

# Trendline

## Fourth Quarter 2018 - Employee Benefits



### At a glance

Q4 2018 proved to be a poor one for equity markets globally with all major indices printing negative returns as investor sentiment waned and volatility returned to markets amidst mixed data.

Global bonds proved to be defensive in the selloff.

Geopolitical risk remained in the spotlight as the trade standoff between the US and China created uncertainty, whilst renewed concerns around a hard Brexit raised its head as Theresa May postponed a key vote.

Fitch affirmed SA's long term foreign credit rating at BB+ with a stable outlook.

The local market (FTSE/JSE) did not escape the rout as it ended the fourth quarter in negative territory.

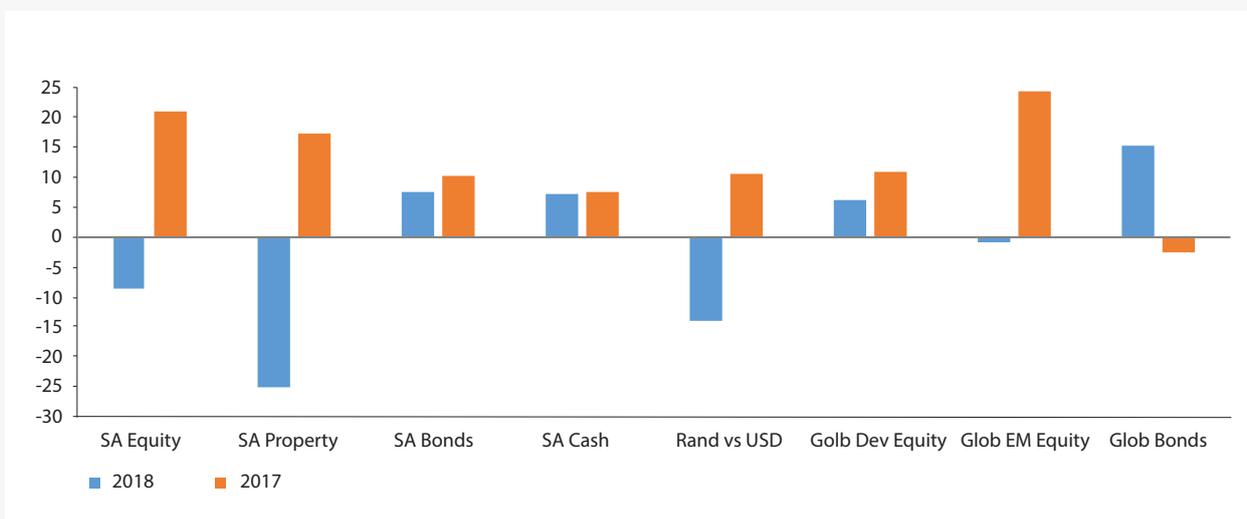
The SA economy officially exited the recession after two consecutive quarters of negative growth.

SA headline CPI annual inflation rate came in at 5.2%, up 0.1% from October 2018's reading.

SA lost 16,000 jobs in Q32018 as manufacturing, construction and mining sectors contracted.

# Annual review

Asset class returns 1 year to December (%)



Source: FactSet/GTC

2018 proved to be a risk off year, with markets weighed down amidst a cocktail of trade war rhetoric, the rise of political populism and concerns around a slowdown in growth in the US and China. Fiscal stimulus in the US saw the US markets steaming ahead before concerns around a potential slowdown saw markets decline in Q4.

Locally, the JSE All Share 2018's -8.5% decline once again saw the market slip into a sideways trajectory over five years, after starting the year very strongly on the back of a change in leadership within the ruling party. SA property took a beating in 2018 as concerns around the Resilient group of companies saw the index shedding 25%.

Despite net foreign sales, the SA All Bond Index returned 7.7% - only being eclipsed by global bonds which returned 15.2% as the best asset class for 2018, thanks mainly to a weaker Rand (-13.9%). Global equity markets returned 6.1% buoyed by US markets on the back of tax cuts and strong consumer and employment data. Emerging markets ended the year down -0.7% as investors fled to the safe haven of US bonds amidst the uncertainty and trade standoff between the US and China.

The divergence in returns between calendar years 2017 and 2018 as depicted in the above chart is reflective of the volatility of measuring returns over short periods. Notwithstanding, equity markets have failed to compensate investors in respect of the risk premia over the last five years.

# Global - Macro slowdown or recession?

Volatility in global markets epitomised the fourth quarter of 2018 as investors' sentiments were tested with mixed data amidst increased geopolitical concerns surrounding the trade standoff between the US and China, weakening Chinese economy, and the possibility of a hard Brexit landing.

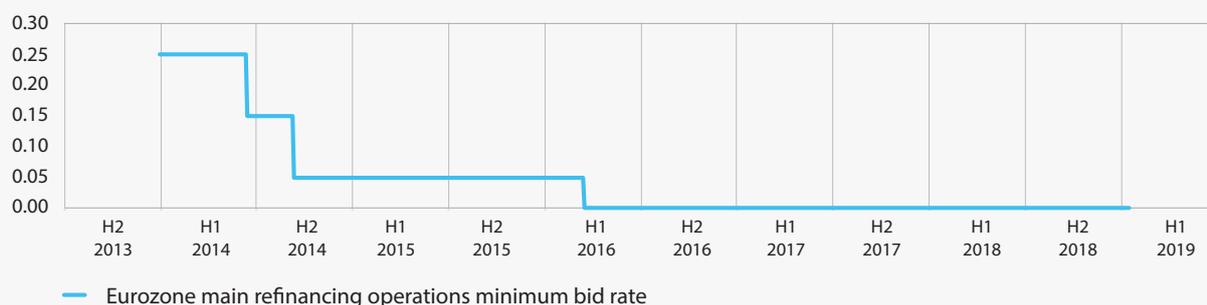
October saw the sharpest one month decline since May 2012, with the MSCI World shedding -7.3% with Emerging Markets eclipsing the fall tabling at -8.7%.

November provided a brief respite and recovery, only for December to table a -7.6% fall as the US fell 9.0% - despite US jobs data exceeding 3% for the first time since April 2009. A key measure of US inflation picked up as expected in November on rising costs for housing, medical care and used cars, reinforcing expectations that the Federal Reserve would raise interest rates.

The core consumer price index, which excludes volatile food and energy costs, rose 0.2% from the prior month and 2.2% from a year earlier, matching the median estimates in a Bloomberg survey of economists. The broader CPI was unchanged from the prior month as energy prices declined.

The US Federal Reserve raised rates as expected and kept most of its guidance for additional hikes in 2019, dashing investor hopes for a more dovish policy outlook. But the slight revision was not enough to ease market fears over a further US economic slowdown on the back of trade tensions, a declining boost from tax cuts and higher borrowing costs for companies.

## EU Borrowing Rate



Source: FactSet/GTC

The European Central Bank will halt its €2.6tn stimulus programme, despite concerns that the Eurozone is poised to slow down over the next couple of years. Mario Draghi warned that rising uncertainty had forced the bank to downgrade its outlook for the Eurozone next year and the effects would continue to be felt in 2020. He said growth would be limited to 1.7% in 2019, owing to the persistence of uncertainties related to geopolitical factors, the threat of protectionism, vulnerabilities in emerging markets and financial market volatility.

The European Commission said it has reached an agreement with Italy on its budget plans, which the EU's executive arm had warned could break the Euro's rules and lead to legal action.

The Commission said it had been reassured by new fiscal measures provided by the Italian government. Italy's revised plans call for a budget deficit of 2.04% of GDP, down from the original 2.4% that had sparked the EU alarm.

A slowdown in export orders due to a drop in demand in China, raised concerns on the impact that the trade war is having on the global economy.

In France, widespread unrest surrounding the cost of petrol saw President Macron announce a cut in fuel duty costs and further stimulus in an attempt to ease tensions.

The UK saw increased focus on the possibility of a Brexit hard landing as Theresa May postponed a key cabinet meeting, a clear admission by the prime minister that she did not believe she could get the unpopular EU withdrawal agreement through the House of Commons. The deadline for the vote is 21 January 2019, not leaving Prime Minister May with much time to not only convince opposition parties, but also doubters within her own party to back the exit agreement.

The Japanese economy shrank 0.6% quarter-on-quarter, twice the preliminary estimate of a 0.3% drop and market expectations of a 0.5% decline. It is the steepest contraction since the second quarter of 2014, following a downwardly revised 0.7% expansion in the previous quarter. Forecasts for economic growth and consumer prices for the current and next fiscal years were cut, as natural disasters and weakening export demand weighed on the economy. Japan's economy will grow 0.9% in fiscal 2018, which ends in March, down from its previous projection of 1.5% growth.

The Chinese economy advanced 6.5% year-on-year in Q3 2018, missing market consensus of 6.6% after a 6.7% growth in Q2 2018. It was the lowest growth rate since the first quarter of 2009 during the global financial crisis. China's November retail sales grew at the slowest pace since 2003 and industrial output rose the least in nearly three years, as domestic demand softened further, underlining rising risks to the economy as the potential tariff war with the US approaches. A temporary truce between the US and Chinese leaders gave emerging markets some hope.

Presidents Donald Trump and Xi Jinping agreed to keep their trade war from escalating. The leaders pledged to halt the imposition of new tariffs for 90 days and intensify their talks as the world's two largest economies negotiate a lasting agreement. Chinese authorities have indicated that they will soon provide specific details. China moved toward cutting its trade-war tariffs on imported US made cars. A proposal to reduce tariffs on cars made in the US to 15% from the current 40% had been submitted to China's Cabinet for review approval. Top Chinese and American trade officials held telephonic discussions signalling that dialog between the two nations on trade issues was at least continuing.

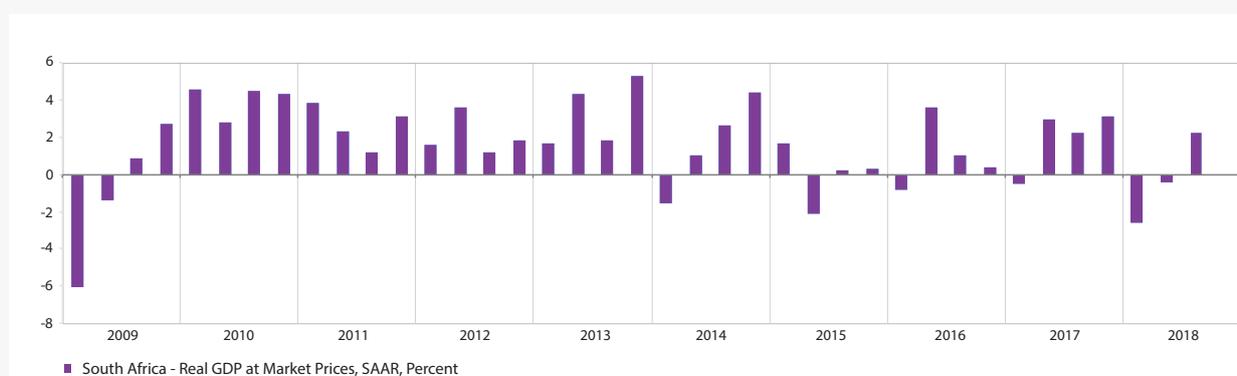


## Local - Time to turn the leaf

The JSE All Share Index fell in line with global markets, tabling a -4.9% (ZAR) decline over the quarter with Industrials (-6.5%) and Resources (-5.0%) leading the overall index lower. Property was down -4.0% as Nepi Rockcastle came under selling pressure amidst another report by Viceroy Research claiming overstatement of profits.

The All Bond index ended the quarter up 2.74% as the SA Reserve Bank kept rates unchanged, while tabling a 7.7% return over the year as the bond market's defensive attributes came to the fore. The STEFI cash composite returned 1.77% over the quarter, while the Rand closed at 14.39 to the US Dollar.

### GDP Growth



Source: FactSet/GTC

The SA economy officially exited the recession after reporting 2.2% GDP growth for Q3. The rebound was in line with the expectations of economists who projected positive growth of between 0.8% and 2.5%. Economists polled by Reuters had predicted a 1.6% expansion. Stats SA announced that GDP growth for Q2 was revised from -0.7% to -0.4% after figures for the mining and manufacturing industries were revised upward. Data on agriculture and construction were revised downwards.

The main drivers of growth during Q3 were secondary industry, which grew by 4.5% and the tertiary sector which grew by 2.6%. While manufacturing helped boost the growth of the secondary sector, the electricity and construction sectors contracted by 0.9% and 2.7% respectively.

The tertiary sector was boosted by growth in the trade (3.2%), transport (5.7%), finance (2.3%), government (1.5%) and personal services (0.7%) industries. The primary industry slumped by 5.4% in Q3. While agriculture grew by 6.5%, mining slumped by 8.8%, largely due to the decrease in production of platinum, iron ore and gold.

Data showed that the South African Reserve Bank's composite leading business cycle indicator rose 0.2% in October month-on-month, boosted by more job adverts and commodity exports. The indicator collects data on vehicle sales, business confidence, money supply and other factors to gauge the economic outlook.

In November, the headline CPI annual inflation rate came in at 5.2%, 0.1% higher than the 5.1% from October 2018. On average, prices increased by 0.2% between October and November 2018. The annual percentage change in the PPI for final manufactured goods was 6.8% in November 2018. From October to November 2018 the PPI for final manufactured goods increased by 0.4%.

Ratings agency Fitch has affirmed SA's long-term foreign-currency issuer default rating (IDR) at 'BB+' and maintained its stable outlook. However, the agency warned that low growth and the rising debt of state-owned firms posed a risk to the country's ratings.

Mining production increased by 0.5% year-on-year in October 2018. The largest positive contributors were PGMs, diamonds and manganese ore.

The largest negative contributors were iron ore and gold. Seasonally adjusted mining production increased by 3.3% in October 2018 compared with September 2018.

This followed month-on-month changes of 0.7% in September 2018 and 1.1% in August 2018. South African gold output contracted for a thirteenth consecutive month in October, the longest streak of declines in six years, as the industry battles unprofitable mines and labour strikes. Manufacturing production increased by 3% year-on-year in October 2018. The largest positive contributions were made by the following divisions: food and beverages, motor vehicles, parts and accessories and other transport equipment, and basic iron and steel.

Seasonally adjusted manufacturing production increased by 1.1% in October 2018 compared with September 2018. This followed month-on-month changes of -0.8% in September 2018 and 0.2% in August 2018.

Statistics SA said the number of employed South Africans fell by 16,000 in the third quarter of 2018, driven largely by a fall in the number of those employed in the manufacturing, construction and mining sectors. Despite exiting the recession, the weak economy has kept the pace of job creation muted, with recent business confidence surveys showing that most firms reported downward pressure on payrolls.

In the second quarter the economy shed 69,000 jobs. However compared to a year ago employment increased by 17,000 or 0.2% year-on-year with an increase of 25,000 in trade, 22,000 in community services and 21,000 in business services. On a year-on-year basis, gross earnings by employees increased 5.6%, and 4.2% on a quarterly basis.

The retail sector experienced bigger than expected growth at the start of the fourth quarter. Retail trade sales increased 2.2% year-on-year in October 2018 after a contraction of 0.7% in September. The boost came from retailers in household furniture, appliances and equipment, all "other" retailers, retailers in pharmaceuticals and medical goods, cosmetics and toiletries and retailers in textiles, clothing, footwear and leather goods. Compared to the month prior, retail trade sales increased 0.6% in October 2018.

## GTC Fund performances - December 2018

Client Portfolios	1Year %	*3Year %	*5Year %	*7Year %	*10Year %
GTC EB Conservative	1.31	4.62	4.91	6.23	6.77
CPI+1%	6.46	6.52	6.43	6.44	6.26
GTC EB Moderate	-2.09	3.57	4.43	7.19	8.48
CPI+3%	8.46	8.52	8.43	8.44	8.26
GTC EB High Equity	-5.91	3.08	4.52	7.89	9.05
CPI+5%	10.46	10.53	10.43	10.44	10.26
GTC EB Market Plus	-6.53	2.92	4.48	9.11	9.99
Composite Benchmark	-6.27	3.45	5.70	9.67	9.80
FTSE/JSE All Share Index (ALSI) ^	-9.90	2.78	4.20	9.06	10.96
FTSE/JSE Shareholder Weighted Index (SWIX) ^	-13.00	2.15	4.35	9.37	11.35
BEASSA All Bond Index (ALBI) ^	6.09	9.43	6.12	6.21	6.09
Cash (SteFi)^	5.72	5.83	5.34	4.90	5.13
MSCI World Index (R)^	4.50	0.84	8.14	14.55	10.61

\*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 longer term periods. Equity markets remain the key driver of performance.

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

The **GTC High Equity Fund** (previously Aggressive) lagged its inflation adjusted target as equity markets detracted over the short and medium term.

The **GTC Market Plus Fund** was ahead of its target over the long term and lagged over the short term.

Our manager blend has a component of protection which we feel is prudent in the current environment.

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