Market Update - Employee Benefits

January 2018

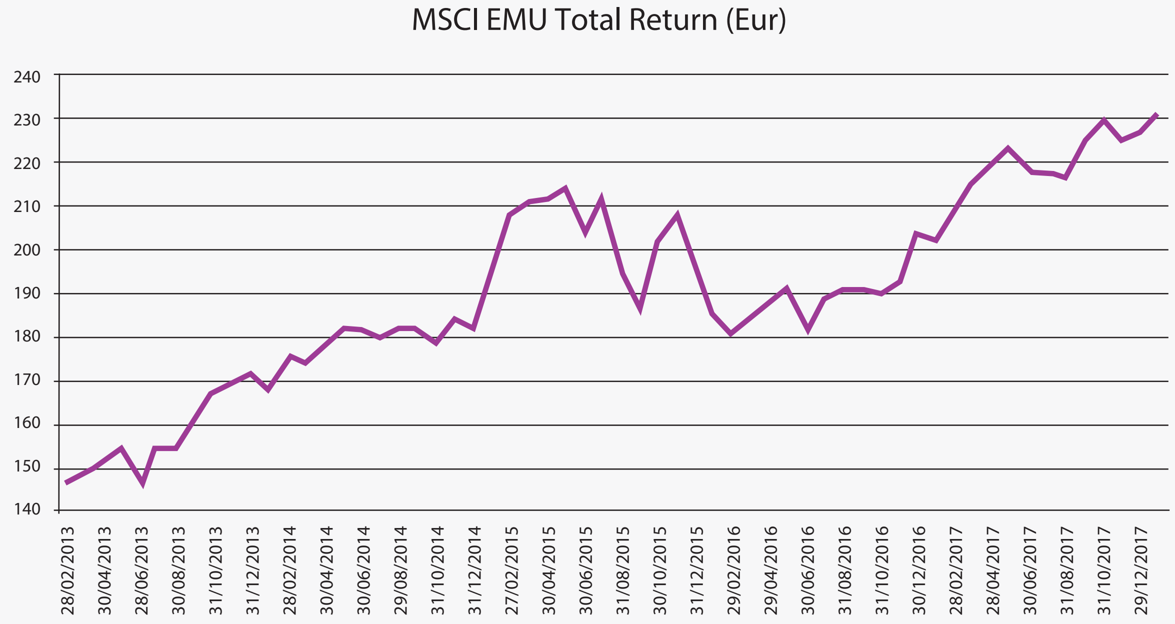
At a glance

- The MSCI Emerging Market Index comfortably outperformed the MSCI World Equity Index, with the former returning 8.3% and the latter 5.2% both in total return terms.
- Global macroeconomic data remained positive, which helped drive global equities to new highs whilst government bond yields rose on the back of renewed inflation fears.
- US equities remained buoyant as economic data continued to underpin the market, but a distinct tone of caution was evident at month end.
- Economic data from the Eurozone continued to reflect improving economies, which drove equity markets higher, but some weakness was evident on the suggestion that the European Central Bank would soon end its quantitative easing policy.
- London's FTSE All Share was the one index out of step with global markets, reflecting negative returns for the month as sterling strengthened against a weaker Dollar.
- Japanese equities gained over the month, with investors focused on the Bank of Japan's forays into the bond market suggesting perhaps that reduced purchases were indicative of a change in economic policy.
- Emerging markets performed particularly well in a risk-on environment, with strengthening global growth as well as Dollar weakness underpinning performance.
- Local market performance was very subdued with the JSE/All Share gaining a paltry 0.10% while the Top40 gained 0.20% both in total return terms.

Global: Stretched valuations?

US equities continued to improve over the month, as fresh economic data provided additional momentum to the market which began the year on a very positive note. Inflation continued to rise on the back of higher energy prices, and retail sales were indicative of a robust economy. Employment numbers also remained healthy with the unemployment number remaining unaltered at 4.1%.

Of significance was the first indication that the long awaited improvement in wage growth had become a reality as average hourly wages rose 2.5% in December, following on a similar rise in November. This development suggested that the Federal Reserve might in future adopt a more rigorous approach in terms of rate hikes. The Dollar eased over the month, which added additional impetus to export oriented stocks, but towards month end market enthusiasm waned.



Source: GTC/FactSet

In the Eurozone markets continued to improve, with the MSCI EMU Index returning 3.2% in total return terms. Minutes from the European Central Bank's December meeting indicated ongoing economic expansion in the region, as opposed to previous meetings where recovery was the watch word. This change in emphasis gave rise to concerns that the previous loose monetary policy might soon be replaced by a more conservative approach.

This possibility resulted in bond yields rising and the Euro strengthening. The higher bond yields resulted in the banking sector attracting considerable interest from investors. GDP data indicated a growth rate of 0.6% for the region which annualised, is indicative of a growth rate of 2.5% which is the highest since 2007. The flash PMI provided the highest reading in some 12 years, while German industrial production continued on its growth path with the unemployment number declining to 8.7%. The German economy grew 2.2% in 2017, the largest expansion in six years.

Dollar weakness resulted in sterling strengthening and as a consequence the London FTSE All-Share delivered a negative return of -1.9% for the month. Sterling also rose as expectations for further base rate increases on the part of the Bank of England gathered momentum.

This resulted in overseas focused companies, as well as large caps, coming under some selling pressure. In line with other global markets, bond yields rose following a broad based sell-off in gilts. Better than expected Chinese macroeconomic data helped the mining sector buck the overall market trend. Adding to the market's woes, annual GDP also decelerated to its lowest level in five years.

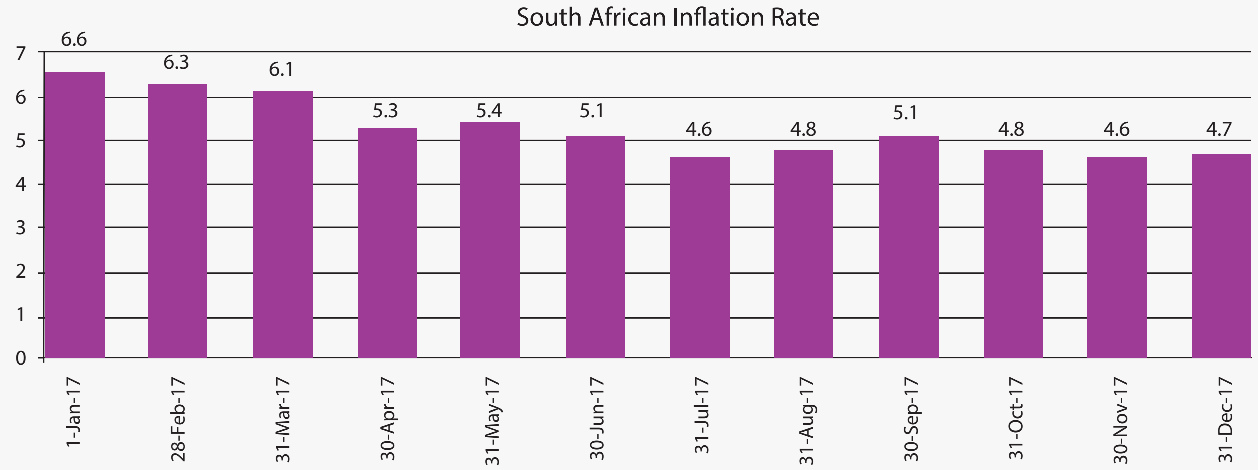
Japanese equities started off 2018 with a bang, but later in the month interest faded and the market provided a total return of 1.1%. Investors' main concerns centered on the Bank of Japan's forays into the bond market, which suggested a possible reduction in bond purchases and hence a change in overall economic strategy. However, investors' fears were subsequently allayed as it transpired that the slowdown in bond purchases was based on specific yield targeting and not a change in policy.

Emerging market equities posted robust returns, following on strong capital inflows as global growth and trade continued to improve. Chinese markets registered strong returns as macroeconomic data revealed better than expected GDP growth coming in at 6.9% year-on-year in 2017.

Domestic: Improved political and economic sentiment

A perceived reduction in political risk, and a renewed sense of positive global economic growth, resulted in a risk on environment prevailing on the JSE. Equity prices in December had already started to reflect this more positive sentiment. However, an inhibiting factor in January was the strength of the Rand which traded at its highest level against the USD in two and a half years.

The resulting outcome was that the prices of the dual listed stocks that form a large part of the JSE All-Share Index came under pressure. It was for this reason that the All Share Index returned a paltry 0.10% and the Top40 0.20% both in total return terms.



Source: GTC/FactSet

The headline CPI annual inflation rate in December 2017 was 4.7%. This rate was 0.1% higher than the corresponding annual rate of 4.6% in November 2017. On average prices increased by 0.5% between November 2017 and December 2017.

The average annual consumer price inflation was 5.3% for 2017 still within the 3-6% target band. Core inflation also eased from 4.5% to 4.4%. The annual percentage change in the PPI for final manufactured goods was 5.2% in December 2017. From November 2017 to December 2017 the PPI for final manufactured goods increased by 0.6%.

Manufacturing production increased by 1.7% in November 2017, compared with November 2016. This increase was mainly due to higher production in food and beverages and basic iron and steel, non-ferrous metal products, metal products and machinery. Seasonally adjusted manufacturing production increased by 0.9% in November 2017 compared with October 2017. This followed month-on-month changes of 0.8% in October 2017 and -1.0% in September 2017.

Mining production increased by 6.5% year-on-year in November 2017. The largest positive contributors were PGMs, iron ore and coal. Gold decreasing by 8.3% was a significant negative contributor. Seasonally adjusted mining production decreased by 0.7% in November 2017 compared with October 2017. This followed month-on-month changes of 2.7% in October 2017 and -6.8% in September 2017.

Retail sales increased by 8.2% year-on-year in November 2017. The main contributors to the 8.2% increase were: general dealers, retailers in textiles, clothing, footwear and leather goods. Seasonally adjusted retail trade sales increased by 4.0% month-on-month in November 2017. This followed month-on-month changes of -0.1% in October 2017 and -0.4% in September 2017
South Africa's seasonally adjusted Absa Purchasing Managers' Index (PMI) fell for the first time in four months in December with business activity and new sales declining sharply. The index which is compiled by the Bureau for Economic Research, fell to 44.9 in December from 48.6 in November. The deterioration was broad-based with all five subcomponents of the headline index falling compared to November's level.

Domestic vehicle sales ended 2017 on a weak note, with aggregate industry new vehicle sales for December recording a decline of 2.4% compared to the total new vehicle sales in the corresponding month of December 2016. In contrast, export sales recorded a decline and reflected a fall of 7.1% compared to exports during December 2016. For the first time in four years new vehicle sales in South Africa recorded a year on year improvement albeit at a modest 1.8% in volume terms. The World Bank has forecast GDP growth in South Africa to improve to 1.1% in 2018, from the previous year's 0.8%. The bad news is that this makes SA a laggard among emerging markets, which are expected to average 4.5% growth this year and places SA far below the global average of 3.1%.

South Africa's business confidence index rose for a second month in a row in December, due in part to political developments that have raised expectations of policy certainty and economic reforms, the South African Chamber of Commerce and Industry's survey showed. The SACCI monthly business confidence index rose to 96.4 in December from 95.1 in November. Markets continued to make new highs with valuations becoming over stretched as bond yields started to rise. The sense of euphoria might well see equities experiencing some downward correction until such time as earnings justify the very high P/E ratios.

GTC fund performances - January 2018

Client portfolios	1 Year %	3 Year* %	5 Year* %	7 Year* %	10 Year* %
GTC EB Conservative	7.10	5.84	6.38	6.87	7.38
GTC Conservative Inflation Target - CPI+1%	5.59	6.52	6.46	6.58	6.83
GTC EB Moderate	8.44	5.77	7.54	8.26	9.09
GTC Moderate - Inflation Target - CPI+3%	7.59	8.53	8.46	8.58	8.83
GTC EB High Equity	11.33	6.94	8.78	9.46	10.24
GTC High Equity Inflation Target - CPI+5%	9.60	10.53	10.46	10.58	10.84
GTC EB Market Plus	12.70	6.79	10.24	10.82	10.68
GTC EB Market Plus - Benchmark	11.74	6.79	10.25	11.31	9.28
FTSE/JSE All Share Index (ALSI)^	14.37	6.61	9.60	11.22	9.67
FSTE/JSE Shareholder Weighted Index (SWIX)^	15.64	6.10	10.60	12.42	10.75
BEASA All Bond Index (ALBI)^	9.15	3.79	5.06	6.98	7.23
Cash (SteFi)^	5.91	5.58	4.95	4.69	5.52
MSCI World Index (R)^	7.42	8.95	14.15	14.08	7.91

*Annualised

GTC Performances are shown net of all fees

^Benchmark returns include 1.5% fees

The **GTC Conservative Fund** was ahead of its inflation adjusted target over one year and longer term periods. Equity markets remain the key driver of performance.

The **GTC Moderate Fund** was ahead of its inflation adjusted target over one year and in line over longer term periods. Equity markets remain the key driver of performance.

The **GTC High Equity Fund (previously Aggressive)** was ahead of its inflation adjusted target over one year and lagging over longer term periods due to real rate detraction from equity markets' impacts over the medium term.

The **GTC Market Plus Fund** was ahead of its target over the short term and in line over the long term. Our manager blend has a component of protection which we feel is prudent in the current environment.

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