SYGNALS

KEY INDICATORS

SEPTEMBER 2014

		1 MONTH	3 MONTHS	6 MONTHS	1 YEAR	2 YEARS	3 YEARS	5 YEARS
J203T	FTSE/JSE All Share Index	-2.6%	-2.1%	4.9%	15.4%	21.1%	22.2%	18.0%
J200T	FTSE/JSE Top 40 Index	-2.6%	-2.9%	4.3%	15.2%	21.9%	22.4%	17.9%
J210T	FTSE/JSE Resources 20 Index	-5.9%	-6.6%	-4.0%	8.7%	8.0%	6.6%	6.5%
J211T	FTSE/JSE Industrials 25 index	-1.3%	-1.0%	8.3%	17.1%	30.8%	33.5%	27.3%
J212T	FTSE/JSE Financials 15 Index	-1.8%	-0.5%	8.2%	24.2%	24.2%	28.0%	20.0%
J403T	FTSE/JSE SWIX Index	-2.4%	-0.5%	6.2%	18.0%	21.6%	23.3%	18.9%
J303T	FTSE/JSE CAPI Index	-2.6%	-2.1%	5.0%	15.5%	21.2%	22.2%	18.2%
J253T	SA Listed Property Index	2.2%	7.2%	12.0%	15.1%	12.7%	20.3%	19.8%
ALBI	BEASSA All Bond Index	-1.6%	2.2%	4.7%	5.8%	4.4%	8.5%	9.3%
STeFI	STeFI Index	0.5%	1.5%	2.9%	5.6%	5.4%	5.5%	5.9%
	MSCI World Index in SA Rands	3.0%	3.8%	9.8%	26.2%	35.3%	31.7%	20.2%
	Rand/US Dollar Exchange Rate	5.8%	6.1%	7.1%	12.5%	16.5%	11.7%	8.5%
	Rand/Euro Exchange Rate	1.7%	-2.1%	-1.8%	5.1%	15.5%	9.6%	5.3%
	Headline CPI	0.4%	1.5%	3.4%	6.4%	6.4%	5.9%	5.3%
	PPI	0.0%	0.8%	3.2%	7.2%	6.9%	4.6%	6.2%

"Being able to change borders in Europe without consequences, and attacking other countries with troops, is in my view a far greater danger than having to accept certain disadvantages for the economy."

German Chancellor Angela Merkel commenting on Putin's aggression in the Ukraine

SYGNIA
THE SUM OF ALL THINGS

MARKET OVERVIEW

Geopolitical tensions and the outlook for interest rates in the US loomed large through September, with emerging markets bearing the brunt of the uncertainty and speculation.

Russian President Vladimir Putin played cat-and-mouse with his Ukrainian counterpart, Petro Poroshenko, on the surface agreeing on the outlines of a cease-fire for Ukraine, but encouraging tensions behind the scenes and calling for greater autonomy for the region.

The EU finally agreed to impose more sanctions on Russia, including the blocking of loans for five big state banks and curbing EU business with Russian oil and defence firms. Although Europe is reliant on Russia for gas, the situation is temporarily under control with sufficient volumes of fuel in underground inventories to minimise the risk of shortages during the coming winter.

In the Middle East, the US, supported by Saudi Arabia, Jordan, the UAE, Qatar and Bahrain, launched an air-borne offensive against ISIS bases in Syria and Iraq.

After an emotion-charged independence referendum, Scotland voted to remain part of the UK, but only after wringing promises of more financial and political independence.

In Hong Kong pro-democracy supporters clashed with police in the worst unrest since China took back control of the island from the UK two decades ago.

In the first half of September the risk on/off switch was largely in the hands of the ECB (under pressure to do more to restore growth in the eurozone), which cut its refinancing rate from 0.15% to a new low of 0.05% and its deposit rate to -0.20%. ECB President Mario Draghi also pledged to increase the ECB's balance sheet to the €2.7 trillion level of 2012, an increase of €700 billion. His main liquidity- injection strategy centres on buying asset-based securities (ABS), rather than bonds of sovereign nations, for which he would need unanimous support. However, the ABS purchase scheme received lukewarm response from member states, with only "simple and transparent" bundled securities qualifying. More risky forms of debt would require member states to extend guarantees to the ECB, a step too far for countries like Germany.

Yet another liquidity-injection tool used in September was the first allotment of a cheap four-year bank-funding scheme, called the targeted long-term refinancing operation (TLTRO). The take-up by banks was a disappointing €82.6 billion.

It is an open secret that the ECB is aiming for significant devaluation of the euro which would increase the cost of imports and boosts exporters' competitiveness, aiding the effort to revive inflation.

The second half of the month belonged to the US Federal Reserve and the concern that interest rates might increase sooner than anticipated on a mixed bag of economic results. The US unemployment rate fell to 6.1% in August, down from 6.2% in July, but employers added only 142 000 new jobs to the economy. On the other hand, manufacturing and non-manufacturing activity, consumer sentiment, factory orders and retail sales all strengthened from the second quarter. The month ended with the news that the US economy grew at an annualised 4.6% during the second quarter, its strongest pace in three years, increasing the probability of earlier rate hikes.

The US dollar rallied against peer group currencies, while commodity prices retreated, despite assurances from the US Fed that they will use broad measures to assess the health of the job market. The US Fed confirmed it would end its bond-buying programme in October.

The strong US dollar weighed on the rand which fell to a low of R11.28/$ by month-end.

Emerging market currencies were further hit by the continuing flow of weak economic data from China. The news that the People's Bank of China injected US$81 billion into the nation's largest banks and a better than expected preliminary HSBC Chinese manufacturing PMI, which rose to 50.5 in September, did little to stem the sell-off.

A similar picture emerged from Europe where both manufacturing and services growth slowed to the weakest pace in a year. Consumer prices rose by an annualised 0.3% in September, less than a quarter of the ECB's target. The OECD cut eurozone's GDP growth forecasts to 0.8% this year, down from a 1.2% forecast in May.

Despite the geopolitical uncertainty, gold fell sharply in September (5.5%) as the outlook for higher US interest rates and a stronger US dollar curbed demand for inflation hedges.

Oil also had a poor month with brent crude falling below US$100 to US$97 a barrel for the first time since June 2013 amid abundant supply and a slowdown in exports to China, the world's second-biggest oil consumer. The OECD's energy watchdog, the International Energy Agency, cut its global oil demand growth forecasts, prompting OPEC to consider cutting production targets. According to the IEA, demand is growing at its slowest since 2011, while the US shale boom means production outside OPEC is rising by the most since the 1980s.

360 DEGREES ROUND THE WORLD

UK: In its clearest guidance to date, the Bank of England indicated that it will start to raise interest rates early next year. With unemployment at 6.2%, the lowest level since 2008, and positive across-board economic data, there is a lot of room to manoeuvre.

GERMANY: German business confidence hit its lowest level in more than a year as most economic indicators signalled a slowing momentum. This is not good news after the contraction of the second quarter. Continuing tensions with Russia and weakening fundamentals across the eurozone have dimmed prospects for exports which to date have been the back-bone of Germany's recovery.

FRANCE: The OECD cut its growth forecast for France to a mere 0.4% this year, while the country's budget deficit is expected to widen for the first time in five years to 4.4% of GDP, on low inflation and reduced tax receipts. There is unfortunately little change to look forward to as President François Hollande's government, although surviving a no-confidence vote in Parliament, failed to win a clear majority which would enable it to push through badly needed pro-business reforms.

ITALY: The OECD also drastically cut its growth forecast for Italy, predicting that the economy will contract by 0.4% this year and that the depression will drag on through most of 2015. With inflation at a negative 0.2% in August, and the country's debt levels predicted to peak at 136% of GDP in 2014, the second-highest in the eurozone, Italians are growing increasingly disappointed with Prime Minister Matteo Renzi, who rose to power on a promise of a fast turnaround of the economy.

SPAIN: Spain's inflation fell by 0.5% in the year to August, making it more likely that the eurozone's fourth-largest economy will fall into outright deflation.

GREECE: S&P downgraded Greece to emerging market status as the country held talks with its troika of lenders to demonstrate that its austerity measures are on track.

ARGENTINA: Argentina passed a new bill designed to enable the government to resume debt payments to bondholders in defiance of a US court ruling. The country needs to make a US$200 million coupon payment in September to prevent a broad default, but needs to route the funds through channels beyond the reach of the US judge who ruled that Argentina must first settle a legal fight with a group of New York hedge funds over unpaid debt from a massive 2002 default before servicing its performing debt.

USA: Alibaba made history by becoming the largest IPO on the New York Stock Exchange, raising US$21.8 billion which placed the company's valuation at US$168 billion. The IPO makes Alibaba the third most valuable internet company traded in the US after Google and Facebook. Alibaba is China's biggest e-commerce company, with transactions totalling US$248 billion last year, more than those of eBay and Amazon combined. The company controls over 70% of China's online shopping market.

JAPAN: Japan's GDP shrank by an annualised 7.1% in the second quarter, the most since 2009. The contraction has been largely attributed to April's 3% hike in the sales tax to 8%. In its first sign that it is concerned about the effect on the economy, the government indicated that a back-up stimulus plan is being considered. The hike contributed to the 3.1% year-on-year increase in inflation in August. Stripped of the effect of the sales tax, inflation rose by 1.1%, well ahead of wage increases. The OECD has cut its 2014 economic growth forecast for Japan to 0.9%.

CHINA: A broad range of indicators, including credit expansion, retail sales, industrial production and fixed investment, continue to point to an economy losing momentum. The only bright light is exports which are benefitting from the rebound in the US economy. In a 180 degrees reversal of its previous liquidity-oriented policy, the Chinese government is determined to push through the purge of the financial system and the property market and wean the economy off its exorbitant debt levels irrespective of the impact on growth. Third quarter GDP growth is now expected to ease to between an annualised 6.5% to 7%. The Chinese government seems willing to tolerate lower growth provided the economy continues to generate jobs.

UKRAINE: Russian President Vladimir Putin called for negotiations over greater autonomy for the war-torn regions of the Ukraine. NATO's supreme military commander, US Air Force General Philip Breedlove, labelled the offer a ploy to lock down rebel control of chunks of Ukrainian territory in the east and south, close to the border with Russia. It is unlikely that Putin will settle for less than broad autonomy for Ukraine's mainly Russian-speaking regions of Donetsk and Luhansk, including the right to reject key decisions at the national level, such as joining NATO. It appears that Putin is willing to wait until November, after Ukraine elects a new parliament, to ensure his goals are met.

SOUTH AFRICA

South African markets remained at the mercy of global events throughout September. The first half of the month saw the JSE hit a new high of above 52 000 on the ECB's decision to cut interest rates, before retreating sharply on weak commodity prices and outflows from emerging markets. The rand slumped to a six-month low, pulled lower by a disappointing trade balance figure which recorded a R16.3 billion deficit in August.

The economic indicators came in slightly better than expected after a bruising strike season. The Kagiso manufacturing PMI increased to 49.0, business sentiment improved and retail sales numbers strengthened. Unfortunately, the current account deficit deteriorated more than expected to 2.8% of GDP in the second quarter as strikes, declining commodity prices and weak global demand weighed on exports.

Consumer prices increased by 6.4% year-on-year in August, up on the 6.3% seen in July. The figure is expected to trend downwards from September on lower petrol prices and food inflation. Producer price inflation moderated to 7.2% year-on-year in August from 8% in July, reflecting easing costs for local manufacturers. These expectations are, however, at risk given the recent depreciation of the rand.

The Reserve Bank kept its benchmark interest rate unchanged at 5.75%, but revised its growth forecasts down to 1.5% for 2014, 2.8% for 2015 and 3.1% for 2016. The Reserve Bank Governor, Gill Marcus, announced that she will not renew her contract when it expires in November. One of her two deputies, Lesetja Kganyago or Daniel Mminele, is likely to take over as the tenth governor.

The Reserve Bank also announced the appointment of a commission of inquiry into the collapse of African Bank. Its task is to determine whether the bank had been reckless, negligent or fraudulent before it had to be placed under curatorship.

Electricity provision grabbed the headlines once again after the National Treasury confirmed its plans to bail out Eskom. At the same time Russia's Rosatom State Atomic Energy Corporation announced that it has reached an agreement with South Africa for a large-scale nuclear power plant development aimed at procuring 9.6 gigawatts of nuclear power by 2030. The details of the deal are scant.

On the corporate front, Bidvest, South Africa's second biggest company by sales, announced that it was considering a separate London listing for its international food business to tap into cheaper funding.

Anglogold Ashanti attempted to simulate BHP Billiton's move by splitting its assets, creating a debt-free multi-commodity local company and a large London-listed gold-focused company holding a suite of international mines and growth assets. The proposal was blocked by shareholders.

The Heineken family, owners of Dutch brewer Heineken, turned down a takeover bid from SABMiller. SABMiller made the offer to help defend itself against a potential bid by Anheuser-Busch InBev, the world's largest brewing company. SABMiller has grown rapidly through acquisitions to become the world's second-biggest brewer, ahead of Heineken and Carlsberg. The big-four brewers account for about half of the world's beer market. AB InBev's market value is just shy of R2 trillion, while SABMiller is worth approximately R983 billion and Heineken R488 billion.

ODDS AND ENDS

SOUTH AFRICA SLIPS AGAIN

South Africa continued to slide in world competitiveness rankings on factors such as poor labour-employer relations, weak economic growth and poor standard of education and training . The country's ranking fell to 56th out of 144 countries in the World Economic Forum's Global Competitiveness Index for 2014, down from 53rd position in 2013. South Africa ranked 144th in labour-employer relations.

EBOLA UPDATE

The Ebola epidemic has killed more than 2 400 people in Guinea, Liberia, Nigeria and Sierra Leone to date. In September US President Barack Obama issued a global call to action to fight West Africa's Ebola epidemic, warning the deadly outbreak was unprecedented, "spiralling out of control" and spreading "exponentially". The UN estimated that the response to the crisis would require U$1 billion. The World Bank has so far approved US$105 million to help people cope with the economic impact of the crisis and strengthen public health systems.

HONG KONG STANDS UP TO CHINA

Tens of thousands of pro-democracy activists took to the streets of Hong Kong to protest against China's increased political interference and to demand free elections and public nominations for the chief executive position. China had previously pledged to give Hong Kong citizens universal suffrage starting in 2017. In August, China announced that all candidates for the chief executive position will be screened by a committee, which would effectively give Beijing a veto over anyone viewed as unfriendly to the central government. In response, the activist group Occupy Central With Love and Peace vowed to organise mass protests. In September China added fuel to the fire by asserting that Hong Kong's mini-constitution, the Basic Law, supported its view that candidates are to be nominated by committee rather than directly by voters.

PIMCO LOSES ITS KEY ASSET

Bill Gross, the 70-year-old billionaire who co-founded Pimco in 1971 and was its Chief Investment Officer, announced that he is leaving the firm to join Janus Capital. Pimco manages US$1.97 trillion in assets and has been one of Sygnia's long-standing international bond managers. However, in the past year, we have become increasingly concerned about structural changes at the firm and have been reducing our exposure to Pimco. The recent event has led us to terminate that mandate in its entirety.

Gross, who managed the world's biggest bond fund, leaves after a tumultuous year which also saw the departure of Pimco's Chief Executive Officer, Mohamed El-Erian. Gross's resignation seems to be motivated by a dispute with senior management over future strategy of the company in the face of recent redemptions. Gross's long-term investment performance track record remains outstanding, boosted by his avoidance of the subprime debt trap in 2008. More recently, however, his performance has faltered amid wrong calls on the direction of US Treasuries. Daniel Ivascyn has been appointed as Pimco's new Chief Investment Officer.

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