GTC Trendline

2nd Quarter 2016

Global: "Out wins the day"

Global markets began Q2 on a quietly confident note, but subsequent developments were overshadowed by the somewhat unexpected vote by the U.K. to exit the European Union. The MSCI World Index ended the quarter in positive territory returning 1.21% while the MSCI Emerging Markets Index returned -0.32% both in US Dollar terms.

U.S. markets enjoyed a positive quarter with the S&P 500 gaining 2.5%. Volatility was a key note of performance over the quarter in the wake of the U.K.'s "Brexit". The U.S. market managed to hold onto gains that were achieved earlier in the quarter as comments by the Federal Reserve Bank, and more notably from Chairperson Janet Yellen, suggesting that any further interest rate rises were certainly on the back-burner for the moment.

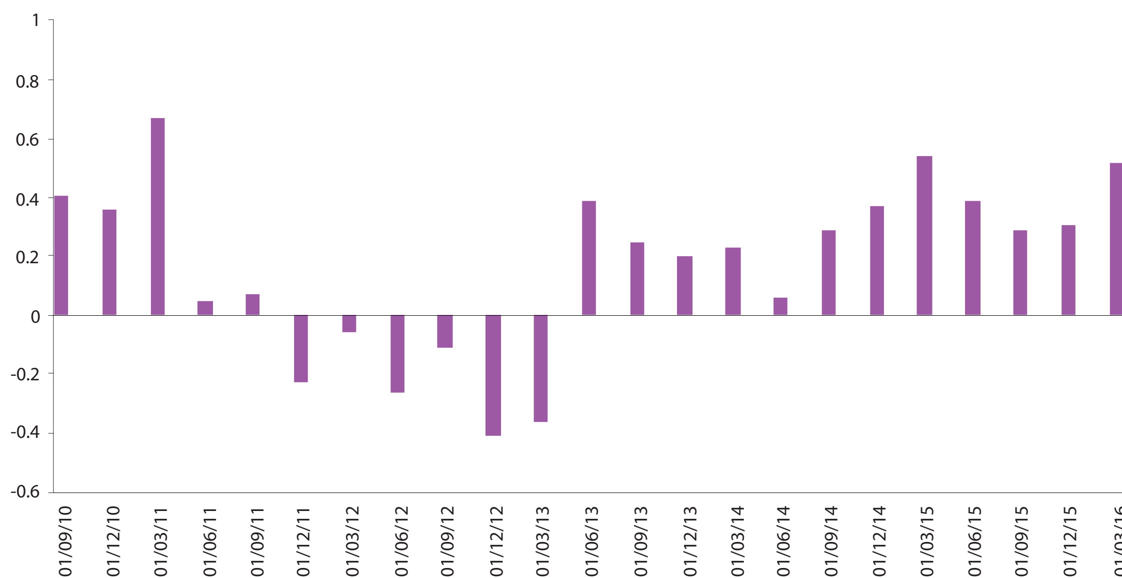
Macroeconomic data coming out of the U.S. in May continued to show improvement with the S&P 500 advancing 1.8% for the month. The revised first quarter GDP number, up from 0.5% to 0.8%, allayed any fear's surrounding the sustainability and durability of the improved economic growth. The slew of positive and better than expected data lent credence to the possibility of further interest rate rises with a concomitant recovery in Dollar strength.

Minutes from the Federal Open Market Committee's meeting in April revealed a strong bias towards a rate rise in June should economic data continue to strengthen. These gains were however reversed in June as the probability of an imminent interest rate rise faded rapidly.

Mixed economic data which began emerging in June soon dampened investors' enthusiasm with May's poor non-farm payrolls number of 38,000 being of particular significance. This, coupled with the unexpected exit of the U.K. from the European Union, led Janet Yellen to repeatedly warn of the considerable uncertainties that surrounded global economic growth. No potentially imminent interest rate rise, helped underpin the improved market sentiment.

The Eurozone experienced very different circumstances with the MSCI EMU Index returning a negative -2.2%. The Index had improved both in April and May but any gains were reversed in the wake of the U.K.'s European Union exit. The uncertainties as to the time frame and economic implications surrounding the exit created sufficient uncertainty as to weigh negatively on markets throughout the region.

Euro-zone GDP growth



Source: GTC / I-Net

Financial stocks bore the brunt of the sell-off with banks being particularly hard hit with the Italian banks coming under substantial selling pressure. The Italian government is seeking ways in which to recapitalize this sector of the market.

Oil prices improved considerably over the quarter which was evidenced by the energy sector delivering a strong performance. Investors favoured safe-haven stocks with consumer staples and healthcare attracting the most attention. As expected, the European Central Bank kept monetary policy unchanged but provided additional details regarding its corporate bond repurchasing programme. The Bank is now permitted to buy corporate bonds in both the primary and secondary market with maturities ranging from six months to thirty years. Bonds issued by insurers are also eligible thus widening the potential scope of the repurchase programme significantly.

Economic data continued to improve with Q1 GDP growth being revised upwards to 0.6% q/q with inflation creeping up to a positive 0.1% in June following May's negative -0.1%. Indicative of a slight slowing down in manufacturing activity Eurozone PMI declined to 52.8 in June from May's 53.1.

The number which missed economists' estimates was hit by French manufacturing and services PMI both of which came in below 50. German composite PMI was at 54.1 in line with estimates indicating that Europe's largest economy is showing little sign of weakness.

Contrary to market reaction in Europe the U.K. market stormed ahead on the back of the "Brexit" vote with the FTSE All Share gaining some 4.7% as a result of the sharply declining value of Sterling. In spite of the ensuing volatility the U.K. equity market rapidly clawed back early pre-Brexit losses and closed at even higher levels. Banking shares came under considerable pressure on concern that Britain's vote to leave the European Union may force those with a large presence in the UK to undergo costly relocations. HSBC is among banks who have warned that they may have to shift jobs from the UK to elsewhere in Europe as a result of the Brexit vote.

The UK quitting the EU raises the prospect of financial firms operating out of London losing so-called passporting rights that allow access to the region's single market.

The improved market was further strengthened by comments by the Bank of England Governor Mark Carney who indicated that the central bank was ready and able to supply additional monetary stimulus should such be required. This certainly helped calm the volatile conditions. Stocks which derived the bulk of their earnings off-shore gained strongly which included oil and gas, consumer goods and healthcare. Sector rotation was very evident as investors became consciously risk averse.

Japanese economic data showed a steady improvement over the earlier part of Q2 but the uncertainty surrounding the possible global fall-out following "Brexit" saw investors flocking to the safe haven Yen resulting in a sharp appreciation of the currency with a resultant collapse of the local market which declined 7.4%.

Trade data emanating from China over the quarter continued to suggest a further slowing of the economy as exports declined even further indicative of global economic malaise and imports were even further reduced. In order to stimulate the economy, The People's Bank of China continued to weaken the Yuan, the currency depreciating both in May and June to close the quarter down -2.9%. The equity market experienced considerable volatility but ended the quarter basically flat.

Domestic: Ratings retained by a whisker

Locally market sentiment was dominated by two major events during the quarter- the first being eagerly anticipated rating announcements and the second being the unexpected decision by the U.K. to exit the European Union. The latter announcement came late in June catching the majority of investors off guard and resulting in significant panic amongst investors. The heightened volatility coming as late in June as it did saw the JSE/ALSI decline 3.02% over the month. The Top40 shed 4.12% while the 30 day volatility leapt from 12.30 to 20.55.

Financials was the worst performer over the quarter losing 4.34% with Industrials flat (0.51%) while Resources returned 6.50% on the back of a heightened gold price. Property was up 0.43% over the quarter.

The All Bond Index (ALBI) rallied a commendable 4.04% with the longer dated maturities capturing the bulk of the outperformance. The 12+ year maturity sector gained 4.73% while the 7-12 year sector returned 4.33%. Inflation linked bonds returned 1.96% with cash returning 0.59%.

Moody's confirmed South Africa's credit rating at Baa2 and adjusted the outlook from stable to negative. The ratings agency said the ratings reflect the view that the country is likely approaching a turning point after several years of falling growth. The negative outlook speaks to the implementation risks associated with the structural and legislative reforms that government, business and labour recently agreed on in order to restore investor confidence. Standard & Poor's rating agency reaffirmed South Africa's sovereign debt rating just one notch above junk while keeping the negative outlook intact citing low GDP growth.

Fitch kept its outlook unchanged at BBB-minus with a stable outlook while Statistics South Africa announced that the country's GDP had contracted by -1.2%.

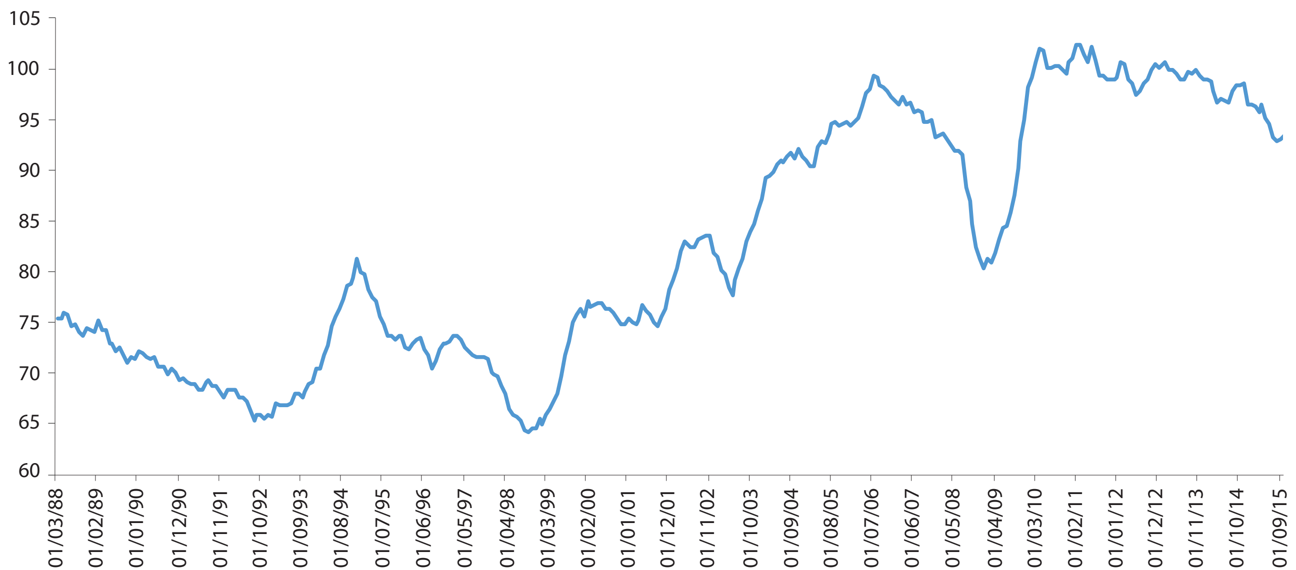
In affirming South Africa's rating Fitch says government efforts to boost growth are likely to have only a marginal impact. In its statement Fitch said the 'BBB-' rating reflects low trend GDP growth, significant fiscal and external deficits and high debt levels which are balanced by strong policy institutions, deep local capital markets and a favourable government debt structure.

SA's current account deficit widened in the first quarter of 2016 to 5% of gross domestic product from 4.6% in the fourth quarter of 2015. Economists had expected the deficit to narrow from the previously reported fourth-quarter figure of 5.1% putting the first-quarter figure at 4.8%.

The shortfall widened mainly because SA paid more dividends to foreign investors for their investments in the country than it received from its investments abroad. The shortfall on the services, income and current transfer account widened by R24bn to R174bn.

The widening in the current account deficit was offset by an improvement in the trade balance. The trade deficit narrowed to R38bn in the first quarter of 2016 from R41bn in the fourth quarter of 2015 as higher international prices of certain commodities such as platinum, coal and iron ore and a weaker rand supported an increase in the value of exports. The value of imports advanced at a slower pace over the period which helped support the narrowing of the trade deficit.

SA leading indicator



Source: GTC / I-Net

The composite leading business cycle indicator fell to 90.9 points in April from 91.7 points in March raising the fear of a possible recession this year and may encourage the Reserve Bank to keep interest rate increases on hold.

The central bank's leading index, which was set to 100 in 2010, reached a maximum of 102.1 points in February 2011. It has been in decline since November 2014 when it reached 98.4.

The South African Reserve Bank kept the repo rate steady at 7% in a majority 5:1 vote but revised its GDP forecast down to 0.6% from the previous 0.8%. One of the main drivers for this decision was that consumer inflation slowed to 6.2% in April from 6.3% in March. Core inflation which excludes the prices of food, non-alcoholic beverages, petrol and energy, was at 5.5% y/y in April from its big downside surprise to 5.4% y/y in March. Month-on-month it was at 0.3% from 0.9% in March. Food price inflation, however, saw a strong monthly gain in April, up 1.9%. Y/y food price inflation is at 11.3%. Vegetable prices rose a staggering 24.4% y/y; fruit went up by 19.6% y/y and bread and cereal by 17.5% in April 2016.

Mining production decreased by 18.0% year-on-year in March 2016. The largest negative contributors being PGMs, coal, iron ore and manganese.

Manufacturing production decreased by 2.0% in March 2016 compared with March 2015. This decrease was mainly due to lower production in the following divisions: basic iron and steel, non-ferrous metal products, metal products and machinery.

Following on the fallout from the "Brexit" decision, our investment analytics team issued a bulletin calling on our clients to exercise caution and not panic at the turn of events. As so often happens unexpected global outcomes lead to a knee-jerk reaction on the part of investors whilst a calm and cool head is what is called for. This call on our part was certainly justified considering the improved stability that has returned to global equity and bond markets.

GTC Fund performances - June 2016

Client Portfolios	1Year %	*2Year %	*3Year %	*4Year %	*5Year %
GTC High Equity - Provident	3.81	4.84	9.48	10.92	10.28
GTC High Equity Inflation Target CPI+5%	11.13	10.35	10.78	10.72	10.71
GTC High Equity - Pension	3.65	4.86	9.45	10.80	10.13
GTC High Equity Inflation Target CPI+5%	11.13	10.35	10.78	10.72	10.71
GTC Moderate - Provident	3.80	4.11	8.15	9.53	8.96
GTC Moderate Inflation Target CPI+3%	9.13	8.35	8.77	8.72	8.71
GTC Moderate - Pension	3.73	4.10	8.09	9.50	8.93
GTC Moderate Inflation Target CPI+3%	9.13	8.35	8.77	8.72	8.71
GTC Conservative - Provident	5.10	5.01	6.14	7.35	7.13
GTC Conservative Inflation Target CPI+1%	7.13	6.34	6.77	6.72	6.70
GTC Conservative - Pension	5.32	5.08	6.47	7.60	7.35
GTC Conservative Inflation Target CPI+1%	7.13	6.34	6.77	6.72	6.70
GTC EB Market Plus - Pension	3.73	5.31	10.44	12.70	11.33
GTC EB Market Plus - Benchmark	6.16	7.60	12.30	13.95	13.30
GTC EB Market Plus - Provident	1.86	3.73	10.35	12.63	11.28
GTC EB Market Plus - Benchmark	6.16	7.60	12.30	13.95	13.30
FTSE/JSE All Share Index (ALSI) ^	2.28	2.76	11.36	13.28	12.13
FSTE/JSE Shareholder Weighted Index (SWIX) ^	2.58	5.53	13.11	14.57	13.97
BEASA All Bond Index (ALBI) ^	3.68	5.13	4.71	4.71	6.30
Cash (SteFi)^	5.26	4.98	4.60	4.38	4.33
MSCI World Index (R)^	13.55	13.26	18.21	22.52	20.07

*Annualised

^Benchmark returns include 1.5% fees
GTC Performances are shown net of all fees

The **GTC Market Plus Funds** are lagging their targets on the back of equity market volatility. Within our manager blend, exposure to attractive and depressed materials exposure has detracted in the short-term.

The **GTC High Equity Funds** (previously Aggressive) are lagging their inflation targets as short-term detraction from equity markets impacts performance.

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

The **GTC Moderate Funds** are performing in line to their inflation adjusted targets over longer term periods. Equity markets remain the key driver of performance.

The **GTC Conservative Funds** are lagging their inflation targets over the short-term as detraction from equity markets impacts performance but are ahead of their inflation target over the longer term. Equity markets remain the key driver of performance.

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