THE QUART 40IFO

OFFICIAL QUARTERLY NEWSLETTER OF **THE OSRIN GROUP**
INCORPORATING OSRIN WEALTH & OSRIN ADVISORY

Quarter 2 in Review

Introduction –
The First Pitch

Welcome to the second quarterly edition of The Quart, 2019.

We have already moved into Q3. It's hard to believe that we have already passed the shortest day (optimist's view), alternatively the longest night (pessimist's view) of the year, and are swiftly approaching Xmas (only 173 shopping days left!).

The Osrin Group has had a very busy quarter with presentations and updates from the various onshore asset managers (Allan Gray, Ashburton, Investec, Prudential, Sanlam and Coronation), as well as presentations in Cape Town and Johannesburg from the London-based CEO of Stenprop and the CIO of Stenham Asset Management.

I am heading off to London and the Channel Islands next week to undertake due diligence on some potential investment opportunities and receive updates from a number of global asset managers and fiduciaries, who cover equities, bonds, hedge funds, real estate, private equity and trust companies.

I look forward to hearing their views on the various asset classes they cover, and to better understand what they see when they gaze into their global market crystal balls.

I will obviously provide feedback to clients upon my return.

Many clients are currently embarking, with our assistance, on an exercise of evaluating the ratio of their overall onshore to offshore investment exposure.

As you will denote from this edition of The Quart, it is a difficult time to be overexposed to local assets, but also tricky to time offshore investing with the Rand and international asset prices quite volatile.

You will note that The Quart Judge has taken up the H2O Risk Index this quarter.

We realise that in this environment, many clients are now looking to achieve stable interest/fixed coupon/dividend returns as an important component of a diversified portfolio.

The Osrin Group website, which will host Osrin Advisory and Osrin Wealth, is nearing completion and we hope to launch next month.

We will advise on the launch date closer to the time, and look forward to receiving your feedback on the site in due course.

The Judge has had an extremely difficult time condensing all the moving parts of the world economy over the past quarter, into a few pages.

With unpredictable moves by world leaders such as Trump, Putin, Xi, and Johnson (he looks like winning the Tory leadership race) it is, as the Chinese curse goes, a case of living 'in interesting times.'

With The Quart's focus on tariff wars, trade sanctions and the ever-evolving balance of world power, I'd like to suggest an interesting read, recommended to me by a long-standing Durban-based client. The book is called: **'The New Silk Roads: The Present and Future of the World'**, and is written by Peter Frankopan.

We always appreciate your feedback, including from the previous edition, and continue to take on board all your suggestions so as to continue to improve The Quart. All the best from all of us at the Osrin Group.

Jonathan Osrin

OSRIN WEALTH and OSRIN ADVISORY

[A QUART] Def; A unit of liquid measure of capacity, equal to one fourth of a gallon, or 57.749 cubic inches (0.946 liter) in the U.S. and 69.355 cubic inches (1.136 liters) in Great Britain. Or a unit of dry measure of capacity, equal to one eighth of a peck, or 67.201 cubic inches (1.101 liters).

The Quart is in Session – A More Moderate Points Haul

The second quarter (Q2 2019) has been characterised for the most part by greater risk aversion, and much higher asset price volatility, itself a reflection of investor anxiety. However, since the Federal Reserve (Fed) meeting June 18-19, and ahead of resumed US-China talks, risk has been in vogue again.

Market fear for the most part has attached itself to trade policy uncertainty, more specifically the so-called weaponization of trade by President Trump through the escalation of tariffs to achieve a variety of policy goals, some commercial, others less related to trade, such as immigration and foreign policy.

The unknown effects of heightened tariffs and the broader trade tensions they occasion, be they the potential dislocation of old trading and political alliances, a disruption of existing supply chains, slower global growth, higher input costs for businesses and ultimately higher import prices, present enormous challenges to central bankers, investors, corporates and consumers alike.

This has been the predominant theme of Q2 and is a recurring theme of this edition of The Quart.

These risks have played out more obviously in the developed world, where growth slowed markedly towards the end of 2018 and into this year, and where trade tensions are more keenly felt. They have improved prospects of rate cuts in the US in Europe and additional liquidity (new cash) being provided in Japan. They have, to a degree, prompted a rate cut by the Reserve Bank of Australia.

All this has served to keep global benchmark rates in check, and has capped developed world currencies. The Euro and Pound have been held down anyway by internal risks. Even though the yen has benefited from its role as the pre-eminent safe-haven currency, it is coming off very low levels.

More importantly for us here in South Africa, even though the US Dollar had a firm two months to end-May, in June the trade-weighted US dollar index (DXY) fell 2.5%, as expectations grew that the Fed would loosen monetary policy (cut rates).

The Rand is up 2.3% on the half-year and 0.53% on the quarter. Stable currencies serve to keep imported inflation in check in emerging markets (EM's), allowing central banks there (India and Russia for example) to begin cutting rates, or in SA's case to begin to contemplate such cuts in order to stimulate growth.

Equities are riskier assets than say bonds, so it stands to reason that their gains have been more muted this quarter. By the end of Q2 2019, the Dow Jones Industrial Average (DJIA) had added just another 3.1% to its Q1 2019 rise of 11.2%, for a total return of 14.3% year-to-date (YTD). The S&P500's Q1 ramp-up of 13.1%, the largest quarterly advance since 1998, has been supplemented by a more modest 4.25% increase in Q2 for a YTD gain of 17.35%. The Nasdaq's 16.50% Q1 performance was added to in Q2 by only 4.16%, for a YTD addition of 20.66%.

These figures are still very impressive though. The YTD performance of the S&P is the best since 1997. The equity run-up in late June saw the strongest DJIA and S&P June monthly showing since 1938 and 1955, respectively.

At the same time, bond yields pretty much everywhere have been falling on lowered economic expectations and hopes for lower rates, meaning that bonds themselves (the capital values) are rising, i.e., bonds are becoming more expensive.

In the US, the yield on the benchmark 10-year Treasury bond fell on June 25 below 2.0% to 1.994%, its lowest level since November 2016. At the beginning of the year, the yield hovered around 2.7%. The yield on the equivalent German bund fell to a record low minus 0.33%, meaning if you want to acquire German debt for a 10-year period, currently you will have to pay Germany for the privilege.

For a period from May 31, both equity and bond markets were running hard. This is unusual to say the least, for when equities do well investors are pricing in better future economic outcomes, whereas when bonds do well investors are pricing in worse future outcomes.

To market watchers this was a red flag. It demonstrated what many knew; that in fact the US economy, particularly the large consumer base, was still doing quite well. Equities were rising more because of possibly exaggerated anticipation for far lower rate outcomes from the Fed. Moreover, the greatest threat to economic outcomes is the trade war, the outcomes of which are determined by the US President. Trump, despite strong criticism of the Fed for not slashing rates, will like Presidents before him, do all he can to facilitate a strong US economy and flourishing markets ahead of an election year.

The pace of equity gains decelerated until late June, but bond markets are performing well, because the rate of global growth is slowing and perceptions exist that trade conflict will have unpredictable knock-on effects, although the two side are talking again.

Quarterly Themes

1. The Fed and The US Outlook – Powell The Playmaker

The US economy grew 3.1% on the first quarter, accelerating from 2.2% expansion in Q4 2018. It is still regarded by many at the Fed as being in a 'good place' with the consumer and the labour market still seen as 'strong', based on more recent retail data. Yes, economic activity is set to moderate from solid levels, but not to the extent that it will reverse course in the near-term.

That said, US business investment is 'soft'. And inflation remains stubbornly below the Fed's 2% objective. The Fed is also extremely concerned not just about trade, but about other global risks such as Brexit and Iran.

You will remember that the Fed was seen by end-2018 as being too insensitive to a tightening of US financial conditions and was forced to adopt more soothing language. It introduced the word 'patient' to indicate that it would not rush to any decision, it could a good while before a policy change.

But by May, even this commitment was deemed insufficient, for it indicated that while the Fed would take its time and was likely to keep rates constant in 2019, its still had a longer-term tightening or at least a neutral bias. US stocks fell quite sharply on the month.

With global risks intensifying, US business investment stagnating, corporate profits dwindling, and consumer sentiment softening, the spectre of a future recession appeared to loom large.

Economists, investors and the President alike, began calling for the Fed to move to a rates' easing bias. The tone of the speeches of Fed officials began to moderate. The futures markets started pricing in three 25 basis point rate cuts in 2019, one at the June meeting, one in September and one in December. Just a week before the June meeting, the USD was discounting a 100% chance of a cut.

Well, this did not come about. But the Fed signalled openness to future rate cuts. Now, in light of current 'uncertainties' amid 'muted' inflation, it would monitor incoming data and 'act as appropriate to sustain the expansion'. The word 'patient' which had become synonymous with a more neutral policy orientation, was dropped.

The Fed made no promises about a rate cut. The median view of the Federal Open Market Committee (FOMC) was for no rate cuts this year and for growth above 2%.

However, Powell made it clear that even in circumstances where growth was moderate, rate cuts could be contemplated where inflation expectations were falling.

And risks had served to put the Fed on alert. Conditions currently made the case for additional policy accommodation (rate cuts) 'stronger than before'.

This was all the markets needed to hear. Stocks in June regained all their May losses and more.

Even though the futures market is currently implying a 75% probability to a July rate cut, and a 61% probability to three cuts by December, I am not so sure this is warranted at least for July. More data is required to assess the likelihood of a downturn.

We asked in the last edition about the chances of a US recession. Risks have intensified, and US data has worsened in many areas, although for now the biggest contributor to US growth, the consumer, is for the most part employed, and enjoying above-inflation wage increases.

Under these conditions, my projection for a future business cycle US recession, say next year or in 2021, has risen to 30%. I would put the H2O Investment Risk Index at a level of 7 right now.

2. The US-China Tariff War – Frantic Deadline-Day Trades

If tariffs are the most significant risk to the global economy, we must understand how the dispute arose and how it might play out.

First, it is important to understand what type of economic policy President Trump favours.

His view is that to make the US 'great again', he must maximise the number and value of its exports. He is in economic parlance, a 'mercantilist'.

In this respect, his thinking is similar to that of leaders of EM economies, who favour goodsí exports, underpinned by a cheap currency, making their exports more competitive.

This policy resonates strongly with Trump's political base. They ask why the US should tolerate barriers preventing US exports to many markets, and yet levy tariffs at a rate which is among the lowest in the world, allowing all and sundry to export to the US.

The trade deficits the US runs as a consequence, mean that the US (ultimately the US taxpayer), constantly owes the world a lot of money.

This is why the President rails at the Fed. His argument is that the central banks of most major trading partners are providing massive stimulus so as to keep their currencies cheap.

Well, this may be true of Europe, but it is not true of China. The Chinese authorities actively buy Yuan and sell US Dollars in the forex market to prevent the Chinese currency from becoming undervalued. They have allowed it to weaken of late, to counter the first round of tariffs imposed last year, but have promised not to let it weaken above 7/ USD.

The real problem that President Trump has with China is that the US runs such a massive trade deficit each year with that country, a deficit of nearly US$420 billion last year. The fact is that the US habitually runs trade deficits with most of its trading partners, because it chiefly exports high-end goods and services, and imports large quantities or cheap resources, and lower-value goods.

Starting in March 2018, the US administration began raising tariffs. In May this year, Trump lifted a 10% tariff imposed last year to 25% on US$200 billion's worth of Chinese imports, alleging that the Chinese had reneged on a trade agreement. He threatened the Chinese with a similar tariff on all categories of goods not yet covered (US$300 billion). The Chinese retaliated by taking up the average tariff on US goods and agricultural products to around 20%. The trade war had now broken out into the open. And markets responded very negatively.

There are really four dimensions to the dispute.

The first is the trade deficit itself, which the US wants drastically narrowed by the opening of Chinese markets to American products.

The second entails a series of American grievances that are really complaints about how the Chinese conduct business; accusations of a failure to protect intellectual property (IP) rights, compulsory technology transfers, extensive state subsidies of leading companies, as well as barriers to entry, including non-tariff barriers, essentially making it difficult for US firms to operate on the mainland.

The third dimension has to do with state, or in the case of China, Communist Party control over Chinese companies' operations outside China. This issue is well illustrated by the criminal cases launched against Huawei, whose 5G platform arguably allows the Chinese authorities to illegally collect information in foreign markets about foreign citizens, companies and governments.

If the Trump administration had stuck to the deficit issue, there is no doubt the Chinese would have acquiesced.

But I think the Trump administration overreached itself in thinking that it could change the way in which China does business and more generally the manner in which it runs its economy.

That said, China raises unfair tariffs and many illegal non-tariff barriers to entry to the Chinese market. Companies doing business in that market know they can be singled out for special 'treatment' if their government gets into a fight with Beijing.

China's trade model is also extremely exploitative as many countries, which have mortgaged key infrastructure, or have lost the bulk of their natural resources, have come to understand.

I need not tell you that for US and Chinese securocrats all of this is a side-show. We are not now talking about who makes cheaper rubber bands, steel washers and paper clips. We are now focused on trade in infrastructure components and goods containing cutting-edge technology like 5G, AI and the like.

China has poured considerable resources into these technologies, as has the US, for obvious reasons. These technologies are the future. Whoever has them, secures better future outcomes.

The problem for the US is that these high-value goods cannot be mass produced, and therefore these technologies cannot be massified, and made commercially viable and useful, in any other part of the world other than South-east Asia. This is a region that has abundant imported natural resources, a vast pool of relatively skilled and highly productive labour, high quality infrastructure, and all the other necessary logistics requirements, including a very sophisticated supply chain management cohort.

It is for this reason that many European countries, Israel, powerful Asian economies as well as poorer countries in Africa all use Chinese companies to build, maintain and run critical infrastructure.

And it is for this reason too that many US companies like Apple produce their products in China, for to do so in the US, would increase prices substantially and unaffordably.

The US does retain control over swathes of the world's financial order, and benefits from the global reserve-currency status of the USD giving it massive leverage over countries and companies that do not do its bidding, against which it can introduce sanctions for unspecified national security reasons.

This is the fourth dimension of the dispute, which at this level goes to how the future world order will unfold. And for both China and the US, and all the countries caught in between, it is therefore an existential issue. But that is not the way in which the debate is being framed for now.

So how will the trade war play out? My baseline scenario is that some deal will be forthcoming this year. The Fed is alert to the dangers of a no-deal scenario, but I think the argument that no deal equates to a likely global recession, is somewhat overblown.

Both sides stand to lose if the fight continues. But who has more to lose? I think the answers lie in the latest Chinese trade figures. Despite the imposition of higher tariffs in May, China's overall trade surplus widened twice as much as expected.

So, for what it's worth, I believe that the US has more to lose in a no trade deal scenario.

This is because it cannot import the volume of cheap goods that China supplies, and which serve to cap its domestic inflation, from any single other supplier. It will have to reconfigure supply chains to source independently from many markets. Most goods in the South-east Asian periphery (Vietnam, Laos and Cambodia), are actually made by Chinese companies. So, the US will have to look elsewhere.

It is not commonly known, but China imports a lot of goods from the US. In 2018, this amounted to over US$120 billion. Such goods included aircraft, machinery, electrical machinery, optical and medical instruments and motor vehicles. Further, China imports nearly US$10 billion's worth of agricultural products from the US annually, including soybeans, hides, pork, and some grains.

Research indicates that China has far greater ability to manoeuvre between markets, much like Germany. If one market closes to its companies, it has the ability to find other markets very readily. And some of these will no doubt be in Europe. American companies are not nearly as flexible.

At least the G20 Summit is a start. I do not expect a deal on July 29, but the two sides will have belatedly resumed talking.

It is said that the deal is 90% complete, but that residual 10% represents 100% of the problems.

I think President Trump will feel more comfortable and perhaps more amenable to compromise in a one-on-one interface with President Xi.

But even so, and more generally, Trump's weaponizing of US economic power via tariffs, has longer-term implications for other trading partners of the US. The President's tariff threat against Mexico was a deliberate attempt to get the Mexican government to make a commitment to increasingly police immigration and accede to US demands in the revamped North American trade agreement, the USMCA. There is just no guarantee that even if a China deal is achieved, the conflict will not merely shift to another theatre (Europe, India etc).

3. May Taken Off for Johnson – Can The Sub Make a Difference

Q2 saw the demise of British Prime Minister Theresa May, who announced she would resign on May 24 and tearfully confirmed her resignation two weeks later. She will actually relinquish her role when a new Tory Party leader is chosen.

Whatever you think of May as a politician, a leader, or even as a human being, I believe she is much maligned. She delivered on her only mandate, namely to secure the best possible deal under which Britain could exit the European Union with transitional arrangements in place to secure the economy until the country could re-negotiate its relationship with the EU.

She not only did this, with European officials like Donald Tusk of the European Commission claiming it to be 'the best deal Britain will ever get', she managed to extend the Brexit deadline initially to April 12, and then to October 31.

The problem is that her negotiated deal, which on three occasions was rejected by Parliament, could not meet the schizophrenic needs of a divided electorate and a divided Westminster. For the Remainers it failed to provide sufficient economic benefits, and for Leavers it failed to provide sufficient guarantees of sovereignty.

Obviously there are several scenarios that can play out, such as a no-deal Brexit, a second referendum, a general election, and/ or a revised deal. But these will not play out in the coming quarter.

For now, it is a matter of selecting a new Tory leader. This contest has entailed a complicated process of weeding out contestants via a number of rounds of voting, initially by Tory lawmakers.

Boris Johnson, a prominent Brexiteer, came out triumphant in the first round of party balloting on June 13. His success continued as other leading candidates such as Dominic Raab (2nd round), Rory Stewart (3rd), Sajid Javid (4th) and Michael Gove (5th), were eliminated. In that fifth round of voting, Johnson triumphed by a massive 83 votes, with Gove just missing out to Jeremy Hunt who secured 77.

Hunt was a Remainer, and once supported the idea of a second referendum, but has pledged to deliver Brexit with a favourable deal. Johnson, who at one stage sought to argue for a no-deal Brexit stating that the Europeans could not re-impose tariffs, a claim repudiated by no less than the Governor of the Bank of England, is now said to be open to other options.

Johnson and Hunt will contest the race for the Conservative Party leadership position in a vote that will be undertaken on July 22, after engaging the public with their respective policy platforms, via regional meetings (hustings), and TV debates. Ballots have been sent to 160,000 Tory Party members, who are eligible to vote. The result will be announced on July 23, a day after which Theresa May will finally step down.

In my opinion, what matters principally for now is whether a chaotic no-deal Brexit is a viable outcome in October. Even the possibility of such an outcome in the upcoming quarter will send sterling lower and see additional capital flight. Already, some services and manufacturing activity has been displaced from the UK to Europe. Up to 150,000 UK exporters have not completed the requisite paperwork to continue activities in a no-deal scenario.

My view is that there is only a miniscule probability of such an outcome. Some deal will be struck with Europe, although it will almost certainly not be on terms more favourable to Britain, only possibly on terms more beneficial to the Europeans.

Johnson's approach will almost certainly soften given the realities of governing. While he did muster the support of at least 170 party members for a hard Brexit during the initial negotiations, he knows that were this approach to be put before the House of Commons, as it must be ahead of the Brexit deadline, it will be soundly defeated.

This would open the way for a general election and a possible Labour victory. For most Tories, that is the greater of the two evils.

A hard Brexit is so unlikely that it should not now be over-discounted by sterling and sterling-denominated assets.

4. Polarisation in Europe – The Italian Defence Comes Unstuck

The Euro area faces two principal risks, one more near term, and one more for the future. They are closely intertwined.

The first concerns political instability in Italy. The ruling coalition government comprising the M5S (Five Star Movement) and the Lega (League) Party is very tenuous, and could well fall in the near future.

Despite differences, the parties do share a populist economic agenda, which is to increase government spending and lower taxes, i.e. engage in fiscal stimulus, even where Italy's 2018 gross public debt was over 130% of GDP. Both parties spending and borrowing plans would entail the budget (fiscal) deficit getting to around 3.5% of GDP by 2020.

The problem is that if you want the benefits of eurozone and even EU membership you have to play by the rules, one of which is not to breach the 3% fiscal deficit threshold.

Prime Minister Conte's present unhappiness stems from the fact that while he might understand the coalition parties' view that the budget rules are 'outdated and harmful', a view shared by the way by many Europeans still recovering from the crisis of 2011, his argument is that the rules must still be respected. Conte is a relative moderate and he could be overborne by radical populism. Given that Italy is the third largest euro economy, and that its finances are precarious, this outcome poses a real risk to financial stability in the common currency area.

The recent European parliamentary elections were significant. They showed that just as in the US and other parts of the world, more mature, established parties are increasingly being discarded and being supplanted by more populist parties of all ideological persuasions.

Extreme right wing and hard-line nationalist parties doubled their representation in the European Parliament, and even the more mainstream euroskeptic formations improved their showing. On the centre and left, the Greens and liberal parties did well, but regionalists who favour more autonomy, and are therefore a threat to the EU, also prospered.

The net result is that politically, the European project is becoming less palatable for more of its citizenry. And this is sure to become a major concern for markets over time.

5. A Commodity Quarter – Heading Into Yellow After The Climbs

Trade and Iran risks resulted in exaggerated movements in some commodities in Q2 2019.

Gold is in a sweet spot right now. To the extent that the Fed is prepared to cut rates, and provide an environment of greater liquidity, real yields will fall to zero in the US, making gold which generates no yield, more attractive.

Further, additional cash in the financial system has more recently been directed, at least in part, towards speculative activity. This has massively benefited gold before.

Prospective policy easing has led to a softer US dollar, which has seen commodities generally move upward, because as the US dollar weakens, their US dollar-denominated prices get stronger.

These factors in tandem are probably sufficient to take gold above US$1,300/ounce. Yet, since May 22, the yellow metal has surged from US1,272/oz to June 25 peak of US$1,436/oz, a 6-year high, and a lift of over 12.5%.

During this period, the Japanese yen strengthened from nearly JPY110/ USD to JPY106.75 (+2.9%), which is an enormous move for a currency in such a short timeframe.

The conclusion is obvious. Gold, like the yen, is attracting support due to its safe-haven status. In this case, the final push was almost certainly due to rising tensions between the US and Iran.

Last May, President Trump took the US out of the 2015 Iran nuclear deal, and imposed wide-ranging sanctions on the Iranian government, aimed at crippling its lifeline oil industry.

In April this year, Trump terminated the waivers that allowed certain countries to continue to acquire Iranian oil. This had the effect of taking about two-thirds of Iranian oil production of just under 2 million barrels per day, off the market. Later in the month there were two attacks on oil tankers in the Strait of Hormuz, which Iran controls and which is a vital waterway for 30% of global oil supply. The US blamed Iran for one of these attacks. But matters really heated up when an unmanned US drone was shot down by Iran.

It later transpired that a US air strike on Iranian military targets was planned, Iran informed via an Oman back-channel, but that President Trump had cancelled the strike at the last moment. This is when gold really spiked. He later turned up the heat by imposing sanctions on the Iranian Supreme Leader. Matters were getting personal.

The President has repeatedly said he does not want war with Iran, a view echoed by the Iranian leadership. But then again, Trump has not ruled out the prospect.

During the week of the aborted US attack, US benchmark oil spiked over 9%, and Brent crude went up approximately 5%. But for the Iranian crisis, oil would most likely have come off on economic growth concerns, which would have encouraged producers to break rank, and increase supply so as to amass as much hard currency as quickly as possible. This leads to a feedback loop further weakening the price.

Markets should continue to reflect fear that an escalation of the conflict into direct war, or a flare up in any number of proxy wars between US allies and Iran (in Yemen and Syria, for example), will lead to an attack on US interests and specifically US oil supply. I would identify this as the pre-eminent risk impacting markets as at the quarter-end.

6. The ANC and The Government – Who Controls The Dressing Room?

The May 8 general election saw the ANC emerge victorious but it lost 19 seats to 230, the DA surrendered 5 to 84, but the EFF added 19 to 44, making it far and away the biggest overall winner in percentage terms.

The EFF has grown to around half the size of the official opposition, which given its often inciteful (never insightful) rhetoric, is quite alarming. That said, support among the under-30 youth voting category, which largely stayed away from the polls, was not that impressive.

The ANC was negatively affected by a low supporter turnout in the urban areas where trust in the party as opposed to Cyril Ramaphosa himself, has evaporated.

At the provincial level, the DA easily held onto power in the Western Cape with 55.5% of the vote. The ANC will be concerned about its showing in the other economic heartland provinces, Gauteng (50.2%) and KZN (54.2%).

I think it evident that President Ramaphosa, despite dithering over populist 'rallying cry' policies like expropriation without compensation, has positioned himself as a reformer.

But was the President's victory, one for reform? Interestingly only a few ANC officials, most notably Fikile Mbalula, actually came out and said that the ANC had won because of Ramaphosa's intention to initiate a decisive move away from the Zuma era.

In my view, his success was indeed one for reform. This view is premised principally on the high number of split votes, and also on the fact that while the EFF impressed, it could have done far better, as well as on the reality that voting numbers for opposition parties with a history of better governance and delivery in urban areas, were impressive.

The President's choice of Cabinet Ministers was initially hailed as very reformist, with solid choices in the financial cluster, Ronald Lamola positioned at Justice, and Senzo Mchunu at Public Service and Administration. These are key positions for reforming the criminal justice system, and reducing state expenditure. However, Ramaphosa appeared to make some serious compromises in his choice of Deputy-Ministers. In any event, policy is implemented by the political administration (the DG's), and changes here will be slow, even if they are to be widespread.

In Parliament, the list system ensured many pro-Zuma or at least anti-Ramaphosa MPís were selected, with several notables associated with Zuma predation now heading up oversight committees.

Factional opposition now is emerging from two sources. One is ANC HQ (Luthuli House), in the shape of the ANC Secretary-General and policy co-ordinator, Ace Magashule, who has spoken publicly and dangerously about the SARB mandate. The second is the office of Public Protector, Busisiwe Mkhwebane, which is investigating Ramaphosa for alleged money laundering linked to his ANC presidential fundraising campaign.

There is no doubt that these are the deliberate actions on behalf of forces wishing to bring down the President, one by weakening economic outcomes, the other by implicating him in malfeasance.

In truth, the President has very broad constitutional powers, as South Africans found out to their detriment during the Zuma epoch, and while there is serious opposition to CR from within the ANC, creating in effect two centres of power, it is extremely unlikely that he will be recalled by his party.

The President has largely ring-fenced the financial cluster – Treasury, SARS, the parastatal boards, financial regulation and regulatory bodies, albeit that efforts at reforming the parastatals have been met by opposition from the existing managerial echelon, the unions and even within the Cabinet.

Even though there has been outspoken support for the President from the labour movement, and the Communist Party, as well as ANC heavyweights such as Gwede Mantashe, the capacity to derail the President's economic reform programme should not be underestimated.

7. The SA Economy – A Wilting Protea

In 2018, the local economy grew 0.8%, a bit better than expected, albeit that growth of 1.4% in the last quarter was lower than forecast. However, things took a distinct turn for the worse in Q1 2019.

The reversal was severe with GDP contracting 3.2% on the quarter. A fall of this magnitude was last seen during the 'Great Recession' in 2009, making this a very significant development. On a year-on-year basis growth flatlined completely. We are where we were a year ago.

Mining, wholesale and retail trade, and construction are all in recession.

If you look at economic activity per se, and not by sector, the combined effect of lower exports, weaker fixed investment, and falling household spending was to contract SA GDP by a full 3.4%.

The problems are associated in the main with very low levels of business and consumer confidence evident during the period. In truth, these have not really picked up since the release of the GDP report in the wake of the elections.

In many parts of the world the pace of growth is returning to levels last seen in the aftermath of the 2008/09 financial crisis. In circumstances where global rates are low, and inflation subdued, economic weakness makes the case for rate cuts pretty much unassailable in many countries, including South Africa, notwithstanding political and policy risks that could negatively affect the rand.

This was confirmed by the SARB at its policy meeting in May. The Bank said that while the inflation forecast had improved with risks evenly balanced, the growth outlook had worsened, with risks to the downside.

As a consequence, and while the Committee majority voted to keep rates on hold, two members dissented, opting for a cut, and the SARB lowered its forecast path for the repo rate, now implying one rate cut by the end of Q1 2020. This development, hopefully even sooner than currently anticipated, will be welcome indeed.

The Quart is adjourned
By order of the Judge (GPP)

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