INVESTMENT REVIEW

APRIL 2018

BRIDGE FUND MANAGERS

"We know what we are, but know not what we may be."
William Shakespeare

ECONOMIC OUTLOOK

The US economy expanded by 2.3% in the first quarter of 2018 (chart 1). Although the rate of growth was above market expectations, it does represent a slowdown following growth of 2.9% in the fourth quarter of 2017. The deceleration in growth reflected a slowdown in consumer spending and residential investment. The rate of growth was, however, higher than in the corresponding period in both 2016 and 2017, confirming the US Federal Reserve's (the Fed) latest assessment on the improving health of the economy and the need to continue raising official interest rates. US consumer inflation has been rising steadily since the middle of last year and is now above the Fed's targeted rate of 2% (chart 2).

Amid growing uncertainty about Brexit, the UK's economy expanded by just 0.1% in the first quarter of 2018, the slowest growth of any economy in Europe. The slower growth will allow the Bank of England to hold off raising interest rates when they meet again in May. According to some economists, the UK could experience a mild recession if it failed to reach a deal with the European Union. Inflation could also surge above 3%, which would place significant pressure on the Bank of England to raise official interest rates. Brexit negotiations have stalled on the Irish border issue and are at risk of breaking down completely.

Index	April %	12m %	YTD %
Dow Jones	0.3	18.1	-1.6
S&P 500	0.4	13.3	-0.4
FTSE 100	6.4	4.2	-2.3
EURO STOXX 50	5.8	2.0	1.8
Nikkei 225	6.2	17.0	-1.3
Hang Seng	2.4	25.2	3.0
Australia	3.5	2.1	-1.6

Source: IRESS

In South Africa, consumer confidence rose to record levels in the first quarter of 2018. The FNB/BER's consumer confidence index increased by 34 points from -8 in the fourth quarter of 2017 to 26 in the first quarter (chart 3). The reading surpassed the previous record of 23 index points, achieved in the first quarter of 2007 when South Africa's economy was growing by more than 5%. The surge in the value of the index, which has been in negative territory for the past 3 years, reflects increased optimism following Cyril Ramaphosa's victory at the ANC's elective conference in December last year.

South Africa's consumer inflation rate dropped further to 3.8% in March, from 4.0% in February (chart 4). Lower food price inflation and a significant drop in the price of petrol and diesel in March were the main contributors to the lower inflation print. Consumer inflation is expected to start rising again in April, following a 1% increase in VAT, higher petrol and diesel prices and a lower base for food prices. Inflation is likely to remain within the South African Reserve Bank's (SARB) targeted range of between 3% and 6% throughout 2018 and 2019, but is unlikely to prompt the SARB to cut official interest rates again.

MARKET OUTLOOK

Global equity market volatility has risen significantly since the start of the year. During 2017, the S&P 500 increased or decreased by more than 1% in a single day on just 8 occasions. After just four months in 2018, the S&P 500 has increased or decreased by more than 1% in a single day on 31 occasions. The Chicago Board Options Exchange's volatility index (VIX) has risen as high as 50 index points during 2018, only the second time it's been that high since it peaked at close to 80 index points in October 2008, at the height of the global financial crisis. Investors are concerned about the prospect of higher interest rates in the US, rising global bond yields and increased tariffs as the US and China appear to have entered a trade war.

The yield on 10-year US Treasury notes topped 3% for the first time since January 2014 (chart 5), although it was unable to hold above that level and closed the month at 2.96%, an increase of more than 20 basis points. With inflation rising, due to higher commodity prices and higher expected official interest rates in the US, bond yields are expected to continue rising in 2018. Global listed property markets staged a modest recovery during April after US REITs posted stronger earnings numbers during the first quarter. Following a period of relative underperformance, current listed property valuations are attractive relative to global bonds.

Index	April %	12m %	YTD %
All Share	5.4	11.4	-0.9
Resources	8.7	20.0	4.5
Financials	3.2	17.2	-0.4
Industrials	5.2	5.7	-3.2
Property	7.7	-0.5	-13.4
Bond	-0.7	13.7	7.3
Cash	0.6	7.4	2.3

Source: IRESS

South Africa's equity market rallied in April on the back of a weaker rand and higher commodity prices. The Resources sector surged 8.7% during the month as the threat of a trade war between the US and China pushed metal prices higher. Amongst the large industrial rand-hedges, Richemont's share price soared 11.4%, while Naspers posted a more modest 5.8% gain. Bucking the trend, British American Tobacco's share price declined a further 1.3% in April and is now down 17.2% since the start of the year (chart 6). For the year to date, South Africa's equity market is now down just 0.9%.

The yields on South African bonds rose in April as the rand weakened and 10-year US Treasury yields moved closer to 3%. The yield on government's benchmark R186 bond rose to 8.18% from 7.99% at the end of March. A substantial rebound in the share prices of the Resilient group of companies meant listed property was the best-performing asset class in April, returning 7.7%. Resilient announced that it would unbundle its stake in Fortress B to simplify the group's structure. Fortress remains a substantial shareholder in Resilient. The one-year forward yield on South African listed property is now 7.9%.

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

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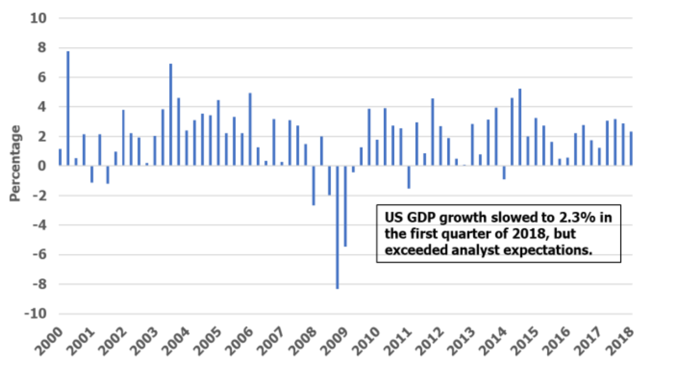
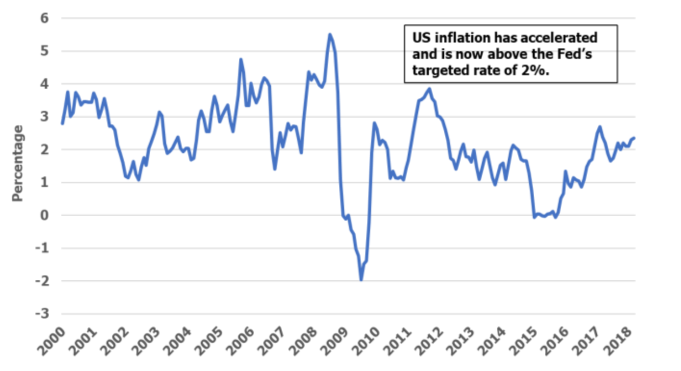
CHARTS

Chart 1: US Federal Funds Rate (%)



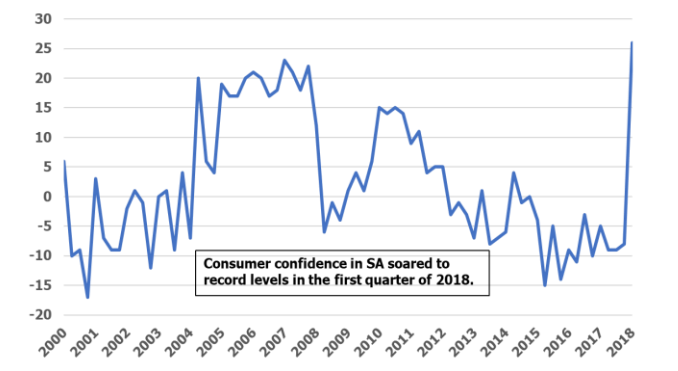
Source: IRESS

Chart 2: US Consumer Inflation (%)



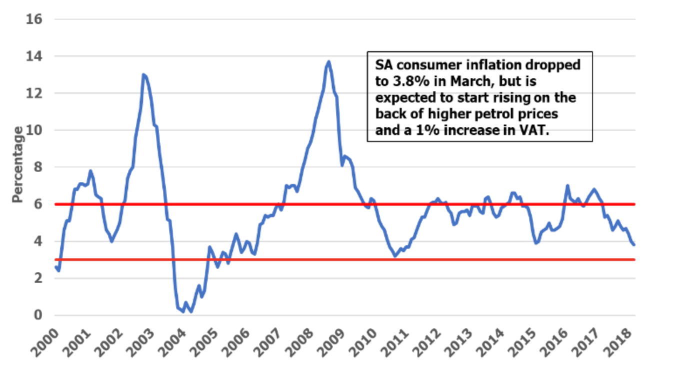
Source: IRESS

Chart 3: FNB/BER Consumer Confidence Index



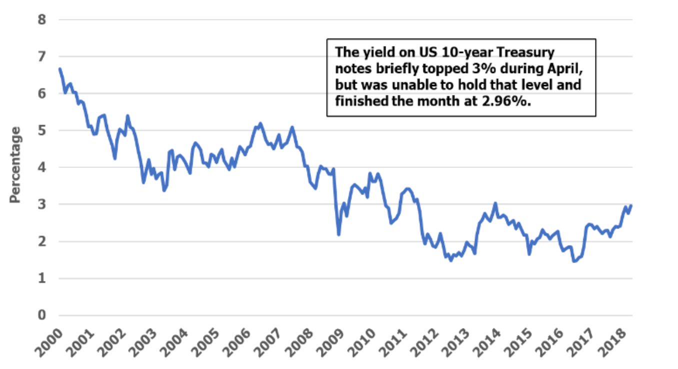
Source: IRESS

Chart 4: SA Consumer Inflation (%)



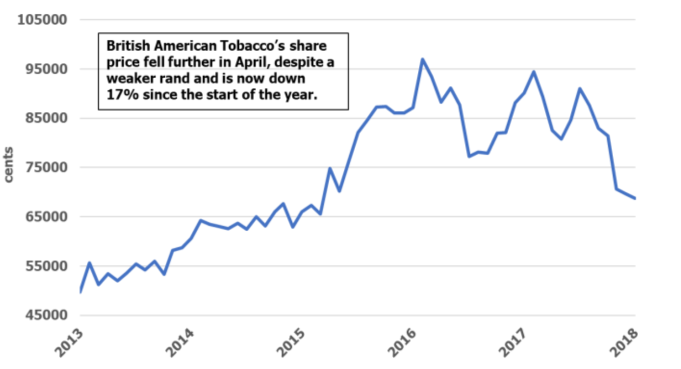
Source: IRESS

Chart 5: US 10-year Treasury Yield (%)



Source: IRESS

Chart 6: British American Tobacco plc (cents)



Source: IRESS

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