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Trendline - Wealth management

First Quarter 2018

At a glance

With 2018 having commenced on a very positive note, equity markets declined in Q1, rattled by concern over the prospect of rising US interest rates, coupled to renewed threats of a global trade war precipitated by President Donald Trump imposing trade restrictions on certain Chinese imports.

These concerns were reflected in the MSCI World Equity Index returning a negative -1.3% for the quarter and being outperformed by the MSCI Emerging Markets Index which returned a positive 1.4% both in total return terms.

In line with other global markets, Eurozone equities posted negative returns as the implications for a protracted global trade war, as well as a return to a normalisation of interest rates, weighed on the market.

Whilst global macroeconomic events impacted the UK equity market, their situation was further exacerbated by Sterling strength amid expectations that the Bank of England may raise interest rates sooner than expected.

The Nikkei 225 followed a pattern similar to other major global markets, ending the quarter in negative territory. The Yen's safe haven status also impacted the equity market as the currency attracted nervous global investors and strengthened considerably.

In spite of greatly increased volatility and general uncertainty, emerging market equities delivered somewhat unexpectedly positive returns for the quarter, with Chinese markets displaying relative stability in spite of the looming threat of trade sanctions on the part of the US.

Global bond markets reflected higher inflation concerns, with the majority of government bond yields rising. In the US the rise was most marked as expectations for growth and higher inflation witnessed a rotation from equities to treasuries.

In spite of an improving political outlook, coupled with encouraging macroeconomic data, particularly in the form of domestic GDP, the JSE/ALSI failed to live up to expectations, returning a negative -4.18% whilst the Top40 declined by -4.28% both in total return terms.

Global: The golden bear vs The dragon Xi

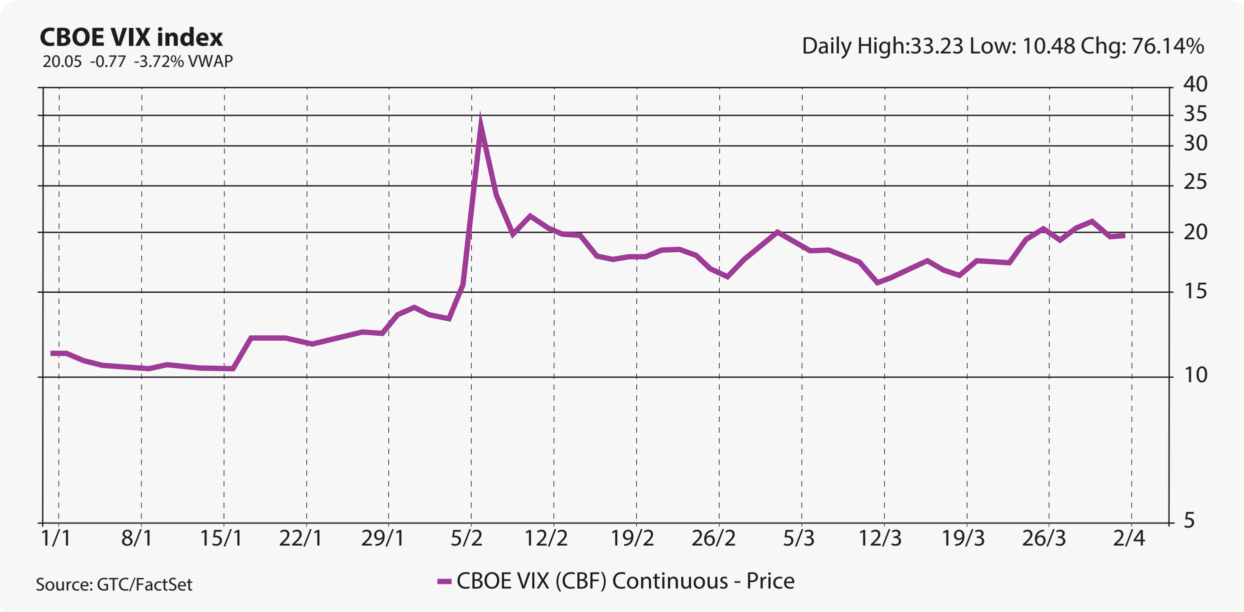
From the start of 2018, US equities looked set for an exceptional year. Economic data, robust earnings and confirmation of tax reforms heralded a new period of prosperity.

This was further confirmed with business confidence reaching an all-time high in March and the Federal Reserve upwardly revising GDP for Q4 2017 from 2.7% to 2.9%.

The Fed also raised its growth expectations for 2018 from 2.5% to 2.7%. However, towards the end of the quarter, volatility in the equity markets suddenly rose to unexpected levels after having spent a protracted period in the doldrums.

This was predicated to an extent by evidence of rising inflation and hence the necessity for the Federal Reserve having to intervene more aggressively. Not unexpectedly the Fed raised interest rates by 25 basis points in March and maintained its stance on a possible three interest rate hikes for 2018.

This announcement did temporarily help ease volatility, but the sudden escalation of the whole US/China trade sanctions issue resulted in a fresh bout of hectic volatility. The uncertainties surrounding these events resulted in a sell-off of equities the S&P 500 down -2.69%, the Dow Jones down -3.7% and the tech heavy NASDAQ down -2.88%.



Over the quarter technology and discretionary stocks were the only ones to deliver positive returns, while the worst performers were telecoms and consumer staples.

Global volatility jumped to its highest level in two years after the CBOE VIX Index rose to a high of 37.32 points.

This was a precursor of the market mayhem that was to follow.

In line with other global markets, Eurozone equities began 2018 on a positive note, but as the quarter progressed global concerns began to impact on market performance.

Bond proxy stocks, such as healthcare and telecommunication which offer stable returns and are a favourite of investors when interest rates are low, fell out of favour amidst expectations of rising US interest rates and were the worst performers over the quarter.

Encouragingly Eurozone economic data remained on the front foot with GDP growth for Q4 being confirmed at 0.6% quarter-on-quarter. Unemployment at 8.6% for January suggested a stable employment environment.

The Purchasing Managers Index for March showed a marginal decline to 53.3, which nevertheless still suggests solid growth. Inflation still remains stubbornly below the targeted 2% coming in at 1.1% in February.

A further positive factor is that ECB chairman Mario Draghi has confirmed that interest rates will not rise until well past the current end to the quantitative easing programme.

In the UK the downturn in world economic events resulted in bond yields rising in line with the broad-based sell-off in global bonds.

This was occasioned amid signs that the global economy is shifting from a recovery phase to one of expansion, creating an increase in inflationary pressures and hence tighter monetary policy.

The rise in yields resulted in rotation away from the more defensive areas of the market but a further contributing factor was the strength of Sterling.

Foreign interest in UK equities remains at a low level, with the outlook for the economy being clouded by the uncertainty of the political situation, as well as sluggish economic growth.

Global developments and continuing uncertainty resulted in the Japanese Yen once again finding favour as a safe haven investment, and this in turn coupled with global investment sentiment resulted in the Nikkei ending the quarter with a negative return of -4.7%. However, corporate results up to the end of 2017 are most encouraging.

Of particular concern for Japan was the surprising turn of events and stance of all the players engaged in discussions over the North Korea nuclear problem.

Although the outcome of any negotiations remains completely opaque at the moment, any indication of a reduction in tensions in the region would be most welcome.

Economic indicators suggest a marginal slowdown in Japanese GDP for Q1 2018 with consumption and production numbers slightly down. The rapid spikes in market volatility seen in February and March resulted in stark divergence in market sector returns.

The one bright star in a disappointing first quarter of 2018 remained emerging markets, which in Dollar terms delivered a positive 1.4% and outperformed global markets, in spite of tremendous market volatility emanating from the global trade discourse.

Although Chinese equities experienced volatility given the potential US trade sanctions, the market delivered positive returns.

Chinese economic data remained stable, although there was evidence of a gradual slowdown with PMI coming in at 50.3.

Domestic: Ramaphosa recovery?

An air of renewed hope and confidence in the local economy heralded the start of 2018. Political change, together with a new sense of optimism in South Africa's future, set the tone for the year ahead.

But there were some significant bridges still to cross and one of the most significant of these was to avoid a downgrade by all of the recognised rating agencies of our sovereign debt to junk status.

Ultimately this determination rested in the hands of one agency which was Moody's and indeed not only did they maintain our current rating, but also raised hopes by upgrading our outlook from negative to stable.

This confirmation of South Africa's ratings reflects Moody's view that the previous weakening of South Africa's institutions will gradually reverse under a more transparent and predictable policy framework.

Furthermore, the recovery of the country's institutions will, if sustained, gradually support a corresponding recovery in the economy, along with a stabilisation of fiscal strength.

Both its rival ratings agencies Fitch and S&P downgraded SA to junk status last year.

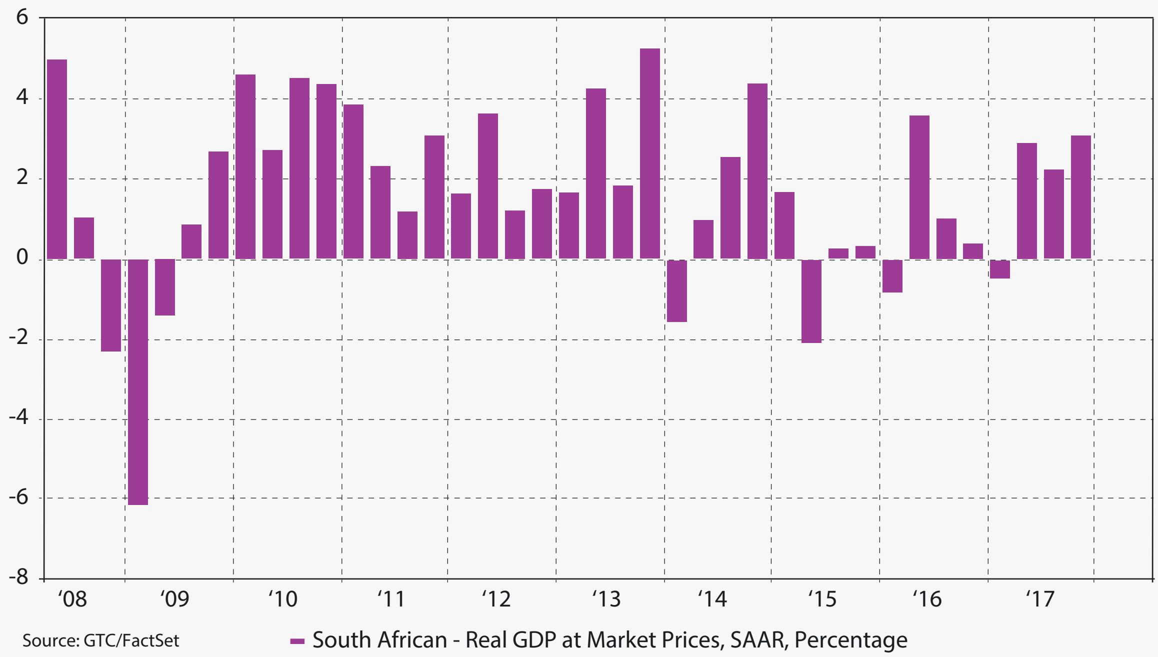
National Treasury welcomed the decision, saying government was working to improve the country's investment and economic prospects by providing policy certainty.

Politics took centre stage in February after SA welcomed Cyril Ramaphosa as the new president following the resignation of Jacob Zuma.

Over and above a change in the Union Buildings, the highly anticipated budget speech was also greeted with optimism.

Highlights of the statement included a 1% VAT increase, while higher education was allocated a considerable R57bn over the next three years.

SA GDP quarterly growth rate (percentage)



Source: GTC/FactSet

From an extremely low base recorded in the first half of 2017, very encouraging news was that our gross domestic product increased by 3.1% in the fourth quarter of 2017, following an increase of 2.3% in the third quarter.

The largest positive contributors to growth in the fourth quarter were the agriculture, forestry and fishing industries. The trade, catering and accommodation industries also increased, as well as manufacturing, finance, real estate and business services. Mining and quarrying decreased and contributed negatively to GDP growth. The median estimate of 14 economists surveyed by Bloomberg was for growth of 1.8%. Gross domestic product expanded 1.3% last year - more than National Treasury's forecast of 1%.

The headline CPI annual inflation rate in February 2018 was 4.0%. This rate was 0.4% lower than the corresponding annual rate of 4.4% in January 2018. On average prices increased by 0.8% between January and February 2018. Core inflation was unchanged at 4.1% year-on-year in February while on a month-on-month basis it quickened to 1.1% from 0.2% previously.

Further good news on the back of these developments was that the monetary policy committee of the SA Reserve Bank decided to reduce the prime interest rate by 25 basis points. This means that the repo rate has been reduced to 6.5% and the prime lending rate to 10%. This rate reduction will hopefully stimulate the economy even further.

For the first time in five years, consumer spending in January grew at the same pace as during the festive season, signifying economic recovery. This is according to the MasterCard Spending Pulse report. The report, which provides a macroeconomic analysis of retail spending trends in SA, showed that consumers started 2018 on a stronger footing amid a downward trend in the inflation rate.

Consumer spending in January climbed 3.8% year-on-year after accounting for the effects of inflation. This is the same pace of growth the retail industry experienced during the December peak season, which was also the strongest monthly performance since May 2013. When the effects of inflation are included, retail sales for January 2018 grew 7.3% year-on-year.

E-commerce in South Africa is exploding and is estimated to have amounted to about R10bn during 2017, according to Visa. There is a massive growth opportunity in the digital commerce sector. It is driven by high mobile penetration, rising consumer confidence in online transactions, and the expansion of brick and mortar retailers into the online sphere by adopting a multi-channel approach.

Extensive changes are in the offing at the troubled state-owned companies as new Public Enterprises Minister Pravin Gordhan moves to tackle their many management and financial failings. Power utility Eskom Holdings and several other state entities have been caught up in graft and management scandals over recent years, and repeatedly called on the state to bail them out as their debt ballooned to unsustainable levels. Virtually every entity that Minister Gordhan's Public Enterprises is supervising or is responsible for is going to have changes as far as the board is concerned.

Steinhoff, Intu Properties plc, and the Fortress and Resilient property funds have been removed from the JSE's Top40 index. In their place is Imperial Holdings and three retailers: Truworths, Foschini, and Spar. Steinhoff and Resilient/Fortress' exit from the Top40 now puts them into the JSE's Mid Cap index which represents the next 60 largest companies from the All Share Index by full market capitalisation. This is a significant change and could make trading the Mid Cap index a good deal more difficult.

The first quarter of 2018 has indeed been a difficult, and in fact disappointing period for investors both locally and abroad. Importantly, markets experiencing high levels of volatility tend to instill an element of concern regarding investments but it remains important to try and hear through all the noise.

If we examine the underlying global macroeconomic data, there is considerable reason to be confident in the global economy going forward. For South African investors the quarter has been even more trying in that all indicators were beginning to point in the right direction until almost the last weeks of the quarter. However, now that a degree of stability has returned, remaining fully invested would appear to be the prudent watchword.

GTC Fund performances - March 2018

Client portfolios	6Mth %	1Year %	3Year* %	5Year* %	7Year* %	10Year* %
GTC Fixed Income Fund B	4.03	8.33	7.33	6.93	6.54	7.34
Cash (SteFi)^	2.81	5.87	5.63	5.02	4.72	5.46
GTC Wealth Protector Fund of Funds B	1.03	6.64	5.38	5.98	6.40	7.54
CPI + 1% target	2.91	4.93	6.73	6.41	6.57	6.79
GTC Capital Plus Fund of Funds B	0.43	6.40	4.66	6.10	6.40	7.22
CPI + 3% target	3.87	6.93	8.74	8.41	8.57	8.79
GTC Balanced Wealth Fund of Funds B	-0.46	6.70	4.74	6.41	7.25	8.24
CPI + 5% target	4.83	8.93	10.74	10.41	10.57	10.79
GTC Prosperity Wealth Fund of Funds B	0.13	7.91	4.67	6.96	7.97	8.79
Composite Benchmark	-0.75	5.45	4.20	8.96	10.49	8.12
GTC Wealth Accumulator Fund of Funds B	2.86	9.69	2.87	6.04	6.88	8.48
FTSE/JSE Shareholder Weighted Index (SWIX)^	1.46	7.79	2.94	9.19	10.82	9.29
GTC Equity Fund Class A	-0.50	9.61	N/A	N/A	N/A	N/A
FTSE/JSE ALSI Top 40^	-0.78	9.34	N/A	N/A	N/A	N/A
FTSE/JSE All Share Index (ALSI)^	0.28	7.98	3.49	8.40	9.71	8.05
FTSE/JSE Shareholder Weighted Index (SWIX)^	1.46	7.79	2.94	9.19	10.82	9.29
FTSE/JSE ALSI Top 40^	-0.78	9.34	3.35	8.22	9.26	7.38
BEASSA All Bond Index (ALBI)^	9.64	14.52	7.04	6.12	7.80	8.01
Cash (SteFi)^	2.81	5.87	5.63	5.02	4.72	5.46
MSCI World Index (R)^	-9.36	-2.46	3.89	11.60	13.91	6.08
GTC Conservative Absolute Growth (R)	-12.50	-11.45	-2.40	5.59	9.03	N/A
GTC CAGs Composite Benchmark (R)^	-9.98	-6.07	1.69	7.18	10.35	N/A
$/R exchange rate	-12.25	-11.85	-0.65	5.13	8.50	N/A
GTC Global Conservative Absolute Growth ($)	-0.29	1.38	0.55	1.41	2.02	0.28
GTC Global CAGs Composite Benchmark ($)^	2.60	6.57	2.36	1.94	1.69	1.13

*Annualised
^Benchmark returns include 1.5% fees
Not all fund class returns are shown. Class B refers to indirect investments.
Significant strategy changes were made in September 2015 including incorporating offshore exposure. Prior to that funds were 100% SA domestic.

The **GTC Fixed Income Fund** delivered outperformance against the Cash (SteFI) benchmark over all periods.

The **GTC Wealth Protector FoF** was ahead of its inflation target over the short and longer term as equity markets rerated.

The **GTC Capital Plus FoF** was lagging its inflation adjusted target as equity markets detracted over the short and medium terms. Equity markets remain the key driver of performance.

The **GTC Balanced Wealth FoF** was lagging its inflation adjusted target as equity markets detracted over the short and medium terms. Equity markets remain the key driver of performance.

The **GTC Prosperity Wealth FoF** was ahead of its inflation target over the short and medium term, but lagged the inflation target over the long term as equity markets trended sideways.

The **GTC Wealth Accumulator FoF** was ahead of its benchmark over the short term in what has been a very narrow market.

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