FG ASSET MANAGEMENT

ECONOMIC EXPRESS

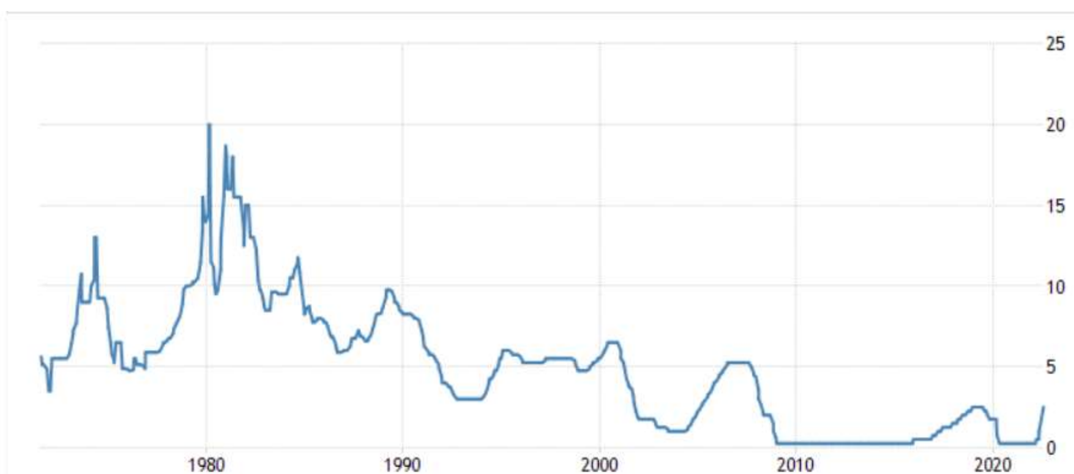
JULY 2022

Global financial markets welcomed a month of stronger returns given the poor performance experienced in the first half of this year. The positive sentiment was driven by expectations that global monetary policies will pause in their future tightening as growth starts slowing and inflation starts receding. Local markets continue to be driven by global inflation, growth, and monetary policy developments.

The closely watched US inflation continued to surprise with the annual inflation rate released for June showing prices accelerating by 9.1% compared to this time last year. This was a significant jump from the prior month's 8.6% and well above the market's 8.8% expectation. Energy and food prices continued to be key drivers behind the acceleration, however shelter, which makes up a third of the CPI basket, has also started to contribute meaningfully. The inflation print reinforced the market's expectations of another sizable rate hike at the end of the month.

The US Federal Reserve (Fed) held their meeting at the end of the month where they raised rates by a second consecutive 0.75% to the new range of 2.25% - 2.5%, (the upper limit of the previous rate hiking cycle). This was in line with expectations and the steepest tightening of monetary policy since the 1980's.

Figure 1: US Federal Funds Rate



Source: Federal Reserve, www.tradingeconomics.com (1970 -2022)

The Fed chairman, Jerome Powell, stated that, going forward, the central bank would refrain from giving clear forward guidance as has been the practice up until now but would rather do so on a "meeting-by-meeting" basis as the data becomes available. The market expects that the Fed will begin to lower rates again in 2023 as inflation pressures reflect signs of easing and/or the economic momentum starts to slow meaningfully. In contrast, the statement from Powell reiterated that the Fed would continue to be focussed on getting inflation lower, despite the cost to economic growth. Powell commented that they would need to see "compelling evidence that inflation is moving down". The divergence between the market and the US Fed's rate expectations for 2023 will continue to be a source of volatility, which is expected to converge as the path for future inflation and growth becomes more certain.

The US second quarter's GDP (Gross Domestic Product) reflected that the economy contracted by 0.9% annualised, following on from a 1.6% contraction in the first quarter. This is seen as a technical recession, given that it is the second consecutive quarter of GDP contraction. However, in the US, a recession start date is officially classified by the NBER (National Bureau of Economic Research) which looks at six macroeconomic indicators (not only GDP) and currently only one is in negative territory.

Local annual inflation jumped to 7.4% from 6.5% coming in higher than the 7.2% expected by the market. It is the highest level of inflation since 2009. The main drivers continued to be fuel and food, with food inflation rising to 9% and fuel inflation remaining elevated at 45.3% from a year earlier. Inflation is expected to remain high for at least the rest of the year as the weakness from the exchange rate and higher administered prices is expected to add further upward pressure.

The South African Reserve Bank (SARB) raised interest rates by 0.75% to 5.50% in the second half of the month. The SARB has increased the repo rate by 2% in total since they started hiking in November last year. The decision was not unanimous as one of the five members voted for a 1% increase and another by 0.5%. The market was expecting a 0.5% increase; however this was not surprising given the larger than expected inflation rate that was released two days prior to the meeting. The SARB remains committed to reducing elevated inflation especially as it is becoming broader based. They also increased their inflation forecasts, with inflation now expected to remain elevated at 7% over the second half of this year, before it drops below their upper limit of 6% in the second quarter of next year.

Another notable local development, following weeks of severe loadshedding, was when President Cyril Ramaphosa made the announcement of several measures to address the short fall in electricity supply. The measures included further deregulation of the renewable energy sector, support to stabilise Eskom and incentives for private investment in new generation capacity. Many welcomed the announcement but remain sceptical about its implementation. If the announced measures can be implemented successfully, it will be a significant driver for growth in South Africa going forward.

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Index	Asset Class	JULY 2022
STEFI Composite Index	Local Cash	0.40%
FTSE/JSE All Bond (Total Return)	Local Bonds	2.44%
FTSE/JSE SA Listed Property (Total Return)	Local Property	8.81%
FTSE/JSE Africa All Share (Total Return)	Local Equities	4.22%
JP Morgan World Govt Bond index (USD)	Global Bonds	1.91%
FTSE EPRA/NAREIT Global Index (USD)	Global Property	8.36%
MSCI AC World (USD)	Global Equities	7.02%

Source: Morningstar

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