as the most market friendly among the Democratic candidates. As such, with Biden being a forerunner and Warren's chances fading, US assets are not showing a lot of stress. Should online polls begin to indicate more confidence in Sanders' or Warren's electability, asset markets could show more uncertainty. The probability of Trump being re-elected is rising, but varying probabilities will introduce volatility into the US, particularly the dollar, supporting our view that the dollar bull has ended.

Chart 3: Presidency probabilities from online markets

Source: Standard Chartered Bank

Figure 3: Presidency probabilities from online markets

%



Note: Selected online markets if the probability implied by the bid-ask midpoint of Betfair and Smarkets. The median Oddschecker probability is the probability implied by the median Oddschecker quote.Source: Betfiar, Smarkets, Oddschecker, Standard Chartered Research

UK: The end of the beginning

Prime Minister Boris Johnson's Brexit deal cleared its final hurdles in Parliament, marking the end of the beginning after the country voted to leave the European Union almost four years ago. The EU parliament approved the withdrawal agreement with tears, hugs and a communal singing of Auld Lang Syne. Britain will now enter a transition period, scheduled to last until the end of the year; it will continue to be bound by EU laws until it has negotiated a new trade deal.

The big picture: Pound volatility is likely to remain as the EU and UK debate the trade deal during 2020. We remain with certain hedges on our GBP positions.

Local Outlook

World Bank downgrades SA growth on Eskom risks

Unplanned breakdowns reached almost 16 000 MW in early January, resulting in further unexpected load shedding. The energy disruption caused the World Bank to cut its economic growth forecast for South Africa to 0.9% for 2020. Eskom Chairman Jabu Mabuza fell on his sword after the unexpected breakdowns and resigned from his post. On an unrelated note, Mabuza's name is tied up in a potentially irregular R11 billion boiler maintenance contract.

The big picture: This should make it easier for new CEO Andre de Ruyter (who started on 6 January) to make the sweeping changes needed to improve operations. Improved functionality at Eskom will mean better SA growth and investment confidence.

South African Reserve Bank finally cuts rates

The ANC committed to the independence of the South African Reserve Bank in a policy statement, while also supporting its current mandate. This should allay fears, at least for now, that the party will not pursue its 2017 policy of nationalising the central bank. Inflation rose to 4% year on year but is still below the bank's target of 4.5%. This finally allowed the SARB to unanimously cut the repo rate by 25 bps, and the bank's models forecast another cut later this year. The repo rate dropped to 6.25% and the prime lending rate changed to 9.75%.

The big picture: This will stimulate the residential property market and encourage corporates to invest their growing piles of lazy cash. We believe this is a big positive for South Africa's economy, and we have increased our equity allocation despite the event risk in February. The National Budget presentation on 26 February will give insight into what Moody's is likely to do at the 27 March review.

Naspers starts share buy-back

Naspers announced the sale of around 22m N shares of Prosus, which will increase Prosus' free-float to 27.5%, while Naspers' stake will fall to 72.5%. All of the proceeds received by Naspers will be repatriated to South Africa, and Naspers will use the cash to buy back shares.

The big picture: Given the large 19% weighting of Naspers in the Shareholder Weighted Index (SWIX), this is very positive for the market. The repatriation of the cash proceeds should also prove positive for the ZAR in the short term. Sygnia is a firm believer in the benefits of the SWIX index, although we do actively manage the Naspers risk.

Key indicators

		1 month	3 months	6 months	1 year	2 years	3 years	5 years	10 years
J203T	FTSE/JSE All Share Index	-1.7%	-0.3%	0.5%	7.1%	0.3%	5.3%	5.0%	11.0%
J200T	FTSE/JSE Top 40 Index	-1.4%	0.1%	0.3%	7.9%	0.7%	6.1%	5.2%	10.8%
J210T	FTSE/JSE Resources 10 Index	-3.6%	2.0%	7.8%	17.5%	17.2%	14.6%	6.3%	3.2%
J211T	FTSE/JSE Industrials 25 Index	2.1%	1.7%	-1.7%	12.2%	-3.6%	3.8%	4.1%	15.6%
J212T	FTSE/JSE Financials 15 Index	-5.9%	-6.5%	-4.1%	-11.0%	-3.4%	4.6%	2.5%	11.7%
J403T	FTSE/JSE SWIX Index	-1.8%	0.2%	0.7%	4.1%	-2.3%	3.9%	3.6%	11.2%
J433T	FTSE/JSE Capped SWIX Index	-2.6%	-1.0%	0.5%	1.2%	-3.5%	1.8%	2.3%	-
J303T	FTSE/JSE CAPI Index	-2.0%	-0.9%	0.4%	5.6%	-0.2%	4.2%	4.6%	10.9%
J253T	FTSE/JSE SA Listed Property Index	-3.1%	-4.3%	-5.7%	-9.5%	-9.5%	-5.2%	-0.8%	10.5%
ALBI	JSE All Bond Composite Index	1.2%	3.3%	4.5%	8.5%	8.6%	9.3%	6.7%	9.0%
STeFI	STeFI Index	0.6%	1.7%	3.5%	7.2%	7.3%	7.3%	7.2%	6.5%
	MSCI World Index In SA Rands	6.7%	4.5%	13.0%	33.2%	17.9%	15.6%	14.7%	17.6%
	Rand/US Dollar Exchange Rate	7.3%	-0.6%	4.7%	13.1%	12.4%	3.7%	5.2%	7.0%
	Rand/Euro Exchange Rate	6.0%	-1.2%	4.7%	9.6%	6.1%	4.6%	4.8%	4.7%
	Headline CPI	0.3%	0.4%	1.2%	4.0%	4.3%	4.4%	5.0%	5.1%
	PPI	0.2%	0.2%	0.4%	3.4%	4.3%	4.6%	5.1%	5.9%