OVERBERG MARKET REPORT

Tuesday 11th May 2021

IN THIS WEEK'S BOTTOM LINE

Contributed by Nick Downing

- The ruling elite needs to live up to the "Proudly South African" maxim. The ANC's decision that Secretary General Ace Magashule step aside is a good start. Even better would be if politicians generally were able to "step aside" from their interventionist economic policies, which are the death knell of jobs growth. Read more in the Bottom Line.

SOUTH AFRICA ECONOMIC REVIEW

Contributed by Werner Erasmus

- The IHS Markit whole-economy PMI increased to a nine-year high of 53.7 index points in April, from 50.3 in March. The headline IHS Markit PMI is a composite indicator of private sector business performance. It is derived from indicators for new orders, output, employment, suppliers' delivery times, and stocks of purchases. Any figure greater than 50 indicates an overall improvement in the sector. The May reading is encouraging and points to the strongest expansion in the country's private sector since March 2012 with all five subcomponents of the PMI in positive terrain. The two largest contributors to the May PMI figure, the Output and New Orders Indices, both rose sharply during the month and to multi-year highs. As a result of global markets continuing their recovery from the Covid 19 pandemic, firms expanded their staff levels for the first time in a year and a half. Meanwhile, increasing demand for inputs and widespread reports of supply problems contributed to a steep rise in purchasing costs in April, with the rate of inflation increasing to the highest in nearly five years. Also, output charge inflation accelerated markedly from March. Finally, business confidence jumped to the highest since July 2015, amid hopes that the COVID-19 pandemic will end and that business conditions will improve. The outlook for the overall economy remains positive as other major economies reopen, and the vaccine roll-out continues globally. Nevertheless, it remains to be seen if South Africa can continue its recovery amidst an uncertain political environment, unstable electricity supply, and the potential of a third Covid-19 wave.

- South Africa's main budget deficit for the 2020-21 fiscal year was smaller than the government projected. Treasury earlier projected a deficit of 14%, but in the end, South Africa recorded a shortfall of 11.2% of GDP. The smaller deficit comes as main budget spending for 2020/2021 was R16.2bn less than the February estimate and revenue collected by the tax agency exceeded forecasts for the first time in five years. That allowed the Treasury to announce a R900m cut to its weekly debt auctions on Monday, the second reduction in the amount on sale since March. The Treasury said in February that achieving a primary budget surplus was its most critical fiscal anchor. It projected a positive primary balance of 0.1% of GDP in 2024/2025, which will allow the government to stabilise the debt ratio at 88.9% of GDP in the following year.

SOUTH AFRICA: THE WEEK AHEAD

Contributed by Ingrid Breed

- Manufacturing Production, due Tuesday 11 May. The manufacturing output data for March is expected to show an improvement with the consensus forecasting that it increased 0.7% year-on-year and 0.8% month-on-month compared with contractions of 2.1% year-on-year and 1.2% month-on-month in February. This anticipated improvement is in line with the PMIs which have shown an improvement over the reporting period.

- Mining Production, due Thursday 13 May. The consensus forecast is that mining production recorded a strong 15.8% year-on-year expansion in March, benefitting from last year's low base when production only increased by 0.8%. On a month-on-month basis production is expected to have recorded a slight contraction of 1.8%.

GLOBAL

Contributed by Nick Downing

- Commodity prices are booming. The S&P GSCI composite commodity index has almost doubled over the past 12 months, powered by increases across oil, metals and agricultural commodities. The price gains are attributed to the reopening of economies and pent-up demand, fuelled further by massive fiscal stimulus. Investors are also drawn to commodities due to their natural hedge against rising inflation risks and to their hedge against the potential for US dollar weakness. Copper has captured the attention of the investment community over the past week after breaking above its previous all-time high recorded in 2011 during the commodity "super-cycle", which was led by China's rapid industrialisation. While copper and other metal prices are showing the characteristics of another super-cycle, most economists are sceptical as China is transforming from an investment-led to a consumer-led economy. However, other economies are taking up the baton helped by extravagant infrastructure spending plans and the race towards a net zero carbon footprint within the next 30 years. The mass adoption of renewable energy and electric vehicles will lead to a step change in demand for copper and other key "green" metals. Meanwhile, the hangover from the last super-cycle means mining companies have been reluctant to develop new capacity. Due to the extended period taken to develop new mines, the existing supply constraints may last several years and potentially squeeze commodity prices even higher. Ivan Glasenburg, CEO of Glencore said the copper price needs to rise another 50% from current levels to unleash the new capacity required to meet burgeoning demand forecasts.

NORTH AMERICA

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- The monthly increase in nonfarm payrolls slowed dramatically in April to just 266,000 well below the consensus forecast of 1 million new jobs and the downwardly revised figure of 770,000 in March. The unemployment rate inched higher from 6.0% to 6.1% as more people entered the labour market. Total employment is still down by 8.2 million compared with February 2020. The employment data surprise is attributed to enhanced unemployment benefits of $300 a week which run until September, creating a disincentive to work in lower paying jobs. Home child-care and continued fear of the Covid virus are also keeping people from joining the labour market, contributing to the unusual combination of labour shortages and high unemployment. Average hourly earnings unexpectedly increased in April by 0.7% month-on-month, supporting the anecdotal evidence of rising labour shortages in certain sectors. Despite the extenuating circumstances, the subdued labour data should help ease fears of an over-heating economy and its inflationary risks and anxiety over the Federal Reserve lifting its accommodative monetary policy settings earlier than expected. The jobs data should also add extra impetus to Joe Biden's proposed infrastructure spending plans.

- In its semi-annual Financial Stability Report, the Federal Reserve stated that Covid 19 was the biggest threat to financial stability but also warned against high asset valuations and the risk of significant declines. The Fed had issued a warning over inflated asset prices in its last report in November. Prices have moved even higher since then. According to the report, "Should risk appetite decline from elevated levels, a range of asset prices could be vulnerable to large and sudden declines, which can lead to broader stress to the financial system." The listing boom in special-purpose acquisition vehicles (SPACS) was cited as evidence of unusually high investor risk appetite. The Fed's report also highlighted difficulty in monitoring hedge fund leverage and associated risks, citing the collapse of Archegos Capital Management. Although the collapse caused several billion dollars of bank losses, the Fed was comforted by the general health of bank balance sheets and household finances. Moreover, the Fed advised that businesses were well positioned to service their debt with help from strong earnings growth and low interest rates.

- Treasury Secretary Janet Yellen spooked financial markets which are anxious that the Federal Reserve sticks to its accommodative monetary policy guidance, when she said, "It may be that interest rates will have to rise somewhat to make sure that our economy doesn't overheat". As it stands, the Fed expects the fed funds rate will remain at its current setting of 0-0.25% until 2024. Political appointees do not usually interfere with Fed policy and given the statement's impact on financial markets she quickly offered further explanation later the same day, mirroring Fed chair Jay Powell's view that inflationary pressures would not be persistent. She also added that Joe Biden's $4 trillion infrastructure and social development spending plans would not lead to an over-heating of the economy as spending would be spread out over 8-10 years. Moreover, the planned expenditure would enhance productivity, thereby constraining inflation.

CHINA

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- China posted upbeat economic data over the past week. Trade volumes continued to surge, with exports rising in April by 32.3% year-on-year up from 30.6% in March. Exports to Southeast Asian countries were especially strong, rising by 40% on the year. China's imports also gained by a solid 43.1% on the year, attributed to surging commodity prices but also recovering domestic demand. Consumer spending, the relative laggard in China's post pandemic recovery, appears to be making a comeback with anecdotal evidence of significant growth in tourism travel and box office expenditure in May's Labour Day holidays. The Caixin/ISM service sector purchasing managers' index (PMI) also surged higher in April from 54.3 to 56.3 its highest in five months, indicating increased expenditure on consumer services. In contrast with last year, consumer spending is likely to take over from manufacturing as the main driver of China's economy in 2021. Nonetheless, the manufacturing Caixin PMI also gained in April from 50.6 to 51.9, contributing to an increase in the composite PMI from 53.1 to 54.7, well above the neutral 50-level which demarcates expansion from contraction. However, Wang Zhe, senior economist at Caixin cautioned against rising inflationary pressures, "In the coming months, rising raw material prices and imported inflation are expected to limit policy choices and become a major obstacle to the sustained economic recovery."

JAPAN

Contributed by Carel la Cock

- Japan's Consumer Confidence Index declined in April, falling by 1.4 points to 34.7 and breaking the upward trend that started in February. Consumer optimism was down across all sentiment sectors - Overall Livelihood (-1.1), Income Growth (-0.6), Employment (-1.9) and Willingness to buy durable goods (-1.9). The percentage of respondents expecting prices to rise in the year ahead increased by 4.7% points to 76%, marking the highest level since February 2020. Only 6.3% of respondents expect prices to go down, falling by 2.7% from March. The latest survey results points to ongoing pessimism amongst Japanese consumers. However, high savings ratios recorded last year, and the expectation of higher prices could become the catalyst for a consumer led recovery as the global economy starts to build momentum.

- Japanese private service sector activity continued to stabilise in April according to the latest Jibun Bank Flash Japan Services PMI. The headline Services Business Activity Index, tracking the change in the volume of business activity from the month before, came in at 49.5 compared to 48.3 in March and just below the key 50-level separating expansion from contraction. Demand for services has stabilised and is back at levels last recoded at the start of 2020, before the covid-19 pandemic became widespread. It marks the lowest contraction in business activity in 15 months and reflects the lower restrictions on firms during April, partly offset by the reintroduction of certain restrictions at the end of the month. Encouragingly, employment levels improved for a third straight month and job creation was the strongest in two years. Costs were also notably higher, driven by higher staff costs and raw materials but were passed on to customers, leading to services price inflation for the first time since February 2020. Overall firms in the private service sector expect activity to keep expanding in the year ahead and remain confident that a successful vaccination program would support a further recovery in demand.

- Meanwhile, Japanese manufacturing expanded in April and showed the strongest improvement in operating conditions since 2018. The Jibun Bank Manufacturing PMI reading at 53.6 in April was 0.9 points higher than March and the highest since April 2018. Production volumes improved and output saw a third monthly improvement and at the fastest pace in three years. An uptick in demand has been singled out as the main driver and anecdotal evidence points to an increase in client confidence in both domestic and international markets as the global economic recovery gets underway. Employment levels also expanded as firms anticipates higher order volumes although the rate of new positions created was only marginally higher overall. Upward pressure on input prices continued in April leading to the rate of inflation rising to the highest since November 2018. Firms passed on the increased costs to clients marking the fifth consecutive month of higher output prices. Looking ahead, manufacturers reported increased confidence about business conditions in the next twelve months based on the belief that a broad economic recovery will be realised once the pandemic is over.

EUROPE

Contributed by Carel la Cock

- The eurozone's economy contracted for a second consecutive quarter at the start of the year, leading the single currency block to slide into a technical recession for a second time in the past year. The economy contracted by 0.6% quarter-on-quarter following the 0.7% fall in the last quarter of 2020 and came off the back of a resurgence in covid-19 cases at the start of the year with more stringent lockdown measures to prevent a third wave of infections. Germany, the largest economy in the eurozone, reported a 1.7% quarter-on-quarter contraction with higher manufacturing exports more than offset by lower consumer spending. In Spain, household consumption and subdued manufacturing, and in Italy, lower services sector activity, caused both economies to suffered similar fates, contracting 0.5% and 0.4% respectively. Portugal fared even worse, contracting 3.3% following the spike in covid-19 cases in the first quarter. France managed to buck the trend, reporting growth of 0.4% and helped by improved consumer spending and a recovery in construction. Expectations for a swift recovery in the second half of the year remain intact and supported by the latest PMI survey results. The Eurozone Composite Output Index was stable at 53.8 in April while the Eurozone Services Business Activity Index showed an expansion in April, rising from 49.6 in March to 50.5. Economists expect a consumer driven recovery this year, predicting that consumers will unleash an additional €170bn in spending as they whittle down their excess savings from last year. The recovery expectation is underpinned by increased vaccinations which will lead to further relaxing of restrictions. The European Central Bank (ECB) expects the economy to expand by 4% and 4.1% in the next two years, returning to pre-pandemic levels by 2022.

UNITED KINGDOM

Contributed by Carel la Cock

- Economic growth in the UK is expected to be better than previously expected according to the latest meeting notes from the Monetary Policy Committee (MPC). Andrew Bailey, Bank of England (BoE) governor, said that the central bank expects gross domestic product to grow by 7.25% this year, improving from the expected 5% growth predicted only three months ago. The faster recovery will be driven by a recovery in consumer spending while unemployment will ease from a previously expected peak of 7.75% to a new expected peak of 5.5%. Inflation is expected to rise from the current 0.7% hitting the 2% target later this year and is likely to then recede. However, the BoE has indicated that it will wait for signs of sustained inflationary pressure before thinking about hiking rates. Consequently, the Monetary Policy Committee (MPC) voted to keep the benchmark interest rate at 0.1%. Markets are pricing in a rate hike by next year only, expecting rates to remain at historic lows for the remainder of the year.

- PMI and job survey data released last week have corroborated the view of the MPC. The KPMG and REC UK Report on Jobs showed that permanent placements have improved at the fastest pace since 1997 and that the availability of candidates has dropped causing wages to rise. The improved employment conditions were due to further easing in lockdown restrictions and improved business confidence following the successful rollout of vaccinations. The UK services sector improved again in April, according to the CIPS UK Services PMI which reported a Business Activity Index reading of 61.0, up from 56.3 in March and the highest reading since October 2013. Private sector service firms confirmed the flow of pent-up demand and expect demand to improve as the successful vaccine roll-out keeps supporting consumer confidence. Signs of inflationary pressures remain a concern as many firms indicated that higher staff costs and increased raw material prices have added to their business costs rising at the fastest pace since February 2017. Manufacturing continued to expand in April, although the rate of expansion has fallen below that of the services sector. Similarly, input price inflation in the manufacturing sector, has seen average costs rising at the fastest pace since November 2017. The outlook for both services and manufacturing were the strongest since 2012.

EMERGING MARKETS AND THE FAR EAST

Contributed by Carel la Cock

- Asian countries are seeing a broad-based economic expansion according to the latest IHS Markit Asia Sector PMI figures. Of the 18 sectors being tracked, no less than 16 increased output in April and 13 indicated higher employment levels. Automobiles and Auto parts saw the quickest growth and maintained the momentum gathered in the last three quarters. Other manufacturing sectors such as chemicals, technology equipment, machinery and equipment and household and personal use chemicals all showed promising growth, outpacing the gains made in March. The April reading of the IHS Markit ASEAN Manufacturing PMI figures also showed a steep rise in output and new orders. Vietnam reported the best growth of the ASEAN nations with their PMI hitting a two and a half year high followed by Indonesia which hit a record high. Business confidence across the region was the strongest in over a year. Service sectors also improved especially in healthcare, transportation, and industrial services, but their recovery is still lagging manufacturing. As the global economy continues to gather pace, the region is well placed to benefit from higher global demand and trade.

KEY MARKET INDICATORS (YEAR TO DATE % AND LEVEL)

JSE All Share	+ 15.10	68377
JSE Fini 15	+ 5.64	12740
JSE Indi 25	+ 9.97	85665
JSE Resi 20	+ 25.25	72111
R/$	- 4.60	14.05
R/€	+ 5.35	17.04
R/£	+ 1.24	19.83

S&P 500	+ 11.51	4188
Nikkei	+ 7.56	29518
Hang Seng	+ 5.01	28595
FTSE 100	+ 10.26	7123
DAX	+ 12.26	15400
CAC 40	+ 15.03	6385
MSCI Emerging	+ 4.27	1346
MSCI World	+ 10.09	2961
Gold	- 4.18	1815
Platinum	+ 17.34	1255
Brent oil	+ 31.81	68.28

BOTTOM LINE

Contributed by Nick Downing

- It is a privilege to travel in the Covid age. Although there is the inconvenience of Covid testing before crossing borders, it is well worth the extra delay and discomfort. The nasal swab is not everyone's idea of a holiday activity. I had to endure four on a recent camping trip through Namibia and Botswana. The first test was retaken and thankfully proved to be a false positive.

- Covid is bad for tourism although some recovery is soon expected, based on the recent gains in BEACH shares (Bookings, Entertainment, Accommodation, Cruises and Hotels). For tourists though, it couldn't be better, wonderful bargains are available and it means less crowding, if a little bit of peace and quiet is what you're after.

- As long as you are happy to share your camp with hungry lions and hyenas and don't mind the occasional elephant tripping over your guy ropes, Botswana is a wonderful country to visit. It is blessed with natural splendour and boasts incredible flora and fauna. Nearly 40% of the country is made up of national parks and wildlife reserves. The sunsets and open skies are unequalled. Yet what struck me most is how the country is at peace with itself. There is no animosity or racism, foreigners are welcomed with open arms. There are no such things as farm murders, violent crime and gender-based violence. Botswana is a law-abiding nation.

In a country half the size of South Africa but with a population of just 2 million, one would not imagine social distancing to be an issue and yet everyone wears a mask. There is little litter although it is not as pristine as Namibia.

- The Botswana people are proud. The impression is that they are proud of their achievements and qualities and of the country's peace and success. The country has been a peaceful democracy since its independence in 1966, the longest surviving democracy on the continent. It is telling how few Botswana immigrants there are in South Africa. The reason is that they enjoy a much higher standard of living at home. The unemployment rate is admittedly quite high at 23% but this is due to the Covid impact on tourism, which plays a big role in the economy. Before Covid, unemployment was 18%. The fiscus is well managed, presumably helped by an absence of corruption. The budget deficit is 3.9% of GDP, and government debt to GDP is only 17.7%. These are remarkable achievements in the context of the Covid pandemic and allow for competitive taxation rates. The corporate tax rate is 22% and the marginal personal income tax rate is 25%.

- The contrasts with South Africa are stark. The unemployment rate and the marginal personal income tax rate are almost double, while the budget deficit and debt to GDP are more than quadruple. But most striking is the lack of harmony. Within 5 hours of crossing the Tlokweng border back into South Africa in the North West province, we came across service delivery protests in the town of Warrenton. Riot police were out en-masse and burnt-out vehicles were still smouldering amid widespread vandalism and other evidence of civil disobedience.

- We were reminded upon our return that South Africa is undeniably a wealthier country than Botswana, illustrated by the slick and well cambered roads, the smart game fences, shiny shopping malls and well-appointed One-Stop petrol stations, but in many respects the country is bankrupt.

- Unlike its harmonious neighbour, South Africa is not at peace with itself. There is an underlying throb of racism, farmers fear for their lives, and violent crime is a fact of life which with rising unemployment will inevitably become worse. Without en enabling environment for job creation, South Africa's unemployment rate and its Gini coefficient will deteriorate further. South Africa is a proud nation but there needs to be more evidence of this pride from the ruling elite, not the hubris that has been exposed at the Zondo commission.

- The ruling elite needs to live up to the "Proudly South African" maxim. The ANC's decision that Secretary General Ace Magashule step aside is a good start. Even better would be if politicians generally were able to "step aside" from their interventionist economic policies, which are the death knell of jobs growth. Employment growth would go a long way to restoring the country's pride. The ruling elite should behave like a pride of lions rather than a pack of hyenas and hunt their own food rather than scavenging off the scraps of others. They need to step aside from their regulations and taxes and give the private sector the incentive and confidence to create jobs.

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