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Newsletter

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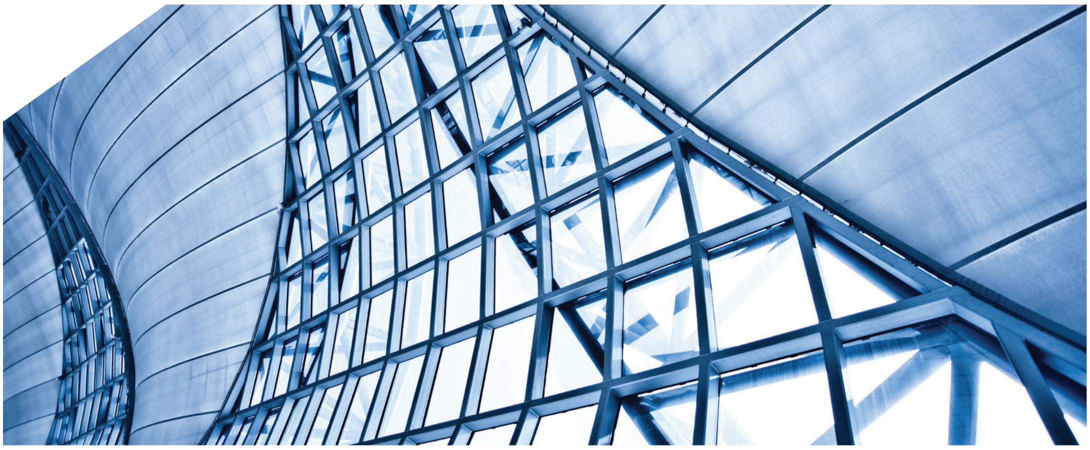

ECONOMIC COMMENTARY

- By Francois Stofberg

Local is lekker

Last week the markets experienced a lot of ups and downs, both internationally and locally. In the end the Asian markets came back strong, the US recovered some, but SA lagged most. A depressed-sentiment hangover continues to keep local markets tight.

We've explained that the negative sentiment towards SA originates from both local and international sources. Internationally, the persistent dislike towards emerging markets pulls at the JSE's earnings multiples. Local analysts noted that buyers of JSE-listed stocks continue to wait for more direction about the ongoing trade war between the US and China before they'll be willing to dive in.

Locally, we are all very much aware of how poor policies, politics, and political appointees (a certain Head of IT at SARS comes to mind) have pulled our economy into the slumps. In their recent publication, the Centre for Risk Analysis (CRA) showed that SA is currently in the longest downward cycle it has ever been in since the end of the second world war – the earliest time from which data is reasonably available. Their research uses business-cycle data from the South African Reserve Bank (SARB) and shows that our current cycle started in December 2013 and will therefore soon be 5 years old. Business-cycle models from the SARB use average long-term trend rates to discern if we are above or below trends of various leading and lagging growth indicators. The conclusion is that we are well below trend and have been for a very long time. But it's not all just doom and gloom, especially not for firms listed on the JSE. Economies have a way of working themselves back to some form of a long-term trend rate (albeit at a new lower trend rate).

Last week we explained how SA has the right pillars in place to ensure a move back towards trend-growth rates; a working democracy, a free press, an independent central bank, liquid financial markets, a strong judiciary. But, even if you don't subscribe to this notion and believe the absolute worst about SA's economic future, local firms continue to print positive earnings growth. This makes valuations look ridiculously cheap, especially if you factor in the very poor performing rand. In an interesting interview on Bloomberg, one of the world's largest asset managers shared this view with us.

Fed minutes came out last week and were perceived by markets to be more hawkish. This weighed many emerging markets down on fears that the Fed might hike rates even faster and drain even more liquidity from those emerging markets. Hawkish-fears continue to grow despite President Trump's Tweets against the Fed's current tightening policy. The truth is that the US is still surprising everyone who wants to believe that the current bull market, the longest one in US history, will soon be coming to an end. In yet another good earnings quarter, US firms showed strong growth despite trade wars and growing social-politic risks. Most notably was Netflix who surprised analysts when they reported much more favourable subscription results, causing a substantial rally in the stock. Chinese markets were boosted by aggressive talk from the ruling Communist Party of China, explaining once again that they will do whatever it takes to grow their economy at the required, and planned rate. This came after the latest growth report showed that the colossus slowed to its weakest quarterly performance since 2009, an annual growth rate of 6.5% during the third quarter of 2018.