The Monthly Bulletin

SygniaSygnals

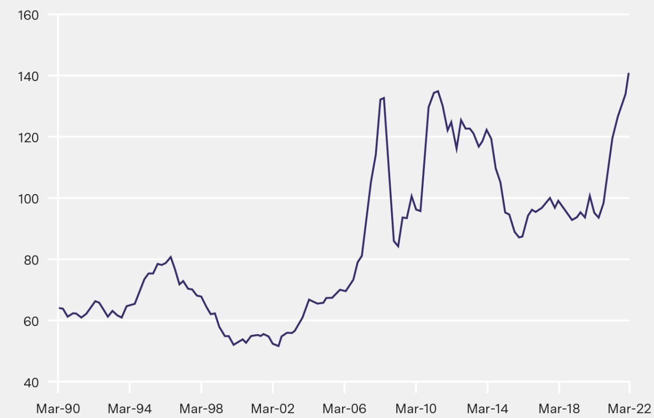
April 2022

By Kyle Hulett
Head of Investments

Market review

March saw central banks, surging prices and global investor enthusiasm for China compete for our attention with the atrocities on the ground as the war in Ukraine rumbled past the one-month mark. President Putin's invasion ousted Covid as public enemy number one as the somewhat shell-shocked analysts of the world recalibrated their global macro-economic stances. The war served as a reminder of the US' precarious policy position, with Jerome Powell's Fed stuck between a rock and a hard place. The situation in the US is mirrored by much of the world, as inflation risks run away on the back of an impending global energy-cost crisis and soaring food prices, with the UN World Food Price Index hitting an all-time high. The Russian contribution to world energy output risks the weaponisation of oil and gas in a game of sanctions, while Chinese policy makers promised "whatever it takes" to set China up for success on the back of strong fundamentals.

Chart 1: The UN World Food Price Index has hit an all-time high



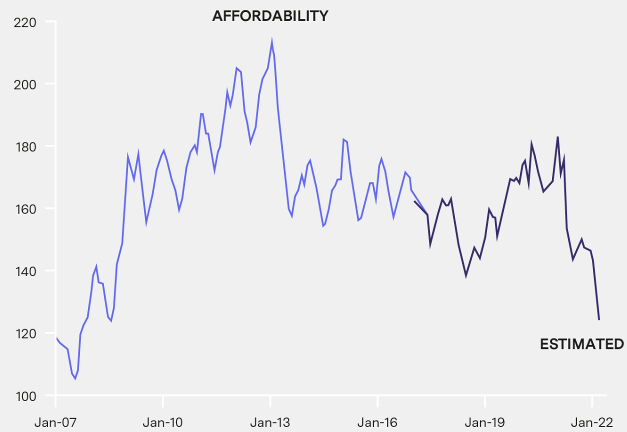
Source: Bloomberg

> The situation in Ukraine is firmly in the global spotlight. In the short term, we expect a continuation of elevated uncertainty in related assets that are susceptible to volatility.

US: Fed finally reaches lift-off and talks up rates, but likely to remain calm

- **Fed caught between austerity and credibility**
- **Fed unlikely to be able to hike as much as forecast**

Chart 2: US housing affordability is at its lowest level since 2007



Source: Standard Chartered

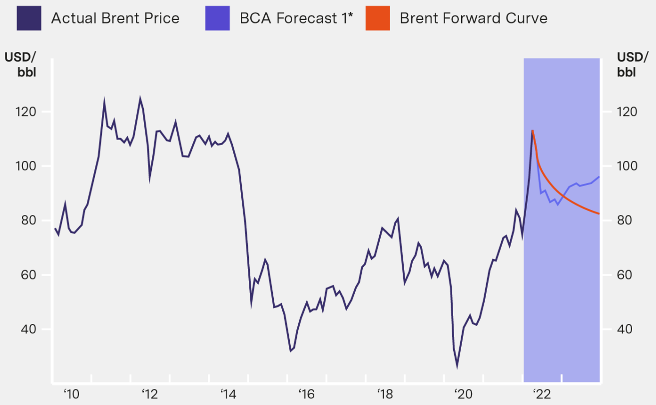
In the first hike since 2018, the Federal Open Market Committee (FOMC) raised rates by 25 bps to 0.5%, lauding strengthening economic indicators and downplaying "elevated inflation reflecting supply and demand imbalances related to the pandemic, higher energy prices and broader price pressures". The Fed ramped up its rate-hike projections to seven overall for 2022, with an additional three or four in 2023. Powell left the door open to a striking 50bps hike in the sequence.

To maintain its credibility without crashing the economy, the Fed needs to talk up the rate-hiking cycle – a high-risk move with little hope of completion. Balance-sheet reduction will be announced at a "coming" meeting – probably a May announcement. The likelihood of the Fed completing a straight sequence of eight rate hikes (which the market is currently pricing in) is very low. With the Fed already on the monetary-policy back foot, Treasury is unlikely to oppose inflation eating away at the national debt pile for a while, either; avoiding a recession is paramount. Rising yields have seen US home affordability at its worst level since 2007, which will slow housing activity, house price increases and growth via a lower wealth effect. The US is in a very difficult position. Fortunately, with the real yield curve still negative up to three years, there is no chance of a recession and at 2.4%, US bonds are starting to offer value for the first time in many years.

Russia: Destruction, commodity prices and inflation

- **How the Russians weaponise an energy oligopoly**
- **Peace talks stumble closer to a solution in Turkey**

Chart 3: Russian energy dominance impacting oil forward curve



*This forecast excludes the additional 1 - 1.3 MMB/D of oil supply from Iran for the forecast period.
Note: Shaded area denotes BCA research forecasts.
Source: BCA

The Russian invasion of the Ukraine has escalated beyond most people's wildest nightmares. War atrocities sent shock waves throughout the world as we witnessed the bombing of civilian areas in key Ukrainian cities, and financial markets responded with a dramatic sell-off across risk assets.

The West has responded with sanctions, turning Russia's dominant position in world energy into the elephant in the room. Russia is the world's third largest exporter of oil, and Europe buys around 60% of Russia's oil exports. The continuation of the war is pitting the West's own domestic financial interests against their political interests abroad. As Western powers put more pressure on the Russian energy economy in recent weeks, oil reached its highest level since 2008 ($139 per barrel) in March. While the US failed in a lone attempt to ban Russian oil, US Secretary of State Antony Blinken is still engaging with European and Japanese allies to test appetites for a more concerted ban. Russia makes billions in oil exports and could weaponise the commodity, with importers of Russian oil unable to protect their economies from price escalations caused by the supply interruptions that are a result of sanctions. OPEC (Saudi Arabia, the UAE and Kuwait) should be able to increase production above and beyond the volumes they agreed to in a July 2021 deal, but the collapse of US–Iran nuclear talks is likely to keep an extra million barrels a day out of supply.

New talk of compromise from Moscow and Kyiv for Ukraine's status outside of NATO have lifted global markets, but the odds of a breakthrough are not quite favourable yet. Ultimately, the war's impact on global growth will depend on how long it lasts. BCA's geopolitical strategists expect the conflict to escalate in the coming weeks, warranting a somewhat cautious near-term stance despite a positive 12-month outlook.

And it's not just oil: China-Europe rail routes are used to move more than a million containers via Russia across the 6 000-plus miles of railway that link western Europe to eastern China. These containers must now find new routes via sea, adding to costs and threatening to worsen global supply-chain chaos.

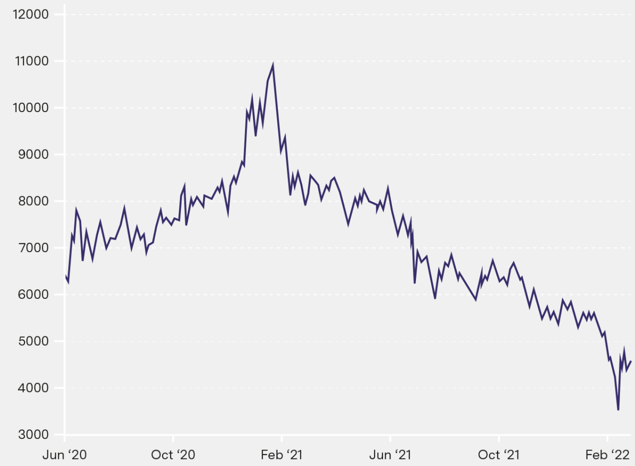
European natural gas prices shot up 34% as Putin said he would only accept payment in rubles. No mention has yet been made of Russian gas import restrictions, which would pose major issues for European economies, as 40% of their gas needs are met by Russia. Sanctions on the export of natural gas from Russia to the EU or UK are unlikely.

By Steven Empedocles
Head of Indexation

China: "Whatever it takes"

- **State council announces "whatever it takes" moment**
- **Tough streak, but with strong fundamentals**

Chart 4: Hang Seng Tech Index declines 70%



Source: Bloomberg

China's Hang Seng Technology Index fell nearly 70% from its peak, and Chinese stocks entered their deepest bear market since 2008 as concerns about the country's ties with Russia, a surge in Covid cases and continued regulatory pressure on the technology sector sent shares on a downward spiral.

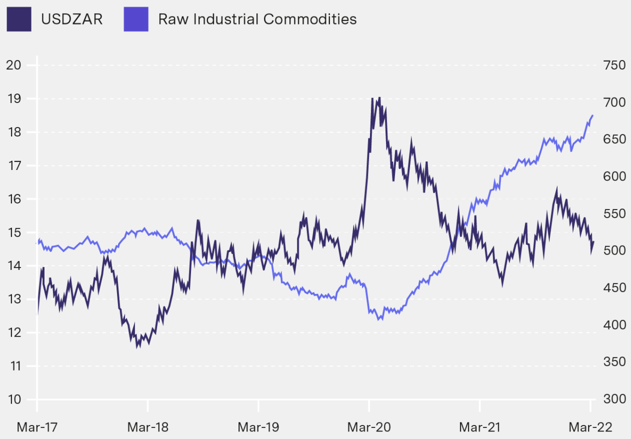
Moscow had sought military equipment from Beijing, and the US warned China of consequences for supporting the Kremlin. China's Foreign Minister, Wang Yi, says he wants to avoid US sanctions, and the US and China held high-level in-person talks that they described as "substantial" and "constructive". On top of the delicate situation around Russia, US regulators continue to pursue a multiple-year impasse over audit access to Chinese companies with US investors. The US Securities and Exchange Commission named its first Chinese stocks as part of a crackdown on foreign firms that have refused to open their books to US regulators, heightening delisting risks and further decoupling the world's two largest economies. The battle with the US over existing issues and now Russia comes as China is weakened domestically by yet another Covid outbreak. Nearly 30 million people are under lockdown in China as surging Covid-19 cases have led to the return of mass tests on a scale not seen since the start of the pandemic, leading to worries about a slowdown in growth and further global supply disruptions pushing up inflation in the People's Republic.

China has reached what Mario Draghi termed the "whatever it takes" moment of the Grexit crisis. China's state council has addressed all the biggest concerns for investors, pledging to keep Chinese capital markets stable, support overseas stock listings, work with the US, address the fragile property development sector and end Big Tech regulations. Coupled with positive fundamentals, the strong rhetoric supporting the economy that key stakeholders want to see in China is shaping up as a catalyst.

China's economy registered strong, above-expectation growth in the first two months of 2022, and the growth of industrial production, retail sales and fixed-asset investment accelerated. Earnings remain solid and the MSCI China Index is trading at roughly nine times its 12-month forward-earnings estimates, well below the five-year average of 12.6, suggesting that global risks are priced in. Macro-growth levers remain in place, with the Chinese currency remaining strong despite the Russian wild card – and unlike anywhere else in the world, the PBOC is still cutting rates. Together with the positive catalyst from the state council, we remain bullish on China.

South Africa: Rand roaring ahead on higher commodity prices

Chart 5: Rand strengthens on the back of strong commodity prices



Source: Bloomberg

- **Benefits from rising commodity prices, but oil is hurting**
- **SWIX, Capped SWIX unite**

South Africa is of course expected to be hit by the rise in energy prices and then by raised inflation. The silver lining is that inflation pressures are muted for an economy with growth as low as South Africa's. The SARB's monetary policy committee (MPC) opted to hike the repo rate by a further 25bps, to 4.25%. Three of the MPC members were in favour of a 25bps hike, while two pushed a more hawkish 50bps rise. While the SARB will continue to raise rates, they are unlikely to do so too quickly, and we think bond yields will not price in inflation concerns for too long. Core inflation for February remained steady at 3.5% year-on-year. The strong rand will certainly help cushion the blow of rising oil prices. The rand is significantly outperforming other emerging market (EM) currencies on the back of higher commodity prices.

Locally, the Capped Shareholder Weighted Index (SWIX) completed its transformation in the quarterly index rebalance on 18 March. Naspers fell below the Cap, and the SWIX and Capped SWIX now have almost identical exposure to Prosus and Naspers, at around 9%. MTN had a small dip due to the cap in the Capped SWIX index. We remain very comfortable benchmarking our SA Equities against the SWIX index.

By Iain Anderson
Head of Investments

Outlook and positioning

The situation in Ukraine is firmly in the global spotlight. In the short term, we expect a continuation of elevated uncertainty in related assets that are susceptible to volatility. Oil is easy to single out here, with gas, wheat and other commodities also at risk. The increases in inflation centred on global energy and food uncertainty are bound to draw central banks into a mud fight, particularly those in the US, with consumer expectations that could hamper growth. Unlike the 1970s, though, long-term inflation expectations remain well anchored, and economies are more energy efficient. Central banks can remain cool and align with Treasury department's willingness to let inflation eat away at the world's debt. Finally, our cyclical global recovery base for this year remains intact, primarily by virtue of its underpinnings in recovering underlying economic activity as a result of eased Covid restrictions. Equity is expected to continue a rotation to value, with sustained emerging market outperformance due to rising real bond yields as global growth remains resilient – if lower than expected – at the start of the year.

Key indicators

		1 mo.	*3 mos.*	*6 mos.*	*1 yr.*	*2 yrs.*	*3 yrs.*	*5 yrs.*	*10 yrs.*
J203T	**FTSE/JSE All Share Index**	0.0%	3.8%	19.6%	18.6%	35.1%	14.2%	11.4%	11.9%
J200T	**FTSE/JSE Top 40 Index**	-0.8%	3.6%	20.5%	17.6%	34.6%	14.9%	12.3%	12.2%
J210T	**FTSE/JSE Resources 10 Index**	-2.0%	18.2%	44.4%	31.7%	58.4%	26.9%	26.2%	9.6%
J211T	**FTSE/JSE Industrials 25 index**	-4.9%	-13.9%	0.6%	-4.7%	14.3%	7.7%	5.5%	12.3%
J212T	**FTSE/JSE Financials 15 Index**	12.2%	20.2%	22.8%	49.7%	43.3%	7.6%	8.6%	11.2%
J403T	**FTSE/JSE SWIX Index**	1.4%	5.7%	14.5%	12.9%	30.8%	10.6%	8.3%	10.7%
J433T	**FTSE/JSE Capped SWIX Index**	1.5%	6.7%	16.0%	20.4%	36.3%	11.9%	8.1%	10.6%
J303T	**FTSE/JSE CAPI Index**	0.3%	4.9%	20.0%	22.5%	38.1%	15.0%	11.4%	12.1%
J253T	**FTSE/JSE SA Listed Property Index**	5.1%	-1.3%	7.0%	27.1%	30.7%	-3.8%	-4.9%	5.0%
ALBI	**JSE All Bond Composite Index**	0.5%	1.9%	4.8%	12.4%	14.6%	8.4%	8.9%	8.1%
STeFI	**STeFI Index**	0.4%	1.0%	2.0%	3.9%	4.2%	5.2%	6.1%	6.1%
	MSCI World Index in SA Rands	-2.8%	-13.2%	-0.7%	9.0%	17.8%	15.7%	14.4%	18.3%
	Rand/US Dollar Exchange Rate	-5.4%	-8.4%	-2.9%	-1.0%	-9.5%	0.6%	1.7%	6.7%
	Rand/Euro Exchange Rate	-6.3%	-10.4%	-6.8%	-6.3%	-9.1%	0.3%	2.6%	4.8%
	Rand/Pound Exchange Rate	-7.2%	-11.0%	-5.2%	-5.6%	-6.8%	1.0%	3.0%	4.7%
	Headline CPI	0.6%	1.4%	2.4%	5.6%	4.2%	4.4%	4.2%	5.0%
	PPI	1.1%	2.6%	5.6%	10.5%	7.2%	6.3%	5.5%	5.7%