OPPORTUNITY

PRIVATE CAPITAL

Economic Snapshot August 2023

LOCAL ECONOMIC INDICATORS	NEWS
• All-Share Index mid-August: +-74,646 • All-Share 1y return: 5.2% • Market PE ratio: 11.66 • USD/ZAR currently at R19.11/$, • South Africa 10Y Government Bond yield: Current 10.34% (Data: Bloomberg; ShareNet; tradingeconomics.com)	• The war in Ukraine is still dragging on, with recent attempts at peace talks showing that even China may be getting frustrated with the unprovoked war. • Many were hoping for the Chinese economy to properly kickstart the global post-Covid economic engine, but recent reports from China reveal weak employment, deflation and large looming corporate defaults. Only time will tell if the Jinping government can pull a stimulus rabbit out of the hat after starting with a 15bp rate cut on Tuesday. • NVIDIA's share price rose from $207 on 22 Feb to $474 on 18 Jul, signposting investors' belief in the new artificial intelligence regime of natural language programming. Recent breakthroughs have been heralded as the biggest news since the internet (which caused an economic boom in the USA in the 90s).

The great Mexican standoff

Global bond and share markets represent two different but interlinked sections of global capital markets. Both these markets are sensitive to economic events and monetary policy. They *normally* also share a common valuation trait, namely that both discount future cashflows (whether earnings or coupon payments) to produce a valuation estimate for the trade of the securities.

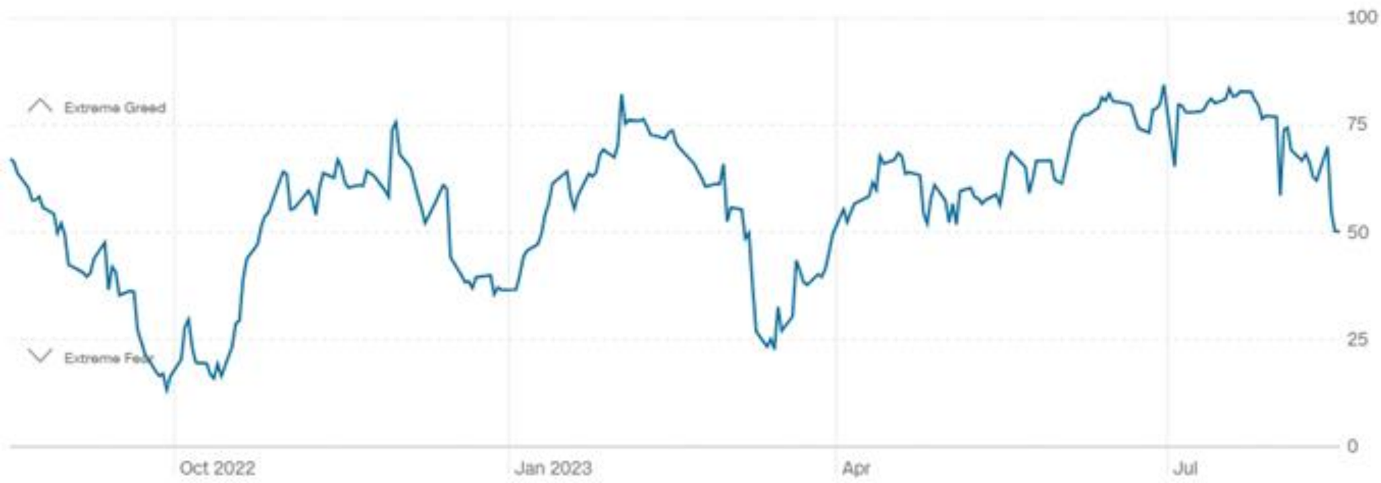
The interesting thing is that we are in a period of seeming valuation disconnect, and the big question is who will blink first? Bond markets are forecasting interest rates to be higher for longer, with the US yield curve in particular recently rising for all maturities (while still being inverted as seen on worldgovernmentbonds.com, normally being an advance indicator of a recession). This is on the back of inflation remaining stubbornly high, with some economists now forecasting no US recession, subsequent inflation runs, and the expected reaction of central banks either raising interest rates further or holding them higher.

Both recessions and higher interest rates normally do not bode well for share markets. This is because earnings are expected to decrease during recessions, and higher interest rates should theoretically result in lower share prices. But until 1 August share prices had NOT fallen, in fact we saw the S&P500 reaching highs not seen since the end of 2021. One possible explanation for this disconnect was that investors are focusing more on the growth potential of individual companies rather than broader economic indicators.

Whatever the reason for the recent valuations, we were in a period where share markets were deemed to be in an 'Extreme Greed' phase (see the CNN index below), signalling a true Mexican standoff where something had to give. It seems that the recent weak data from China has finally made the share markets flinch, and we have rapidly returned to a more neutral share market valuation. The Chinese economic slowdown is acting as a global deflationary pulse, but we have some way to go until inflation subsides.

We may not be wearing masks anymore, but the effects of Covid are still being felt, albeit more on our wallets.

GRAPH OF THE MONTH: - The CNN Fear and Greed Index



Source: https://edition.cnn.com/markets/fear-and-greed

Compiled by Dr. Rousseau Lötter (Head of Portfolio Analytics, Craigs Investment Partners, NZ).