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INVESTMENT REVIEW

MARCH 2018

BRIDGE FUND MANAGERS

"Success is the ability to go from one failure to another with no loss of enthusiasm."
Sir Winston Churchill

ECONOMIC OUTLOOK

The US Federal Reserve (the Fed) raised official interest rates by 0.25% following the conclusion of their March policy meeting. The move was widely anticipated by economists following continued improvements in US economic data. The Fed also increased their forecasts for US GDP growth in both 2018 and 2019. This is the sixth interest rate increase since December 2015 (chart 1) and according to current forecasts will be followed by a further two increases of 0.25% each in 2018. The Fed does expect economic growth to moderate after 2019 as the $1.5 trillion in tax cuts, announced by the Trump administration, will be in the base and are not expected to have a sustainable impact on economic growth rates.

The US and China have recently entered into a trade war, with both countries threatening tariffs of up to 25% on a range of goods. The US announced they would impose an additional tariff of 25% on approximately $50 billion of imports from China, while China responded by announcing a retaliatory tariff of 25% on a range of goods it imports from the US, also valued at approximately $50 billion per annum. At these levels, the trade war is unlikely to have a meaningful impact on global economic growth although it will have an impact on those industries, such as US auto manufacturers, most affected by the tariff increases.

Index	March %	12m %	YTD %
Dow Jones	-3.6	19.4	-2.0
S&P 500	-2.5	14.0	-0.8
FTSE 100	-2.4	-3.6	-8.2
EURO STOXX 50	-2.2	-1.7	-3.8
Nikkei 225	-4.1	11.9	-7.1
Hang Seng	-2.4	24.8	0.6
Australia	-4.1	-0.6	-4.8

Source: I-Net Bridge

In South Africa, the Monetary Policy Committee of the South African Reserve Bank (the SARB) lowered official interest rates by 0.25% following the conclusion of their policy meeting in March. The move was widely expected following a period of rand strength and lower consumer inflation (chart 2). The SARB has lowered its inflation forecasts despite expecting the rand to weaken from current levels. They also increased South Africa's economic growth forecasts although they remain below current market expectations for GDP growth in both 2018 and 2019. For the SARB to cut interests again in 2018, the rand would need to strengthen from current levels.

Following a decision to put South Africa's sovereign credit rating on downgrade review in November last year, Moody's decided to keep the rating at the lowest level of investment grade and upgrade the rating outlook from negative to stable. This was positive for the country's bond and currency markets as a downgrade from Moody's would have seen South African government bonds excluded from a number of global bond indices and would have led to another massive exodus of foreign investor capital. Given the improving outlook for South Africa, it is unlikely that the country will be downgraded to junk status in 2018.

MARKET OUTLOOK

The prospect of a global trade war, with the US and China as the main protagonists, weighed heavily on global equity markets during March. The S&P 500 index was down 2.5% in March and is now marginally lower in 2018 (chart 3). Technology companies were particularly hard hit towards the end of the month following tweets from President Donald Trump that suggested that Amazon was a "no-tax monopoly" and that the company's CEO, Jeff Bezos, is using the Washington Post, which he owns, as a lobbyist weapon against Congress. The sell-off in equities was not limited to the US and most global equity markets declined by more than 2% during March. Volatility has also increased and is likely to remain elevated while the US and China "trade blows".

Although the more lasting impact of a trade war is higher inflation, the more immediate concern for market participants is the impact it will have on global economic growth and the trajectory of short-term interest rates. As a result, global bond yields reversed their upward trend and fell as much as 20 basis points in March (chart 4). The yield on 10-year US Treasuries, which was hovering close to 3% at the end of February, is now down to 2.75%. Global listed property prices gained almost 3% in March following Kleppiere's bid for Hammerson. Lower global bond yields also helped bolster listed property returns during the month.

Index	March %	12m %	YTD %
All Share	-4.2	9.6	-6.0
Resources	-2.1	10.4	-3.8
Financials	-3.1	17.6	-3.6
Industrials	-5.5	5.7	-8.0
Property	-1.0	-7.1	-19.6
Bond	2.1	16.2	8.1
Cash	0.6	7.4	1.7

Source: I-Net Bridge

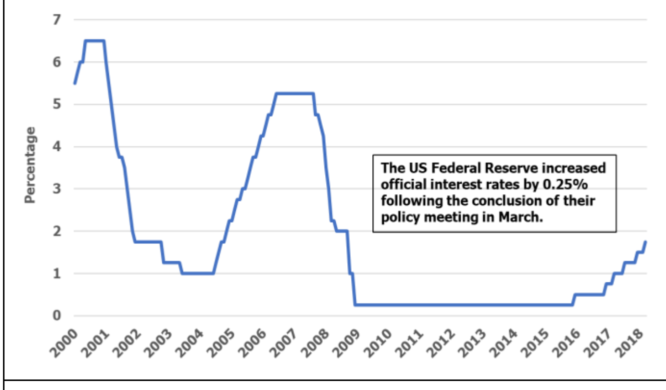
Despite the reprieve from Moody's and a 0.25% reduction in official rates, South Africa's equity market tumbled 4.2% in March (chart 5). This was the worst monthly performance by the South African equity market since June 2013. Naspers led the price declines, shedding 11.6% after announcing the sale of up to 2% of Tencent's shares. Tiger Brands (-12.8%) and AVI (-8.8%) also suffered large price declines as the source of the deadly listeriosis outbreak was traced back to a Tiger Brands facility. Amongst the big winners in March were retailers like Truworths (+8.7%) and Clicks (+7.7%) as well as hospital group, Netcare (+9.8%).

The yields on South African bonds fell further in March, following Moody's decision to upgrade the rating outlook from negative to stable. The yield on government's benchmark R186 bond dipped below 8% for the first time since April 2015. Although the prices of the Resilient group of companies continued to tumble in March, the SA listed property sector only declined by 1.0% during the month. Since the start of the year, listed property is the worst performing asset class in South Africa, having tumbled 19.6%, principally on the back of a 70% decline in the price of Fortress B and a 65% decline in the price of Resilient (chart 6).

BRIDGE FUND MANAGERS

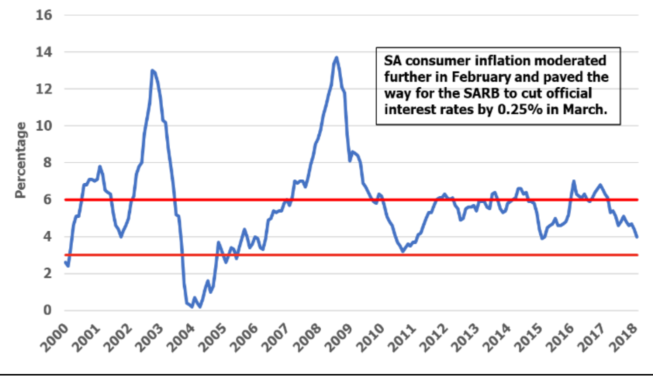
CHARTS

Chart 1: US Federal Funds Rate (%)



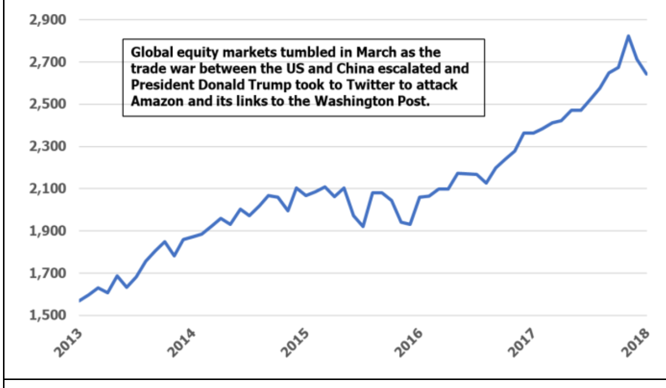
Source: IRESS

Chart 2: SA Consumer Inflation (%)



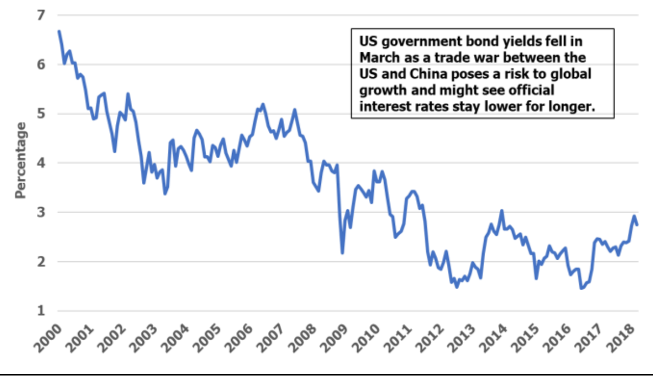
Source: IRESS

Chart 3: S&P 500 Index



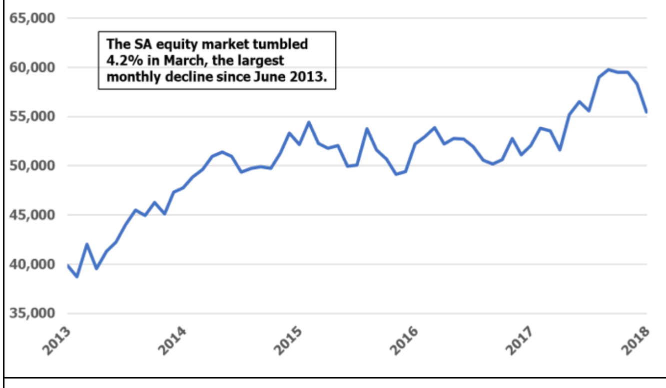
Source: IRESS

Chart 4: US 10-Year Treasury Yield (%)



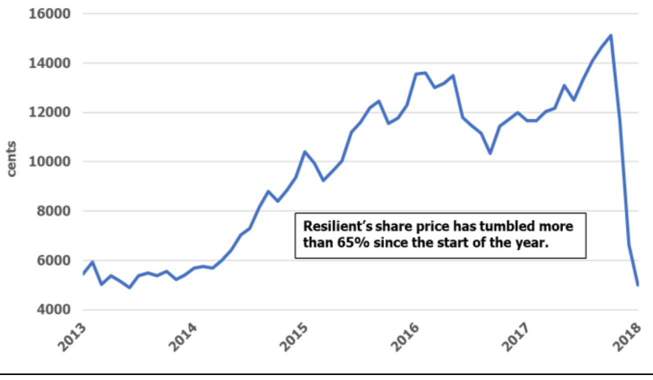
Source: IRESS

Chart 5: FTSE/JSE All Share Index



Source: IRESS

Chart 6: Resilient REIT Limited (cents)



Source: IRESS

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