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The Investment Specialists

Quarter 2 – 2021
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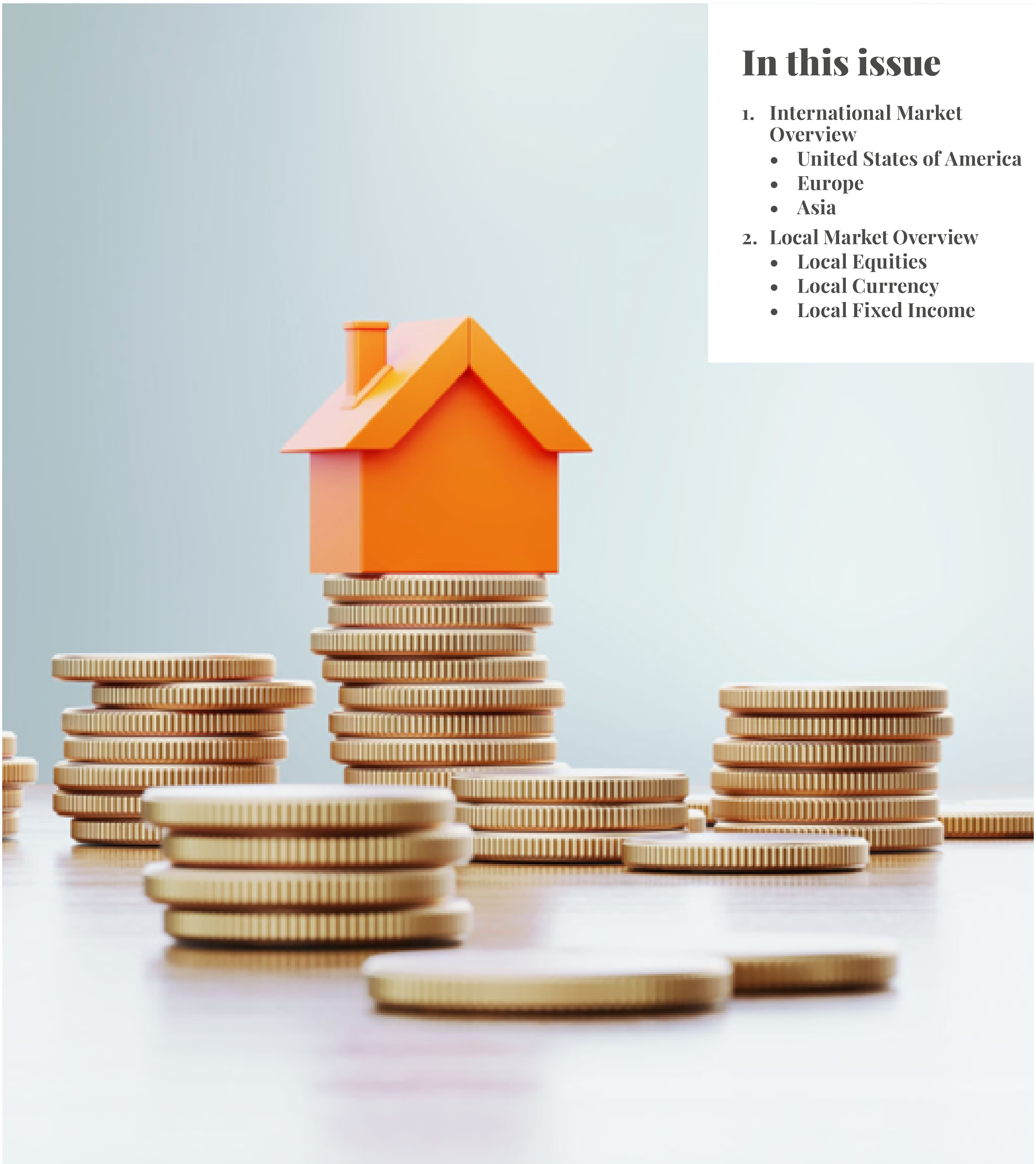
ASSET MANAGEMENT House View



In this issue

International Market Overview

World markets continued the positive tone set in the first quarter, new variants of Covid-19 notwithstanding.

The momentum of the world economies gathered a head of steam as corporate earnings in the US and economic activity surprised on the upside. The MSCI World index increased during the quarter, delivering its best month in April since November 2020. America continued to set new record highs in their major indices, while Europe relaxed restrictions imposed during 2020 and the early part of 2021.

United States of America

US markets continued to see a significant recovery with all major indices hitting new record highs as sentiment and positive corporate earnings continued to boost the expectation that the economic recovery will happen a lot quicker than anticipated. During the period we witnessed a number of positives, with economic activity nearing pre-pandemic levels. In April, President Biden addressed a joint session of Congress in which he introduced a $2tln infrastructure plan, as well as a $1.8trln plan for families, children, and students. The stimulus cheques sent out in January ($600), and March ($1400) not only boosted personal consumption expenditure (soaring 10.7% on an annualised basis), but also business investment (up 9.9% on an annualised basis).

A further impact of the stimulus was reflected in the GDP numbers for the first quarter, released in April (accelerating to 6.4%), and by 6.5% for the second quarter of 2021. Jobless claims also came in lower over the period, further indicating that the economy was moving closer to the pre-pandemic level. The FED kept rates unchanged at zero at the June meeting, which was broadly expected, with a creep upwards in their 2021 inflation forecasts. The FED did spring a surprise on the market, however, by signalling that there could be two rate hikes in 2023, bringing forward the expectation of the first hike from early 2024 to the third quarter 2023. Consumer confidence continues to rise on the back of a growing optimism in the US labour market as the economy reopens, which may calm some of the lingering inflation concerns.

Europe

Markets in Europe followed their American counterparts firmer as optimism around an economic recovery in Europe continued to drive markets higher, the FTSE was up by 4.8%, the DAX up by 3.48%, and the CAC up by 7.26%.

Economic data out during the quarter showed that economic sentiment had climbed to a three year high with inflation in the eurozone falling back to 1.9%, which is within the target range of the European Central Bank (ECB), whilst the reading for core inflation (excluding energy alcohol and food) fell yoy to 0.9% vs. 1.0% in May.

During the first quarter of 2021 the UK economy showed signs of a slowdown as the economy shrank by 1.6% which was higher than the expected estimate of a GDP contraction of 1.5%. This translated to the economy being 8.8% lower than it's prep-pandemic levels (It must be noted that the data covered the period when the UK was in their third lockdown). The BoE has indicated that the growth of the economy is expected to be around the 5% level for the second quarter of 2021, providing the covid restriction are lifted, and the UK continues rolling out the fastest vaccination programme in Europe. Europe's largest economy Germany, declined in June as their unemployment rate stayed at 5.9%, whilst the number of people out of work was down by 38,000 to 2.69 million in seasonally adjusted terms.

The French economy had a revision of their strong quarter one GDP print of 0.4%, with the economy contracting by 0.1% in that period, pushing France into a technical recession.

Asia

The markets in Asia ended the quarter largely in the black, as the covid impact continued to weigh through the region. For the quarter, the Shanghai Composite Index was up 4.34%, the Hang Seng up by 1.58%, whilst the Nikkei ended the period down by 1.33%

Economic data out of China indicated a contraction of their May PMI numbers to 51.0 vs Aprils 51.1, with consensus of 51.1. This number fell further in June to 50.9, as the region continues to be heavily impacted by both the increasing numbers of new covid cases, and factory output being dampened by the continued chip supply shortage. Retail sales in Japan for the same period fell by a seasonally adjusted 4.5% month on month missing consensus estimates of a month on month gain of 2%. The year-on-year retail sales number jumped 12% (admittedly off a low base), but again missing the consensus number of an expected year on year gain of 15.3%. In the second period of the quarter the Japanese unemployment rate declined from the 2.8% level in April, to 3% in May, this is the highest level in almost five-months. The Japanese government, cognizant of the renewed risk of the new covid variant, extended their already declared state of emergency to more parts of the country.

SOUTH AFRICAN LOCAL MARKET OVERVIEW

Local Equities

Resources

Resources were the worst performing sector for the second quarter, with the FTSE JSE Resources 10 (FTSE JSE Resi10) down -5.5% compared to the JSE ALSI which was up +1.07%. Furthermore, the FTSE JSE Resi10 was the strongest performing sector in the first quarter up +18.75%, thus indicative of a significant pullback in the valuations among resources. Platinum Group Metals and gold miners were among the largest detractors in the index, with Anglo American Platinum (the worst performing resource stock for the quarter) and Impala Platinum down -23.37% and -15.5%, respectively. Anglogold Ashanti was the worst performing gold miner and the second worst performing resource stock at -20.4% for the quarter. Diversified miners Glencore, BHP and Anglo American returned +7.74%, +0.84% and -2% respectively, in the second quarter. Glencore was the best performing counter in the Resi10. The global commodity giant has enjoyed a period of rising commodity prices as the S&P GSCI (a commodity index consisting of metals, energy and agriculture commodities) rose 13% over the quarter. In the past, the share price has been depressed due to concerns surrounding ESG (environmental, social and governance) standards, costly legal battles, and the changeover of leadership as veteran CEO Ivan Glasenberg retired in June, making way for Gary Nagle. Nagle, who took over as CEO on 1 July 2021, has been at Glencore for 22 years and was the previously head of Glencore's coal business. Moving onto oil, Sasol traded slightly lower in the second quarter, down -2%.

Industrials

Industrials experienced a similar pull back to that of resources, with the INDI25 dropping -2.17% in the second quarter from a strong first quarter run of +12.4%. From the middle of the second quarter all attention was on Naspers as management announced a proposed share swap between Naspers and Prosus. The share swap is aimed at reducing the growing discount to NAV which is currently witnessed in the Naspers share price. There has been significant push back from shareholders, however, with regards to the proposed share swap and in June 36 asset managers petitioned the Naspers management against the proposal. The petition cited complexity in the overall company structure and the misalignment of management's incentives as potential issues that could further widen the discount gap. Furthermore, the uncertainty surrounding Chinese regulation of the technology sector added to the risks weighing on Naspers' share price. Naspers and Prosus were the largest detractors in the INDI25 for the second quarter, down -19.38% and -18.77%, respectively.
The Foschini Group (TFG) was the best performer in the INDI25 for the quarter, up +29.9%. The group benefited from a strong uptick in revenue from its largest segment, TFG Africa, as revenue for the full year increased by +1.6%, despite lockdown restrictions. According to TFG, revenue growth was due to a strong recovery in the second half of the year, the inclusion of Jet and record online sales. With regard to its record online sales, the group stated that, "total online sales grew by 33% during the year, with the strongest online growth coming from South Africa - which grew by 132%".
Moving to other industrial shares, the following showed strong performances over the second quarter: Richmont (+21.6%), Truworths International (+20%), MTN (+20,77%) and Life Healthcare Group (+19,58%).

Financials

Financials were the best performing sector for the second quarter, with the FINI15 index returning +9%, leading the JSE ALSI up +1.07%. Investec was the best performing stock in the index, strengthening by +25.82% for quarter. Investec was also the top performer for the first quarter, returning +20%. Capitec was the second-best performing stock for the quarter, up +22.61%, followed by Nedbank, up +20.99%. Staying in the banking sector, FirstRand and Standard Bank returned +4.87% and +4.79% over the second quarter, respectively.

Turning to the insurers, Old mutual was the best performing insurance company, gaining +11.49%, with Sanlam also up +10.44%. Discovery was the biggest insurance laggard, down -4.79%. Quilter (formerly Old Mutual Wealth) was the largest detractor in the FINI15 index, down -11.55% for the second quarter.

Local currency

The local currency remained volatile over the second quarter. At the start of the quarter the USDZAR was 14.63, with the rand steadily appreciating to USDZAR 13.42 until the start of June. June saw a rapid depreciation of the rand to USDZAR 14.29 where it closed off the second quarter. Notable events during the quarter included the SARB keeping interest rates unchanged as inflation remained within the target range and the US Federal Reserve's June hawkish update, which indicated the possibility of rate hikes in 2023 and a rising inflation forecast. At quarter end, the local currency had appreciated by +2.33% from where it started the quarter.

Local Fixed Income

Market Review

The second quarter of 2021 was characterised by the continuation of the global economic recovery, albeit it an uneven pace. The recovery persisted despite restrictions imposed by certain countries due to a third wave of covid-19 infections dominating the landscape. Some key developed markets, however, such as the US and Europe, are returning to near normal as vaccination rates rise rapidly. Key emerging markets still lag developed markets, however, as vaccine availability remains an issue. The strength of the post-pandemic recovery and fiscal support have kept yields elevated since the start of the year. The 10-year generic US yield ended the quarter at 1.47%, with the German 10-year generic yield remaining negative to end the period at -0.21%. The French 10-year yield closed the quarter at 0.13%, with its UK counterpart ending at 0.71%.

The local bond market rebounded from its negative trend in the previous quarter, delivering 6.86% over the three-month period. This was largely due to the reduced amount of issuance in the weekly bond auctions which was prompted by improved revenue collections. Rand strength also supported local yields, but this dissipated somewhat toward the end of the quarter as developed market currencies started to regain their strength following improvement in global growth factors. The SARB voted to keep the repo rate unchanged during its May meeting, highlighting concerns about price growth, but emphasising the need for fiscal prudence to be maintained.

Money Market yields once again moved higher over the quarter despite the monetary policy committee keeping rates on hold. The rise in rates was more pronounced on the medium and long end of the money market curve as demand for bank issued money market investments remained weak.

The bond market (JSE All Bond Total Return Index) was up 6.86% for Q2 2021.

We continue to seek value along the yield curve with careful duration risk positioning of our portfolios.