THE QUART 40IFO

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

Quarter Four 2023 in Review

Introduction

Welcome to the Q4, 2023 edition of The Quart.

What a year it has been. Most of us have hopefully had a chance to take some time off, catch our breath and recharge our batteries over Christmas/New Year and are ready to face the challenges that 2024 will most certainly present.

From a market perspective there are two major interconnected points to highlight for the quarter:

1. **Strong recovery of the equity markets in Q4 of 2023 – details in section 1 on market activity during the quarter.**

2. **The signalling by the Fed and other global monetary policy bodies of the approaching end to further interest rate increases and possible rate cuts for 2024 – see references in the first quarterly theme on the Fed.**

[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).

Reading Elon Musk's book by Walter Isaacson over the holiday period (love him or hate him - well worth a read), it struck me how on one hand humankind is making incredible technological progress with driverless electric cars and space missions employing reusable rockets and yet on the other hand engaging in brutal conflict in so many parts of the world - Russia/Ukraine, Middle East, Iran/Pakistan, and potentially on the Korean peninsula and between China/Taiwan to mention a few examples.

With seven of the world's 10 most populous nations holding elections this year (US, UK, SA, Russia, Mexico, Indonesia, India, Bangladesh and Pakistan), countries that are home to almost half the world's population will go to the polls, the Judge highlights some of the geo-political risks that we should take cognisance of when making investment portfolio decisions (see the second quarterly theme below).

In section 3 the Judge outlines the SA outlook in more detail. It is interesting to note at this time of the year, the yearly starting values of the USD/ZAR exchange rate from 2010 to 2024:

Year	**USD/ZAR Exchange Rate**
2010	R7.38
2011	R6.56
2012	R8.01
2013	R8.41
2014	R10.47
2015	R11.60
2016	R15.45
2017	R13.73
2018	R12.37
2019	R14.37
2020	R14.00
2021	R15.41
2022	R15.93
2023	R16.89
2024	R18.32
22 January 2024	R19.14

The SA elections due to be held mid-year certainly are set to be one of the most interesting elections held since the democratic transition. What will the impact be on the ZAR? Can the ANC retain full control? What does coalition politics in SA look like? The Judge will cover these points of interest in a future edition.

Our Osrin Group team remains at your service as we continue to evaluate existing client portfolios and explore new investment opportunities both locally and abroad. We look forward to interacting with each and every one of you over the coming months.

(You will note the cricketing theme running through the headings of the various sections. This to make up for a 5-day Newlands test ending in a day and a half).

We wish all our clients all the best for 2024 and hope that you find this edition of The Quart of interest.

Kind regards,
Jonathan and Bernard.

Jonathan & Bernard

OSRIN GROUP

The Quart is in Session

Market Activity - The Tail Wags

Major US indices had a stellar last quarter, ending the year with a nine-week run of gains. The Dow Jones Industrial Average (DJIA) finished the December quarter higher by 12.5% for a 13.7% annual gain. The DJIA hit a record closing level of over 37,710.10 on December 28th.

The S&P500 ended October in correction territory but ramped up 8.9% in November and ended the final quarter higher by over 11% with a better than 4% performance in December alone. It closed the year just shy of a new record, having come within 9 points of a new intra-day high. The S&P500 rose 24.2% for the year the fourth positive year out of the last five. It is now over 30% above its most recent trough, which puts it in bull market territory. Approximately 40% of the total gain has been the performance of leading tech stocks like Nvidia, Amazon, Meta (Facebook) and Alphabet (Google). The Nasdaq Composite (Nasdaq) also ended the month with nine consecutive up-weeks. October marked the index's third down month. But in November fortunes turned and the Nasdaq gained 10.7% and was up over 6% in December for a final quarter performance of over 14%. For the year the Nasdaq climbed 43.4%, marking its best year since 2020.

Strength in the November/ December period can be attributed to:

- A more dovish outlook from the Federal Reserve amid hopes for rate cuts in 2024.
- Indications that key inflation measures were moderating.
- The prospect of a soft landing ie. the avoidance of a US recession when the Fed ends its tightening cycle.
- A retracement in the price of oil.
- A degree of rapprochement between the US and China after Presidents Biden and Xi met in San Francisco.

In Europe the German DAX30 was better off by 19.04% for the year, while the French CAC40 improved 14.75%. The FTSE100 by contrast was only up by 2.94% in 2023.

Amongst emerging markets Brazil's Bovespa surged 24.53% in 2023, Russia's RTS was higher by 15.66%, India's Sensex rose 18.88%, but the Shanghai Composite ended the year lower by 4.3%. The MSCI Emerging Market Index, which is denominated in US dollars, was 7% higher. Locally the FTSE/ JSE AllShare Index (Alsi) put on 5.18% for the year and the FTSE/ JSE Top 40 Tradeable Index (Top 40) added 5.20%. The rand fell 8.2% with the result that local indices did a lot worse off in US dollar terms and underperformed most Emerging Market peers.

For 2023 crude oil fell over 10% for the first time since 2020 and despite Middle East tensions, but gold showed an increment of over 13% for the year, comfortably getting through the US$2,000/oz level.

Quarterly Themes

1. The Fed - Playing the Drive Rather Than the Cut

The Federal Reserve (Fed) ended Q3 2023 on a slightly hawkish note with Chairperson Powell observing that while much had been done, the process of getting inflation sustainably down to 2.0% had "a long way to go".

The minutes of the September meeting of the Federal Open Market Committee (FOMC) were released on October 11. In the minutes it was noted that inflation data had moderated but that inflation was still unacceptably high. Currently inflation was "well above" the longer-run goal of 2%. Further progress was needed to get inflation to the 2% objective. A majority of meeting participants judged that one more increase in the target federal funds rate at a future meeting would likely be appropriate, while some judged it likely that no further increases would be warranted. The vast majority of FOMC members continued to judge the future path of the US economy as "highly uncertain". Most Committee members continued to see upside risks to inflation. All meeting participants agreed that monetary policy should remain restrictive for some time until the Committee was confident that inflation was moving down sustainably toward its objective.

Chair Powell, speaking at the Economic Club of New York on October 18 acknowledged that inflation measures had turned lower in what he described as a “very favourable development”, but inflation remained too high. Unusually, declining inflation had not come at the expense of higher unemployment and lower economic activity. The Committee remained steadfast in its commitment to returning inflation to a level of 2% over time and in so doing had to balance tightening too little which could entrench inflation and tightening too much which could unnecessarily damage the US economy. At this stage in the quarter the fed funds futures market was pricing in a 50% chance of a rate cut in June 2024 and that the fed funds rate would remain at or above 5% for the whole of the year. On November 1 the FOMC issued its monetary policy statement. The target range for the fed funds rate was kept unchanged at a range of 5.25% to 5.5%. This was the second time in a row that the Fed left rates unchanged after 11 successive rate hikes since March 2022 to a 22-year high. The statement noted that US economic activity had expanded at a strong pace in the third quarter (4.9% annualised), that job gains had moderated since earlier in the year but remained strong and that inflation continued to be “elevated”.

In the press conference after the statement’s release Chair Powell emphasised that inflation remained “well above” the 2% objective but readings had moderated. However, it would take more than a few months of more favourable inflation data to give the Committee the confidence that the inflation rate was moving sustainably towards the 2% goal. This process still had a long way to go. Reducing inflation was likely to entail a period of below-potential growth and some softening of the labour market conditions. He added that financial conditions had tightened significantly in recent months driven by higher bond yields. At its present level the fed funds rate remained restrictive, which is to say tight monetary policy was putting downward pressure on economic activity and inflation. Participants agreed that the Committee was in a position to proceed “carefully”.

The markets interpreted the comments particularly that the FOMC would proceed “carefully”, as somewhat dovish and the fed funds futures market now factored in a 25% chance of a rate hike in December, down from a prior 40%. Yields on Treasuries came off and the US stock market continued a three-day rally.

In the minutes of the October 31-November 1 meeting released on November 21, participants restated the view that US inflation remained “unacceptably” high and well above the 2% longer-run target. All participants agreed that the Committee was in a position to proceed “carefully”. All participants in addition judged that it would be appropriate for policy to remain at a “restrictive stance” for some time until inflation was “clearly moving down sustainably toward the Committee’s objective”. The market took the text to imply that the FOMC was prepared to keep rates on hold for the remainder of the year and the fed funds futures market was now factoring in a decision to hold rates steady at the Fed’s December meeting.

In a speech on December 1, Chair Powell stated that it would be premature to conclude with confidence that the Fed had achieved a sufficiently restrictive stance, or to speculate on when policy might ease. But the Fed was prepared to tighten policy further if it became appropriate to do so. Markets interpreted these comments as dovish and possibly signifying that the FOMC would not raise rates further given that inflation was “moving in the right direction”. Treasury yields came off sharply just as US stocks ramped up. The fed funds futures market started pricing in a greater than 50% likelihood of five rate cuts in 2024.

Meanwhile, a CNBC Fed Survey found that the majority of respondents thought the Fed would start cutting rates in June 2024. The average respondent forecasted 85 basis points of rate cuts in 2024. And 47% of respondents thought that a soft landing would eventuate, an improvement of 5 percentage points from the prior survey.

In the policy statement released on December 13, the FOMC noted that the growth of economic activity had slowed from its strong pace in the third quarter. In another change in the text of the previous statement, the FOMC said that inflation had “eased over the past year” although it still remained elevated. For the third time in a row the Committee left the target range for the fed funds rate unchanged at 5.25% to 5.5%.

The Summary of Economic Projections accompanying the policy statement was illuminating. The median view of members of the Committee for US GDP was lifted to 2.6% for 2023 from 2.1% in September, but taken down to 1.4% in 2024 from a prior 1.5%. The median view for the Fed’s preferred inflation benchmark, the core Personal Consumption Expenditure price index, was lowered substantially to 3.2% for 2023 from a previous 3.7% and to 2.4% from a prior 2.6% in 2024.

The median view for the trajectory of the fed funds rate fell to 4.6% by end-2024 implying three cuts from 5.1% (one rate cut) before and to 3.6% by end-2025 implying a further four rate cuts. In his post statement release press conference Powell said that US inflation had eased from its highs and this had come about without a significant increase in unemployment.

“That is very good news”, he added.

The three rate cuts projection drove equity markets sharply higher with the DJIA reaching a new all-time record. Treasuries rallied as well and the yield on the 10-year dipped under 4.0% its lowest level since July.

2. Geo-Political Risk - Evading Bouncers

Geo-political risk can be defined as risk in the political sphere arising out of the relationship between countries and within countries. Geo-political risk pertains to trade relationships, security partnerships, alliances, multi-national initiatives, and supply chains. The principal drivers of geo-political risk are conflicts and elections.

In a recent Fortune Deloitte CEO outlook poll, 51% of respondents said that they were pessimistic about the current state of geo-politics as many as were pessimistic about inflation. So geo-politics matters. And it plays out in markets in unpredictable ways. When Russia invaded Ukraine in February 2022, few would have envisaged the manner in which the conflict would affect world food markets. Who knew that Ukraine produced 11.3% of global cereals (wheat, corn and coarse grain) and that in 2020, 52% of sunflower seeds and oil came from Ukraine. Ukraine is also a major producer of fertilizer components such as phosphates. With Russia controlling access to the Black Sea as well as bombarding Ukraine's cereals stockpiles, Ukraine was forced to divert its exports via road and rail bringing exports down by around 85%. Russia's considerable exports of grain were also halted. This led to a spike in grain and fertilizer prices and global food shortages. The Black Sea Grain Initiative brought some calm to the markets. The deal was extended twice but the Initiative expired in July 2023. Grain prices have since fallen on increased production by other countries like Argentina and China that are making up the shortfall from Ukraine.

The war in Ukraine has become something of a stalemate with Ukraine's much vaunted summer counter offensive achieving territorial gains of only 17 kilometres. The country is now struggling to secure much needed military assistance. Congressional Republicans are seeking to make an additional aid package conditional on US immigration reform. €50 billion in EU aid has been blocked by Hungary, a Putin ally. Russia is exploiting the impasse by launching its most intense aerial bombardments of the war.

The invasion of Israel by the Hamas terrorist organisation and Israel's response in Gaza raised the spectre of increased oil prices. But oil markets remained relatively calm after an initial 5% spike to factor in a war risk-premium. The price of benchmark Brent crude oil actually decreased over 10% in 2023, its worst showing since 2020. This was due to projections for falling demand out of China and Russia's flooding of eastern markets with cheap oil. Russia made approximately US$850 billion from sales of oil and natural gas in 2023 despite a raft of sanctions being introduced by the US and EU. However, should the war between Israel and Hamas broaden to take on a regional character, specifically should Hezbollah and Iran and the US become engaged, oil prices would most certainly increase sharply. Hezbollah is far better equipped than Hamas and has years of fighting experience alongside Iran and Russia in support of the Assad regime in Syria.

In an unexpected development Iranian-backed Houthi rebels in Yemen started launching missiles and drones at cargo ships and oil tankers in the Red Sea threatening trade through the Suez Canal. This is an example of how geo-political risk can produce unanticipated consequences with implications for the global economy. Four of the world's five biggest container-shipping companies, CMA CGM, Hapag-Lloyd, Maersk and MSC, have paused or suspended using the Red Sea shipping lanes. In 2023 approximately 24,000 vessels utilised the Suez Canal, accounting for some 10% of global seaborne trade by volume. That number includes 20% of the world's container traffic, nearly 10% of seaborne oil and 8% of liquefied natural gas. The cost of shipping a container from Asia to Northern Europe has increased 173% and between Asia and the Mediterranean, has more than doubled.

It now takes 10 days to two weeks longer to deliver goods by ship from China to Europe. The whole saga threatens a new round of supply chain disruptions, which will help stoke global inflation and reduce productivity.

The war with Hamas has been a costly one for the Israeli economy. Around 20% of Israeli employees were initially called up and are not working at present and approximately 80,000 of its residents have been displaced. The war has also brought an end to most Palestinian labour in Israel. The absence of workers had cost the economy NIS13 billion or approximately US$3.6 billion to end-November 2023. The tech industry which accounts for 18% of Israeli GDP and 50% of exports is struggling. But the largest blow has been to the tourism sector. It is estimated that Israel will lose up to NIS5 billion in earnings from inbound travel. Outbound departures from Israel are also down approximately 50%. Domestic consumption in November had fallen about 12% year-on-year. The three major rating agencies, S&P, Moody's Investor Service and Fitch Ratings, have all warned that any escalation in the Gaza conflict could lead to a downgrade of Israel's sovereign credit rating. The Israeli shekel depreciated over 5% versus the US dollar after the war started to a 14-year low. The Bank of Israel was compelled to intervene in the currency markets to support the shekel by selling foreign currency reserves, which fell by US$7.3 billion in October alone. Since then, the shekel has reclaimed most of its losses. sThe TA-35 Index of stocks fell to a multi-year low. It too has subsequently regained its losses.

The Bank of Israel in October cut its domestic growth projection to 2.3% from a prior 3.0%

The impact of the war on Israel's Arab neighbours Jordan, Lebanon and Egypt is more uncertain but estimates put the cost at 2.3% of regional GDP and the figure will be much higher for Lebanon if Israel's conflict with the terrorist group, Hezbollah, intensifies. Egypt stands to lose around US$6-US$9 billion a year in revenues from the Suez Canal if cargo ships continue to divert their courses away from the Red Sea.

Generally, the Israel-Hamas war has been good for safe haven assets like gold, the US dollar and Treasuries as well as for the performance of defence contractor stocks like Boeing and Lockheed Martin.

Even the Fed has weighed in. Fed Chairperson Jerome Powell in an address in October referred to "highly elevated" geo-political tensions which "posed important risks to global economic activity." But for now, at least, the prevailing view as evidenced in the global oil market for example is that the economic impact of the Israel-Hamas war will be contained. This might well be an under-pricing of geo-political risk.

The focus of global geo-political risk in 2024 will most probably shift to election outcomes, in particular the Taiwan election in January and the US election in November. These events will be covered in future editions of The Quart.

3. South African Outlook - Extras Pile Up

On October 23 South African Reserve Bank (SARB) Deputy-Governor and Monetary Policy Committee (MPC) member, Kuben Naidoo, tendered his resignation. His term was due to end in 18 months' time. Speculation was rife that Naidoo, a perceived monetary policy dove was unhappy with the hawkish tone of South African monetary policy. The two SARB MPC meetings held last quarter in July and September saw rates kept on hold in split decisions by 3 votes to 2. Prior to that the SARB had hiked the benchmark repurchase rate by 475 basis points to 8.25% from November 2021 to May 2023. Naidoo's resignation still has to be accepted by the government and a replacement found. In the interim he remains an MPC member.

On November 23 the SARB MPC unanimously held the repo rate unchanged at 8.25%. The Committee stated that although loadshedding had declined, economic growth in the near term was likely to remain muted. In addition to loadshedding, logistical problems were also hindering growth. Nonetheless with an improving electricity outlook, the SARB lifted its forecast for the 2023 SA GDP growth rate to 0.8%

from a prior 0.7% and to 1.2% in 2024 (previously 1.0%) and 1.3% (1.1%) in 2025. A further sustained decrease in loadshedding or greater supply of electricity from other sources would have a significantly positive effect on growth. However, the operation of ports and rail were serious growth constraints. The risks to the medium-term domestic growth outlook were said to be balanced. The Committee said that domestic headline inflation had increased more gradually than in many other emerging and developed economies. Nonetheless the South African inflation rate remained susceptible to shocks.

- Fuel price inflation was seen at 0.4% for 2023, but lowered to 3.2% in 2024 from 5.8% previously.

- The food price inflation forecast remained high at 10.6% for 2023 (from 10.4%) moderating to 5.5% in 2024.

- The outlook for headline inflation for 2023 was taken down to 5.8% from 5.9% and for 2024 to 5.0% from 5.1%. Inflation was seen stabilising at 4.5% in 2025 and 2026.

- Risks to the inflation outlook remained to the upside. Electricity prices continued to present clear inflation risks, and with logistics constraints, were likely to have broader effects on the cost of doing business and the cost of living.

It was against this backdrop that the MPC held the repurchase rate steady at 8.25%. At that level policy was restrictive ie. was placing downward pressure on inflation and growth. The policy stance aimed to anchor inflation expectations around the mid-point of the target band (4.5%) and to increase confidence that the inflation target could sustainably be achieved over time.

The Bank of America's Fund Manager Survey found inter alia that investors believed the SA rate tightening cycle to be over and expected a rate cut from the SARB in late Q2 2024. In early November South Africa hosted the latest African Growth and Opportunity Act (Agoa) Forum. President Ramaphosa used the meeting to call for a 10-year extension of the Act which allows 35 African countries duty free access for their goods to the US market. Agoa is due to expire in September 2025, but a decision to renew by Congress could be made as early as 2024. Agoa has facilitated an increase in South African exports such that South Africa habitually runs sizeable trade surpluses with the US. In 2021, a third of SA exports to the US were allowed in duty free by Agoa in an amount of US$2.7 billion. The principal export items were motor vehicles, jewellery, ferroalloys, fruit and nuts and beverages and spirits. 70% of South African agricultural product exports relied on Agoa. The US remains South Africa's second largest export market after China.

The US government has the discretion to exclude country members of Agoa where their policies with the US threaten the US' security and foreign policy interests. Recently the US excluded the Central African Republic, Niger, Uganda and Gabon from Agoa and earlier in the year Ethiopia's benefits were suspended and Guinea and Mali were also excluded. All the countries concerned were alleged to have committed human rights violations or in some cases had undergone coup d'états. South Africa's support of Russia and Hamas in the current conflicts in Ukraine and Gaza threaten to derail South Africa's membership of Agoa. A group of Congressmen lobbied for President Biden to move the Agoa Forum away from South Africa and to exclude South Africa from Agoa's benefits. For the time being anyway South Africa remains a substantial beneficiary of the legislation.

On November 1 Finance Minister Enoch Godongwana presented the 2023 Medium-Term Budget Policy Statement (MTBPS). In his speech Godongwana stated that the domestic economic outlook over the medium term (three years) remained weak, reflecting the cumulative effect of power cuts, the poor performance of the logistics sector, high inflation, rising borrowing costs, and a weaker global environment. As a consequence, Treasury had cut its forecast for South African growth to 0.8% from a February projection of 0.9%. The GDP growth rate was set to average 1.4% in 2024 and 2025.

- South Africa's fiscal position was said to have deteriorated by R54.7 billion compared to projections in the 2023 Budget in February. The deterioration came on the back of lower revenue collection, more particularly lower company and specifically mining company tax receipts than projected (although personal income tax receipts were higher than forecast). In addition, the public sector wage bill had increased and debt servicing costs were higher than once projected.

- As a consequence, the main budget deficit in fiscal year 2023/24 was seen as materially widening to 4.9% of GDP from a prior forecast of 4.0% of GDP.

- The government annual borrowing requirement had risen to R553 billion per annum over the medium term.

- Gross government debt was set to increase from R4.8 trillion in the current fiscal year to R5.2 trillion in FY2024/25 and to over R6 trillion by FY2025/26. Gross government debt was seen stabilising at 77.7% of GDP by fiscal 2025/26 up from a prior estimate of 73.5%.

- Over the next three years, debt servicing costs were slated to rise from 20.7% of revenue to 22.1%. Over this period interest costs would amount to approximately R1.3 trillion.

- In the current financial year, spending had been revised down by R21 billion. Further reductions of R64 billion in 2024/25 and R69 billion in 2025/26 were proposed. Government budgeted R74 billion over three years for wage increases in the personnel heavy Departments of Health, Education, and Police Services. R34 billion was allocated to the Covid-19 Social Relief of Distress (SRD) grant for another year. The Presidential Employment Initiative would be extended for another year through repurposing of a portion of funds from existing public employment programmes such as the Expanded Public Works Programme and the Community Works Programme.

- The Minister also said that R15 billion in unstated new taxes were slated for the FY2024 budget.

- He stipulated a plan for providing municipal debt relief and confirmed the partial takeover by the government of R254 billion in Eskom debt from FY2023/24 to FY2025/26 on terms that were to be legislated.

- The Minister announced reform measures covering the energy transition, logistics' challenges, inadequate infrastructure investment, strengthening procurement and fighting crime and corruption.

The Finance Minister is in a no-win situation.

He was slammed by the left for fiscal austerity by only extending the SRD grant for a year when it has been shown to support around half of the population. He was criticised too for shifting funds away from public employment programmes. The more fiscally conservative, however, accused the Minister of fiscal profligacy arguing that the budget was a populist one and that higher spending on inter alia salary increases was drawing the country's economy ever closer to the fiscal cliff.

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

The views and opinions expressed in this article are those honestly and genuinely held by the author. They are based on an analysis of information available in public domain. They are not intended to be, neither should they be construed to be, financial advice of any kind, nor as a definitive analysis of any financial or related issue. Individuals must not rely on this information in order to make an investment, financial, trading or like decision. If they nevertheless choose to do so, they do so entirely at their own risk.

OSRIN GROUP

20th Floor, No2 Long Street, Cape Town, South Africa
PO Box 7256, Roggebaai, 8012, South Africa
Tel **+27 21 421 7110** Fax +**27 21 421 7191** Email **info@osringroup.co.za**

OSRIN WEALTH
Authorised Financial Services Provider **FSP No. 49766**

OSRIN ADVISORY
Authorised Financial Services Provider **FSP No. 32532**