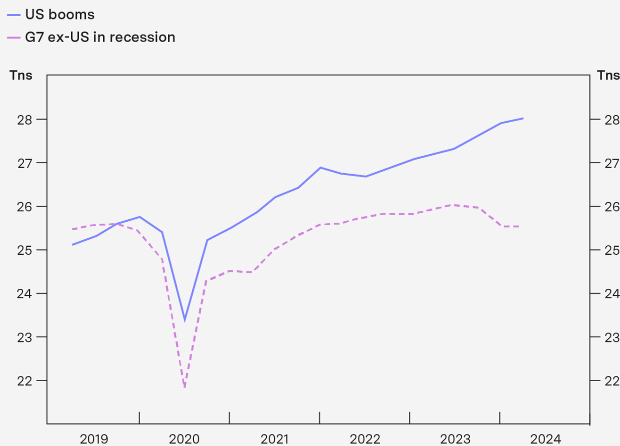
The Monthly Bulletin
SygniaSygnals
June 2024

Chart of the month – Equity bull market continues as central banks begin rate cuts

By Kyle Hulett
Co-Head: Investments

US real GDP has grown as non-US developed economies have stagnated



Source: BCA

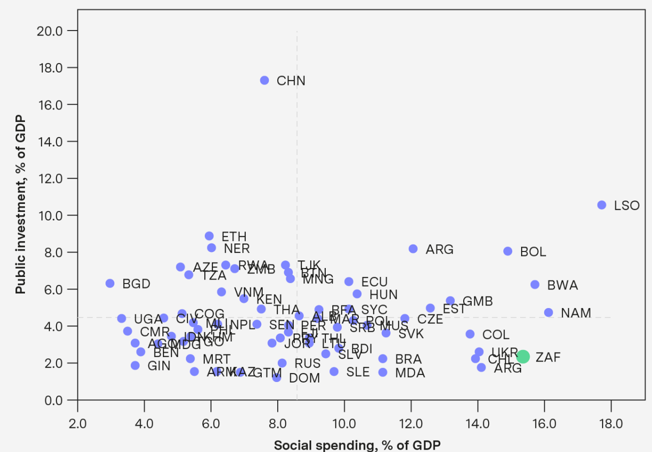
- For the first time in its 128-year history, the Dow Jones Industrial Average rose above 40 000.
- Copper surged to its highest-ever level, rising above $11 000 a ton.
- Markets have been supported by rate cuts in select markets, with Swedish Riksbank joining the Swiss National Bank in cutting its policy rate. Many emerging markets have also cut rates in 2024, including Brazil, Colombia, Mexico, Hungary and the Czech Republic. The European Central Bank and Canada are expected to cut in June, with the US only likely in September.
- The bull market continues despite cooling US economic growth, even as inflation remains sticky.
- Heightened geopolitical risks have also continued: Suez Canal traffic remains 80% below December's volume, and Israel is expanding its military operations against Hamas in the southern Gaza city of Rafah after 1 million civilians evacuated.
- Global growth has been led by the US, which has seen exceptional GDP growth over the last six years, even as the remaining developed economies have stagnated. US growth was initially driven by strong fiscal support while more recently it has been driven by AI investment and higher productivity levels.

Don't spend more – spend better

By Haroon Bhorat
Chair: Investment Committee

While there is significant (and appropriate) concern about government's debt-to-GDP ratios, debt-servicing costs and so on, insufficient attention may be being paid to what government is actually spending on. The graph below compares investment spending against social spending (spending on social grants, education, health and other social services offered by the state) at the cross-country level. The data show that South Africa is an outlier in spending on social services and grants, allocating some 15% of GDP. Our social spending is higher than almost all countries in this sample, with the exception of a few African and Latin American nations. Much more importantly, however, government is also simultaneously a very poor allocator of revenue to investment spending.

Public investment and social spending as % of GDP by country, latest year



Source: World Bank and IMF

The data show that South Africa spends only about 2% of its GDP on those areas of the economy that will ultimately increase – or "crowd in", to use the Keynesian term – private sector investment. Simply put, South Africa's revenue base is disproportionately used to provide social services, including grants, relative to actually kick-starting the economy. Hence, we spend too much on these services instead of, for example, infrastructure needs such as roads, energy, ports, firm investment incentives and the like. The global investment leader is China, which spends the equivalent of 18% of the revenue it raises on public investment, with only 8% used for social services.

One could argue that we should be spending on social services in an unequal society like ours, but our returns are abysmal for spending such a significant quantum on education and health (for example). The World Bank notes that in education, South Africa's "learning

poverty, at 79% in 2016, was still much higher than the average of 29.5% reported by upper middle-income countries." Our much-lauded social assistance programme is actually costlier to implement than that of many other countries, including Brazil and Mexico.

In parallel with this social services spending – 70% or so of which goes to wages – is that our fiscal multiplier is essentially zero. Estimates from the SA Reserve Bank show that, where the fiscal multiplier was 1.5 in 2010, at its latest estimate it is 0 – meaning that for every R1 of fiscal spending, the contribution to GDP to encourage private sector investment and economic growth is essentially zero. Over this same period, government has raised taxes in a supply-constrained economy to finance ongoing consumption-dominant expenditure. This has fuelled rising public debt-to-GDP ratios, which in turn has led to rising risk premiums in bond markets amidst concerns about the fiscal consolidation path.

Ultimately, though, we need a government spending profile more geared to kick-starting economic growth and higher investment levels. This can only happen by increasing the efficiency of social services spending (and in the process spending less) while allocating much higher shares of individual and company tax revenue to investment expenditure that can generate higher levels of economic growth – supply-side economics of a good type.

Top-performing Sygnia funds

By Phumlile Smith
Head: Manager Research

1-month absolute performance

Rank	1 month	Return
1	Sygnia Itrix FANG.AI Actively Managed ETF	6.7%
2	Sygnia 4th Industrial Revolution Global Equity Fund	4.6%
3	Sygnia Itrix S&P 500 ETF	4.1%
4	Sygnia Transnational Equities Fund	3.3%
5	Sygnia Itrix MSCI US ETF	2.8%

FANG stocks dominated again after excellent results from Nvidia buoyed the sector. This lifted the US market, with US-based funds in four of the five top spots. The Sygnia Transnational Equities Fund is the only South African fund in the top five this month.

12-month absolute performance

Rank	12 month	Return
1	Sygnia FANG.AI Equity Fund	35.9%
2	Sygnia Itrix S&P 500 ETF	20.5%
3	Sygnia Life Berkshire Hathaway Portfolio	19.1%
4	Sygnia Itrix MSCI US ETF	18.6%
5	Sygnia Listed Property Index Fund	18.4%

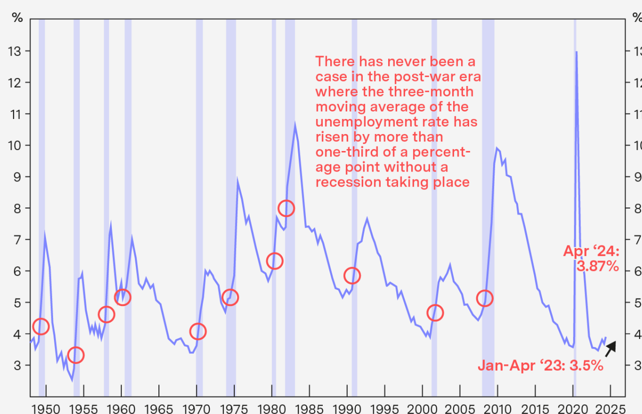
There is little change over the one-year period, with FANG and US exceptionalism driving returns. However, the SA property sector popped up to fifth place as it recovered from record lows.

US growth – Economy is cooling, commercial real estate risks rise, but AI support remains strong

By Steven Empedocles
Head: Indexation

April's core consumer price index (CPI) fell to 3.6% year on year, in line with expectations. This soothed some concerns about reaccelerating price pressures, but one data point does not change monetary policy. Federal Reserve Chair Jerome Powell said it will likely take more time than previously thought to attain the confidence needed to lower interest rates. "We did not expect this to be a smooth road," said Powell.

US unemployment flirting with recession-inducing levels



* As shown as a 3-month moving average.
Note: Shaded areas denote NBER-designated recessions; Circles in the chart denote the times when the 3-month moving average of the unemployment rate increased by more than one-third of a percentage point from prior lows.Source: BCA

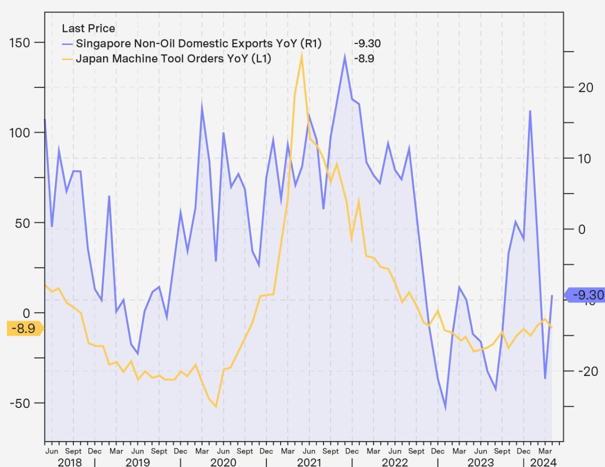
The US economy appears to be slowing, with a number of disappointing economic updates: US retail sales fell below expectation, contracting -0.3%, down from 1.1%, as US consumers finally ran out of excess pandemic savings and started tightening their belts on discretionary items and spent on necessities instead. US industrial production also stalled in April, and the new orders component for both PMI and ISM surveys continues to point to slower growth. The commercial real estate sector could pose further risk: for the first time since the Great Financial Crisis, investors in the AAA portion of commercial real estate debt experienced 25% losses, and lower-ranking creditors were wiped out. A slowing economy could put further pressure on US unemployment, which is on the cusp of a recession. In the post-war era, the three-month moving average of the unemployment rate has never increased by more than a third of a percentage point from its cycle low without a recession following. More importantly, the rise in the unemployment rate has typically been swift and sharp once this threshold has been breached.

However, Nvidia's earnings beat expectations again, and AI continues to fuel the S&P 500 rally. In fact, due to higher productivity most likely a result of AI integration in a number of sectors, unit labour costs in the US are below the Fed's 2% inflation target. US non-financial-sector productivity is rising at a 3.5% annual rate. Where the rise of the internet lifted US labour productivity by about 1–1.3% per year from the late 1990s to the early 2000s, AI could do the same for the coming years.

Rest of world growth – Synchronised global rebound may be stalling

By Bashaarit Khan
Portfolio Analyst

Some indicators suggest a synchronised growth rebound is stalling



Source: Bloomberg

The global growth revival continued in April. The JPM Global Manufacturing PMI came in at 50.3, marking its third consecutive month of expansion, while investor and business sentiment continued to improve in the eurozone. The ZEW Expectations series for the eurozone (+3.1 to 47 in May) strengthened to 27-month highs. However, global growth will have to strengthen more meaningfully for eurozone and Japanese equities to outperform US equities for more than a tactical timeframe. Some forward indicators are starting to show a slowdown in the global recovery. Total Singaporean non-oil exports to the US and Europe are contracting, and exports to China are rolling over. The Japanese economy is also highly exposed to the global manufacturing cycle, and its preliminary release of April machine tool orders contracted sharply.

China – Housing stimulus ramps but so do tariffs

By Wessel Brand
Head: Thematic

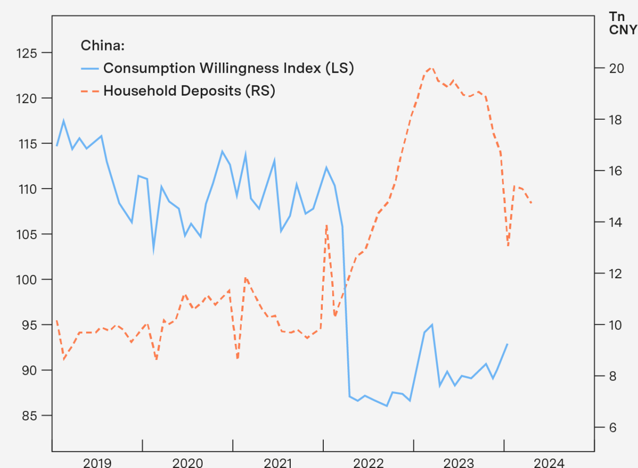
US President Joe Biden unveiled sweeping tariff hikes on a range of Chinese imports, targeting semiconductors, batteries, solar cells and critical minerals. The electric vehicle (EV) tariff was quadrupled to 100%, but this is likely to have little impact, as the US accounts for less than 2% of China's EV, integrated circuit and solar cell exports. China has retaliated in the chip war and created a $47.5bn chip fund to back the nation's chip firms.

The larger issue is that China produces 30% of the world's goods but consumes only 15%, so domestic Chinese consumer confidence is vital to a sustainable recovery. Consumer demand in China remains sluggish due to the property downturn. Unsold housing inventory is at an eight-year high, and with construction work halted and developers defaulting, about 5 million people are at risk of unemployment or reduced incomes. After April's home prices saw their biggest fall in a decade, Xi Jinping's government announced a multi-pronged approach in its most forceful attempt to rescue the Chinese property market:

- Demand support: The People's Bank of China removed the minimum mortgage rate and lowered the minimum down-payment ratio for first-time buyers to 15%, and to 25% for second homes. This is a record low, lower even than in the aftermath of the Asian Crisis in the 1990s and the Great Financial Crisis in the 2000s.
- Supply correction: Beijing is urging local governments to buy unsold homes from developers at reasonable prices and turn them into affordable housing. CNY300bn ($42bn) of central bank funding has been set aside to help government-backed firms buy excess inventory from developers. Beijing is also encouraging local governments to dispose of idle land stock to developers.

The plan will help mop up excess unsold homes, give developers revenue and provide affordable housing. At CNY300bn, the numbers are not big enough yet, but Beijing is hoping it can catalyse the property market and that consumers will deploy their excess savings. Bloomberg estimates that government expenditure of CNY1tn (more than three times than has been announced so far) in the second half of 2024 would boost growth by 0.28 percentage points (ppt) for 2024 and by 0.35 ppt for 2025, lifting 2024 growth to around 5%. For now, then, the plan is not a game changer – but it has the potential to become one.

China's consumer confidence remains depressed



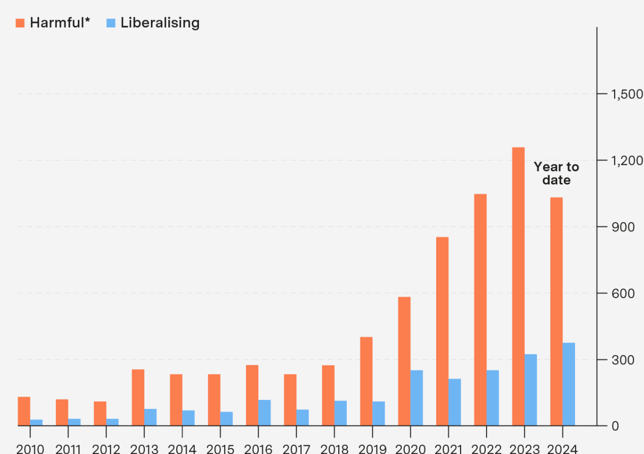
Source: Alpine Macro

> "Beijing is urging local governments to buy unsold homes from developers at reasonable prices and turn them into affordable housing. CNY300bn ($42bn) of central bank funding has been set aside to help government-backed firms buy excess inventory from developers."

Outlook

By Iain Anderson
Co-Head: Investments

- We are in a seasonally tricky time of year, with a challenging combination of higher inflation and slowing US growth.
- Geopolitical risks remain elevated and the global election cycle is just warming up, with 60 of 77 elections still to come across key geographies, including the US, UK, India, Mexico and South Africa. We expect further sabre rattling ahead of these elections. The world's three dominant economies have entered a combative phase that threatens to challenge decades of free-market and global trade. The death of Iran's president could also see a radical shift in Iran. South Africa's election results are in; with just 58.6% voter turnout, it marked the lowest turnout in 30 years. The ANC lost it's majority, dropping from 57.5% to 40.2%, with the MKP the standout winner, going from nowhere to 14.6%. The DA increased from 20.8% to 21.8% and the EFF fell from 10.8% to 9.5%. We now wait for the final coalition parties to form. The first sitting of the National Assembly must be held within 14 days of the announcement of the election results.
- While there are some signs that the global synchronised recovery is slowing, onshoring, friend-shoring and de-risking will all lead to a sustained rise in capital investment in the manufacturing sector. Industrial metals – usually the first to sniff out a recession – peak on average 12 months ahead of a recession (according to research by BCA), and copper is not slowing down. However, future price performance is likely to be tempered by a strong dollar as the rest of the world cuts rates ahead of the US.
- The combination of rising productivity growth and a lack of domestic demand in China is indicative of sustained global goods deflation, which is good for global inflation.
- For now, given the strong AI investment in the US and high levels of productivity growth, we maintain our overweight equity and overweight US positioning.



Note: *Including tariffs and subsidies
Source: Bloomberg

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%	7.3%	3.6%	6.3%	7.4%	8.6%	10.7%	8.0%
J200T	FTSE/JSE Top 40 Index	0.9%	8.1%	3.1%	4.5%	7.8%	8.8%	11.2%	8.2%
J210T	FTSE/JSE Resources 10 Index	0.3%	23.9%	6.8%	-5.9%	-6.6%	2.2%	12.6%	5.5%
J211T	FTSE/JSE Industrials 25 index	1.7%	6.1%	4.6%	6.5%	19.5%	9.5%	11.3%	8.5%
J212T	FTSE/JSE Financials 15 Index	-0.4%	-1.3%	0.3%	21.1%	4.3%	12.7%	4.6%	6.4%
J403T	FTSE/JSE SWIX Index	1.0%	6.9%	4.3%	9.7%	5.5%	6.3%	7.8%	6.6%
J433T	FTSE/JSE Capped SWIX Index	0.9%	6.9%	4.4%	9.7%	5.3%	7.5%	8.5%	6.4%
J303T	FTSE/JSE CAPI Index	0.9%	7.2%	3.7%	7.1%	6.9%	8.8%	10.9%	8.0%
J253T	FTSE/JSE SA Listed Property Index	0.2%	-1.4%	13.6%	20.3%	8.4%	10.7%	0.2%	3.0%
ALBI	JSE All Bond Composite Index	0.8%	0.2%	1.8%	13.0%	6.5%	6.2%	7.2%	7.8%
STeFI	STeFI Index	0.7%	2.1%	4.2%	8.5%	7.5%	6.3%	6.0%	6.5%
	MSCI World Index in SA rands	4.4%	1.9%	14.5%	19.0%	24.3%	18.6%	18.7%	15.6%
	Rand/US dollar exchange rate	0.0%	-1.9%	-0.6%	-5.0%	9.9%	11.1%	5.2%	5.9%
	Rand/euro exchange rate	1.5%	-1.5%	-1.1%	-3.3%	10.6%	6.8%	4.6%	3.6%
	Rand/pound exchange rate	1.6%	-1.2%	-0.1%	-2.4%	10.5%	7.1%	5.4%	3.1%
	Headline CPI	0.3%	2.0%	2.0%	5.2%	6.0%	6.0%	5.1%	5.0%
	PPI	0.5%	2.1%	1.0%	5.1%	6.8%	8.9%	6.9%	6.0%