INVESTMENT NOTE
IT'S NOT JANUWORRY FOR INVESTORS

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WEALTH

Last year ended on a high note. Equity markets surged in December and 2019 turned out to be a good year for investors with almost all global asset classes posting positive returns.

REVERSE

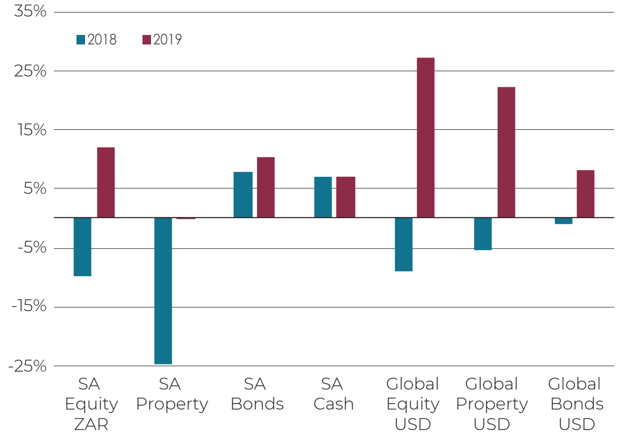
This was the exact reverse of 2018, when virtually every major global asset class was negative, offering investors nowhere to hide. The macro-worries that caused the late-2018 slump, namely rising US interest rates, trade wars, Brexit and a slowing global economy faded in 2019. The US Federal Reserve cut rates three times in the second half of the year, having gone into 2019 expecting to hike three times. It has signalled that rates will remain at current levels for the remainder of the year, while it will continue to add reserves to the banking system to ensure the smooth functioning US money market. Other major central banks have cut or are cutting, and the "lower for longer" view of global interest rates is firmly in place. The US and China agreed to a 'phase one' trade deal that was officially signed at a White House ceremony last week. The US Treasury also removed China from its list of currency manipulators. Boris Johnson's decisive victory in the December election (by number of seats won, not total votes) means Britain will now leave the European Union by the end of the month in an orderly fashion with a withdrawal agreement in place (though the hard work of negotiating a new trade regime lies ahead).

While the global economy is still stuck in a low gear, the worst of the slowdown in economic activity and corporate profit growth seems to be behind us.

With all this as a backdrop, the benchmark US equity index, the S&P 500 returned 3% in December on the way to fresh record highs. This lifted the 2019 total return to a very impressive 31%. The MSCI All Countries World Index, combining developed and emerging markets, returned 3.5% in dollars in December on the way to a new record high and a 2019 total return of 27%. Global bonds (as per the Bloomberg Aggregate Index) returned 8% in dollar terms last year, and global listed property 22% (FTSE EPRA/NAREIT Developed Index).

Local equities followed developed markets higher in December. The FTSE/JSE All Share Index returned 3.3% in December, boosting the 2019 return to 12%. Local bonds returned 10.3% for the year, ahead of the 6.9% return from cash. Among the major asset classes available to local investors, only listed property delivered a negative return. However, the FTSE/JSE All Property Index's -0.4% 2019 return was significantly better than 2018's -25%. A good balanced portfolio will have delivered a double-digit return in 2019, well ahead of inflation.

CHART 1: 12-MONTH ASSET CLASS RETURNS IN 2018 AND 2019



Source: Refinitiv Datastream

SURPRISES

Predictably, there have been a few surprises in the first days of January. The first shock was the killing of a top Iranian general in a US drone strike, setting off fears that the longstanding conflict between the two countries could escalate into all-out war. However, neither countries seem to want war and ironically, the tragic accidental downing of a passenger jet by Iranian anti-aircraft missiles also served to defuse the situation by removing any claim Iran might have had to the moral high ground. After the initial knee-jerk sell-off, the market reaction has been muted.

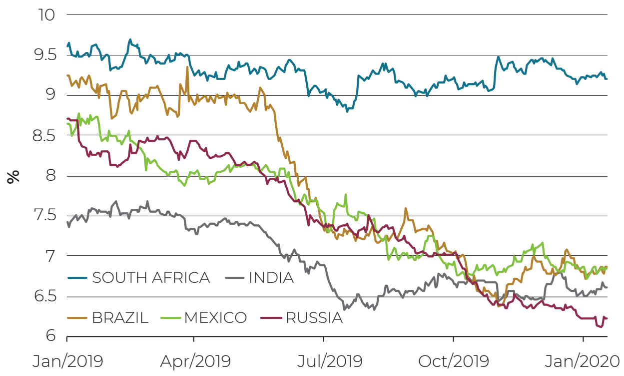
Due to sanctions, Iran is currently a much smaller participant in global oil markets and unlike in 1979, it was never going to be able to engineer a doubling of oil prices. It can jeopardise shipping in the Gulf, particularly at the chokepoint at Hormuz, and thereby cause supply disruptions, but this could end up alienating the few allies it still has (notably China). Due to the shale revolution, the US is now the largest oil producer on earth, and therefore higher prices could on balance help rather than hurt it. Importantly, the world today uses much less oil to generate a unit of economic growth, and higher oil price will much less damaging than in 1970's.

Brent crude oil is therefore still trading well within the $55 to $75 per barrel range of the past three years, and global equities continue to push higher. South Africa is still on course for a modest petrol price cut in February. Though the situation can still change, this was a good lesson in keeping calm, ignoring the headlines and focusing on the underlying reality.

CHART 2: BRENT CRUDE OIL, $ PER BARREL

Source: Refinitiv Datastream

CHART 3: 10-YEAR GOVERNMENT BOND YIELDS FOR MAJOR EMERGING MARKETS



Source: Refinitiv Datastream

REPO RATE RELIEF

The second, much more pleasant surprise was the 0.25% rate cut announced by the Monetary Policy Committee of the SA Reserve Bank last week. It is about time. Inflation declined through the course of 2019, hitting a seven-year low of 3.6% in November, while the economy is struggling. The decline in inflation expectations as measured by Bureau for Economic Research surveys continued in the fourth quarter (though the MPC wants to see even further declines). The SARB now expects inflation to stay close to the midpoint of the target range, averaging 4.7% in 2020 and 4.6% in 2021.

Meanwhile, the economic growth outlook has been cut sharply as load-shedding seems likely to persist through the course of the year. The SARB expects 2019 growth will be reported as 0.4%, while the 2020 growth forecast has been downgraded to 1.2%. The latter might still be on the high side, but it will depend on how persistent and severe the electricity blackouts are.

The shift in the MPC's stance is notable. On the growth front, it resisted rate cuts on the grounds that they could not do anything about structural constraints such as electricity shortages. Although inflation had been declining through the course of last year, the MPC persistently highlighted risks that could result in higher inflation. In particular, the MPC has long worried that rising government debt would lead to further ratings downgrades and destabilising capital outflows. For this reason, the market expectation was for it to remain on hold until after Moody's announcement in March (following the February Budget Speech). Fortunately, the MPC did not wait, and in fact it signalled the possibility of another, much-needed, rate cut. Even after last week's cut, South Africa's real short- and long-term interest rates remain among the highest of developed and major emerging markets.

The likelihood of a Moody's downgrade to junk status (the other ratings agencies already rate South Africa as junk) has definitely increased. Load-shedding weighs on economic activity, which in turn reduces government's tax take, forcing it to borrow more if it keeps spending unchanged. Deep spending cuts are politically unpopular and therefore unlikely, and could also be counterproductive. The question for investors, however, is how much of this is priced in already. Certainly no one will be surprised if Moody's gives us the chop, so a severe market reaction should be unlikely. The high yields on South African government bonds relative to other similar emerging markets suggest that the bad news is largely in the price. Similarly, although the JSE had a better year in 2019, the valuations of many locally-focused companies are cheap, reflecting the tough economy.

WHAT MATTERS IS THE PRICE YOU PAY

Howard Marks, the billionaire American investor and founder of Oaktree Capital, released his annual memo last week, and is worth a read as always. It highlights two of his guiding principles: "Success in investing doesn't come from buying good things, but from buying things well" and "It's not a matter of what you buy but what you pay for it." Marks made his name and fortune in the high yield (junk-bond) market, so he knows a thing or two about risk. He noted that the bonds he bought were junk-rated by Moody's (and other ratings agencies) for "failing to possess the characteristics of a desirable investment", but that Moody's "never asked about the price". In other words, the ratings agencies never express an opinion on the returns that can be generated. If the price more than compensates for the risk, the returns can be great.

The 2020 outlook for South Africa is certainly not cheerful as we confront a by-now familiar list of problems: consumers under pressure, load-shedding, low growth, rising government debt and a slow government response to urgent matters. However, as investors we need to remember that with such bad news comes opportunities to buy investments at discounted prices. Meanwhile the global backdrop remains supportive of decent returns from investments not directly linked to South Africa (including the many global companies listed on the JSE whose share prices are unaffected by local gloom). It need not be Januworry for your portfolio.

EQUITIES - GLOBAL

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
Global	MSCI World	US$	2 416.0	1.60%	2.46%	2.46%	22.27%
United States	S&P 500	US$	3 330.0	1.99%	3.06%	3.06%	26.33%
Europe	MSCI Europe	US$	1 801.0	1.12%	0.95%	0.95%	17.41%
Britain	FTSE 100	US$	9 983.0	0.74%	-0.19%	-0.19%	12.47%
Germany	DAX	US$	1 392.0	-0.71%	100.22%	0.20%	18.57%
Japan	Nikkei 225	US$	216.6	-0.55%	-0.51%	-0.51%	15.97%
Emerging Markets	MSCI Emerging Markets	US$	1 147.0	1.15%	2.87%	2.87%	13.68%
Brazil	MSCI Brazil	US$	2 330.0	-0.43%	-1.81%	-1.81%	7.32%
China	MSCI China	US$	89.5	1.51%	5.16%	5.16%	20.80%
India	MSCI India	US$	608.7	1.33%	2.83%	2.83%	10.48%
South Africa	MSCI South Africa	US$	471.0	0.00%	-1.46%	-1.46%	-0.63%

EQUITIES - SOUTH AFRICA (TR UNLESS INDICATED OTHERWISE)

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
All Share (Capital Only)	All Share (Capital Index)	Rand	59 002.0	2.64%	3.36%	3.36%	10.42%
All Share	All Share (Total Return)	Rand	8 954.0	2.65%	3.38%	3.38%	14.24%
TOP 40/Large Caps	Top 40	Rand	7 968.0	2.91%	3.79%	3.79%	15.19%
Mid Caps	Mid Cap	Rand	18 120.0	2.34%	2.30%	2.30%	16.75%
Small Companies	Small Cap	Rand	17 285.0	0.24%	0.38%	0.38%	-6.31%
Resources	Resource 20	Rand	3 466.7	2.69%	2.74%	2.74%	29.90%
Industrials	Industrial 25	Rand	14 743.0	4.34%	6.98%	6.98%	16.79%
Financials	Financial 15	Rand	9 245.0	-0.02%	-1.59%	-1.59%	-3.85%
Listed Property	SA Listed Property	Rand	1 873.1	0.20%	-0.21%	-0.21%	-1.78%

FIXED INTEREST - GLOBAL

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
US Aggregate Bond Index	Bloomberg Barclays	US$	510.9	-0.01%	-0.15%	-0.15%	6.37%

FIXED INTEREST - SOUTH AFRICA

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
All Bond	BESA ALBI	Rand	701.1	0.19%	0.37%	0.37%	9.46%
Government Bonds	BESA GOVI	Rand	693.1	0.18%	0.34%	0.34%	9.30%
Corporate Bonds	SB JSE Credit Indices	Rand	53.6	0.38%	-3.94%		
Inflation Linked Bonds	BESA CILI	Rand	260.3	0.16%	0.12%	0.12%	1.47%
Cash	STEFI Composite	Rand	442.2	0.13%	0.32%	0.32%	7.28%

COMMODITIES

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
Brent Crude Oil	Brent Crude ICE	US$	65.1	0.14%	-1.38%	-1.38%	6.70%
Gold	Gold Spot	US$	1 557.0	-0.32%	2.17%	2.17%	20.32%
Platinum	Platinum Spot	US$	1 022.0	4.61%	5.25%	5.25%	27.11%

CURRENCIES

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
ZAR/Dollar	ZAR/USD	Rand	14.47	-0.71%	-3.27%	-3.27%	-5.20%
ZAR/Pound	ZAR/GBP	Rand	18.83	-0.32%	-1.43%	-1.43%	-5.36%
ZAR/Euro	ZAR/EUR	Rand	16.05	-0.44%	-2.24%	-2.24%	-2.62%
Dollar/Euro	USD/EUR	US$	1.11	0.00%	0.99%	0.99%	2.70%
Dollar/Pound	USD/GBP	US$	1.30	0.41%	2.24%	2.24%	-0.06%
Dollar/Yen	USD/JPY	US$	0.01	0.55%	1.33%	1.33%	0.80%

Source: I-Net, figures as at 17 January 2020

THE WEEK AHEAD

SOUTH AFRICA

- Consumer inflation

US

- Existing home sales
- Markit flash purchasing managers' index
- Leading indicator

EUROPE

- European Central Bank interest rate decision
- Germany ZEW Economic Sentiment Index
- Markit flash purchasing managers' indices

JAPAN

- Bank of Japan interest rate decision
- Trade balance
- Inflation
- Markit flash purchasing managers' index

The Old Mutual Wealth Investment Note is published on a weekly basis to keep our clients and financial planners informed of what is happening in financial markets and the economy and to share our insights. Markets are often very volatile in the short term and similarly, economic data releases or central bank actions may cause concerns for investors. This does not mean that investors should take action based on the most recent events. It is better to be disciplined and remain invested in well-diversified portfolios that are designed to achieve long-term objectives. Our Strategy Funds are actively managed, with asset allocation changes based on valuations and in anticipation of future real returns, and not in response to the most recent market noise. The future is always uncertain and that is why our Strategy Funds are diversified and managed with a long-term focus.

WEALTH