The Daily Brief

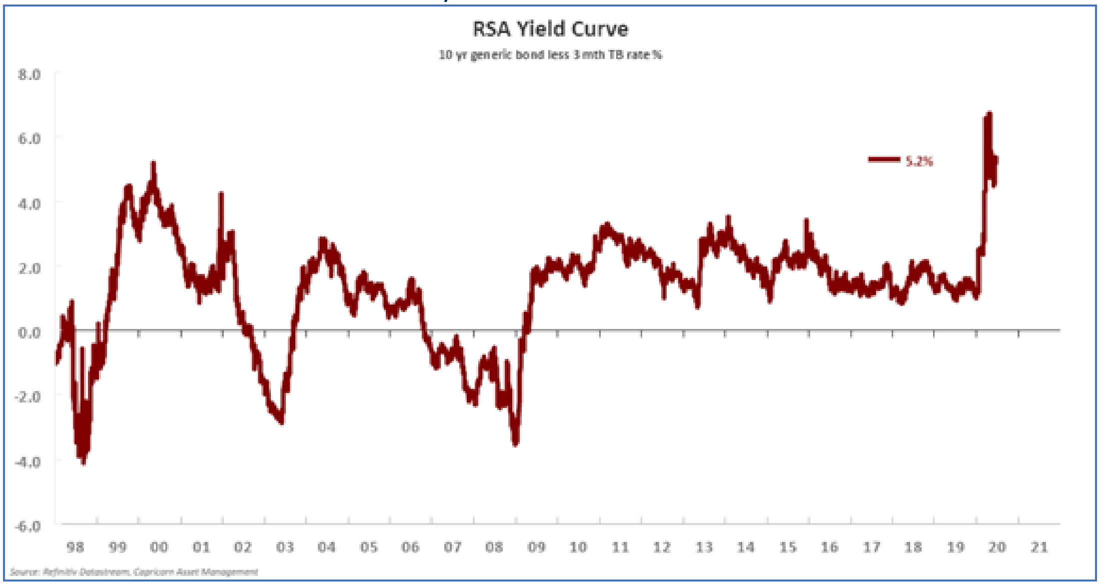
Capricorn Asset Management

Market Update Thursday, 25 June 2020

South African Budget

Our bullet-point summary:

- Weakest global macro since… 1930, WWII, 1870. Take your pick.
- Re-cap of Covid response:
  - R500bn Package. R190bn spending. R70bn tax policy. R200bn guarantees
  - Temporary Covid grants to 18m people = R41bn and Healthcare spending
  - SARB cut rates and supports bond market. Regulatory easing to assist credit flow
  - Banks' payment holidays. Insurers premium holidays
  - UIF = R23bn to 4.7m workers
  - Solidarity Fund, Sukuma Relief Program, South African Future Trust
- SA Fiscal mess was building before Covid, Legacy of overspending, overborrowing. Weak growth. Corruption.
- Deficit 14.7%, Debt 81.8% in a world of 10%+ deficits and 100%+ debt = accepted in the crisis
- Creditworthiness will deteriorate
- SOE's. Landbank gets R3bn (equity). Others barely mentioned. Gov support to be reformed.
- Market reaction to Budget was muted, it already moved ahead of time
- Inflation outlook being lowered. Policy rates still on a down trend (2X25bp, some say 2X50bp)
- Expectations are being built up for the October MTBPS. Plans will be unveiled. Cabinet proposals. Reforms
- Expenditure reviews and zero-based budgeting (ambitious)
- Gov is hanging its hat on infrastructure = the flywheel
- Debt trap? MoF found a euphemism = "debt spiral"
- Default on domestic debt still way off



South Africa's budget deficit will be the highest in the post-apartheid era, and the finance minister warned in his emergency budget speech on Wednesday that debt had become a hippo eating their children's inheritance. Public debt is projected to be more than three quarters of gross domestic product, as the coronavirus crisis stifles the economy, the Treasury said on Wednesday.

Finance Minister Tito Mboweni warned that future generations will pay dearly unless South Africa takes tough action to get in control of its borrowing. "Debt is our weakness. We have accumulated far too much debt; this downturn will add more," Mboweni said. "Our Herculean task is to close the mouth of the hippopotamus. It is eating our children's inheritance. We need to stop it now," he added.

Africa's most advanced economy was in recession before the COVID-19 outbreak ravaged the economy, and the lockdown that followed late in March has put further strain on businesses and consumers. This week the number cases in South Africa crossed 100,000 in total, with more than 2,100 deaths, the highest on the continent.

To cushion the economic blow of the pandemic on the economy, President Cyril Ramaphosa announced a 500 billion rand ($28.86 billion) relief package in April, equivalent to 10% of South Africa's GDP. In a supplementary budget in response to the coronavirus crisis, the Treasury projected the main budget deficit would widen to 14.6% of GDP in the current 2020/21 fiscal year - the highest in since South Africa threw off the shackles of its globally isolated apartheid rule in 1994.

The consolidated budget deficit, which also includes spending financed from revenues raised by provinces, social security funds and public entities, was seen hitting 15.7% of GDP. Meanwhile, the Treasury projected that gross government debt would rise to 81.8% of GDP in 2020/21 from 63.5% last year.

The economy is seen contracting 7.2% this year, after the strict nationwide lockdown severely curtailed production across key sectors such as mining and retail. Some lockdown restrictions have since been eased to allow key sectors to resume operations.

South Africa has approached the International Monetary Fund (IMF), World Bank, New Development Bank of the BRICS and African Development Bank to source funding to contribute to the rescue package. The government has also reprioritised previously planned spending to help fight the virus, with the supplementary budget making provision for 145 billion rand for immediate COVID-19 interventions.

Global Markets

Asia's stock markets slipped, bonds rose and the U.S. dollar was firm on Thursday as surging U.S. coronavirus cases, global trade tensions and an International Monetary Fund downgrade to economic projections knocked confidence in a recovery.

MSCI's broadest index of Asia-Pacific shares outside Japan fell 0.7%, Tokyo's Nikkei slumped 1.4% and Australia's ASX 200 tumbled 1.8%. U.S. stock futures also declined 0.7% following on from an overnight slide on Wall Street. Markets in Hong Kong and mainland China are closed for public holidays on Thursday.

Florida, Oklahoma and South Carolina reported record increases in new cases on Wednesday. Seven other states had record highs earlier in the week and Australia posted its biggest daily rise in infections in two months. The governors of New York, New Jersey and Connecticut ordered travellers from nine other states to quarantine on arrival, a worry for investors who had mostly been expecting an end to pandemic restrictions. Texas is also facing a "massive outbreak" and authorities are considering localised restrictions, Governor Greg Abbott said in a television interview.

Australian airline Qantas said on Thursday it doesn't expect sizeable international operations until at least July 2021, as the carrier announced plans to sack a fifth of its workforce and raise $1.3 billion to stay afloat. The International Monetary Fund said it now expects a deeper global recession, with output to shrink 4.9% this year, much sharper than the 3.0% contraction predicted in April.

"There is a little bit of reality bites coming," said Damian Rooney, senior instructional salesman at stockbroker Argonaut in Perth. "I don't think there was a particular straw that broke the camel's back, but people are a little bit twitchy - there are a lot of reasons to be pretty cautious."

Oil prices, a proxy for global energy consumption and economic growth, nursed losses following a 5% tumble overnight as U.S. crude storage hit another record and demand worries resurfaced. The dollar clung on to broad overnight gains which had lifted it from near a two-week low. Yields on benchmark 10-year U.S. Treasuries fell to a one-week low of 0.6724%.

Worries were even more pronounced on Wall Street overnight, and pulled major indexes back to flat for the month. The S&P 500 fell 2.6% overnight and the Nasdaq Composite snapped eight sessions of gains and slipped 2.2%. The Dow Jones Industrial Average tumbled 2.72% with retail-investor darlings in the travel sector hammered.

Anxiety in markets is likely to remain heightened ahead of U.S. jobless claims data due at 1230 GMT, along with virus case figures, and confidence could be dented by disappointment on either count. "Any improvement in jobs might be counteracted if there is another pickup in the case load in the United States," said Kyle Rodda, market analyst at brokerage IG in Melbourne. "It's a potential handbrake on the growth rebound story."

On top of virus concerns, worrying signals on the trade front have unnerved investors. The United States has added items valued at $3.1 billion to a list of European goods eligible to be hit with import duties, as it seeks to keep the pressure on in a long-running dispute over aircraft subsidies. The Trump administration has also determined that Chinese firms, including Huawei and video surveillance company Hikvision, are owned or controlled by the Chinese military, laying the groundwork for sanctions and fresh Sino-U.S. tension.

That has stalled a rally in riskier currencies and dropped the Australian dollar under 69 cents to $0.6864, and had the kiwi stalled around 64 cents. Gold steadied at $1,764.07 an ounce. U.S. crude futures rose by 6 cents a barrel or 0.1% to $38.07 and Brent crude futures were flat at $40.30.

Source: Thomson Reuters

Domestic Markets

South Africa's rand briefly dipped after Finance Minister Mboweni announced a wider budget deficit and soaring debt in an emergency supplementary budget on Wednesday, but the currency recovered as investors looked beyond local issues.

At 1445 GMT, the rand was 0.35% weaker at 17.3000 per dollar, compared with its session low of 17.4100 shortly after the budget.

South Africa's budget deficit is projected to widen and debt to balloon, the Treasury said on Wednesday, as the COVID-19 pandemic stifles an economy that was already in recession.

Several of the country's Eurobonds sank to their lowest in a week, down as much as 0.6 cents, Tradeweb data showed. But local bonds rallied. The yield on the government's 2030 issue fell 17 basis points to 9.165%.

"Make no mistake the numbers are horrifying but there is some recognition from government that things can't continue like this. That's what the rand is reacting to," Quinten Bertenshaw, executive director at ETM Analytics, said.

The treasury projected the budget deficit would widen to 14.6% of gross domestic product in the 2020/21 fiscal year, from a shortfall of 6.8% of GDP seen in February. It said gross debt would rise to 81.8% of GDP in the current fiscal year from 63.5% in 2019, peaking at 87.4% under the treasury's best case scenario. The worst case sees debt breaching the 100% mark by 2023.

"Today's numbers aren't a surprise," said Rachel Ziemba, founder of macroeconomic advisory Ziemba Insights. "The challenge is growth damage will hit revenues, and the capital needs for state-owned enterprises have only increased."

The economy is seen contracting 7.2% this year, prompting Mboweni to warn of a "sovereign debt crisis" unless the government cuts spending drastically. The treasury brought forward the budget in response to the coronavirus outbreak and President Cyril Ramaphosa's 500 billion rand ($29 billion) stimulus package. Since the first case in March, South Africa has had more than 100,000 infections and more than 2,000 deaths.

Stocks ended weaker. The benchmark FTSE/JSE all share index fell 1.96% to 54,389 points and the Top-40 index 2.05% to 50,142 points.

Source: Thomson Reuters

Corona Tracker

GLOBAL CASES SOURCE - REUTERS		25-Jun-2020		4:46
	Confirmed Cases	New Cases	Total Deaths	Total Recovered
GLOBAL	9,438,373	166,093	481,672	4,729,807

It is better to keep your mouth closed and let people think you are a fool than to open it and remove all doubt.

Mark Twain

Market Overview

MARKET INDICATORS (Thomson Reuters)					25 June 2020
Money Market TB's		**Last close**	**Difference**	**Prev close**	**Current Spot**
3 months	➔	4.44	0.000	4.44	4.44
6 months	↑	4.67	0.008	4.66	4.67
9 months	➔	4.78	0.000	4.78	4.78
12 months	↓	4.84	-0.008	4.85	4.84
Nominal Bonds		**Last close**	**Difference**	**Prev close**	**Current Spot**
GC21 (BMK: R208)	↓	4.13	-0.030	4.16	4.15
GC22 (BMK: R2023)	↓	5.93	-0.090	6.02	6.00
GC23 (BMK: R2023)	↓	5.91	-0.090	6.00	5.98
GC24 (BMK: R186)	↓	7.95	-0.120	8.07	7.93
GC25 (BMK: R186)	↓	8.00	-0.120	8.12	7.98
GC27 (BMK: R186)	↓	8.08	-0.120	8.20	8.06
GC30 (BMK: R2030)	↓	9.79	-0.160	9.95	9.83
GC32 (BMK: R213)	↓	10.53	-0.145	10.68	10.50
GC35 (BMK: R209)	↓	11.81	-0.165	11.98	11.86
GC37 (BMK: R2037)	↓	12.30	-0.160	12.46	12.34
GC40 (BMK: R214)	↓	12.68	-0.160	12.84	12.73
GC43 (BMK: R2044)	↓	13.24	-0.130	13.37	13.26
GC45 (BMK: R2044)	↓	13.41	-0.130	13.54	13.43
GC50 (BMK: R2048)	↓	13.40	-0.155	13.56	13.44
Inflation-Linked Bonds		**Last close**	**Difference**	**Prev close**	**Current Spot**
GI22 (BMK: NCPI)	➔	4.49	0.000	4.49	4.49
GI25 (BMK: NCPI)	➔	4.49	0.000	4.49	4.49
GI29 (BMK: NCPI)	➔	5.98	0.000	5.98	5.98
GI33 (BMK: NCPI)	➔	6.70	0.000	6.70	6.70
GI36 (BMK: NCPI)	➔	6.99	0.000	6.99	6.99
Commodities		**Last close**	**Change**	**Prev close**	**Current Spot**
Gold	↓	1,761	-0.29%	1,767	1,762
Platinum	↓	800	-3.53%	829	802
Brent Crude	↓	40.3	-5.44%	42.6	39.9
Main Indices		**Last close**	**Change**	**Prev close**	**Current Spot**
NSX Overall Index	↓	1,054	-0.95%	1,064	1,054
JSE All Share	↓	54,448	-1.85%	55,475	54,448
SP500	↓	3,050	-2.59%	3,131	3,050
FTSE 100	↓	6,124	-3.11%	6,320	6,124
Hangseng	↓	24,782	-0.50%	24,907	24,782
DAX	↓	12,094	-3.43%	12,524	12,094
JSE Sectors		**Last close**	**Change**	**Prev close**	**Current Spot**
Financials	↓	10,124	-0.97%	10,223	10,124
Resources	↓	50,675	-2.41%	51,926	50,675
Industrials	↓	76,118	-1.80%	77,512	76,118
Forex		**Last close**	**Change**	**Prev close**	**Current Spot**
N$/US dollar	↑	17.35	0.70%	17.23	17.41
N$/Pound	↓	21.55	-0.12%	21.57	21.62
N$/Euro	↑	19.52	0.20%	19.48	19.58
US dollar/ Euro	↓	1.125	-0.50%	1.131	1.125
		Namibia		**RSA**	
Economic data		**Latest**	**Previous**	**Latest**	**Previous**
Inflation	↑	2.1	1.6	4.1	4.6
Prime Rate	↓	7.75	8.00	7.25	7.75
Central Bank Rate	↓	4.00	4.25	3.75	4.25

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
- NSX is a Bloomberg calculated Index

Important Note:

This is not a solicitation to trade and CAM will not necessarily trade at the yields and/or prices quoted above. The information is sourced from the data vendor as indicated. The levels of and changes in the yields need to be interpreted with caution due to the illiquid nature of the domestic bond market.

Source: Bloomberg

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