INVESTMENT REVIEW

MARCH 2017

BRIDGE FUND MANAGERS

"The evil of the world is made possible by nothing but the sanction you give it."
Ayn Rand

ECONOMIC OUTLOOK

The US Federal Reserve (the Fed) raised official interest rates for the second time in three months, following their March policy meeting. The move was widely expected after inflation moved above the 2% target (chart 1). The Fed is expected to raise interest rates on at least two more occasions this year, although the timing of each increase will be data-dependant. Interest rate hikes will also depend on the timing and magnitude of fiscal stimulus introduced by the Trump administration following campaign promises to cut taxes and increase spending. Having already failed to repeal and replace Obamacare at the first attempt, questions are now being asked of the new administration's ability to follow through on their promises, which might mean interest rates stay lower for longer.

British Prime Minister, Theresa May, triggered Article 50 of the Lisbon Treaty and in so doing has set the UK on a path to exit the European Union on 29 May 2019. The negotiations are expected to be tough and will create significant political and economic uncertainty in both the UK and Europe. Adding to the political uncertainty in Europe; the first round of the French Presidential election is set to be held on 23 April and although not the frontrunner, there is an outside chance that Marine Le Pen could become the next President of France. Political uncertainty in Europe will then transfer to Germany later in the year.

Index	March %	12m %	YTD %
Dow Jones	-0.6	19.9	5.2
S&P 500	0.1	17.2	6.1
FTSE 100	0.8	18.6	2.5
EURO STOXX 50	5.6	20.1	6.8
Nikkei 225	-1.1	12.8	-3.5
Hang Seng	1.6	16.1	9.6
Australia	3.1	14.6	3.2

Source: I-Net Bridge

In South Africa, President Jacob Zuma reshuffled his cabinet, which included the firing of Finance Minister Pravin Gordhan and his deputy, Mcebisi Jonas. Standard & Poors responded by cutting South Africa's foreign-currency rating to BB+, one notch below investment grade. Although the local currency rating remained investment grade, Standard & Poors moved the outlook on both ratings to negative, suggesting the next move could be downward. In the wake of the cabinet reshuffle and the credit rating downgrade, both the SA Communist Party and the Congress of South African Trade Unions (Cosatu) have called for President Zuma to resign.

The rand depreciated against the US dollar (chart 2), on the back of the increase in political uncertainty. Having been as low as R12.35/US$ during March, the rand finished the month at R13.40/US$ and has weakened further to R13.75/US$ following Standard & Poors' downgrade. The weaker rand and higher bond yields will, in all likelihood, translate into higher inflation and lower economic growth. There is now little scope for the South African Reserve Bank to start lowering interest rates this year, despite a more dovish tone following their policy meeting in March at which one committee member voted for a rate cut.

MARKET OUTLOOK

Global equity markets drifted sideways during March, although European stock markets rallied (chart 3) on improved growth prospects throughout Europe and rotation out of US equities. The Trump administration's failure to repeal and replace Obamacare at the first hurdle has raised concerns among equity investors about the timing and magnitude of fiscal stimulus for the US economy. The share prices of US companies have rallied since Donald Trump was elected president and in the absence of a meaningful boost from lower taxes or increased spending look extremely expensive at current levels. The share prices of European and UK companies have not enjoyed the same rally since November and on a relative basis look far more attractively priced.

Global bond yields were moderately higher in March, mainly on the back of improved growth prospects in Europe. The yield on German 10-year government bonds increased from 0.21% to 0.33%. Global listed property prices declined by 2% in March (chart 4) on the back of higher bond yields and increasing concern about the future of large mall landlords. Large anchor tenants such as Macy's and Sears have announced store closures and productivity in malls has declined in the face of strong online sales growth. Although online businesses like Amazon are creating increased demand for warehousing, that sector is small relative to the malls.

Index	March %	12m %	YTD %
All Share	2.7	2.5	3.8
Resources	2.9	16.7	2.7
Financials	-0.7	-1.8	-1.1
Industrials	4.2	0.1	6.6
Property	0.1	1.5	1.4
Bond	0.4	11.0	2.5
Cash	0.6	7.6	1.8

Source: I-Net Bridge

South Africa's equity market rallied in March, mainly on the back of the weaker rand which helped boost the prices of South Africa resource and rand-hedge industrial companies. The banks and retailers were particularly hard-hit following President Zuma's cabinet reshuffle. The FTSE/JSE Banks index fell 6.1% on the final day on March (chart 5), while the FTSE/JSE General Retailers index fell 3.9%. Both indices have suffered further losses following Standard & Poors' decision to cut South Africa to junk status. Despite the volatility over the past month, the one year forward p/e multiple on the FTSE/JSE All Share index is still 14x, while the one year forward dividend yield has increased slightly to 3.4%.

South African government bond yields spiked sharply following President Zuma's decision to reshuffle his cabinet. Having been as low as 8.3% during March, the yield on the government's R186 bond finished March at 8.84% and has moved higher to 8.96% following the Standard & Poors's decision (chart 6). South Africa's listed property sector experienced an extremely volatile March. At one stage during March, the sector had gained more than 4% as bond yields fell and the rand strengthened, but those gains were wiped out following the cabinet reshuffle and a spike in long bond yields.

DIRECTORS
DP DU PLESSIS* (CHAIRMAN), SA BLADES*
MB LOGAN, DA POLKINGHORNE*, PS STEWART.
*NON EXECUTIVE

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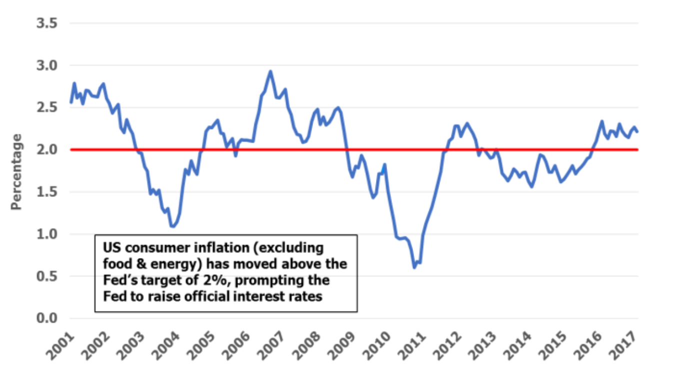
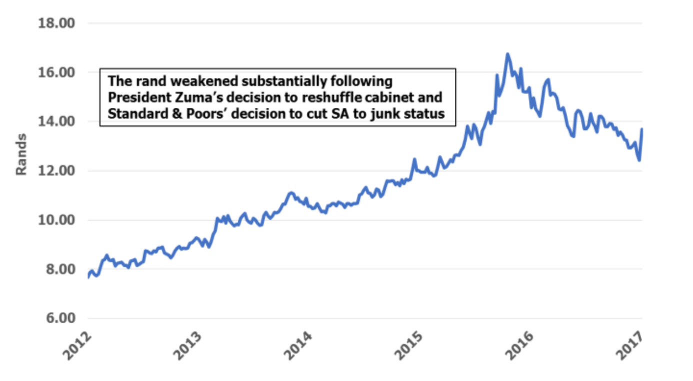
CHARTS

Chart 1: US Consumer Inflation (%)



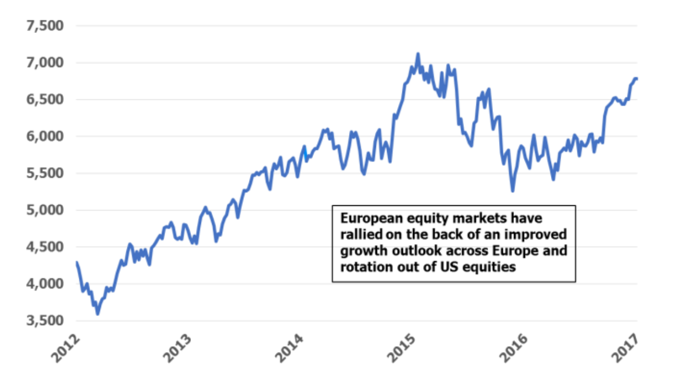
Source: I-Net Bridge

Chart 2: USD/ZAR Exchange Rate (R/US$)



Source: I-Net Bridge

Chart 3: DJ Euro Stoxx Index

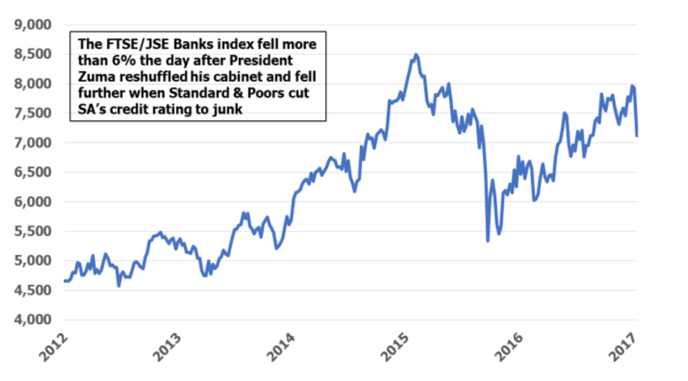


Source: I-Net Bridge

Chart 4: GPR 250 REIT Index

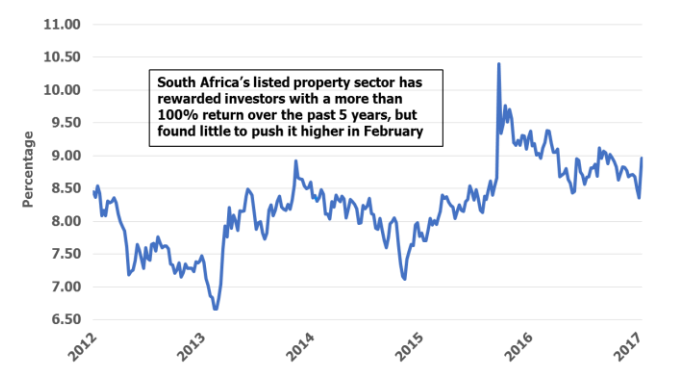
Source: Global Property Research

Chart 5: FTSE/JSE Banks Index



Source: I-Net Bridge

Chart 6: R186 Government Bond Yield (%)



Source: I-Net Bridge

Ian Anderson, CFA, CAIA
Chief Investment Officer