SYGNALS

APRIL 2015

KEY INDICATORS

		1 MONTH	3 MONTHS	6 MONTHS	1 YEAR	2 YEARS	3 YEARS	5 YEARS
J203T	FTSE/JSE All Share Index	4.7%	7.5%	11.2%	14.8%	22.2%	20.1%	17.2%
J200T	FTSE/JSE Top 40 Index	5.2%	8.3%	10.3%	13.3%	22.5%	20.2%	16.8%
J210T	FTSE/JSE Resources 20 Index	7.9%	7.2%	-4.3%	-20.2%	4.3%	-0.8%	0.2%
J211T	FTSE/JSE Industrials 25 index	4.3%	7.2%	14.0%	26.7%	29.6%	31.3%	28.2%
J212T	FTSE/JSE Financials 15 Index	4.9%	10.9%	19.7%	33.4%	29.8%	28.3%	22.1%
J403T	FTSE/JSE SWIX Index	4.3%	7.2%	12.5%	21.0%	24.7%	22.0%	19.0%
J303T	FTSE/JSE CAPI Index	4.7%	7.5%	11.3%	15.0%	22.2%	20.2%	17.4%
J253T	SA Listed Property Index	0.0%	5.9%	18.3%	38.3%	15.4%	24.2%	21.8%
ALBI	BEASSA All Bond Index	-0.5%	-3.8%	3.3%	11.5%	4.0%	8.1%	9.3%
STeFI	STeFI Index	0.5%	1.5%	3.1%	6.2%	5.7%	5.6%	5.8%
	MSCI World Index in SA Rands	-0.5%	8.2%	12.5%	20.5%	28.3%	30.4%	21.4%
	Rand/US Dollar Exchange Rate	-2.8%	1.4%	7.0%	12.2%	14.6%	14.9%	9.8%
	Rand/Euro Exchange Rate	-0.2%	-0.2%	-5.1%	-10.1%	5.3%	8.4%	6.0%
	Headline CPI	1.4%	1.9%	1.9%	4.0%	5.0%	5.3%	5.2%
	PPI	1.8%	1.0%	1.0%	3.1%	5.6%	5.6%	6.4%

"He will have to stop implementing all the sanctions. The responsibility of bringing that into line falls on the shoulders of the President of the United States. However he does it, that's his problem. The resolution will endorse the agreement, will terminate all previous resolutions including all sanctions, will set in place the termination of EU sanctions and the cessation of applications of all US sanctions."

Iranian Foreign Minister Mohammad Javad Zarif, press conference, New York, April 2015

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SYGNIA THE SUM OF ALL THINGS

MARKET OVERVIEW

Market volatility continued throughout the month of April as concerns about Greece's debt situation competed with speculation about the timing of the US Federal Reserve's interest rate increase. The ECB's quantitative easing programme has taken its toll on bond yields across the eurozone. On the economic front, the US alternated between positive and negative data releases, while China continued to slow down.

After a weak start global stock markets rallied after the release of poor US employment numbers which strengthened expectations that US interest rates will remain lower for longer. The ADP National Employment report data showed that only 189 000 jobs were created in March, the weakest level since January 2014. The unemployment rate held steady at 5.5%. Further supporting the expectations was the news that the US economy slowed to a seasonally adjusted annualised 0.2% quarter-on-quarter in the first quarter, weighed down by weaker trade performance, falling business investment and cautious consumers. Although the economy bounced back after a similar slowdown in the first quarter of 2014, the economy is facing more serious headwinds, including the sharp decline in energy prices which is stalling capital investment, a strong US dollar weighing on exports and weakness in the global economy, particularly in China.

The US Fed expects that the US economy will grow at a "moderate pace" despite the weak first quarter, keeping its options open as to the timing of its first interest rate hike. It attributed the slowdown in the first quarter to transitory factors. The ISM manufacturing PMI came in flat for April.

Eurozone economic data, on the other hand, surprised on the upside, driven by the ECB's €1 trillion QE programme and a weak euro. The IMF raised its growth forecast for the region to 1.5% for 2015.

The eurozone is living through a period of record low bond yields as the effects of the ECB's QE takes hold. Germany, France and Italy, in particular, saw strong bond yield compression as the ECB focused their bond buying programme on the safer assets. Sentiment was further boosted after Greece managed to make a key €450m repayment to the IMF and the ECB raised its cap on the emergency liquidity assistance available to Greek banks. Greek banks are totally dependent on the ECB for financing, but the eurozone's central bank no longer accepts Greek sovereign bonds as collateral for loans. Greece's creditors, however, continued to refuse to release a €7.2 billion tranche of bail-out aid until Greece has come up with an acceptable package of domestic economic reforms.

After growing at just 7% year-on-year in the first quarter of the year, its slowest rate of expansion since the depths of the financial crisis, China's economy continued to show signs of weakness in April. Although the official manufacturing PMI came in at 50.1 in March, industrial production and retail sales registered the slowest pace of growth in a decade, while inflation remained at a tepid 1.4% year-on-year, showing little sign that Beijing's recent easing measures have cut deflationary pressures. Poor exports, down 14.6% year-on-year, and weak imports, which fell 12.3% after a 20.5% fall the month before, dragged resource prices down even further.

In response, the People's Bank of China lowered lenders' reserve requirements by the most since the global financial crisis, adding to a reduction in February and two interest-rate cuts since November.

The economic weakness was not reflected in the Chinese stock market which continued to power ahead, reaching a seven year high in April.

Investors continued to bail out of commodity ETFs at the fastest pace on record, and the exodus shows no signs of stopping, as Goldman Sachs predicts a further 20% drop for commodities, already near a 13-year low.

Iron ore prices fell to 2005 levels, before recovering somewhat at month-end, as low-cost supplies from Australia and Brazil swamped the global market, spurring a glut as demand from China slows.

Despite a fairly good April, gold ended the month below the US$1 200 an ounce level as US jobless claims data came in far below expectations pointing to some economic strength.

The oil price staged a modest rally on the back of concerns about unrest in Yemen, expectations of delays in Iranian oil coming back online and the slowdown in US drilling. The seaways around Yemen are some of the most important for the international oil trade with access points to the Red Sea, the Suez Canal and the Gulf. However, a larger than expected surge in US crude stockpiles and Saudi Arabia's production levels reaching record highs kept a lid on prices.

360 DEGREES ROUND THE WORLD

UNITED KINGDOM: Economic growth slowed to its weakest pace in three years in Q1, coming in at 0.3%, half of what it was in the last three months of 2014. The news came at a time when the country is gearing towards the 7th of May general elections which are shaping up to be the most uncertain in decades. It is feared that a possible coalition between Labour and the Scottish National Party may undo much of the economic progress made to date.

GERMANY: Chancellor Angela Merkel indicated that Germany will not divert from its recipe of tighter budgets and economic overhauls in efforts to pull the eurozone out of its malaise. Without mentioning Greece, Merkel lauded euro members including Spain and Portugal for carrying out such measures in return for European bail-out financing. She called Ireland "the growth engine of Europe."

SPAIN: Spain has joined the sub-zero debt club after the Treasury issued €725 million in six-month debt yielding -0.002%. According to Prime Minister Mariano Rajoy, Spain's economy is expected to grow by 2.9% this year.

SWITZERLAND: The Swiss government became the first ever to auction off 10-year debt at a negative yield of -0.055%, as QE and deflationary fears pushed up bond prices. This means that investors are in effect paying the Swiss government for the privilege of lending to it. The biggest problem of negative yields is that it renders conventional valuation techniques redundant. Approximately 57% of all outstanding German government debt with a maturity of more than a year trades at yields below zero, with a third trading below -0.2%, a rate below which the ECB will not buy assets.

GREECE: Greece made little headway in negotiations to end the standoff with its international creditors as its first reform proposal was rejected as too lenient. Greek finance minister Yanis Varoufakis accused Europe's creditors of trying to force his country to its knees by "liquidity asphyxiation". Varoufakis has been particularly heavily criticised for stalling over urgent measures needed to fix the economy. Consequently the markets rose after Greek Prime Minister Alexis Tsipras made changes to the Greek negotiating team to reduce Varoufakis's influence.

RUSSIA: Russia's GDP expanded by 0.6% in 2014, before contracting by 2% year-on-year in the first quarter of 2015. Prime Minister Dmitry Medvedev warned that the contraction could mark the beginning of a deep recession after the double shock of the collapse in oil prices and Western sanctions following Russia's annexation of Crimea. He estimated that the sanctions could cost Russia 4.8% of its GDP.

IRAN: After marathon negotiations in Switzerland, Iran agreed an outline deal that would mean cutting its capacity to produce enriched uranium and slashing its existing stocks. In return the US and EU would gradually phase out economic sanctions. The deal's negotiators, the US, France, the UK, Germany and China aim to reach a final agreement by the end of June. The deal has come under heavy criticism for the fact that Iran is allowed to keep 5 000 of its centrifuges, crucial for enriching uranium. In addition, key clauses will lapse after only 15 years. Iran has the world's fourth-biggest reserves of oil.

US: April hinted at continued weakness in the US economy. Lower than expected private-sector job gains and a larger-than-forecast drop in the ISM manufacturing PMI led to speculation that the US Fed will delay raising interest rates. The consumer price index rose by 0.2% month-on-month in March, bringing the year-on-year number to -0.1%.

JAPAN: April saw the Nikkei 225 Stock Average closing above the 20 000 level for the first time since 2000, the result of a rally underpinned by the performance of international exporters and lesser-known domestic staple goods suppliers. The latter has been driven by expectations of a recovery in consumer demand after the implementation of broad-based wage increases.

AUSTRALIA: According to Goldman Sachs, Australia risks S&P's attaching a negative outlook to its AAA credit rating for the first time in more than two decades as the economy struggles to navigate the end of a mining investment boom, a slowdown in China and a drop in government revenues as a result of falling commodity prices.

SOUTH AFRICA

Eskom and xenophobic attacks dominated the news. However, poor economic fundamentals did little to discourage the flow of foreign money into the South African stock market. The JSE saw a 50% surge in net foreign investment in the first quarter of 2015 from a year earlier. Approximately 46% of the free float of JSE-listed shares is now foreign-owned.

The woes at Eskom continued, with the suspension of four senior executives, unexpected strikes at the Medupi Power Station and ongoing load-shedding. Eskom has applied to Nersa for a further 25% electricity tariff increase and is trying to impose harsher load shedding on municipalities which owe it more than R9 billion. Brian Molefe was appointed as Eskom's acting CEO.

The World Bank cut its economic growth forecast for South Africa to 2% this year, in line with the IMF, while the GDP of sub-Saharan Africa is expected to grow at 4% in 2015.

Public sector wage negotiations raised their head again after the three-year wage agreement expired at the start of April. The trade unions are demanding a 10% increase, an unaffordable number which risks the prospect of 1.3 million public servants going on strike. Finance Minister Nhlanhla Nene has indicated that a 10% hike would add R20 billion to the government's remuneration bill. After other benefits were factored in that could rise to R50 billion. The effect would mean that personnel costs and interest repayments would be more than 50% of the state's budget over the next three years.

On the economic front, the Kagiso manufacturing PMI rose marginally to 47.9 in March as activity in the manufacturing sector struggled to gain momentum on the back of forced power outages and lower commodity prices. The business confidence index fell to a three-month low, and the consumer price index increased to 4% year-on-year in March as rand weakness, electricity tariff hikes and higher food prices translated into higher prices generally.

On a more positive note, South Africa's trade balance shifted back into surplus in March as exports of precious metals and electronics climbed. The trade surplus came in at 0.5 billion rand compared to a revised 8.7 billion rand deficit in February. Private sector credit demand increased by a stronger than expected 8.9% year-on-year in March.

On the corporate front, Naspers hit the R2 000 a share mark for the first time, cementing its position as the most valuable stock on the JSE after British American Tobacco and SABMiller. The share price rallied on the back of strong gains in Hong Kong-based Tencent in which Naspers holds a 34% stake.

ODDS AND ENDS

CALIFORNIA WITHOUT WATER

California has ordered mandatory water restrictions as the state's worst drought in 1 200 years enters a fourth year. They involve a 25% reduction in water use and a ban on new homes unless they feature water-efficient irrigation. California relies on Sierra Nevada mountain snow to irrigate the valleys below but this winter's final reading of Sierra Nevada's snowpack showed that the level of snow was just 6% of normal levels. In addition, record-low rainfall has left traditional reservoirs less than half full. California's drought has also severely impaired its ability to generate electricity with hydroelectric turbines. It has, however, been saved by its rapid deployment of renewable energy.

CAN GREECE BALANCE ITS BOOKS?

Greece needs to find about €17 billion to meet its bills for the remainder of the year, made up of interest payments of about €3 billion and debt rollover needs of over €13 billion. Their sources of funding include domestic primary surplus, the profits on Greek bonds purchased by the ECB through its Securities Market Programme, which will be returned to Greece and the IMF/ECB bail-out payment, when an agreement on reforms is reached. The IMF/ECB could also accelearate payments linked to future reviews. Once added together the funds leave a gap of just €2 billion. The remaining gap could be filled if the ECB raised the cap on the issuance of Treasury bills or through borrowing from the European Stability Mechanism precautionary credit line. It therefore appears that 2015 can be sorted out. What is less clear is what Greece will do in 2016 once it has tapped all available sources of funding.

CAN THE US DOLLAR REMAIN STRONG FOR MUCH LONGER?

The rising US dollar is redistributing growth throughout the global economy as it erodes the competitiveness of the US and countries whose exchange rates track the US dollar, including China. The eurozone and Japan, on the other hand, are cashing in on more competitive exports, while India is benefitting by paying less for energy imports. Emerging markets have had a harder time. The strong US dollar has pushed down commodity prices and increased the burden of US dollar denominated debt.

The debate on whether the US dollar can continue on its upward trajectory is raging. On one hand the current strength seems unsustainable. On the other hand there is an argument that the pent-up demand for the US currency can underpin years of appreciation because the world is “structurally short” the US dollar. Sovereign and corporate borrowers outside the US owe US$9 trillion in debt denominated in US dollars, much of which will need repaying in coming years. In addition, central banks that had reduced their holdings of the currency are starting to reverse course. The US dollar’s share of global foreign reserves shrank to a record 60% in 2011 from 73% a decade earlier, and has since climbed back to 63%. In addition, the prospect of higher US interest rates is appealing. Yet another structural factor is the US shrinking current account deficit. The decline in oil prices has helped the US reduce its trade shortfall to 2.3% of GDP down from a record 5.9% in 2006.

WHO OWNS US DEBT?

Japan surpassed China as the largest foreign holder of US Treasuries for the first time since 2008. Japan’s holdings in February 2015 amounted to US$1.224 trillion, while China’s holdings stood at US$1.223 trillion. On a year-over-year basis, Japan’s holdings increased by US$13.6 billion, while China’s declined by US$49.2 billion. The third biggest holder of US debt is a group of countries known as “Caribbean Banking Centers,” which include the Bahamas, Bermuda, Cayman Islands, Netherlands Antilles, and Panama. Their total holdings stood at US$350.6 billion.

COST OF EDUCATION IN SOUTH AFRICA

According to Statistics SA, the cost of education in South Africa rose by 9.3% year-on-year in March, 5.3% higher than the headline rate of inflation of 4%. The data was based on fees charged by schools and tertiary institutions. Education inflation has consistently outstripped consumer inflation and this trend is likely to continue.

….AND FROM THE HORSE’S MOUTH

42% of financial professionals in the latest Bloomberg Markets Global Poll, who were asked about the most appropriate way for a mid-career person to invest for retirement, opted for index tracking funds. Only 18% recommended actively managed unit trusts. 17% recommended individual stocks and bonds and 14% favoured real estate.

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