

SYGNALS

SEPTEMBER 2015

KEY INDICATORS

		1 MONTH	3 MONTHS	6 MONTHS	1 YEAR	2 YEARS	3 YEARS	5 YEARS
J203T	FTSE/JSE All Share Index	1.0%	-2.1%	-2.3%	4.8%	10.0%	15.4%	14.6%
J200T	FTSE/JSE Top 40 Index	2.0%	-1.5%	-0.7%	4.9%	9.9%	15.9%	14.8%
J210T	FTSE/JSE Resources 20 Index	-9.6%	-16.7%	-20.5%	-36.4%	-16.9%	-9.5%	-5.0%
J211T	FTSE/JSE Industrials 25 index	5.0%	1.6%	3.7%	17.8%	17.5%	26.3%	25.0%
J212T	FTSE/JSE Financials 15 Index	-2.2%	-2.9%	-5.5%	15.3%	19.7%	21.2%	18.5%
J403T	FTSE/JSE SWIX Index	-1.0%	-4.2%	-4.3%	6.1%	11.9%	16.2%	15.7%
J303T	FTSE/JSE CAPI Index	1.0%	-2.1%	-2.3%	4.9%	10.1%	15.5%	14.8%
J253T	SA Listed Property Index	0.8%	6.2%	-0.4%	25.8%	20.4%	16.9%	18.9%
ALBI	BEASSA All Bond Index	-0.1%	1.1%	-0.3%	7.0%	6.4%	5.3%	7.7%
STeFI	STeFI Index	0.5%	1.6%	3.2%	6.4%	6.0%	5.7%	5.7%
	MSCI World Index in SA Rands	0.4%	4.0%	4.6%	16.3%	21.2%	28.7%	24.2%
	Rand/US Dollar Exchange Rate	4.2%	13.6%	13.9%	22.6%	17.4%	18.5%	14.7%
	Rand/Euro Exchange Rate	3.9%	14.2%	17.6%	8.5%	6.8%	13.1%	10.3%
	Headline CPI	0.0%	1.5%	4.1%	4.6%	5.5%	5.8%	5.5%
	PPI	0.1%	0.6%	4.0%	3.4%	5.3%	5.7%	5.4%

"Dangerous currents risk pulling us back into a darker, more disordered world."

US President Barack Obama in a speech to the General Assembly of the UN, New York.

MARKET OVERVIEW

September brought to an end the worst quarter for global equities in the past six years. The combination of the Greek crisis, China's stock market gyrations, currency devaluation strategy and continuing economic slowdown, compounded by the uncertainty over the timing of US Federal Reserve's interest rate increases, have created a toxic mixture which has punished commodity prices, stocks and, in particular, emerging markets and their currencies.

September started with the bad news that China's manufacturing sector shifted from stagnation to contraction in August, experiencing the sharpest one-month decline in three years. Concerns about the slowdown in China and the volatility in financial markets guided the US Federal Reserve's decision not to increase interest rates. Their lack of decisive action means that the volatility is unlikely to stop anytime soon. The Volkswagen emission test scandal and continuing stream of weak economic data from China contributed to the negative sentiment through the month.

The US Fed's Beige Book described the US economy as continuing to grow modestly, largely as a result of increased activity in the housing market and strengthening auto sales. The jobless data painted a mixed picture, with the August unemployment figure dropping to 5.1%, close to the level regarded by the US Fed as "full employment", but with fewer jobs being created than expected. The labour force participation rate remained steady at 62.6%. Not immune to global events, US factory activity hit a two-year low; with the ISM manufacturing-activity index dropping from July's 52.7 to 51.0. Consumer confidence figures also trended downwards.

In migrant-swamped Europe the ECB cut its 2015 growth and inflation forecasts for the eurozone to 1.4% and 0.1%, respectively, on worries about China and other emerging markets. Unsurprisingly, the ECB kept interest rates unchanged, while confirming that it was ready to deploy more stimulus measures if required. However, the events in China have not yet had a significant impact, with Markit's manufacturing and services PMI rising to 54.3 in August, its highest level since May 2011. Inflation, on the other hand, fell by 0.1% year-on-year in September for the first time since the ECB launched its quantitative easing programme in March. The eurozone's jobless rate was unchanged at 11.0% in August.

The People's Bank of China indicated that its foreign currency reserves fell by a record US\$93.9 billion in August after it intervened in the stock and currency markets. Having peaked at US\$4 trillion in June 2014, currency reserves stand at US\$3.56 trillion, nearly a third of all holdings by central banks world-wide. Analysts have compared the fall to "quantitative tightening," with shrinking reserves resulting in higher bond yields, increased borrowing costs and an overall challenge to the central bank's ability to exit monetary easing policies.

The Chinese economy continued to show signs of strain. China's official manufacturing PMI fell to 49.7, the lowest level since August 2012, while the Caixin manufacturing PMI fell to a six-year low. In addition, both factory production and fixed asset investment came in weaker than expected. In a signal of what we may see for 2015 China revised its growth rate for last year to 7.3% from 7.4%. The country's growth target of about 7% for this year is the slowest pace in a quarter century. The World Bank estimates that a 1% decline in China's growth shaves 0.5% off global growth.

The G20 meeting in Turkey resulted in little other than an agreement to step up efforts to increase growth. In a nod to emerging markets financial leaders agreed to avoid surprise or excessive interest rate moves, but gave in to the US by accepting that interest rates in some advanced economies would have to rise. China used the meeting to reassure other members that the correction in China's stock market is almost done.

Global equity markets vacillated on concerns about the direction of US interest rates. The flight to the safety of US Treasuries translated into a stronger US dollar, with the rand touching the R14.01/US\$ level.

The US Fed's decision to leave short-term interest rates unchanged did little to restore calm. The Fed cited concerns about how global events, including market turmoil and weaker growth, would affect the US. It increased its estimate for economic growth over 2015 to 2.1% from the 1.9% projected in June, but cut its long term growth projections to between 1.8% and 2.2% per annum. It expects the unemployment rate to fall to 5.0% by year-end and to 4.8% by the end of next year. Inflation is not expected to reach its 2% goal until 2018. The US central bank will hold two more policy meetings this year, in late October and mid-December, giving it two more chances to increase interest rates this year.

The US Fed's decision encouraged other central banks to relax their monetary stance with the central banks of Norway, Taiwan and Ukraine lowering their interest rates. Other central banks that were expected to respond to a US rate increase with upward moves of their own, including Mexico and Turkey, opted to keep rates on hold.

The end of the month brought another sharp sell-off, particularly in commodities, after China's flash Caixin manufacturing PMI fell to 47.0 in September, its lowest level since March 2009. This was followed by the announcement that Volkswagen had falsified the results of emission tests performed in the US on its diesel-engine cars. The company's share price dropped by more than 20%, pulling down other car manufacturers. The company faces billions of US dollars in fines. As investigations spread to Europe and Asia, Volkswagen confirmed that 11 million cars would be recalled and issued a profit warning with a €6.5 billion provision to cover the cost of addressing the matter. The scandal had an immediate effect on the platinum price which fell below US\$900 an ounce for the first time since January 2009 on fears of reduced demand for diesel cars.

The platinum market is also suffering from a dearth of platinum jewellery buying in China, and from rising supply from South African producers, who have ramped up output after last year's five-month strike.

The sentiment improved somewhat after US Fed chair Janet Yellen confirmed that the Fed was on track to raise interest rates this year to prevent the economy from overheating and to halt excessive risk taking in the financial markets.

Positive reaction was given a further boost by the upward revision of the second quarter US growth rate to 3.9% year-on-year after a meagre 0.6% growth over the first quarter.

Unfortunately, this was short-lived as commodity prices saw another sharp drop at month-end on concerns about China after it reported that its industrial profits fell 8.8% in August from a year previously. The Swiss-based diversified mining company, Glencore, led the sell-off with its share price plummeting by 25% in one day alone and by 75% since the start of the year. The share recovered somewhat the next day after the company dismissed concerns that it was on the brink of insolvency and insisted that it has taken proactive steps to withstand the current market conditions.

Both Brent crude and US crude oil prices hovered under the US\$50 a barrel level on heightened concerns about the growth outlook at a time of a glut in supply. Wall Street's most influential voice in oil trading, Goldman Sachs, cut its 2016 forecast for US crude to US\$45 a barrel and for Brent to US\$49.50. Oil prices have fallen by 60% from their peaks in June 2014.

We expect the volatility to continue until such time as the US Fed increases interest rates, allowing speculation to settle and market participants to refocus. Negative sentiment towards emerging markets will continue until such time as China's economy shows signs of stabilising, punishing the rand and the South African equity market. Commodity prices are unlikely to recover in any meaningful way in the near future.

BRAZIL: S&P's cut Brazil's sovereign credit rating to junk with a negative outlook on the back of a faltering economy and fiscal pressures. President Dilma Rousseff has been unable to find support for her reforms amid an investigation into corruption at the state-controlled oil company that allegedly occurred while she was its chairman. The government now forecasts a fiscal deficit of 0.5% of GDP in 2016 compared to a surplus of 2% targeted at the beginning of this year and a revised objective of 0.7% announced in July. The country's gross debt has climbed to 65% of GDP.

FRANCE: Moody's downgraded France's bond rating to Aa2, from Aa1, with a stable outlook, citing a weak outlook for medium-term growth.

NORDIC NATIONS: Investors are withdrawing from backing wind farms in Nordic nations as the lowest electricity prices in 12 years cut the profitability of new projects. No wind farms were commissioned in Sweden in the second quarter, compared to 50 megawatts in the same period a year earlier. Investment in utility-scale Nordic wind assets fell by 76% to US\$1.2 billion in the three years to 2014.

GREECE: Alexis Tsipras has been re-elected as the prime minister of Greece after his left-wing Syriza party won 35.5% of the vote in the national elections, well ahead of the 28% scored by its closest challenger, the New Democracy party. Tsipras entered into a coalition agreement with the right-wing nationalist Independent Greeks to form a majority government. This enables him to implement the fiscal reforms demanded by Greece's creditors in exchange for the third €86 billion bail-out. Tsipras is expected to abide by the deal in the short term. However Syriza's weak conviction in the economic philosophy behind the programme means that full implementation of the deal is not guaranteed. In preparation for the election Tsipras purged the Syriza party of its most radical leftists, roughly one-third of its members of parliament. The remaining new-look Syriza positioned itself as a more respectable party of the left.

UKRAINE: The EU extended its economic sanctions against Russia for six months. Russian President Vladimir Putin responded by unveiling plans to build a large military base housing 5 000 troops on Russia's border with Ukraine amid indications that he intends to lash out at the West to distract attention from his country's ailing economy.

JAPAN: Real wages in Japan posted their first increase in more than two years, rising by 0.3% in July compared with the same month last year, after being in broad decline for four years. However, the Bank of Japan acknowledged that the country is falling behind in its effort to boost inflation and will not reach its 2% target for the next two and a half years.

AUSTRALIA: Malcolm Turnbull, the communications minister, succeed Tony Abbott as Australia's prime minister after a party rebellion that is expected to moderate the country's stance on issues ranging from same-sex marriage to climate change and economic policy. Turnbull called for a leadership ballot after voter surveys pointed to defeat for the ruling Liberal-National conservative coalition at the federal elections due next year.

RUSSIA: In two quick moves Russia expanded its influence in the Middle East. Firstly it reached an agreement with Iraq, Syria and Iran to share intelligence about Islamic State (ISIS), followed by authorising airstrikes over Syria after a tense stand-off between Russian President Vladimir Putin and US President Barack Obama at the UN General Assembly meeting in New York. Russia has built up forces on the ground in Syria in an effort to support Syrian President Bashar al-Assad.

ZAMBIA: Zambia's kwacha plunged by 17% in one day to a record low against the US dollar on a sharp slide in copper prices and a ratings downgrade from Moody's.

SOUTH AFRICA

Concerns about South Africa's sovereign credit rating came into the spotlight after the rating agency, S&P's, downgraded Brazil's debt to sub-investment grade status. S&P's downgraded South Africa to its lowest investment grade rating, back in June 2014. It reaffirmed that rating, with a stable outlook, in June this year. Fitch and Moody's both rate South Africa two levels above junk.

The economy continued on a weak path with the Barclays manufacturing PMI falling to 48.9 points in August and the business confidence numbers plummeting to a 16-year low. South Africa's trade deficit widened sharply to R9.9 billion in August from R1.1 billion in July. On a positive note, consumer inflation slowed more than expected to 4.6% year-on-year in August from 5% in July, mainly on the back of lower fuel prices. The producer price index rose by 3.4% compared to a year ago, a slower pace than last month.

The Reserve Bank left interest rates unchanged, as expected, citing a better inflation outlook and weak economic growth as the main reasons. It also downgraded economic growth prospects from 2% and 2.1% to 1.5% and 1.6% in 2015 and 2016, respectively, and lowered its inflation forecasts to 4.7% for 2015 and 6.2% for 2016.

On the corporate front, ArcelorMittal announced the moth-balling of two operations and the review of the viability of other plants despite the government agreeing to apply a 10% import tariff on steel last month.

The musical chairs game at parastatal companies continued with Eskom confirming the appointment of Brian Molefe as its permanent CEO, while Denel, the state-owned defence manufacturer, announcing that it has put its CEO, Riaz Saloojee, and CFO, Fikile Mhlontlo, on special leave pending an investigation by the company.

And the institutional market finally woke up to the need to comment on the draft Default Regulations issued by National Treasury in July. The Regulations, which target lowering of costs to retirement fund members, has the potential to fundamentally change the financial services industry.

ODDS AND ENDS

EUROPE HIT BY MIGRANTS

Approximately 160 000 people from the war-torn nations of the Middle East are seeking refuge in Europe. The influx resulted in several countries, including Germany, re-establishing border controls, a move which has dealt a severe blow to two decades of open travel in the 26-nation bloc under the Schengen Treaty. Hungary, Italy and Greece are bearing the brunt of the mass arrivals of people from Syria, Iraq, Eritrea and Afghanistan. The EU backs a strategy of establishing a compulsory quota system to distribute asylum seekers across the EU on an equitable basis.

To put 160 000 migrants in perspective, according to the South Africa's 2011 census, the most recent official figures, there are about 2.2 million immigrants living in South Africa. 2015 estimates published by Statistics South Africa place the number of undocumented migrants between 500 000 and one million.

UNITED NATIONS GENERAL ASSEMBLY AT WORK IN NEW YORK

US President Barack Obama made a forceful defence of diplomacy but also directly criticised Russia, China and Iran in disputes around the world and indirectly took a swipe at his Republican rivals. Syria was the most obvious target.

The US has long cast Assad as the primary source of instability in Syria, with his brutal political crackdowns providing an opening for jihadist groups. According to the US, the crisis cannot be resolved until a political transition is negotiated that requires Assad to leave power. Russia on the other hand, sees the Syrian government as a bulwark against further gains by groups like ISIS and wants the defeat of ISIS to come before a negotiated solution to the Syrian conflict.

THE CRADLE OF HUMANKIND GIVES UP ITS SECRETS

A new species of human ancestor was unearthed at the Cradle of Humankind World Heritage Site. Called Homo naledi after the Rising Star caves' chamber in which they were discovered, the fossils include infants, children, adults and older individuals. Homo naledi was smaller than us humans, with curved fingers, a small skull and a slender body. Research shows the average Homo naledi was 1.5 metres tall, weighed about 45kg and had a brain the size of an orange.

GLENCORE SINKS IN A DEBT PILE...

The shine has come off the commodities giant Glencore which acquired its competitor, Xstrata, for US\$29 billion in 2012. Glencore's business model combines a trading division that buys and sells commodities with physical mining production. Four years after its stock market listing the company was forced to suspend dividends and announce asset sales and a new share issue of US\$2.5 billion to cut its US\$30 billion debt pile. Glencore's share price has fallen by 75% this year, and nearly 90% since listing. Ongoing weakness in China, coupled with soft prices for commodities such as copper and zinc that are central to the company's earnings, have threatened Glencore's viability. The end-of-the-month commodities sell-off saw 25% wiped off the share price in just one day.

...WHILE SAB MAY DISAPPEAR ALTOGETHER

SABMiller's share price spiked after the news spread that its largest competitor, Belgian Anheuser-Busch InBev NV, is planning to make an offer to buy the company. SABMiller has been struggling for a while as a slump in emerging markets, volatility of the exchange rate and weak underlying demand around the world for mass-market beer brands relative to craft beers, wine and spirits, have hit sales. Its failed attempt to take over Heineken last year left it open to a hostile bid. If the sale happens, it is likely that SABMiller will be de-listed from the JSE, unless a significant shareholder such as the PIC makes a continuing listing a condition of sale. The surge in SABMiller's share price saw it overtake Naspers as the largest company by market cap listed on the JSE – for now.

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