OVERBERG MARKET REPORT

Tuesday 16th February 2021

IN THIS WEEK'S BOTTOM LINE

Contributed by Gielie Fourie

- On Thursday evening, 11 February 2021, pres. Ramaphosa delivered his 2021 State of the Nation address in parliament. Read more in the Bottom Line.

SOUTH AFRICA ECONOMIC REVIEW

Contributed by Werner Erasmus

- Mining production increased slightly by 0.1% year-on-year in December. This marked the first annual increase since February 2020 with the main contributors to the December print being manganese ore, diamonds, and coal. In contrast, platinum group metals (PGMs) were the biggest drag on growth. The industry contributes roughly 7% of South Africa's Gross Domestic Product (GDP), but its share has been steadily declining in recent years. Seasonally adjusted mining production decreased 0.5% in the fourth quarter of 2020 compared with the third quarter. For 2020 as a whole, mining production was down by 10.7% year-on-year – the worst overall annual contraction on record. Despite this and other existing economic challenges, total seasonally adjusted mining mineral sales values grew by 9.9% year-on-year measuring R607bn in 2020. Mining export sales values were robust, measuring R570bn up from R459bn in 2019. Looking forward, mining activity should be supported by favourable commodity prices and the anticipated global growth recovery, mainly from South Africa's major trading partners in the near term. Nevertheless, risks exist given the uncertainty about the pandemic's path, delays in vaccine rollouts, vaccine efficacy, unreliable electricity supply and regulatory uncertainty.

- Manufacturing production rose 1.8% year-on-year in December, its first year-on-year increase recorded since May 2019. This too was better than expectations for a decline of 1.2%. Encouragingly, nine out of 10 major manufacturing sectors showed an annual increase in production during December. The increase was largely driven by the production of food and beverages, motor vehicles, basic iron and steel, and wood products. Compared to the third quarter, manufacturing production increased by 5.2% in the final quarter of 2020. However, for the full year, factory output was 11% lower compared to the previous year – the worst performance since the height of the global financial crisis in 2009. Although the South African growth recovery lost some momentum towards the end of 2020, incoming data suggests that the level of Gross Domestic Product (GDP) is set to have increased further in the fourth quarter of 2020, after the impressive initial rebound in the third quarter. For local manufacturing to prosper in the longer-term, government needs to implement measures that meaningfully improve the outlook for industrial activity. These measures include stable electricity supply, deregulation of most business sectors, and progress on government's infrastructure development programme.

- Business Confidence as measured by the South African Chamber of Commerce and Industry (SACCI) increased marginally to 94.5 in January up from 94.3 in December. Nevertheless, the average business confidence for 2020 declined to 86.5 from 92.6 in 2019-the lowest level seen in 35 years. The previous low was in 1985 when the United Nations Security Council called on members to introduce more far-reaching economic sanctions against South Africa over its apartheid policies. South Africa's economy probably contracted the most in at least nine decades last year after lockdown measures shuttered some economic activity for months, leading to business closures, a surge in unemployment and a slump in business confidence. Finance Minister Tito Mboweni's Feb. 24 budget will be a watershed event and should pay urgent attention to implementing medium-term corrections, adjusting public-sector finances, and putting the economy on a growth trajectory, Sacci said. Capital markets are sceptical of the government's plans to rein in expenditure and return public debt to sustainable levels. That means "the only way out of this predicament is to enhance private-sector fixed investment, provide credible economic policy that improves confidence in economic growth prospects, and reduce the role of the state to lessen borrowing levels and public debt servicing costs," the chamber said.

SOUTH AFRICA: THE WEEK AHEAD

Contributed by Werner Erasmus

- Inflation, due Wednesday 17 February. Inflation, as measured by the Consumers Price Index (CPI), is expected to have accelerated slightly in January 2021 after moving closer to the lower band of the South African Reserve Bank's (SARB's) target range of 3-6% in December. The consensus is for CPI to increase 3.3% year-on-year and 0.2% month-on-month in January as the global and domestic economy recover from the pandemic's historical lows and because of food and fuel price increases in January. The SARB stated during its January monetary policy committee (MPC) meeting that it believes inflation is under control and does not feel that there are demand-side pressures building in the economy.

- Retail Sales, due Wednesday 17 February. The annual rate of contraction in retail sales is expected to have slowed to 2.5% year-on-year in December 2020 following the disappointing November figures when retail sales recorded a decline of 4% year-on-year despite the Black Friday promotion. This continued deterioration of retail figures is expected because of the pressure on households' disposable income, the added lockdown restrictions limiting alcohol sales in late December, and depressed consumer confidence.

GLOBAL

Contributed by Nick Downing

- The CRB Commodities Index has surged by 20% over the past three months, building on gains stretching back to the low point in March last year. Surprisingly, the rally has been broad based with all 19 commodities making up the index showing gains. The sharp rally in commodity prices is attributed to growing confidence in a powerful economic recovery, boosted by the successful rollout of vaccination programmes amid continued fiscal spending and monetary accommodation. While demand for commodities is expected to rise, the prospects for a weakening US dollar and rising inflation are also supportive. Commodities are priced in dollars and so benefit from a weakening currency. Commodities also provide a natural hedge against inflation. Meanwhile, supply capacity has been eroded over the past ten years due to a lack of new investment activity. Some analysts believe commodities may be on the cusp of a new "super-cycle", like the one experienced in the five years to 2008 due to China's rapid industrialisation. A super-cycle is more powerful and longer lasting than a normal cycle and could be powered by the record levels of fiscal expenditure, much of which will be directed towards infrastructure spending. The positive outlook especially favours the so-called "green" commodities, such as copper, platinum and nickel, which play an important role in renewal energy and electric vehicles. Platinum, which is used in hydrogen fuel cells, has enjoyed a 20% rally since the start of the year, lifting the price past the $1300 level for the first time in 6 years.

NORTH AMERICA

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- The University of Michigan US consumer confidence index slipped from 79.0 in January to 76.2 in February its lowest since August and still well below the pre-pandemic level of 101.0 recorded last February. The decline is attributed to a sharp drop in the expectations index, measuring anticipated conditions in 6 months' time, which fell from 74.0 to 69.8. The current conditions index was more resilient, dipping from 86.7 to 86.2. The setback in consumer sentiment was concentrated in the lower-income households, but these are most likely to benefit from government aid packages which include once-off check payments and enhanced unemployment benefits. President Biden's proposed $1.9 trillion fiscal stimulus should therefore go a long way towards shoring up consumer confidence, which is a vital component of economic growth. Consumer spending comprises a third of US GDP. Consumer confidence and household spending should recover quickly once the third fiscal aid package is implemented and as social distancing restrictions are lifted. In an early signal of a recovering trend, retail sales increased in January by 1% month-on-month, marking the first gain in three months.

- In a speech last week Federal Reserve chairman Jerome Powell stressed that President Biden's proposed fiscal stimulus package would not bring about an enduring surge in inflation. He stated that the conditions for reducing monetary accommodation, including a full return to pre-pandemic employment levels and for inflation to exceed the 2% average inflation target (AIT) for some time, remain a long way off. Powell stated that "published unemployment rates during Covid have dramatically understated the deterioration in the labour market." Federal Reserve Bank of San Francisco president Mary Daly welcomed the increase in financial market inflation expectations, attributing them to a large extent to the Fed's policy shift from an inflation ceiling of 2% to an inflation average of 2%. Tom Barkin, president of the Federal Reserve Bank of Richmond expressed concern over deflationary as well as inflationary risks. Despite rising inflationary expectations, actual inflation data remains subdued. The Fed's preferred measure, the core personal consumption expenditures index remained at 1.5% in December. Meanwhile, the widely followed core consumer price index, which excludes food and energy prices due to their volatility, remained unchanged in January on a month-on-month basis for a second straight month, rising year-on-year by just 1.4%. The week's "Fed talk" and accompanying data appear to support the Fed's earlier December statement that current ultra-accommodative policy will likely remain in place until 2023.

- President Biden's proposed $1.9 trillion pandemic aid package is currently being discussed in House committees prior to heading for open debate and ratification in the two chambers of Congress. Biden is anxious to avoid the risk of doing too little and perhaps he is the man for the job having learnt the hard way as Vice-President in the Obama administration when the government failed to provide enough fiscal support following the 2008/09 Global Financial Crisis. Several economists have argued, including Fed chair Jerome Powell, that the headline unemployment rate of 6.3% belies the actual damage to the labour market. The bottom income-earners are suffering a much higher unemployment rate, estimated to be closer to 20%. Meanwhile, the Congressional Budget Office has published the beneficial impact of the fiscal aid packages enacted last year, which have resulted in far stronger than expected economic growth. For instance, the $900 billion aid package approved in late December has only added $448 billion to the CBO's estimated budget deficit for the current financial year, illustrating the payback from increased economic output and tax revenues. The deficit also appears affordable. Despite federal debt exceeding 100% of GDP, the CBO estimates net interest costs as a share of GDP will average a surprisingly low 1.2% over the next 5 years, due to historically low interest rates.

CHINA

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- Producer price inflation (PPI) turned positive in January on a year-on-year basis for the first time since February last year. Following 11 straight months of deflation, PPI registered a positive reading of 0.3% on the year. On a month-on-month basis it increased by 1.0%. The data is encouraging and signals a continuation of the positive trend in industrial output as well as a recovery in company earnings growth. Consumer price inflation (CPI) provided contrasting fortunes showing a negative year-on-year reading of minus 0.3%, although the timing of the Lunar New Year may have played a part, landing in January last year rather than February. Prices tend to jump during the festive period. Analysts expect inflation to recover quickly to around 2% but the People's Bank of China (PBOC) 3% CPI target may remain elusive until consumer spending regains its pre-pandemic levels. The economic rebound has so far been concentrated in the industrial sector. For household spending to join the party may require additional monetary and fiscal support, and success in the vaccine rollout. So far, vaccinations have been slower than expected, numbering 40 million inoculations, well below Beijing's target of 100 million by this time.

JAPAN

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- Japan's economy continued its recovery in the last quarter of the year, albeit at a slower pace compared to the third quarter. Gross domestic product (GDP) expanded by 3% quarter-on-quarter in the fourth quarter, below the 5.3% reported in the third quarter, but beating the expected 2.3%. Compared to the same period a year ago, the economy shrank 1.2% and 4.8% for the whole of 2020, placing Japan ahead of the UK and EU, but behind the 3.5% contraction in the US. Growth in the fourth quarter was driven by a recovery in private consumption, up 2.2% quarter-on-quarter and contributing 1.2% points to the growth in output for the quarter. Business investment (+4.5%) and capital expenditure (+3.2%) were two other contributing factors. Exports increased 11% quarter-on-quarter while imports only grew 4.1%, increasing Japan's net external position. While Japan seems to be well on its way to a V-shape recovery, the latest state of emergency will put a dampener on growth in the first quarter. However, the approval of a vaccine and the imminent roll-out to health care workers together with a steady decline in infection rates bodes well for a sustained recovery for the rest of the year with a boost from the summer Olympics later this year. The Nikkei 225 has gained 7.6% since the start of the year and has crossed the 30,000 points mark for the first time since 1990, reflecting growing investor confidence that a swift recovery is likely.

EUROPE

Contributed by Carel la Cock

- In its latest projection, the European Commission (EC) has revised downwards its 2021 economic growth forecast for the eurozone but estimates that the recovery will be sustained in 2022. The economy in the bloc is expected to expand by 3.8% both this year and in 2022, compared to 4.2% in 2021 and 3% in 2022 in earlier forecasts made in November. The EC stated that "there is light at the end of the tunnel" and that the region will return to pre-pandemic levels earlier than previously expected in large thanks to the successful roll-out of the vaccine thus far which will lead to a quicker easing in lockdowns. The economy is expected to make a full recovery to pre-pandemic levels by mid-year 2022 compared to 2023 previously forecasted. Inflation is forecasted to accelerate from 0.3% in 2020 to 1.4% in 2021 because of the temporary base effect of low inflation in 2020, but will moderate in 2022 to 1.3%, still well below the European Central Bank's 2% target. The expected growth in the eurozone is set against a backdrop of GDP growth in the rest of the world of 5.2% in 2021 and 3.8% in 2022 after contracting 3.4% in 2020. Within the EU, the larger nations will have different trajectories. Spain (5.6%), France (5.5%) and Italy (3.4%) will have faster growth this year following steeper declines last year, while both Germany and France will return to pre-pandemic levels this year. The EC has stressed that the region will have to step up its vaccination roll-out efforts otherwise the latest forecast will be undermined. Paolo Gentiloni, the EU's economics commissioner has warned that the 70% minimum vaccination of the adult population by the summer will be "quite challenging". The forecast also assumes that supportive monetary and fiscal policies remain in place for the duration of the year, stressing that an early withdrawal could pose a mayor threat to the recovery. The EU's €750bn recovery fund, which has not been completely accounted for in the forecast due to insufficient data, is set to start paying out this summer and will give an extra boost to the recovery. Some analysts expect that there could be an upside surprise if lockdown measures are lifted sooner given historically high household savings, low financing costs and supportive policies.

UNITED KINGDOM

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- UK GDP expanded by 1% quarter-on-quarter in the fourth quarter of 2020, beating expectations of 0.5% growth, but falling well short of the 16.1% recovery in the third quarter. The economy shrank 9.9% in 2020, recoding the worst fall in output in over 300 years, but green shoots towards the end of last year have prompted "cautious optimism" for a sustained recovery this year from chancellor Rishi Sunak. Compared to the same quarter last year, the economy fell 7.8% in the fourth quarter and fared much worse than its peer group in the G7 nations, highlighting the devastating impact of the pandemic that has caused longer and more stringent lockdowns than the US for example. The latest restrictive measures will likely cause another contraction at the start of this year, but the UK has been more successful than Europe with its vaccine rollouts and a strong recovery in the second and third quarters of the year could mean economic growth will outstrip that of the EU. UK household incomes have remained largely intact thanks to the government's extended furlough schemes and will help to propel the economy forwards once lockdowns ease. Services, production and construction output all showed growth in the last quarter and are set to continue on the path of recovery in the first quarter of the year. Household consumption contracted by 0.2% on the quarter and 10.7% for the full year reflecting the fall in spending on leisure activities in the last quarter but also the stringent lockdown measures throughout the year. Business investment improved in the fourth quarter adding to GDP growth, but was still 10.3% below pre-pandemic levels with anecdotal evidence suggesting that only investment on essential equipment and maintenance is taking place. Imports in the final quarter of the year outpaced that of exports, causing the balance of payments to widen further. Although the latest lockdown measures have negatively impacted economic growth, they have not been as severe as the first lockdown and highlight how quickly the economy has adapted to functioning under restricted measures, which bodes well for any future flare ups.

KEY MARKET INDICATORS (YEAR TO DATE % AND LEVEL)

JSE All Share	+ 12.99	67124
JSE Fini 15	+ 5.66	12743
JSE Indi 25	+ 15.11	89672
JSE Resi 20	+ 13.71	65469
R/$	+ 1.65	14.46
R/€	+ 2.39	17.53
R/£	- 0.08	20.10
S&P 500	+ 4.76	3934
Nikkei	+ 9.62	30084
Hang Seng	+ 10.81	30173
FTSE 100	+ 4.58	6756
DAX	+ 2.85	14109
CAC 40	+ 4.23	5786

MSCI Emerging	+ 11.34	1437
MSCI World	+ 5.19	2829
Gold	- 3.62	1825
Platinum	+ 15.91	1240
Brent oil	+ 22.22	63.31

BOTTOM LINE

Contributed by Gielie Fourie

- STATE OF THE NATION ADDRESS (SoNA): Due to the Covid-19 restrictions, only 50 people could attend the SoNA. Pres. Ramaphosa started his fifth SoNA by referring to the Covid-19 pandemic and the terrible hardships of our nation during the past year. He likened our nation to our unique fynbos and the protea. He added: "What is most unique and special about fynbos is that to be sustainable and survive, it needs fire. Like the hardy fynbos, we too have proven to be resilient in many ways."

- FOUR FOCUS AREAS: Pres. Ramaphosa: "This is no ordinary year, and this is no ordinary State of the Nation Address. I will therefore focus this evening on the foremost, overriding priorities of 2021… First, we must defeat the coronavirus pandemic. Second, we must accelerate our economic recovery. Third, we must implement economic reforms to create sustainable jobs and drive inclusive growth. And fourthly, we must fight corruption and strengthen the state."

- FIRST - DEFEAT THE CORONA VIRUS: Pres Ramaphosa: "The health and safety of our people remains our paramount concern. All medication imported into the country is monitored, evaluated, investigated, inspected, and registered by the South African Health Products Regulatory Authority. The success of the vaccination programme will rely on active collaboration between all sectors of society… We are greatly encouraged by the active involvement of business, labour, the health industry and medical schemes in preparing for this mass vaccination drive."

- SECOND – ACCELERATE ECONOMIC RECOVERY: Pres. Ramaphosa said that when he delivered the 2020 SoNA, none of us could have imagined how – within a matter of weeks – our country and our world would have changed so dramatically. Our plans had to be adapted in response to a global emergency. Budgets had to be reprioritised and many programmes had to be deferred. Over the past year, South Africa has experienced a sharp decline in growth and a significant increase in unemployment. Poverty is on the rise. In the third quarter of 2020, our economy was 6% smaller than it was in the last quarter of 2019. Our unemployment rate now stands at a staggering 30.8%. As a result of the relief measures that we implemented and the phased reopening of the economy, we expect to see a strong recovery in employment by the end of 2020.

- THIRD – IMPLEMENT ECONOMIC REFORMS: Pres. Ramaphosa said that government has taken extraordinary measures to support ordinary South Africans, assist businesses in distress and protect people's livelihoods. The social and economic relief package introduced in April last year was the largest intervention of its kind in our history – about 10% of our GDP – to provide cash directly to the poorest households, to provide wage support to workers and to provide various forms of relief to struggling businesses. A total of 18 million people, or close to one-third of the population, received additional grant payments through these relief measures. Around R18.9 billion in loans have been approved for 13,000 businesses through the loan guarantee scheme. FOURTH - FIGHT CORRUPTION: Ramaphosa mentioned that corruption is one of the greatest impediments to the country's growth and development. The revelations from the Zondo Commission of Inquiry laid bare the extent of state capture and related corruption. Testimony at the Commission has shown how the criminal justice system was compromised and weakened. The Special Investigating Unit (SIU) was authorised to investigate allegations of unlawful conduct with respect to COVID procurement by all state bodies during the National State of Disaster. As it reported last week, the SIU has finalised investigations into 164 contracts with a total value of R3.5 billion.

- ECONOMIC RECONSTRUCTION AND RECOVERY PLAN: Since the launch of the plan four months ago, government has focused on four priority interventions: (1) a massive rollout of infrastructure throughout the country, (2) a massive increase in local production, (3) an employment stimulus to create jobs and support livelihoods, and (4) the rapid expansion of our energy generation capacity.

- LANSERIA SMART CITY: Since the announcement, two years ago, of government's dream of building new cities, new developments are being conceptualized. The Lanseria Smart City, the first new city to be built in a democratic South Africa, is now a reality in the making. The draft masterplan for this smart city – which will become home to between 350,000 to 500,000 people within the next decade – was completed in November 2020 and is now out for public comment.

- THE BUDGET: What the market should watch out for now is the "flip side" of the SoNA, namely Tito Mboweni's budget on 24 February. National Treasury (NT) was to a large extent absent from the SoNA. Commentators says that the NT's role in shaping the country's economic and fiscal policy seems to be waning. Firstly, NT has experienced a brain drain. Secondly, Mboweni is seen as a reluctant minister. He attends around 50% of the cabinet meetings. Thirdly, in the economic cluster, Pravin Gordhan and Ebrahim Patel have more influence than Mboweni. Mboweni was opposed to financing SAA. The fact that he gave in to Gordhan and Patel, shows that he does not have a decisive say in fiscal policy.

Ramaphosa seems to be taking over control of finances and is siding with Gordhan and Patel.

- A SKILLS CRISIS: To deliver on all his promises, Ramaphosa needs to evaluate his team. Some of his ministers are an embarrassment. He will have to replace them with a team that is fit for the purpose. In the past Ramaphosa had to appease all the factions within the ANC. He has solidified his position – he stands stronger now. Expect a cabinet reshuffle, perhaps after the budget in two weeks' time. SUMMARY: Ramaphosa ended by referring to his introduction - the ability of the fynbos and the protea to rise again after being destroyed by fires. Ramaphosa: "As we prepare for the difficult path ahead, we can draw strength From Maya Angelou's great poem 'I rise'. People of South Africa, it is your country that calls on you to rise."

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