Afrifocus
PERSONAL WEALTH
MEMBER OF THE JSE AND ZAR X

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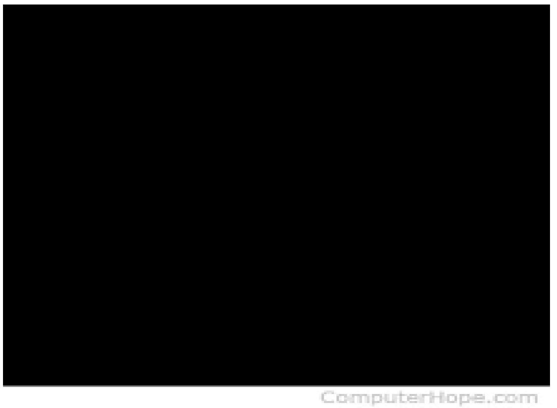
Struggling to keep the lights on

April 2019

Dear Investor,

Having entered 2019Q1 quite positive, we are becoming very concerned on a seemingly inability to fix the Eskom problem.



Source: Google images

Electricity supply feeds directly into GDP growth, and as the graphic below highlights, electricity production started stalling in 2008. The result has been a structural decline in GDP; and the impact on the domestic business confidence and earnings growth of SA Inc. shares is well documented.

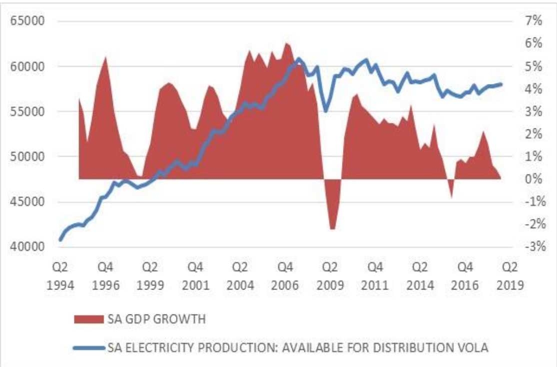


Figure 1 – SA electricity production and GDP

In order to see a meaningful domestic equity rally, the Eskom problem remains the foremost hurdle to fix.

We are entering the final few weeks pre the 2019 General Elections. The rhetoric and mudslinging continues unabated, coupled with the unearthing of many political skeletons within the ruling party. The persistent rumours on the recall of President Ramaphosa post the elections is very worrying.

Globally we had a decent equity rally in 2019Q1, driven by an expectation of a resolution of the trade wars and a view that the US FED will stop hiking interest rates. As expected, the JSE ALSI continued its underperformance of global equities.

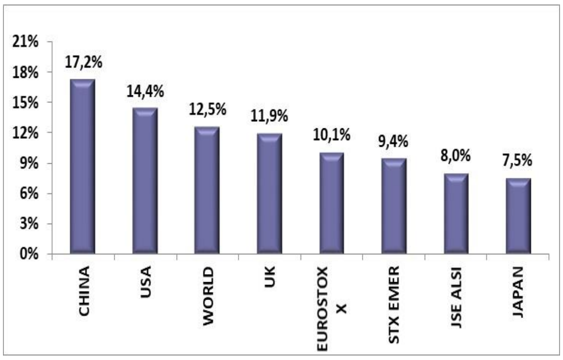


Figure 2 – 2019Q1 equity market performance, ZAR

Growth prospects for South Africa remain benign, as per the lasted IMF forecasts

	Year over Year			
		Estimates	Projections	
	2017	2018	2019	2020
World Output	**3.8**	**3.7**	**3.5**	**3.6**
Advanced Economies	**2.4**	**2.3**	**2.0**	**1.7**
United States	2.2	2.9	2.5	1.8
Euro Area	2.4	1.8	1.6	1.7
Germany	2.5	1.5	1.3	1.6
France	2.3	1.5	1.5	1.6
Italy	1.6	1.0	0.6	0.9
Spain	3.0	2.5	2.2	1.9
Japan	1.9	0.9	1.1	0.5
United Kingdom	1.8	1.4	1.5	1.6
Canada	3.0	2.1	1.9	1.9
Other Advanced Economies 3/	2.8	2.8	2.5	2.5
Emerging Market and Developing Economies	**4.7**	**4.6**	**4.5**	**4.9**
Commonwealth of Independent States	2.1	2.4	2.2	2.3
Russia	1.5	1.7	1.6	1.7
Excluding Russia	3.6	3.9	3.7	3.7
Emerging and Developing Asia	6.5	6.5	6.3	6.4
China	6.9	6.6	6.2	6.2
India 4/	6.7	7.3	7.5	7.7
ASEAN-5 5/	5.3	5.2	5.1	5.2
Emerging and Developing Europe	6.0	3.8	0.7	2.4
Latin America and the Caribbean	1.3	1.1	2.0	2.5
Brazil	1.1	1.3	2.5	2.2
Mexico	2.1	2.1	2.1	2.2
Middle East, North Africa, Afghanistan, and Pakistan	2.2	2.4	2.4	3.0
Saudi Arabia	–0.9	2.3	1.8	2.1
Sub-Saharan Africa	2.9	2.9	3.5	3.6
Nigeria	0.8	1.9	2.0	2.2
South Africa	1.3	0.8	1.4	1.7

Figure 3 – Global growth forecasts, Jan 2019, IMF

We remain concerned that the intervention in US monetary policy will be negative for equities and ultimately benefit one asset class, namely Gold.

Local assets

Market sentiment for the JSE ALSI remains elevated. Equity returns have been poor for the period following extreme positive sentiment. We would from this basis solely be cautious on the aggressive purchasing of shares in this environment.

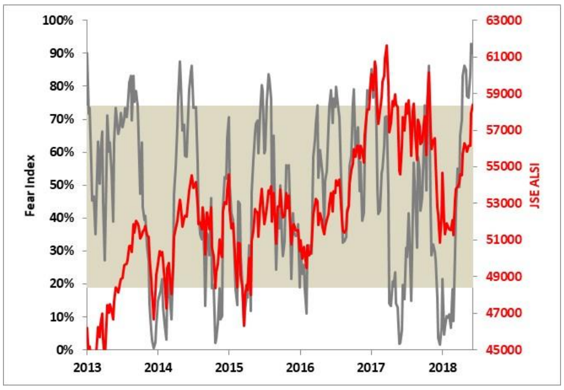


Figure 4 – JSE Fear Index

Despite a strong rally in NASPERS-N (JSE: NPN), we remain positive on the value unlock of the Group. The large discount to NAV is unwinding as we move towards the separate listing of its global technology assets on the Amsterdam Stock Exchange. The unbundling of MULTICHOICE (JSE: MCG) was unspectacular, with the share trading to below R100 prior to a recovery to the R130 level.

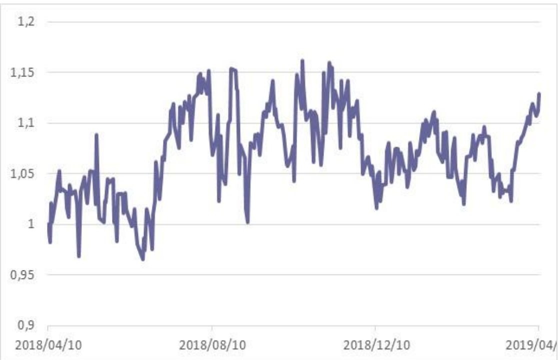


Figure 5 – NASPERS relative to TENCENT [ZAR]

Local resource stocks have had a very strong performance this quarter, as results surprised to the upside. In our managed portfolios we have added AFRICAN RAINBOW MINERALS (JSE: ARI) to the portfolio as a cheap entry into a diversified mining portfolio of assets.

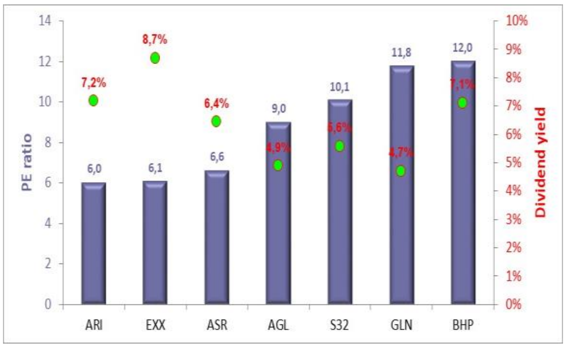


Figure 6 – Diversified Miners - ARI undervalued on a PE of 6x and a 7% DY

We have increased exposure to ASPEN PHARMACEUTICALS (JSE: APN) after the recent collapse. The share is trading on a forward EV/EBITDA ratio of 7.8x, a far cry from the long-term average of 15x. The business model is being questioned given the strong increase in debt within the Group. Indications that the sale of the baby-formulae business will be concluded before June 2019 which will hopefully see a reduction in the debt levels of the Group.

The preference share index continues to rerate with a total return of 21% over the past 12 months.

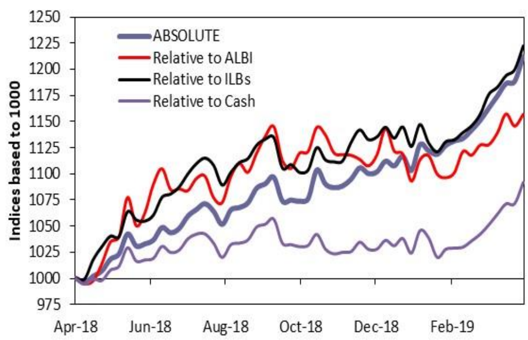


Figure 7 – Performance of JSE Preference Share Index

Compared the cash, the index trades at an elevated 250bps, compared to the long-term average of 185bps. As per our previous newsletter, we remain negative on cash and positive on preference shares as an asset class on a post-tax basis.

The decline in Government Bond yields as measured by the ALBI as a result of continued expectations of a credit downgrade to junk status is presented below. Yields are at levels where future returns over inflation will be decent.

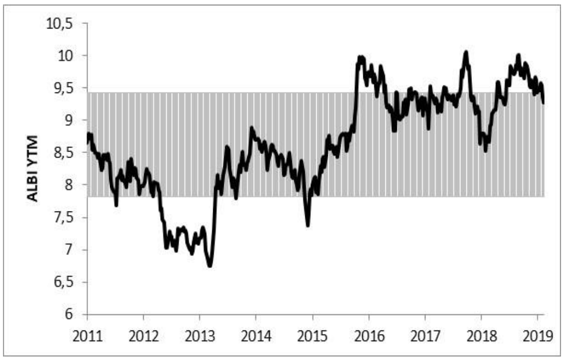


Figure 8 – BEASSA All Bond YTM

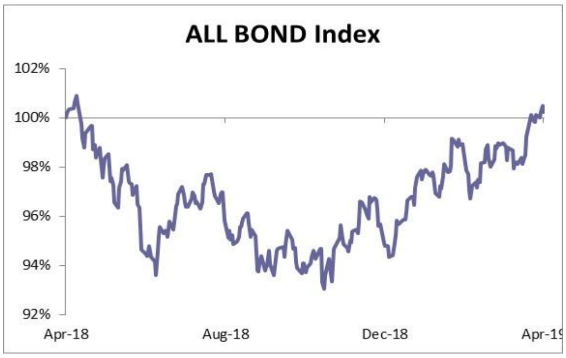


Figure 9 – BEASSA All Bond performance relative to Cash

For those investors shying away from preference shares due to potential default risk in individual issuers, we would recommend investing in Government Bonds via one of the listed ETFs.

Offshore assets

We remain positive on emerging markets as an asset class. Investors can get exposure via the STXEMG ETF. As highlighted in previous newsletters, we believe that the superior growth prospects and relative valuation multiples favour emerging markets over developed markets over the longer-term.

Within the developed market universe European equities (JSE: SYGEU) remain undervalued and oversold.

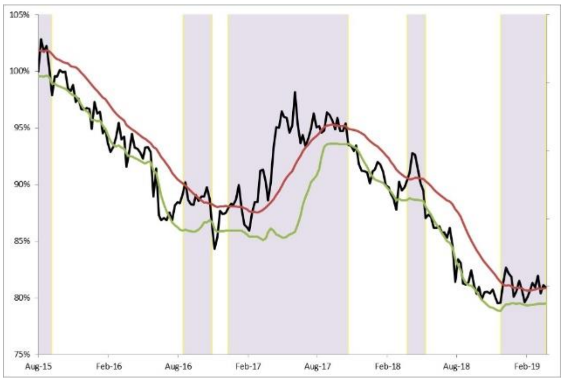


Figure 10 – European equities relative to MSCI World, shaded areas represent relative bull markets

Communication with Afrifocus

Our preferred stocks, ETFs and income assets can be discussed with our Portfolio Managers. They will also provide you with information on Afrifocus Personal Wealth and all our investment products.

Regards

Afrifocus Personal Wealth

Table 1 - Forecast returns for JSE Sectors

11 Apr 2019	INDEX	FPE	FDY	FORECAST GROWTH EPS	FORECAST GROWTH DPS	TARGET	RETURN
ALSI	58412	13,0	3,8%	22%	4%	64982	15%
FINANCIALS	42498	10,1	5,0%	37%	4%	49551	22%
BANKS	9612	10,8	5,1%	9%	9%	10140	11%
LIFE INSURERS	42350	12,0	5,5%	10%	-1%	52881	30%
FINANCIAL SERVICES	3440	8,2	2,9%	558%	1%	4392	31%
SA PROPERTY	484	10,4	9,6%	17%	4%	536	20%
FOREIGN PROPERTY		14,7	2,8%	2%	-13%		46%
INDUSTRIALS	44283	11,0	3,5%	13%	16%	51015	19%
CONSTRUCTION & MATERIALS	17	7,6	5,5%	31%	102%	23	43%
GENERAL INDUSTRIALS	177	11,8	3,2%	14%	13%	199	16%
INDUSTRIAL TRANSPORT	135	10,0	2,7%	1%	-2%	161	22%
ELECTRONIC & ELECTRICAL EQUIP	12610	10,3	6,2%	13%	11%	11834	0%
INDUSTRIAL ENGINEERING	3335	6,2	4,4%	44%	5%	4535	40%
SUPPORT SERVICES	12610	10,3	6,2%	13%	11%	11834	0%
CONSUMER GOODS	53654	15,6	4,0%	11%	8%	58984	14%
FOOD PRODUCERS	7033	13,2	4,7%	13%	5%	8368	24%
BEVERAGES	212	17,7	2,4%	20%	6%	207	0%
PERSONAL GOODS	978	19,4	3,2%	9%	7%	1059	11%
TOBACCO	7230	9,6	7,1%	16%	11%	8007	18%
HEALTHCARE	4442	10,6	3,7%	20%	12%	5378	25%
HEALTHCARE EQUIP & SERVICES	6458	14,1	4,0%	39%	14%	7069	13%
PHARMACEUTICALS & BIOTECH	10618	6,8	3,0%	6%	7%	15590	50%
CONSUMER SERVICES	23111	16,8	3,4%	14%	17%	25528	14%
GENERAL RETAILERS	6467	14,4	4,2%	10%	8%	7198	16%
FOOD & DRUG RETAILERS	11149	19,8	2,7%	11%	10%	12047	11%
MEDIA	855	20,1	3,7%	48%	n/a	926	12%
TRAVEL & LEISURE	4080	9,6	3,5%	16%	12%	5464	37%
TELECOMMUNICATIONS	5231	13,0	6,1%	28%	7%	5689	15%
FIXED LINE TELECOMMUNICATIONS	2388	12,5	4,8%	5%	5%	1867	-17%
MOBILE TELECOMMUNICATIONS	166	12,6	6,1%	27%	8%	185	18%
TECHNOLOGY	32430	30,8	0,3%	34%	28%	37822	17%
BASIC MATERIALS	34324	10,6	5,0%	12%	-2%	35178	7%
GENERAL MINING	12348	10,3	6,3%	6%	-9%	12297	6%
PLATINUM MINING	35	17,5	0,7%	56%	4%	29	-17%
GOLD MINING	1537	12,5	1,0%	70%	78%	1541	1%
CHEMICALS	23124	10,0	3,7%	27%	23%	25402	14%
FORESTRY & PAPER	57038	10,2	4,2%	3%	8%	66727	21%
INDUSTRIAL METALS	24135	10,4	7,3%	0%	-12%	16903	-23%