Market Commentary

July 2023

RISCURA

South African market themes

Rand appreciated 5.9% against the Dollar, then fell 4.2%

South African nominal bond yields decreased; ALBI rose 2.3%

The South African economy has made some meaningful ground in its fight against inflation. Consumer prices have been steadily declining, from 6.8% in April 2023 to 6.3% in May, reaching 5.4% in June. Current inflation prints fall within the South African Reserve Bank's (SARB) target range of 3% to 6%. On the back of this data, the SARB kept interest rates unchanged at 8.25%, with the prime lending rate at 11.75%. While this is positive news for the South African household, the South African Reserve Bank governor, Lesetja Kganyago, quickly added that this does not signal that interest rates have peaked. This is most likely true, given the US Federal Reserve raised its funding rate by 25 bps in July. When considering the interest rate differential between South Africa and the United States, a major component in currency exchange valuations, the Monetary Policy Committee (MPC) will likely aim to maintain an attractive spread between the developing domestic economy and developed economies to attract capital flows.

The Rand had a characteristically volatile month, appreciating 5.9% against the Dollar to close at 17.78. However, this recovery was short-lived as a risk-off sentiment moved through the markets after the US credit rating downgrade. At the time of writing, the Rand fell 4.2% against the Dollar, back to 18.53. South Africa was not the only country to feel the risk-off sentiment, as all emerging market currencies came under pressure. The interest rate differential between SA and the US has been narrowing. This differential will likely be considered in the next MPC meeting. The Committee will attempt to stabilise the currency and manage inflation without hampering economic growth.

The domestic economy had a positive month, with SWIX up 4.1% for July. The financial sector saw the biggest gain, up 7.8%. Resources, bolstered by a rise in commodity prices, rose by 3.16%. Industrials rose a modest 2.6%, taking the sector's year-to-date return to 20.5%. This market optimism coincidentally aligned with an easing in the load-shedding schedule. It was expected that the improvement in power supply, albeit short-term, would lift the nation's manufacturing output, but this was not the case. South African ABSA PMI printed 47.3. The country's manufacturing indicator has been in a contractionary state since February. Manufacturing production volumes are yet to recover fully, down 5.6% from pre-pandemic levels. While load-shedding continues to be the economy's Achilles heel, the private sector continues to build resilience through investment in electricity generation, which will take pressure off the nation's struggling power supply.

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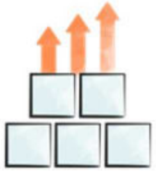
South African nominal bond yields have steadily decreased across the curve in the bond market as global markets reset their expectations for further policy tightening. As the yield curve drops, existing bond prices increase, increasing the All-Bond Index (ALBI) by 2.3% in July. South African 10-year nominal bond yields are currently at 11.5%, and the 20-year is yielding as much as 12.2%. An important factor in bond valuations is an inflation assumption. To get the real return of a nominal bond, one would subtract the inflation rate from the nominal yield to quantify the real return on investment.

If the South African Reserve Bank fulfils its mandate of controlling inflation within the 3%-6% range, South African nominal bonds will offer an attractive yield for both domestic



Copper's 5.7% rise correlates with Chinese stocks

Oil price up 13.3%; adds inflationary pressure

and foreign investors. The Inflation Linked Bond Index (CILI), an instrument designed to hedge long-term investors against inflation risk, rose 1.44%; this decline in yield and rise in price followed the decline in inflation South Africa experienced this month.

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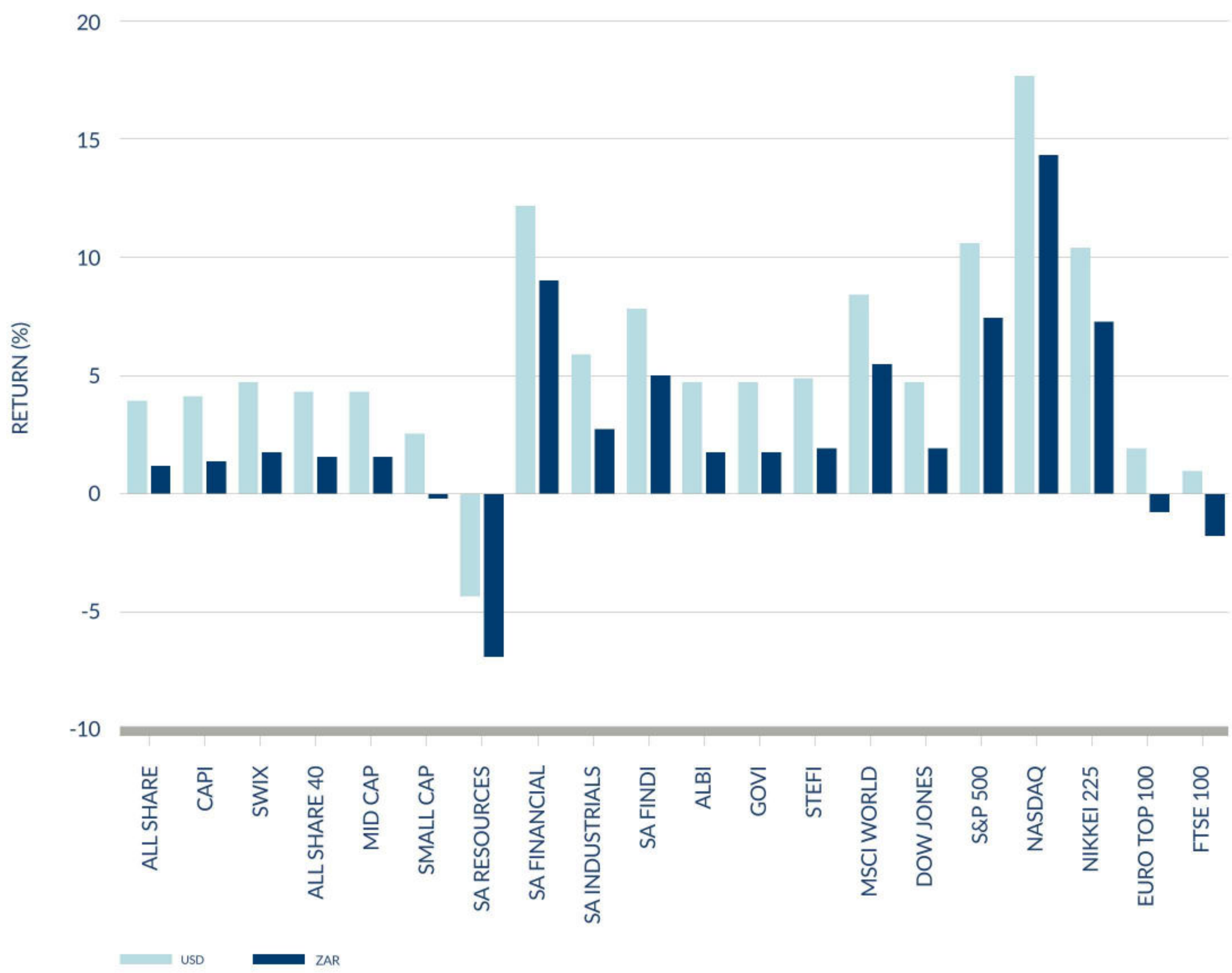
The prosperity of resource-rich countries, like South Africa, is often tethered to the price of commodities. The price of commodities is largely determined by the supply and demand of the global market. From a demand perspective, the production activities of countries like China play a significant role in determining the price of commodities like copper. As we saw in July, the rise in the market value of Chinese stocks shows a correlated move in the commodity sector, with copper rising 5.7%. This factor is an important driver for resource tickers on the JSE, and investors can expect correlated movements between the growth of heavy resource-consuming countries like China, emerging markets, and the price of certain commodities.

On the other hand, oil is imported by South Africa and works in the opposite direction. An increase in oil prices adds inflationary pressures to the economy through added input costs. With the price of oil up 13.3% for July, there will likely be upward pressure on inflation for South Africa going forward as a result.

All returns above are in ZAR.

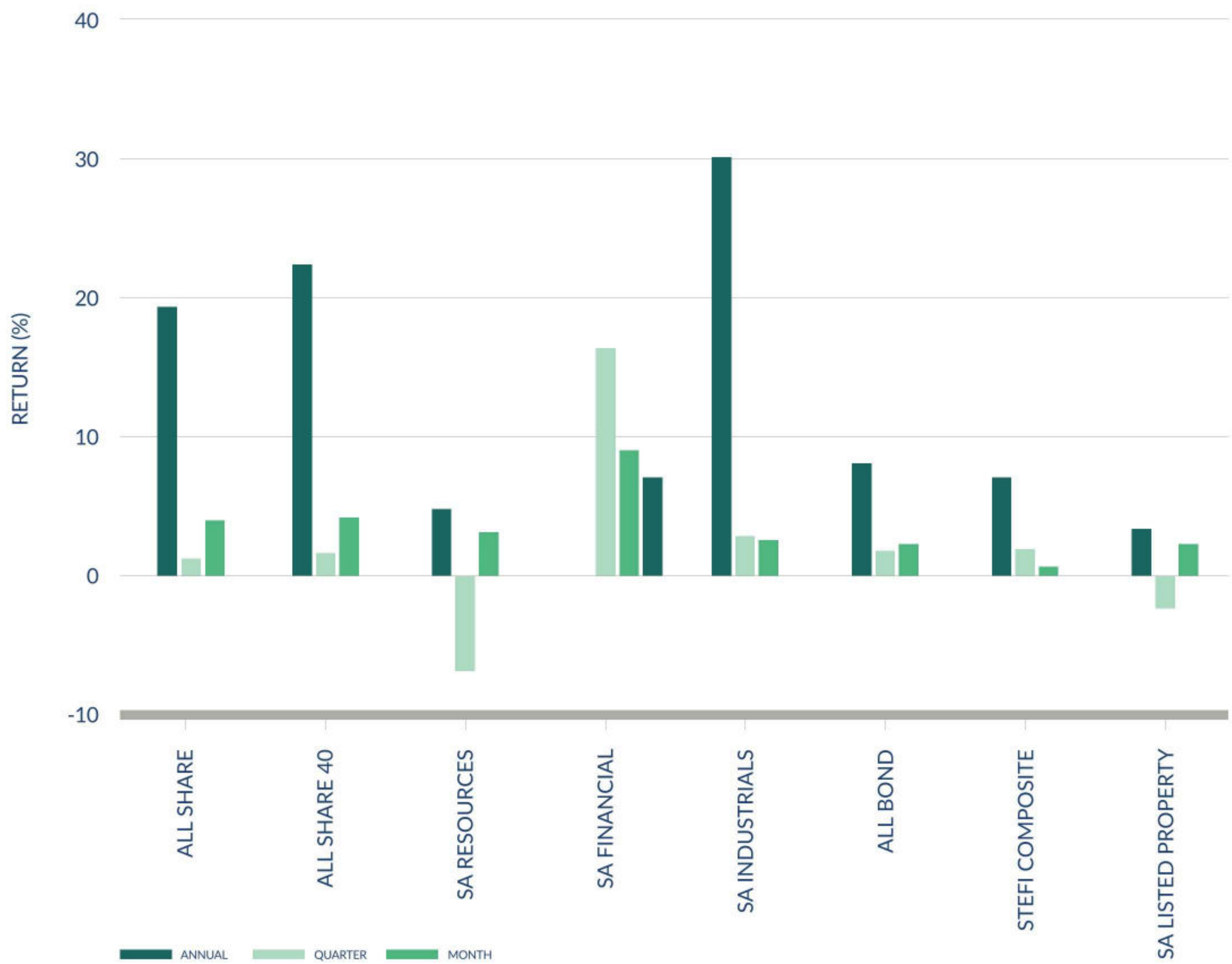
World Market Indices Performance

QUARTERLY RETURN OF MAJOR INDICES



South African Market Indices Performance

RETURNS OF THE FTSE/JSE SECTORS AND INDICES



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