MARKET MATTERS

1 APRIL – 5 APRIL 2019

OF BULLS AND BEARS

Dave Mohr and Izak Odendaal, Old Mutual Multi-Managers

A LONG BULL MARKET

Last month saw global equity markets pass a milestone. It's been 10 years since equity markets bottomed after the Global Financial Crisis (GFC) in March 2009. In other words, the post-crisis bull market is 120 months old and a lot of commentators are worried that it has run for too long. This is a very US-centric view of course, since other major markets have been limping along. In fact while all markets have recovered significantly from their 2009 lows, many major indices have not surpassed their pre-GFC peaks. The FTSEurofirst Index (the largest European companies by market capitalisation) and emerging markets (measured in US$) are still below their 2007 peaks. So most of the non-US markets have in fact experienced a low return environment over the past 12 years.

US DOING THE HARD YARDS

Three reasons stand out for the US outperformance. Firstly, although the post-recession US economic recovery has been very tepid compared to past recoveries, it has been much stronger compared to other developed markets, particularly Europe, which suffered a double-dip recession. The US addressed its fragile financial system early on, and the Federal Reserve was creative in its support of the economy. Secondly, US companies are active buyers of their own stock, much more so than elsewhere. Thirdly, the US is home to the world's leading technology companies, including the fabled FANGs (Facebook, Amazon, Netflix, Google). Only China's Tencent and Alibaba can be mentioned in the same breath. (Local investors can participate in the former through Naspers.)

TIME TO HIT A NEW PEAK

Some commentators prefer to start the date of the bull market not at the bottom of the cycle, but once the previous high has been regained. In terms of this view, the current US bull market started only in March 2013, when the 2007 peak was surpassed, and we are celebrating a six-year instead of a 10-year anniversary. As mentioned earlier, with most other major equity indices not yet having passed their 2007 peaks, they do not meet this definition of a bull market. So not yet time for them to celebrate.

Clearly then, the terms bull and bear market mean different things to different people. One popular definition of a bear market is a 20% to 25% decline in equity values, but this is fairly arbitrary, as a 19.5% decline is no less traumatic to investors. A better way of thinking about a bear market is a significant decline (say 25%+) that takes several quarters if not years to claw back the losses. Historically such bear markets were associated with an economic recession that invariably resulted in falling company profits and rattled investor confidence.

Equity markets often exhibit volatility as investors panic about economic prospects and the outlook for company profits. However, as it becomes clear that economic growth is not going to tank and companies remain profitable, the market recovers quickly. That is market volatility and not a classic bear market.

Share prices will always be volatile in the short term but reflect the underlying economic reality of company profitability in the end, so rather focus on that. When prices diverge too far from this reality, it creates opportunities for investors. Also consider the psychological element. In a bear market, investors become more and more despondent until there is a widespread belief that things cannot get better. This is usually a buying opportunity. In contrast, a bull market is associated with rising optimism that eventually turns into euphoria at the top of the cycle.

A LONGER-TERM PERSPECTIVE

A very different way of looking at bull and bear markets is to ignore shorter-term cycles and focus on longer-term trends. Therefore, the stagflation of the 1970s can be seen as one long bear market for global stocks (irrespective of a few strong short lasting rallies), while the 1990s can similarly be seen as one long technology-supercharged bull market, ignoring the temporary 20% decline in 1992. In the US and other major equities markets the first decade of the new millennium was again a nightmare with two historically severe bear markets resulting in essentially a decade-long bear market.

So the starting point of the current bull market explains a lot about the length of it. Looking at the combined period for the last 20 years, the annualised real return of global equities amounts to a modest 2.2% per year.

There have been three cyclical sell-offs (2011, 2015 and late 2018) but the current broad uptrend is still intact. Each of these sell-offs probably helped to prolong the overall cycle, as they curbed investors' enthusiasm and prevented the dangerous build-up of investor euphoria that characterises the top of a bull market. It is often said that to sustain a bull market investors must constantly climb a wall of worry.

LOCAL EXPERIENCE WAS DIFFERENT

The JSE experienced a very different journey through the 1990s and 2000s. Political uncertainty and transition combined with a drawn-out recession was the story of the first half of the 1990s, followed by rolling emerging crises (Asia and Russia) during the second half. Local equity returns were subpar for the decade. However, the JSE boomed from the early part of the new millennium as emerging markets recovered, China took centre stage on the world economy and commodity prices skyrocketed. The JSE delivered an unequalled real return of 19.2% per year from the late 1990s to the start of the GFC. Then it crashed.

Strictly speaking the low point for the South African market during the GFC occurred in November 2008 with the FTSE/JSE All Share Index hitting 17 814, but the subsequent rally was short-lived and soon tested these levels again in early March 2009. It then followed - as is usually the case – global markets higher from that point on. The massive Chinese stimulus package saw commodity prices quickly recover after the Global Recession until 2011, when slowing Chinese economic growth collided with expanding commodity supply pushing prices lower over the next four years. As this happened, the rand weakened between 2011 and 2015. Non-commodity rand hedges, of which there are many on the JSE, performed very well over this period. The rand and commodity prices bottomed in early 2016. Mining shares have rebounded but are generally not back to all-time highs, while other rand hedges have not done as well. The domestic economic malaise over the past five years has weighed on locally focused companies. Many companies expanded abroad, with mixed success. The SA Reserve Bank data shows that South African companies spent R445 billion on offshore acquisitions during the five years to the end of 2018. Prior to that, the numbers were negligible.

The net result of the above is that while local equities performed well over the 10-year period, it was actually a case of two halves and most of the gains came in the first five years. The second five-year period has seen the market move largely sideways, but at least valuations have substantially improved in the last year. For example, the dividend yield of the JSE is currently the highest in years.

LOOKING AHEAD

So where do we stand now? It would be a mistake to assume that the next 10 years will look like the last 10. However, considering that major US bear markets typically spread quickly to the rest of the world and historically coincided with a US economic recession, how do we assess the risk of such a scenario? Despite the length of the current US economic recovery, the likelihood of a near-term recession seems relatively low. So from that point of view the risk of a major US bear market spreading to the rest of the world also appears to be contained.

From a pricing perspective, equity markets in general seem to be reasonably priced. There have been three cyclical sell-offs (2011, 2015 and late 2018). Each of these sell-offs probably helped to prolong the overall bull market, as they curbed investors' enthusiasm and prevented the dangerous build-up of top-of-the-cycle investor euphoria. It is often said that to sustain a bull market, investors must constantly climb a wall of worry.

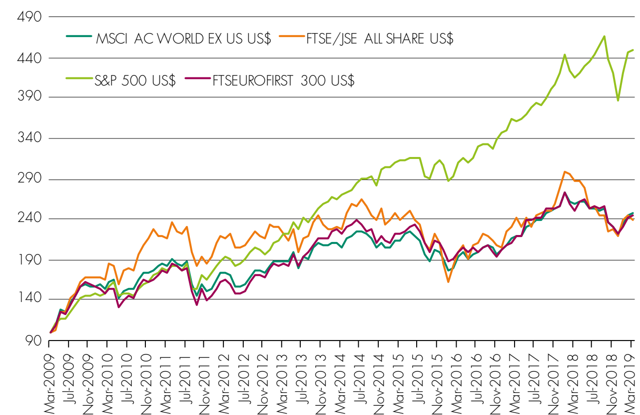
INVESTMENT LESSON OF THE DECADE

The fact that March 2009 was such a volatile month is perhaps a fitting way to celebrate what has often been said to be the most unloved bull market in history. From the outset, no one seemed to believe that the rally had legs. Investors were so scarred by the experiences of 2008 and 2009 that every little bump felt like it could lead to a return to those dark months. Central banks, led by the US Federal Reserve, adopted unconventional policies, first by cutting rates to zero (they would later fall below zero in Europe and Japan) and then by launching quantitative easing (QE) programmes that bought bonds with the aim of driving long-term interest rates down and getting investors to take more risk. But QE was quickly criticised by some quarters as leading the economy down a path of runaway inflation (based on the erroneous assumption that it was simply putting money into the hands of investors and consumers). This criticism was dead wrong as inflation has been missing in action over the past decade. But it did add to the uncertainty and confusion of many investors.

The rally started in March 2009 not because there was suddenly certainty that the GFC was over or clarity over the path ahead but rather, things were getting less bad and the then-chairman of the Federal Reserve Ben Bernanke famously noted that the "green shoots" of an economic recovery were visible. But there was still a great deal of fear after major global equity indices had basically halved and the global economy was still in a bad state. Indeed the US lost a record 800 000 jobs in March 2009.

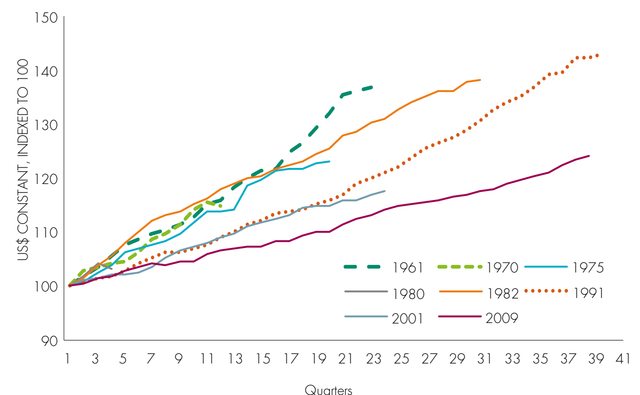
With the benefit of hindsight, those investors who waited for the dust to settle and the fog to clear would've waited a long time and missed an impressive rally. Indeed, with all the raging political uncertainty, they might still be waiting. In contrast, investors who saw a valuation opportunity as markets became cheaper and cheaper were handsomely rewarded, but it meant going against the unsettling media reporting, sensation-seeking investment newsletters and the prevailing sentiment. This is why it is often said investing is simple but not easy. Selling high and buying low is simple in theory but difficult in practice. It again underlines the importance of engaging with a financial adviser, developing a personalised financial plan with the appropriate investment strategy, partnering with an experienced investment team and ignoring the noise and market volatility.

CHART 1: GLOBAL EQUITY INDICES SINCE MARCH 2009



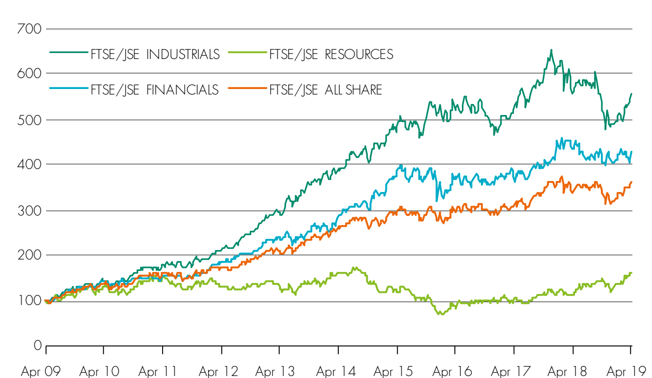
Source: Refinitiv

CHART 2: CUMULATIVE US ECONOMIC GROWTH DURING EACH UPSWING



Source: Refinitiv

CHART 3: JSE MAIN SECTORS SINCE 2009 IN RAND



Source: Refinitiv

INDICATORS

EQUITIES - GLOBAL

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
Global	MSCI World	US$	2 150.0	1.99%	1.99%	14.12%	3.32%
United States	S&P 500	US$	2 893.0	2.08%	2.08%	15.40%	8.64%
Europe	MSCI Europe	US$	1 673.0	2.32%	2.32%	12.58%	-5.32%
Britain	FTSE 100	US$	9 708.0	2.32%	2.32%	13.08%	-3.71%
Germany	DAX	US$	1 263.0	3.87%	3.87%	3.89%	-11.12%
Japan	Nikkei 225	US$	195.2	2.04%	2.04%	0.88%	-3.17%
Emerging Markets	MSCI Emerging Markets	US$	1 085.0	2.55%	2.55%	12.32%	-6.95%
Brazil	MSCI Brazil	US$	2 133.0	2.50%	2.50%	9.72%	-4.78%
China	MSCI China	US$	85.4	3.08%	3.08%	21.31%	-3.13%
India	MSCI India	US$	599.2	0.58%	0.54%	7.38%	3.13%
South Africa	MSCI South Africa	US$	489.0	5.84%	5.84%	9.89%	-15.25%

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	57 776.0	2.33%	2.33%	9.55%	3.61%
All Share	All Share (Total Return)	Rand	8 557.0	2.53%	2.53%	10.70%	6.98%
TOP 40/Large Caps	Top 40	Rand	7 604.0	2.66%	2.66%	11.35%	8.13%
Mid Caps	Mid Cap	Rand	15 982.0	1.49%	1.49%	4.29%	-1.93%
Small Companies	Small Cap	Rand	17 456.0	0.65%	0.65%	-2.78%	-15.97%
Resources	Resource 20	Rand	3 209.5	2.60%	2.60%	19.21%	44.80%
Industrials	Industrial 25	Rand	13 775.0	1.98%	1.98%	10.95%	-1.98%
Financials	Financial 15	Rand	9 676.0	4.39%	4.39%	3.94%	1.29%
Listed Property	SA Listed Property	Rand	1 884.4	0.87%	0.88%	2.36%	-6.06%

FIXED INTEREST - GLOBAL

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
US Aggregate Bond Index	Bloomberg Barclays	US$	487.1	-0.48%	-0.48%	1.71%	-0.32%

FIXED INTEREST - SOUTH AFRICA

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
All Bond	BESA ALBI	Rand	663.6	1.01%	1.01%	4.80%	4.71%
Government Bonds	BESA GOVI	Rand	657.3	1.04%	1.04%	4.90%	4.29%
Corporate Bonds	SB JSE Credit Indices	Rand	97.6	0.39%	0.39%	-4.21%	-19.50%
Inflation Linked Bonds	BESA CILI	Rand	255.4	0.27%	0.27%	0.77%	-3.03%
Cash	STEFI Composite	Rand	418.6	0.14%	0.14%	1.87%	7.27%

COMMODITIES

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
Brent Crude Oil	Brent Crude ICE	US$	70.4	4.20%	3.57%	30.43%	2.07%
Gold	Gold Spot	US$	1 291.0	-0.08%	-0.08%	0.78%	-2.71%
Platinum	Platinum Spot	US$	898.0	6.15%	6.15%	13.24%	-1.32%

CURRENCIES

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
ZAR/Dollar	ZAR/USD	Rand	14.09	2.84%	2.87%	1.85%	-14.97%
ZAR/Pound	ZAR/GBP	Rand	18.37	2.89%	2.89%	-0.27%	-8.66%
ZAR/Euro	ZAR/EUR	Rand	15.80	2.90%	2.90%	4.23%	-7.17%
Dollar/Euro	USD/EUR	US$	1.12	0.00%	0.18%	2.41%	8.93%
Dollar/Pound	USD/GBP	US$	1.30	-0.02%	-0.28%	-1.82%	7.39%
Dollar/Yen	USD/JPY	US$	0.01	0.78%	0.78%	1.94%	4.06%

Source: I-Net, figures as at 5 April 2019

HELPLINE +27 21 524 4430 | **FACSIMILE** +27 21 441 1199 | **EMAIL** ommmclientquery@ommm.co.za | **INTERNET** www.ommultimanagers.co.za

ASSET MANAGER MOVEMENTS

There were no manager movements over the past week.

THE WEEK AHEAD

SOUTH AFRICA

- Mining and manufacturing index

US

- Job openings and labour turnover
- Inflation
- Consumer sentiment

EUROPE

- European Central Bank interest rate decision
- Eurozone industrial production

CHINA

- Inflation
- Exports and imports

Whilst every care has been taken in compiling the information in this document, the information is not advice and Old Mutual Multi-Managers and/or its associates, do not give any warranty as to the accuracy or completeness of the information provided and disclaim all liability for any loss or expense, however caused, arising from any use of or reliance upon the information. Please note that there are risks associated with investments in financial products and past performances are not necessarily indicative of future performances.

HELPLINE +27 21 524 4430 | **FACSIMILE** +27 21 441 1199 | **EMAIL** ommmclientquery@ommm.co.za | **INTERNET** www.ommultimanagers.co.za

Old Mutual Multi Managers ("OM m|m") is a business unit of Old Mutual Life Assurance Company (South Africa) Limited ("OMLACSA"), a licenced Financial Services Provider, Reg. No: 1999/004643/06. OM m|m is authorised to provide financial services on the OMLACSA license, FSP 703.