PRUDENTIAL **INSIGHTS**

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Market Overview: December 2018

Global equity markets closed the month significantly weaker after an exceptionally volatile December on the back of sharp equity declines in the US and an investor flight to safety. Not only was it the weakest December for US equities since the 1931 Great Depression, but the market also recorded its highest-ever one-day gain. Disappointing changes to the US Federal Reserve's (Fed's) interest rate outlook, policy instability in the White House and a potential slowdown in global economic growth were among the main factors weighing on investor sentiment. In South Africa, strong economic data and a weaker rand helped boost the local bourse. Mining stocks were the standout performers as demand for precious metals (gold, palladium) helped drive the sector.

In the US, the Fed adopted a somewhat more dovish stance at its December FOMC meeting. Although it hiked the benchmark interest rate by 25bps as widely expected, it also eliminated one 25bp hike from its 2019 rate outlook and lowered its 2019 GDP growth forecast to 2.3% from 2.5% previously. Still, the market had been pricing in an even easier stance, causing an equity market sell-off. President Trump’s refusal to circumvent a partial government shutdown over a border security budget dispute also weighed on the market. Disappointing economic indicators, particularly out of China, sparked renewed concerns over a slowdown in global economic growth, with the Dow Jones Industrial 30 and S&P 500 reaching their lowest levels in seven and eight months respectively. The yield on the benchmark 10-year US Treasury bond traded lower at around 2.73%, well off its highs of around 3.24% earlier in the year as USTs benefited from their safe-haven status, as well as prospects of a lower-growth environment. In more positive news, the trade-war ceasefire between the US and China appeared to be making progress, with President Trump indicating that both parties were making significant strides towards reaching a consensus.

In the UK, the Bank of England (BoE) left its key interest rate unchanged at 0.75% in line with market expectations. Brexit concerns, however, continued to weigh on the market after Prime Minister Theresa May survived a vote of no confidence. With the Brexit deadline fast approaching, the prospect of Britain leaving the European Union (EU) without a deal is becoming increasingly more likely. Italy, meanwhile, announced an informal agreement with the EU over its budget plan, thereby avoiding disciplinary action. Germany's business confidence softened to its lowest level in two years over concerns that the biggest economy in the euro area may slide into a technical recession.The European Central Bank downgraded the euro area growth forecast to 1.7% for 2019 (down from 1.8%) and 1.9% for 2018 (down from 2%).

In China, disappointing economic data placed downward pressure on the market, with industrial output growing by 5.4% in November (its slowest pace in nearly three years) and retail sales increasing by a modest 8.1% (its weakest growth since 2003).

Looking at global equity market returns (all in US$), the MSCI All Country World Index returned -7.0% in December. Emerging markets outperformed developed markets, with the MSCI Emerging Markets Index returning -2.6% and the MSCI World Index delivering -7.6%. Among developed markets, the S&P 500 produced -9.0%, the Dow Jones Industrial 30 returned -8.6%, while the technology-heavy Nasdaq 100 posted -8.8%. The UK’s FTSE 100 returned -

3.6% and Japan's Nikkei 225 delivered -7.7%. Among the larger emerging markets (all in US$), the MSCI China returned -6.1%, MSCI India -0.1% and MSCI Russia -3.4%. The Bloomberg Barclays Global Aggregate Bond Index (US$) returned 2.0%, while the EPRA/NAREIT Global Property Index (US$) produced -6.0%.

Brent crude was the biggest loser among commodities, closing the month at US$50 per barrel, down 8.4% from the previous month. The decline in the oil price was largely on the back of international oversupply, waning demand and uncertainty around Russia's commitment to support OPEC's decision to curtail further production. Precious metals benefitted from the risk-off environment, with gold closing the month 5.1% higher, silver returning 9.1% and palladium firming by 5.4%. Platinum was the only outlier, closing lower at -0.3%.

Turning to South Africa, the economy moved out of recession as GDP growth expanded by 2.2% (q/q annualised) in the third quarter. Ratings agency Fitch kept South Africa's sovereign credit rating unchanged at sub-investment grade, however warned that low growth and rising debt levels within state owned enterprises continued to pose a risk. Meanwhile, strong economic indicators helped drive the local bourse, with October manufacturing output increasing by 3.0% (y/y) to its highest level since June 2016, while retail sales were up 2.2% (y/y) in October.

Demand for longer-dated government debt was relatively muted with the yield on the South African 10-year government bond increasing marginally to 9.44% at month end. The BEASSA All Bond Index returned 0.6%, inflation-linked bonds (the Composite ILB Index) delivered 0.7%, and cash as measured by the STeFI Composite Index returned 0.6%. Along with other emerging market currencies, the rand weakened amid the heightened risk aversion, losing 4.5% against the US dollar, 5.4% against the euro and 4.9% against the pound sterling.

The FTSE/JSE All Share Index returned 4.3% in December, propped up largely by Resources stocks on the back of the weaker rand and higher gold and palladium prices. Resources were the strongest performers delivering 12.3%, Financials were mostly flat at 0.6%, Industrials returned 2.4% and Listed Property produced -1.1%.

According to Morningstar data, the average general equity fund returned 1.8% for the month, with the average balanced fund delivering 0.5%. The average low-equity balanced fund produced 0.5%, while multi-asset income funds returned 0.6% on average.

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