STANDING OUT FOR THE RIGHT REASONS

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It is ironic that the president of a communist country is now the leading voice in support of free trade and globalisation, but this is the upside-down world we live in now. In a widely anticipated speech, President Xi Jinping of China promised to further open up the world's second largest economy to participation by foreign firms and to lower tariffs, including US-produced cars. He warned against a "Cold War mentality" and while there was nothing much new in his speech, it did calm investors' nerves after weeks of talk of trade wars. So far it is still just talk, and world trade is largely unimpeded. The World Trade Organisation (WTO) last week forecast 4.4% growth in world trade volumes this year, after growth rose to 4.7% in 2017, the best performance in six years. However, the WTO warned that tit-for-tat trade retaliation could dent business confidence and discourage investment.

Although concerns over trade wars have been fading somewhat, fears of other types of war have risen and market volatility remains elevated. There were only seven daily moves of more than 1% on the S&P500 Index last year (which was unusually low), compared to 28 such swings so far this year. The oil price jumped after Houthi rebels attempted a missile strike on Saudi Arabian oil facilities. The US and its allies bombed several sites in Syria, despite Russia's objections. Separately, the US also announced sanctions on key Russian businesspeople and companies who are considered close to the Kremlin.

POLITICAL UNCERTAINTY ACROSS EMERGING MARKETS

Until recently, Russian markets were favoured by investors, buoyed by a resurgent oil price, low inflation and attractive valuations. Russia was upgraded from junk status to investment grade by S&P in March. Russian equities also outperformed the MSCI Emerging Markets Index by 8% in dollars in the first quarter. But the imposition of sanctions saw a market sell-off last week and the rouble lost 15% against the US dollar.

Brazil, which like Russia also suffered a deep recession in 2015 and 2016, remains in the grip of political uncertainty. Brazil will hold a general election in October, and former President Lula da Silva, imprisoned for corruption last week, is still the most popular candidate, according to opinion polls. But if the appeal against his conviction fails, he will be ineligible for participation.

Speaking of former presidents in prison, South Korea's former president Park Guen Hye was last week given a 24-year jail sentence term for corruption. She is the third Korean president to be convicted on criminal charges after leaving office.

Turkey's currency hit a record low against the dollar. Its economy has been booming and grew by 7.4% last year (more than China) largely due to fiscal stimulus. Investors are worried about an overheating economy, but President Erdogan, its increasingly authoritarian leader, will not allow the central bank to raise interest rates. A lack of central bank independence is a red flag for investors. Rising inflation and a widening current account deficit are tell-tale signs of an unbalanced economy that is running too hot.

In Hungary, the nationalist Fidesz party won a third consecutive election victory by a wide margin. Fidesz, headed by Premier Viktor Orban, is accused of systematically undermining democratic checks and balances and suppressing media freedom in Hungary. The country is a European Union (EU) member, but has been increasingly critical of the EU's core liberal values. It is joined by a handful of other Eastern European countries – termed "the rotten fringe of Europe" by the Financial Times – whose tendency towards strong-man rule poses a headache for the EU.

CLEANING UP

It is almost a year ago that South Africa was downgraded to junk status by S&P and Fitch following the midnight axing of then Finance Minister Pravin Gordhan. Last week it was Gordhan who was doing the sacking in his new capacity as Public Enterprises minister. He replaced the board at struggling state-owned arms company Denel, the second SOE to get a new board this year (following Eskom) as the governance clean-up continues under President Ramaphosa.

In other words, among emerging markets, South Africa is increasingly standing out, and this time for the right reasons. After years of deterioration, governance is improving and economic reforms are in the pipeline. There are clearly still huge problems. The process of undoing the political and policy damage of the past few years has just begun, while the country's deep historical structural problems and legacy of racial exclusion still need addressing. The World Bank's latest update on South Africa highlights that it has the highest income inequality (Gini coefficient) of all countries measured, while its low skill levels, dependence on commodity exports and weak integration into global supply chains constrain the country's growth potential. Crucially, the World Bank argues that slow growth and high inequality are mutually reinforcing: inequality leads to "contestation for resources (through taxation, expropriation, corruption and crime)", which in turn discourages the investment and job creation needed to reduce inequality.

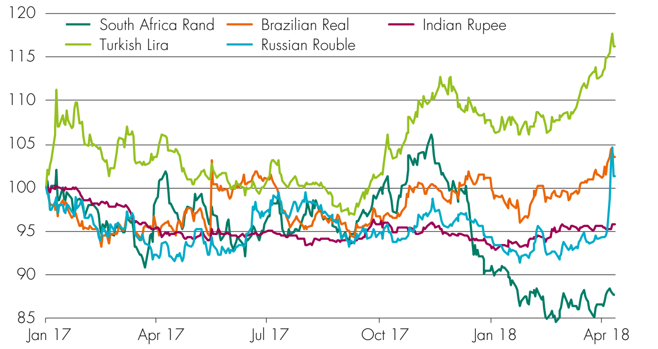
One quick-win to boosting investment and creating jobs is restoring certainty in the key mining sector. Reports that talks towards a revised mining charter are progressing well and expected to be concluded soon are very encouraging. Given the huge amount of upfront capital investment needed to build a mine, regulatory certainty is crucial. Nobody can predict the future, but the greater the likelihood that regulatory goalposts could be shifted during the decades-long life of a new mine, the smaller the chance investors will put up the capital for it (or the higher the expected return will have to be to justify the risk). The mining production numbers released last week showed a 3.1% year-on-year uptick in output, largely from iron ore mines. But on a longer-term view, total mining production is still below 2008 levels, and shows no sign of improvement. Gold production's downward trend remains intact, but at least our athletes in the Gold Coast have been producing gold.

Despite South Africa's serious long-term challenges, optimism has increased in the short term and the rand reflects this, having rallied more than its peer currencies since December and falling by less as the dollar perked up and emerging markets came into the spotlight for the wrong reasons last week.

BOND YIELDS **STILL HIGH**

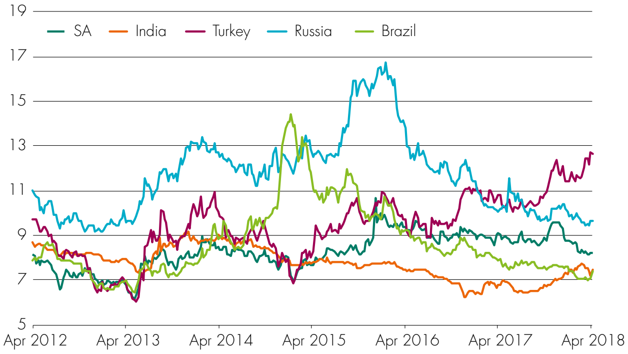
However, South African bond yields don't seem to price in excessive optimism yet. Even after the latest round of sanctions, Russian bond yields are still lower than South Africa's. Investors are pricing lower credit risk and lower expected inflation in Russia over the next ten years than in South Africa. Russia enjoys a higher sovereign credit rating than South Africa after the recent surprise ratings upgrade by S&P and its government debt levels are lower. But Russia defaulted on its debt in the late 1990s, so it hardly has a pristine credit record. Meanwhile, the South African Reserve Bank has proven its commitment to fighting inflation again and again. Investors are clearly still attaching a sizable risk premium to South African bonds, and if this diminishes as investors see more evidence of improvement, bonds should rally.

CHART 1: RAND-US DOLLAR EXCHANGE RATE COMPARED TO PEERS, INDEXED TO 100 WITH LOWER VALUES INDICATING APPRECIATION AGAINST THE DOLLAR



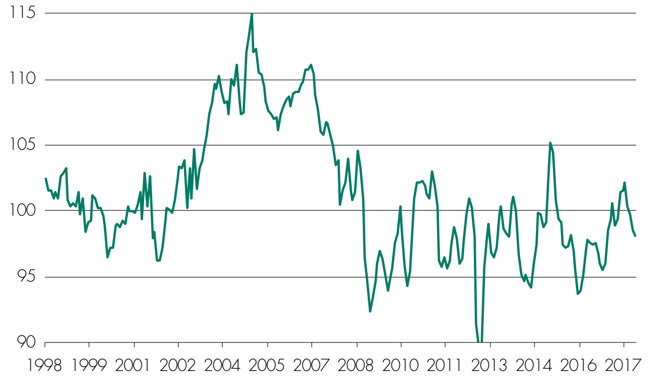
Source: Thomson Reuters Datastream

CHART 2: SOUTH AFRICAN GOVERNMENT 10-YEAR BOND YIELD COMPARED TO PEERS, %



Source: Thomson Reuters Datastream

CHART 3: SOUTH AFRICA'S LONG-TERM MINING PRODUCTION INDEX



Source: StatSA

INDICATORS

EQUITIES - GLOBAL

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
Global	MSCI World	US$	2 091.0	1.85%	1.16%	-0.57%	14.08%
United States	S&P 500	US$	2 656.0	2.00%	0.49%	-0.67%	14.04%
Europe	MSCI Europe	US$	1 792.0	1.53%	2.34%	-0.28%	15.17%
Britain	FTSE 100	US$	10 345.0	2.22%	4.62%	-0.54%	12.91%
Germany	DAX	US$	1 448.0	2.04%	2.70%	-2.83%	23.02%
Japan	Nikkei 225	US$	202.9	0.58%	0.48%	0.39%	19.65%
Emerging Markets	MSCI Emerging Markets	US$	1 177.0	1.29%	0.51%	1.64%	22.22%
Brazil	MSCI Brazil	US$	2 205.0	0.27%	-1.96%	9.00%	22.23%
China	MSCI China	US$	91.4	3.23%	1.44%	3.29%	36.95%
India	MSCI India	US$	586.2	0.66%	3.56%	-4.07%	11.86%
South Africa	MSCI South Africa	US$	578.0	1.05%	0.35%	-4.46%	17.96%

EQUITIES - SOUTH AFRICA (TR UNLESS INDICATED OTHERWISE)

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
All Share (Capital Only)	All Share (Capital Index)	Rand	56 563.0	1.22%	1.96%	-4.94%	5.71%
All Share	All Share (Total Return)	Rand	8 127.0	1.38%	2.28%	-3.82%	8.88%
TOP 40/Large Caps	Top 40	Rand	7 157.0	1.69%	2.58%	-3.91%	10.06%
Mid Caps	Mid Cap	Rand	16 323.0	-0.65%	-0.22%	-3.84%	0.91%
Small Companies	Small Cap	Rand	20 927.0	-0.13%	0.83%	-0.45%	-0.06%
Resources	Resource 20	Rand	2 335.0	4.24%	4.92%	2.13%	12.26%
Industrials	Industrial 25	Rand	14 108.0	0.75%	2.27%	-6.67%	5.48%
Financials	Financial 15	Rand	9 680.0	1.12%	0.81%	-0.28%	24.26%
Listed Property	SA Listed Property	Rand	2 069.7	0.10%	4.48%	-16.00%	-2.92%

FIXED INTEREST - GLOBAL

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
Global Government Bonds	Citi Group WGBI	US$	975.8	0.27%	-0.19%	2.92%	8.10%

FIXED INTEREST - SOUTH AFRICA

DESCRIPTION	INDEX	CURRENCY					
All Bond	BESA ALBI	Rand	633.7	0.09%	-0.23%	7.83%	15.51%
Government Bonds	BESA GOVI	Rand	630.1	0.06%	-0.23%	7.47%	15.21%
Corporate Bonds	SB JSE Credit Indices	Rand	121.2	-0.02%	-1.98%	-3.94%	-15.90%
Inflation Linked Bonds	BESA CILI	Rand	261.3	-0.60%	-0.66%	3.43%	6.14%
Cash	STEFI Composite	Rand	390.8	0.14%	0.27%	2.05%	7.44%

COMMODITIES

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
Brent Crude Oil	Brent Crude ICE	US$	72.5	8.21%	5.12%	8.25%	29.52%
Gold	Gold Spot	US$	1 346.0	0.90%	1.58%	3.78%	4.58%
Platinum	Platinum Spot	US$	928.0	1.31%	-0.22%	-0.22%	-4.72%

CURRENCIES

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
ZAR/Dollar	ZAR/USD	Rand	12.08	-0.45%	-2.15%	2.45%	11.22%
ZAR/Pound	ZAR/GBP	Rand	17.20	-1.40%	-3.43%	-2.67%	-2.33%
ZAR/Euro	ZAR/EUR	Rand	14.90	-0.80%	-2.07%	-0.26%	-4.29%
Dollar/Euro	USD/EUR	US$	1.23	0.00%	0.16%	-2.36%	-13.82%
Dollar/Pound	USD/GBP	US$	1.42	-1.07%	-1.69%	-5.20%	-12.22%
Dollar/Yen	USD/JPY	US$	0.01	0.40%	1.03%	-4.70%	-1.22%

Source: I-Net, figures as at 13 April 2018

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ASSET MANAGER MOVEMENTS

There were no manager movements over the past week.

THE WEEK AHEAD

SOUTH AFRICA

- Inflation
- Retail sales

US

- Retail sales
- Housing starts
- Building permits
- Industrial production

EUROPE

- Germany ZEW Economic Sentiment Index
- Eurozone consumer confidence
- Eurozone current account

CHINA

- First quarter GDP growth
- Fixed asset investment
- Retail sales
- Industrial production

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