Market Update Wednesday, 20 February 2019

Global Markets

Asian stocks advanced to 4-1/2-month highs on Wednesday as investors bet that Chinese and U.S. trade negotiators would be able to secure a deal to de-escalate their year-long tariff war.

MSCI's broadest index of Asia-Pacific shares outside Japan rose nearly 1.0 percent to reach its highest levels since Oct. 2. Hong Kong's Hang Seng gained 1.1 percent to six-month highs, while Korea's Kospi and Taiwan's index recovered to levels last seen in early October. Japan's Nikkei gained 0.75 percent to two-month highs.

Chinese shares rose 0.4 percent, extending their run of gains to 18 percent from their Jan. 4 trough, thanks to inflows of foreign funds.

The gains in Asia topped those in Tuesday's Wall Street session, where the S&P 500 gained 0.15 percent, helped by upbeat results from Walmart. The Nasdaq rose 0.19 percent, logging its seventh straight session of gains.

U.S. President Donald Trump said on Tuesday that trade talks with China were going well and suggested he was open to pushing off the deadline to complete negotiations, saying March 1 was not a "magical" date. U.S. tariffs on $200 billion worth of Chinese imports are currently scheduled to rise to 25 percent from 10 percent if no trade deal is reached by March 1. Investors now expect Trump to meet Chinese President Xi Jinping next month, likely after China's annual congress meeting starting from March 5, to strike a deal, or secure a "memorandum of understanding."

"They will likely agree on China importing a larger amount of natural gas and agricultural products," said Nobuhiko Kuramochi, chief strategist at Mizuho Securities, adding that China will also "open up a part of its domestic financial services and possibly some manufacturing sectors". But he predicted China "will not back down on so-called structural issues. The two countries may perhaps agree to set up a body to continue discussing those issues. Markets are already in the middle of pricing in these things." The two countries started a new round of talks to resolve their trade war on Tuesday, and sessions at a higher level are planned later this week, with Chinese Vice Premier Liu He visiting Washington on Thursday and Friday.

Behind fed's turnaround

Investors are also looking to the release later on Wednesday of minutes from the Federal Reserve's January policy-setting meeting, where policymakers effectively signalled no further rate hikes and possible tweaks to its balance sheet normalisation.

New York Fed President John Williams told Reuters he was comfortable with the level U.S. interest rates are at now and that he sees no need to raise them again unless economic growth or inflation shifts to an unexpectedly higher gear. But he also suggested the balance sheet rolloff would continue at least into next year at its current pace, dampening speculation that the Fed could end the process this year.

In the currency market, the euro firmed to $1.1350, bouncing back from Friday's three-month low of $1.1234, on the back of improving risk appetites. The dollar gained 0.2 percent to 110.80 yen, edging near Thursday's seven-week peak of 111.13. The British pound soared to $1.3063 on Tuesday, gaining 1.09 percent, a move some traders attributed to rising hopes Prime Minister Theresa May will make progress in seeking changes to her Brexit deal with the European Union. It last stood at $1.3070.

The Chinese yuan rose more than 0.5 percent to 6.7243 per dollar, its highest level in about three weeks after Bloomberg reported on Tuesday that the United States was seeking to secure a pledge from China that it will not devalue its yuan currency as part of a trade deal. The yuan's strength also sparked bids for Asian currencies, with the Thai baht hitting five-year highs.

Oil prices hovered near 2019 highs, supported by OPEC-led supply cuts and U.S. sanctions on Iran and Venezuela, but further gains were capped by soaring U.S. production and expectations of an economic slowdown. U.S. West Texas Intermediate (WTI) crude oil futures were at $56.01 per barrel, down 8 cents from their last settlement, but not far off their 2019 high of $56.33 reached earlier this week. International Brent crude futures stood at $66.33 per barrel, having hit a three-month high of $66.83 per barrel earlier this week.

Gold rose 0.4 percent to 10-month highs of $1,346.50, extending its rally sparked in part by signs that the world's central banks are turning dovish. The yellow metal has also attracted safety bids on worries about Brexit, said Tatsufumi Okoshi, senior commodity economist at Nomura Securities. Palladium rose 1.4 percent to yet another record high, having risen about 19 percent so far this year, on expectations of increased demand due to stricter emissions standards.

Source: Thomson Reuters

Domestic Markets

South Africa's rand inched lower on Tuesday, with investors pricing in domestic risks ahead of the annual budget where the financial crisis at state power utility Eskom is set to be addressed.

At 1502 GMT, the rand was 0.09 percent weaker at 14.1475 per dollar, compared with its overnight close of 14.1350 in New York. The rand has tumbled more than 6 percent since ailing power supplier Eskom resumed nationwide electricity blackouts last Monday over technical issues at its creaking fleet of coal-fired plants.

Most of Eskom's debt of about 420 billion rand ($30 billion) is under government guarantee, a major risk to the country's sovereign credit rating which is ranked at junk status by two of the top three ratings firms. Eskom expects to make annual losses of around 20 billion rand this year, and Finance Minister Tito Mboweni is set to announce a bailout for the firm during his budget speech on

Wednesday in parliament. "The composition of Eskom's rescue package is of particular significance to markets," Peregrine Treasury Solutions Corporate Treasury Manager Bianca Botes said in a note.

Bond prices rose. The yield on the benchmark 2026 paper edged lower to 8.87 percent, from Monday's close of 8.855 percent.

On the bourse, stocks struggled to stay positive after a buoyant start to the week, along with emerging market peers as investors awaited outcomes from the U.S.-China trade talks to be held in Washington this week. Weak company results and profit warnings also contributed to the weakness. The Johannesburg All-share index closed 0.12 percent weaker to 55,194 points, while the Top-40 index weakened 0.13 percent to 48,956 points.

EOH Holdings topped the decliners, plunging 16.37 percent at 14.61 rand after a report by Tech Central news site that Microsoft's decision to cut ties with the technology company was linked to a tip-off about a contract with South Africa's defence department. Reuters has not verified the news site's story. EOH said it could not respond each time the media published information but shareholders would be provided with responses to relevant media coverage as appropriate, subject to legal advice. It said the Microsoft investigation formed part of EOH's larger internally-initiated investigation into all public sector contracts over the last five years, and urged shareholders to "exercise caution" when dealing in the company's securities until a further announcement. EOH said last week Microsoft was terminating its channel partner agreement with EOH's subsidiary.

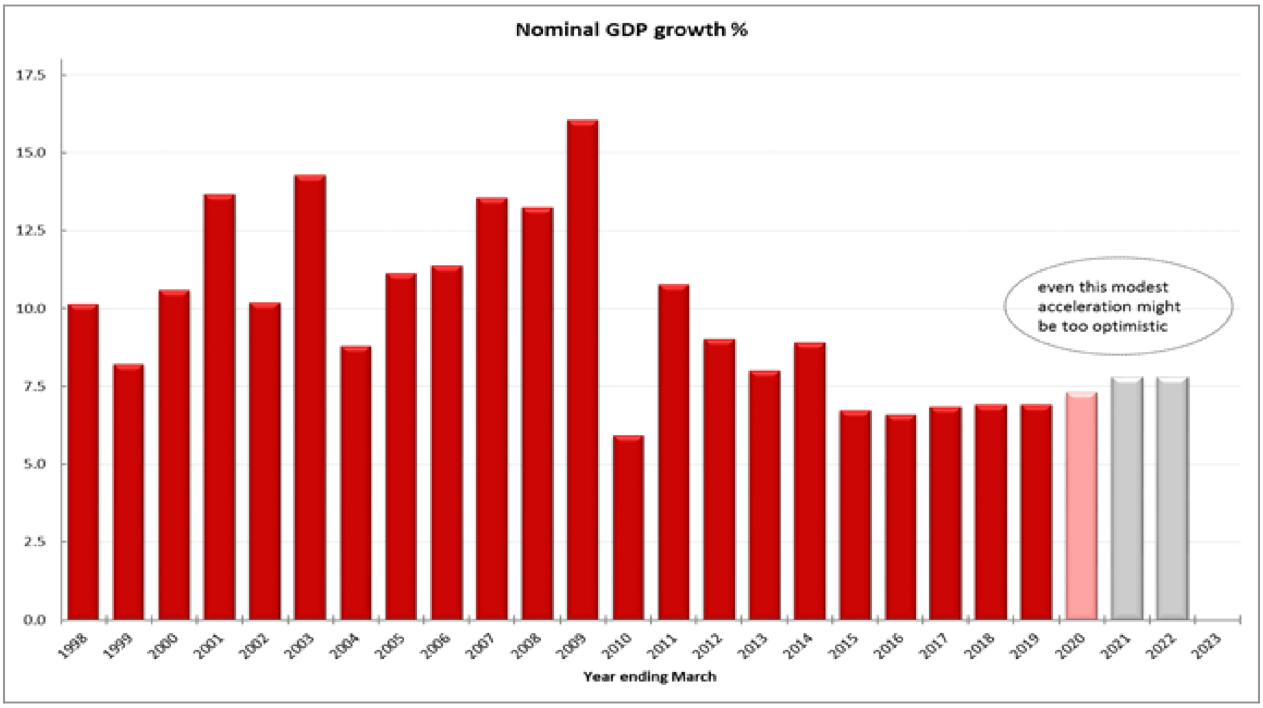
The operator of low-fare airline and British Airways in South Africa, Comair fell 0.17 percent to 5.74 rand after reporting a 38 percent decline in half-year headline earnings per share, while Kumba Iron Ore Ltd weakened 2.64 percent to 376.30 rand after reporting lower full-year headline earnings per share, compared to 2017, when the firm had benefited from the positive impact of an impairment reversal.

Source: Thomson Reuters

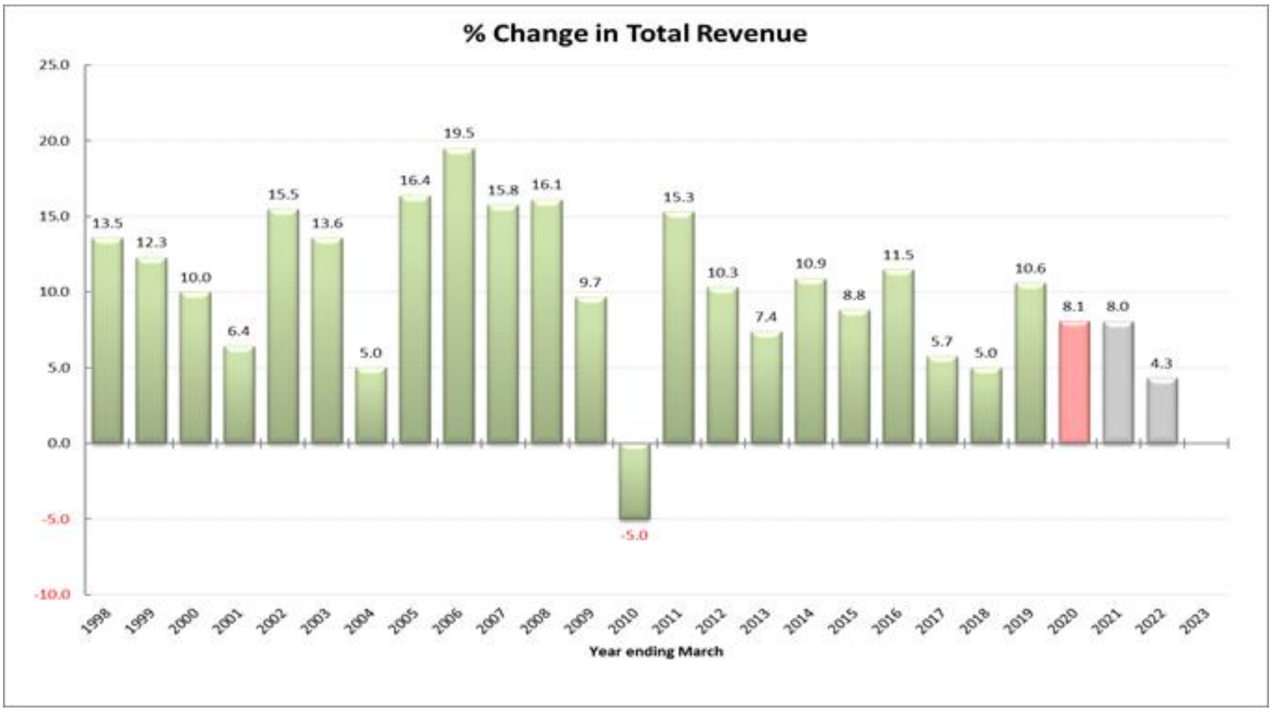
Chart of the Day **-** RSA Budget and fiscal policy

The Minister of Finance (MoF), Tito Mboweni, presents the SA Budget today. IT will be one of the most tricky and challenging Budgets in a long time. It is presented against a background of low economic growth, even recession-like conditions, in an election year – one of the most tricky and challenging elections in a long time. Assumptions about nominal GDP growth is critically important therein that it is the denominator in the fiscal ratios that credit rating agencies gauge in their assessments of a nation's creditworthiness. Furthermore, expectations of Revenue levels and growth rests on expectations of nominal GDP growth. With inflation expectations decreasing (**the number for January is 4%**) and real growth elusive, nominal GDP cannot be expected to growth much above 6.5% p.a. SA National Treasury (NT) has been overoptimistic on this up to now.

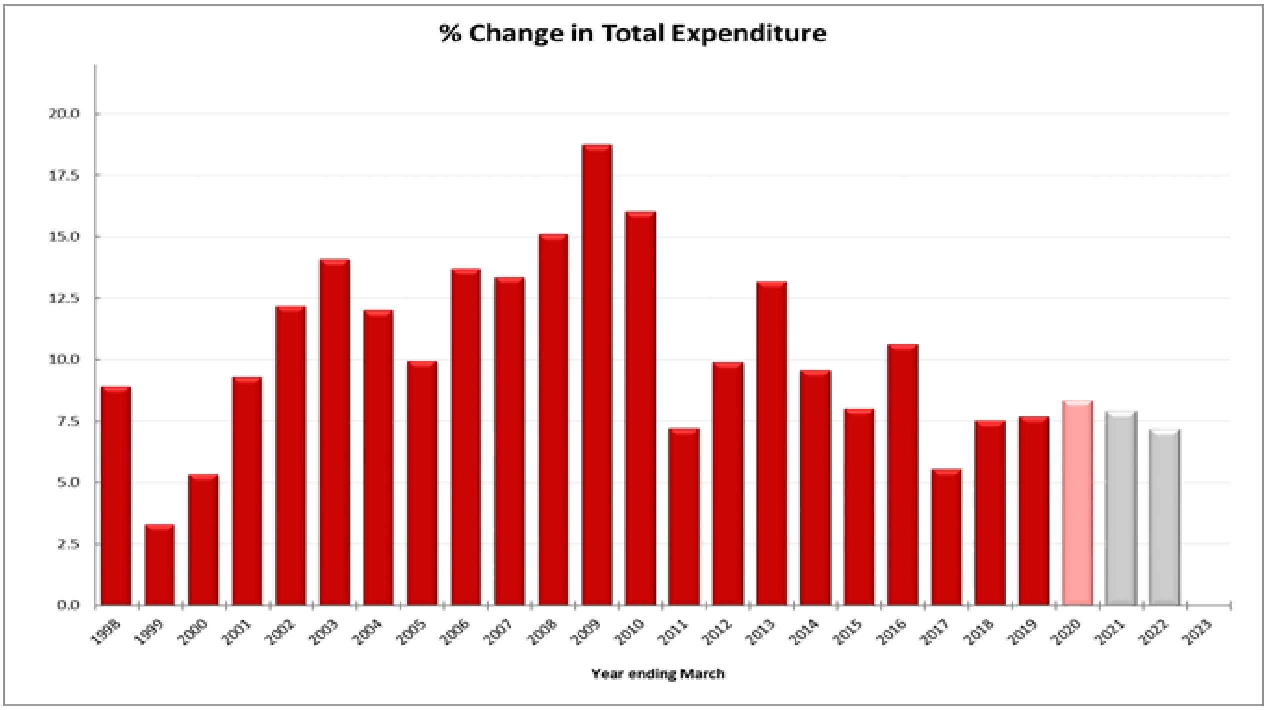
The charts below contains forward estimations, which are preliminary. The final numbers will come out this afternoon.



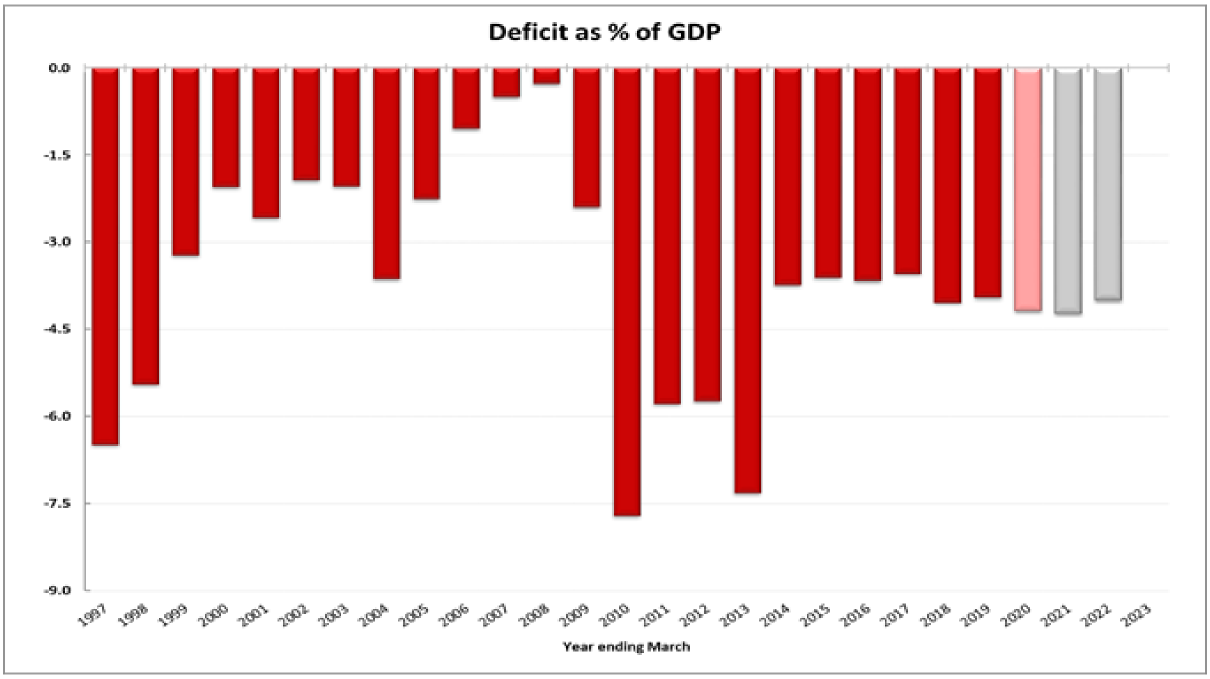
This means that Revenue growth will be under pressure, resulting in little wiggle room to increase expenditures in order to paper over the many cracks, the biggest of which is Eskom. We do not expect any tax rate changes as such, except for the usual "sin taxes" and inflationary or fiscal drag.



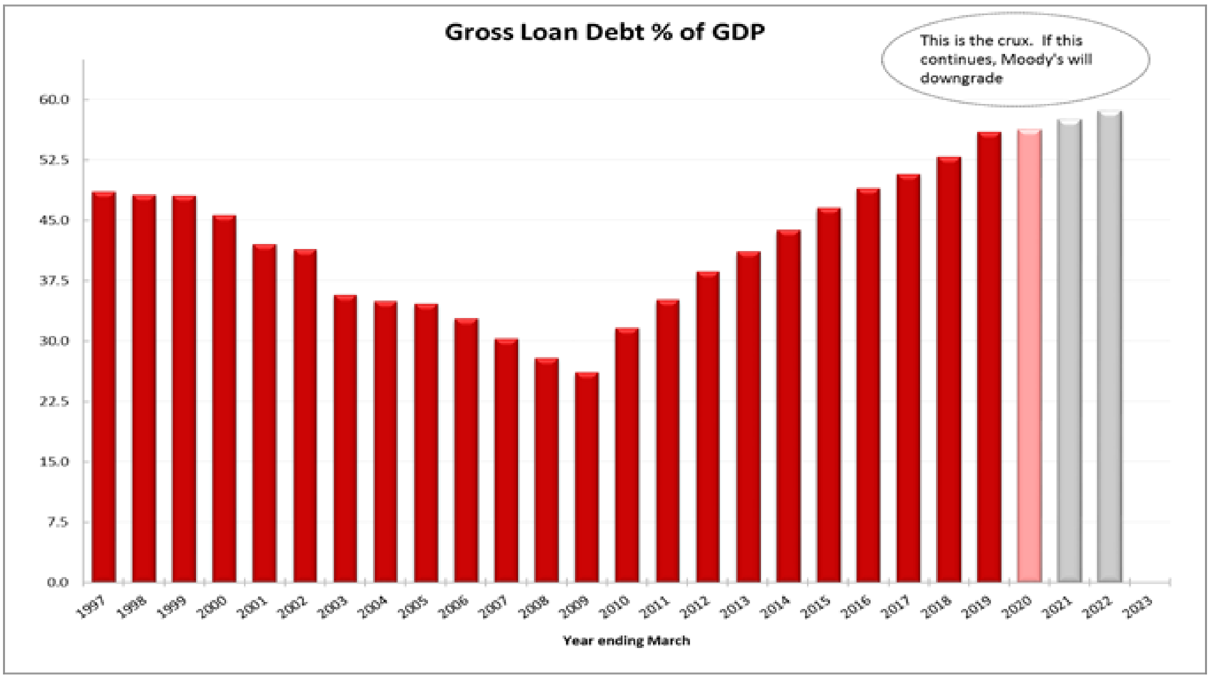
The best one can hope for is that Expenditures will be controlled as was previously budgeted for. We do not expect a sweeping bail-out of Eskom or a comprehensive plan regarding its turn-around. However, there will probably be some short term liquidity support in order to buy time for the troubled SOE. Here is an order of magnitude number: R100bn is equal to about 2% of GDP. Therefore, an expense or a takeover of debt, as has been bandied about, of this size is highly unlikely.



The deficit is likely to remain at 4% plus to GDP. The chart below shows where the psychologically important and fundamentally more healthy 3% ratio lies versus what has been and will likely be achieved. The Deficit is likely to be of the order of R230bn this coming year, rising to R260bn in the outer years. This is bigger than the whole Namibian GDP.



This means that the debt-to-GDP ratio will not stabilise, but rise, which is a key factor in the credit rating that SA is accorded. The ratio is in the mid-fifties as a % of GDP, closing in on 60%. Adding Guarantees and Contingencies (Eskom et.al.) raises this ratio to the mid-seventies!



Market Overview

MARKET INDICATORS				20 February 2019	
Money Market		**Last close**	**Difference**	**Prev close**	**Current Spot**
3 months	↓	6.84	-0.014	6.86	6.84
6 months	↓	7.65	-0.007	7.66	7.65
9 months	↓	8.07	-0.003	8.07	8.07
12 months	↓	8.30	-0.001	8.30	8.30
Bonds		**Last close**	**Difference**	**Prev close**	**Current Spot**
GC21 (BMK: R208)	↑	8.24	0.025	8.21	8.17
GC24 (BMK: R186)	↑	9.77	0.005	9.77	9.76
GC27 (BMK: R186)	↑	9.98	0.005	9.97	10.08
GC30 (BMK: R2030)	↑	10.78	0.015	10.76	10.77
GI22 (BMK: NCPI)	→	4.82	0.000	4.82	4.82
GI25 (BMK: NCPI)	→	5.17	0.000	5.17	5.17
GI29 (BMK: NCPI)	→	5.85	0.000	5.85	5.85
Commodities		**Last close**	**Change**	**Prev close**	**Current Spot**
Gold	↑	1,341	1.13%	1,326	1,342
Platinum	↑	818	1.93%	802	817
Brent Crude	↓	66.5	-0.08%	66.5	66.3
Main Indices		**Last close**	**Change**	**Prev close**	**Current Spot**
NSX (Delayed)	↓	1,332	-0.54%	1,340	1,332
JSE All Share	↓	55,195	-0.12%	55,260	55,195
SP500	↑	2,780	0.15%	2,776	2,780
FTSE 100	↓	7,179	-0.56%	7,219	7,179
Hangseng	↓	28,228	-0.42%	28,347	28,469
DAX	↑	11,309	0.09%	11,299	11,309
JSE Sectors		**Last close**	**Change**	**Prev close**	**Current Spot**
Financials	↓	16,762	-1.02%	16,934	16,762
Resources	↑	45,306	0.87%	44,916	45,306
Industrials	↓	65,740	-0.25%	65,902	65,740
Forex		**Last close**	**Change**	**Prev close**	**Current Spot**
N$/US dollar	↓	14.04	-0.43%	14.10	14.07
N$/Pound	↑	18.34	0.66%	18.22	18.35
N$/Euro	↓	15.92	-0.14%	15.94	15.94
US dollar/ Euro	↑	1.134	0.28%	1.13	1.134
		Namibia		**RSA**	
Economic data		**Latest**	**Previous**	**Latest**	**Previous**
Inflation	↓	4.7	5.1	4.5	5.2
Prime Rate	→	10.50	10.50	10.25	10.25
Central Bank Rate	→	6.75	6.75	6.75	6.75

Notes to the table:

- The money market rates are TB rates
- “BMK” = Benchmark
- “NCPI” = Namibian inflation rate
- “Difference” = change in basis points
- Current spot = value at the time of writing

Source: Bloomberg

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