August 2021

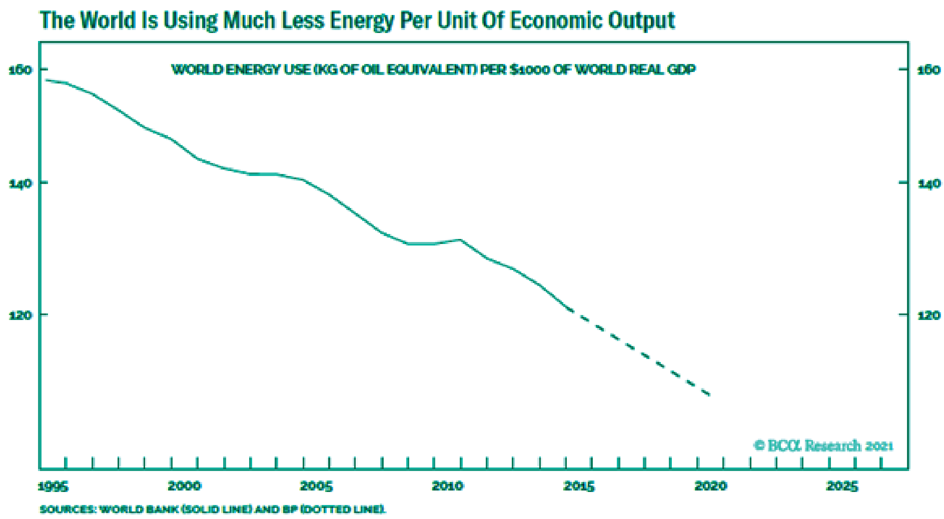
Sygnals

The Monthly Bulletin by Sygnia

Market update

The United Nations Secretary General António Guterres has just proclaimed a "code red for humanity." A landmark climate change report from the UN's Intergovernmental Panel on Climate Change (IPCC) warns that Earth will warm by 1.5°C without drastic large-scale emissions reductions. The past decade was hotter than any period in the last 125 000 years, and carbon dioxide (CO_2) levels are at their highest in two million years. Achieving viable targets requires the whole world to be at net-zero by 2050, and the UN warns that its findings should be a "death knell for coal and fossil fuels". Coal-fired power stations contribute to global warming through CO_2 emissions, but they also produce sulphates, which (while poisonous) the IPCC estimates actually reduce global warming by up to 0.5°C. While the transition to green power is a must, the real win is in reducing overall energy intensity. World energy usage per unit of GDP has consistently fallen over the last 25 years and is forecast to continue falling.

Chart 1: The world reduces energy use.
Source: BCA



Covid-19

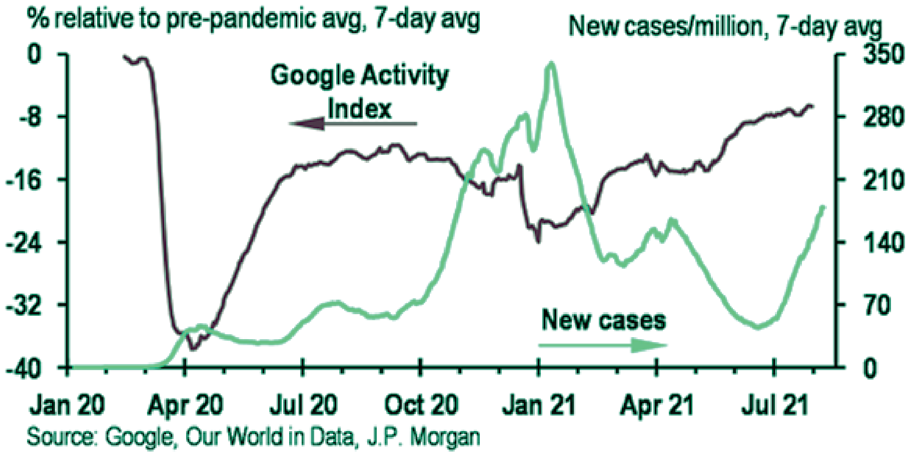
Vaccination take-up in SA seemed to briefly stall but was boosted when the roll-out was extended to adults over 18, with vaccination numbers surpassing 12 million in August.

The Delta variant continues to wreak havoc, with numbers rising significantly in the United States. According to Johns Hopkins University data, the US has had nearly 38 million confirmed Covid-19 cases and more than 629 800 deaths.

The Delta variant has breached New Zealand, breaking its record of being Covid-free and pushing positive cases to more than 100 within seven days. The outbreak prompted a three-day lockdown, which was extended by a further three days. Auckland, which is considered to be the epicentre of the outbreak, will have restrictions in place until at least the end of August.

Despite the delta variant, global mobility has continued to increase as vaccines have assisted developed countries, and governments have learned how to better handle lockdowns. This confirms our view that growth will continue to recover over the next six to twelve months, albeit at a slower rate than before, while the US labour market recovery will drive bond yields up.

Chart 2: Global mobility increases despite third wave.
Source: JP Morgan



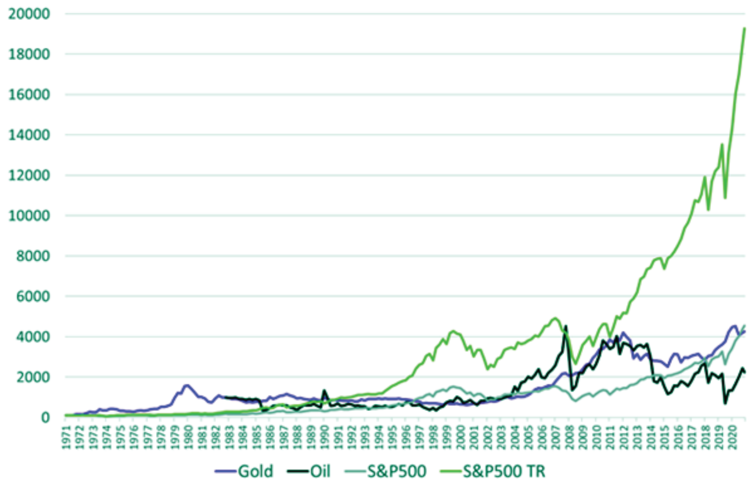
US withdraws from Afghanistan, minor impact on gold

The Taliban took control of Afghanistan in less than 10 days, two decades (and $2 trillion) after they were removed by the US military under President George Bush. The speed of the Afghan government's collapse shocked NATO's allies and prompted condemnation of the US. This is unlikely to hurt President Joe Biden's popularity, however, as Americans have shown little support for the war in the Middle East. The move is part of Biden's larger strategic focus away from the Middle East and towards Russia and China. US-Iran negotiations are key to this move, making a nuclear deal negotiation between the US and Iran more likely. In the near-term, expect heightened volatility on crude oil. Barring a low-probability shutdown of the Strait of Hormuz, the impact is likely to be transitory given the large amount of spare capacity among OPEC 2.0 producers. Brent actually fell in August, but this was related to concerns about the Fed tapering too soon and slowing Chinese growth.

Gold had its "golden" anniversary this month: fifty years ago, President Richard Nixon declared that the US government would no longer convert dollars into the precious metal at $35 an ounce, effectively ending the gold standard. It certainly proved its worth as a real asset, keeping up with the S&P 500 price return index and nearly doubling the price of oil. However, it has severely lagged behind equity returns when dividends are included.

Gold struggled this year despite a weaker dollar and did not bounce on any safe haven demand with the geopolitical risk in the Middle East. In fact, gold does not protect when the going gets really tough, as it is used as a source of liquidity and is sold. We are firm in our belief that tapering QE will be negative for US bonds and the gold price.

Chart 3: Gold retains value in real terms but underperforms without a yield.
Source: Bloomberg



China slows and heralds more regulations

China's economy experienced broad-based weakness in July, with retail sales, industrial production and fixed-asset investment data for July disappointing. China's All System Financing Aggregate fell 71% in July to 1 060 billion yen on the back of new Covid restrictions, severe flooding in central China, de-carbonisation efforts restraining production and global supply chain disruptions, and commodity prices weakened as expected. However, these impacts are mostly transitory, and the government is likely to continue to ease financing requirements to encourage a growth shift to the domestic economy.

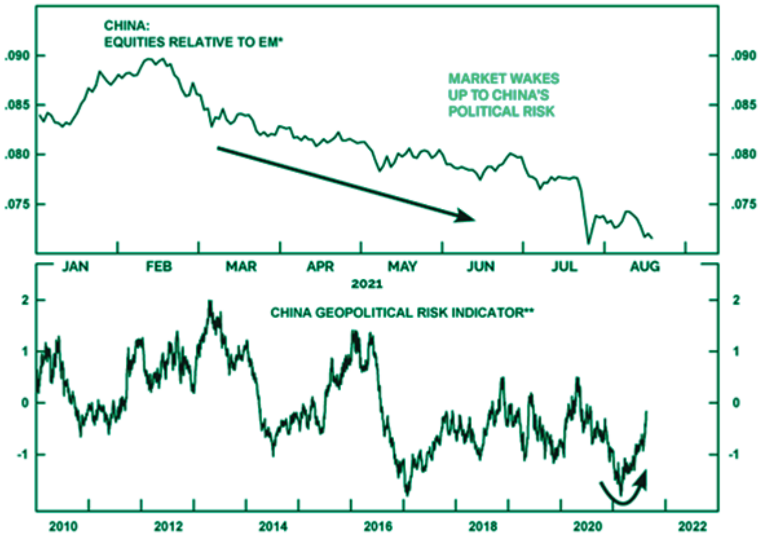
President Xi Jinping laid out a long-term plan for "common prosperity" designed to grow the size and wellbeing of the middle class by 2048, so there is time to transition smoothly. China's State Council and the Communist Party's Central Committee jointly released a five-year blueprint calling for greater regulation; authorities will work on legislation in areas including national security, technology and monopolies. China later passed legislation setting out tougher rules for how companies handle user data, pushing the campaign forward to curb big tech's influence via the Personal Information Protection Law.

China is studying separate proposals to further ensure the rights of drivers who work for online companies and to step up oversight of the live-streaming industry, and the market regulator issued draft rules banning unfair competition among online platform operators. Chinese regulators are also seeking to implement rules that impact the algorithms that technology companies use, forbidding practices that "encourage addiction or high consumption" and any activities that endanger national security or disrupt social and economic order.

To this end, China has further tightened regulations around online gaming service use by teenagers, limiting online game play to three hours a week. China is oversold, and Beijing cannot afford to self-inflict an economic collapse. Monetary and fiscal policy will support the economy over the next 12 months, but we expect volatility to continue in the short term.

Chart 4: China has continued to slow alongside increased regulation.

Source: BCA



South African cabinet reshuffled during worst load shedding year in history

President Cyril Ramaphosa's cabinet reshuffle raised several questions. Given his strong reformist credentials, foreign investors were surprised and disappointed to see Finance Minister Tito Mboweni exit, and the rand sold off on the news. His replacement, Enoch Godongwana, is regarded as a centrist and will hopefully continue Mboweni's conservative path. The upcoming MTBPS will provide some insight, but rising commodity prices mean that Treasury can accommodate some expense overruns this year. The wage deal, which coincidentally runs until shortly after the upcoming elections, will see government employees receive a 1.5% salary increase and a monthly cash "bonus" amounting to between R14 640 and R20 340 per year. The move will increase South Africa's spending on public servant salaries from the already astronomical R650 billion budgeted in February to a new record high of R668 billion. Hopefully this direct reversal of Mboweni's stance on freezing public sector salaries is not a portent of things to come. Calls to transform social welfare grants into a more permanent Basic Income Grant will need to be watched closely from an affordability perspective.

The reshuffle seems to consolidate Ramaphosa's position within the ruling ANC, which will hopefully allow for faster reform implementation. Ramaphosa returned to the State Capture commission to answer for inaction dealing with corruption within the ANC – records from the party's national disciplinary committee dating from 2014 to 2021 reveal a disturbing lack of decisive discipline related to corruption charges.

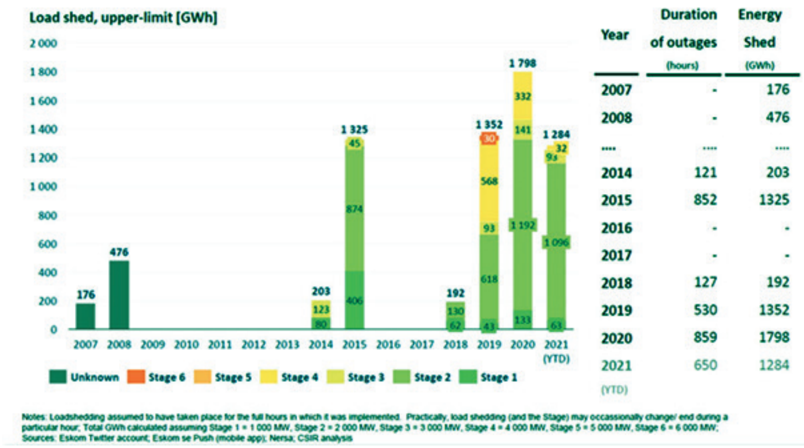
2021 is looking increasingly like it will be the worst load shedding year to date unless Eskom is able to drastically reduce unplanned rolling blackouts in the second half of the year. South Africa experienced 650 hours of load shedding in the first half of 2021 (15% of the time). Happily, the Department of Mineral Resources and Energy has gazetted Schedule 2 of the Electricity Regulation Act, which will enable private entities to generate up to 100 MW of "distributed" or self-generated electricity without a licence.

South Africa's unemployment rate rose to 34.4% – officially the highest in the world – despite GDP being revised 11% higher by Stats SA. The revision had the welcome effect of lowering the debt-to-GDP ratio, but the increase was all on the consumption side, actually lowering potential growth. Reforms are needed more urgently than ever.

The Prosus/Naspers share swap went through and will have the unfortunate consequence of decreasing the weight of South Africa in global EM indices by around 0.5%, to around 3.4%. Foreigners are already boycotting SA due to the lack of reforms, and a reduced weight will make it easier to ignore South Africa. The FTSE/JSE lowered the cap on capped indices from 10% to 6%, but this is selective and temporary and will lead to further unnecessary trading costs. We continue to prefer the uncapped indices.

Chart 5: 2021 on track to be the worst year of load shedding ever.

Source: CSIR



Key indicators

		1 mo.	3 mos.	6 mos.	1 yr.	2 yrs.	3 yrs.	5 yrs.	10 yrs.
J203T	**FTSE/JSE All Share Index**	-1.7%	-0.1%	4.0%	25.2%	14.0%	8.2%	8.3%	11.4%
J200T	**FTSE/JSE Top 40 Index**	-2.4%	-0.6%	2.5%	22.6%	14.8%	8.5%	8.9%	11.5%
J210T	**FTSE/JSE Resources 10 Index**	-4.9%	-0.6%	2.2%	25.3%	28.0%	20.1%	21.0%	6.6%
J211T	**FTSE/JSE Industrials 25 index**	-5.2%	-3.7%	-2.6%	13.2%	10.4%	5.4%	5.0%	14.1%
J212T	**FTSE/JSE Financials 15 Index**	12.4%	8.0%	21.2%	52.2%	2.3%	-1.0%	4.4%	10.8%
J403T	**FTSE/JSE SWIX Index**	0.4%	-0.9%	3.3%	22.6%	10.6%	5.3%	5.5%	10.7%
J433T	**FTSE/JSE Capped SWIX Index**	2.0%	1.5%	9.2%	30.8%	12.4%	5.5%	5.1%	10.4%
J303T	**FTSE/JSE CAPI Index**	-0.9%	1.1%	7.5%	29.9%	15.3%	8.5%	8.3%	11.5%
J253T	**FTSE/JSE SA Listed Property Index**	7.5%	10.4%	21.2%	51.0%	-8.2%	-7.3%	-5.3%	5.3%
ALBI	**JSE All Bond Composite Index**	1.7%	3.7%	6.8%	14.8%	9.4%	10.0%	9.6%	8.3%
STeFI	**STeFI Index**	0.3%	0.9%	1.9%	3.8%	5.1%	5.8%	6.5%	6.2%
	MSCI World Index in SA Rands	1.3%	11.6%	10.9%	10.8%	19.9%	14.3%	14.5%	20.6%
	Rand/US Dollar Exchange Rate	-1.1%	5.4%	-4.5%	-14.6%	-2.6%	-0.6%	-0.3%	7.5%
	Rand/Euro Exchange Rate	-1.6%	1.8%	-7.1%	-15.7%	1.0%	0.0%	0.8%	5.4%
	Rand/Pound Exchange Rate	-2.1%	2.1%	-6.0%	-12.2%	3.6%	1.5%	0.6%	5.8%
	Headline CPI	1.1%	1.4%	3.5%	4.6%	3.9%	3.9%	4.3%	5.0%
	PPI	0.7%	1.8%	4.6%	7.1%	4.5%	4.6%	4.7%	4.9%