



INVESTMENT VIEWS

Market watch: Looking beyond the relief rally

By CHARLES DE KOCK

THE QUICK TAKE

The Government of National Unity has an opportunity to improve South Africa's economic outcomes

However, we are mindful of the obstacles ahead

Market sentiment will ebb and flow as politicians respond to these challenges

As long-term, bottom-up investors, our focus remains on selecting good businesses at reasonable prices rather than attempting to predict these fluctuations



Charles is a portfolio manager with 38 years of investment industry experience.

THE NATIONAL ELECTION dominated news in South Africa in the past quarter. Most polls forecast that the ANC would drop below the 50% needed to form a government and would, therefore, need a coalition partner or partners. The market feared an alliance with the populist EFF. When that did not materialise and instead a more centrist coalition was formed, we saw a rally in the rand, a drop in long-term bond yields and a surge in domestic stocks – the so-called relief rally.

Our multi-asset funds have a full offshore exposure and are relatively light in SA bonds and domestic facing stocks. Our funds will therefore underperform many peers during this relief rally. Our positioning is, however, based on the view that solving the problems facing the economy will take many years of consistent good decision-making and very good implementation. While the Government of National Unity (GNU) is a positive outcome for the country and has the potential to address many of the pressing issues, it will not be easy to manage the day-to-day working of a government consisting of many different points of view and clashing ideologies.

The low growth rut in which we find ourselves is the result of many years of neglected infrastructure spending and poor management of vital state-owned enterprises, such as Eskom and Transnet, to name but two. Without adequate power, water, rail and functioning ports the economy will struggle to reach its potential. Turning these very important parts of the economy into efficient working enterprises will take a monumental effort with the benefits only visible in years to come.





Government has also run up a huge debt burden, which has had the effect of pushing government bond yields very high, making debt servicing costly and borrowing for new investments very expensive. It is likely to take a number of years of running much tighter budgets to improve the fiscal position of the government. And this comes at a time when big spending on neglected infrastructure is absolutely necessary. A way forward that may well be politically unpopular will need to be found. Wise and decisive leadership will be required.

The political road ahead will be a bumpy one. President Cyril Ramaphosa took some time to announce his new cabinet, as forming the cabinet involved wide consultation to try and accommodate as many of the GNU-parties and his own party individuals as he could. The result is a very large cabinet with especially many deputy ministers from many different political backgrounds. All parties in the GNU will have to find ways to make compromises for the benefit of the country. One must expect the sentiment in the market to ebb and flow between hope and despair. Trying to predict these waves is futile and we will continue, as always, to build our funds from the bottom up, selecting good businesses at reasonable prices in both the domestic and global arenas. The same principles of investing apply to the bond and property sectors, where the longer-term outlook will always be more important than short-term volatility.

Globally the European Central Bank started to ease interest rates, and in the US the Federal Reserve Bank is also expected to start the easing cycle during the second half of the year as inflation numbers have been moving in the right direction of late. When the developed world interest rate cycle moves lower it is likely that emerging economies will follow. In our view, the South African Reserve Bank will also be in a position to lower interest rates, although only mild cuts are expected.

In summary, the economic outlook for South Africa has improved. The new government has an opportunity to raise business and consumer confidence levels off an extremely low base by following sound long-term policies and appointing competent individuals in areas where it is needed. The financial markets will no doubt be buoyed by positive announcements. It reminds us of the period immediately following the election of Ramaphosa as ANC President back in December 2017 – a period commonly referred to as “Ramaphoria”. During that time, markets initially surged but later sagged due to disappointment in real delivery for the economy. Investors learn from previous experiences and the market could well be less euphoric in its expectations this time, waiting for real results to materialise. +



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South African Readers

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