2 March 2022

Outlook for the day

The improved tone in early morning US futures trading will be insufficient to overcome the downbeat performance of key US indices in yesterday's session with the inconsistency in the Asian Pacific region and no evidence of decisive additional weakness in the Rand contributing to selling pressure at the outset of today's session. Resource counters and precious metals shares continue to contribute the lion's share of the upside on the JSE at this juncture. Resource counters are much overbought at current levels but as underlying commodity prices continue to improve there is no evidence of meaningful selling pressure as yet. Remaining trading exposure may be retained.

- Biden's State of the Union address
- Inflation in the U.K.
- Brent over $110 and Ukraine's war bonds.

Here's what moving markets

State of the Union

Vladimir Putin "badly miscalculated" with his invasion of Ukraine, President Joe Biden said in his first State of the Union address, calling the Russian leader a "dictator" and warning that the war will leave his country weaker. In a show of solidarity with Ukraine, Biden asked the audience, many of whom held Ukrainian flags, to stand. Ukraine's ambassador to the U.S. was present. Biden also announced that the U.S. will close its airspace to Russian airlines. He vowed that getting inflation under control would be his "top priority."

Further Pain

Inflation is everywhere. The prices of basic goods in the U.K. are rising at the fastest pace in more than a decade and further increases are likely as firms pass on soaring costs to consumers, a business lobby warned. In a survey published Wednesday, the British Retail Consortium said "there are limits to the costs that retailers can absorb" and consumers already facing a cost of living crisis can expect further pain.

Relentless Rally

Brent oil extended its relentless rally above $110 a barrel before an OPEC+ meeting as the International Energy Agency warned that global energy security is under threat following the invasion of Ukraine. Investors will be watching for a response from OPEC+ when the cartel meets Wednesday to discuss April supply, but only a modest increase is expected despite the turmoil. As oil soared, stocks extended a global selloff over fears of slower growth and higher inflation.

War Bonds

Ukraine raised 8.1 billion hryvnia ($277 million) in a sale of war bonds, its latest fundraising effort to tap into the global support for the country in its fight against Russia's invasion.

And retail traders want to buy them. The country also paid about $300 million of bond interest to international investors due Tuesday. Meanwhile, EU ambassadors agreed to call for an initial assessment of Ukraine's chances of joining the 27-nation bloc.

China shifts position on Ukraine somewhat

The semantics are critical: when asked previously whether China respected the territorial integrity of Ukraine it said the "the situation was due to a number of factors". Following a call yesterday between the foreign ministers of Ukraine, Dmytro Kuleba, and China, Wang Yi, China said "it was extremely concerned about the harm to civilians." In effect it signalled it was ready to play a peacekeeping role and said it deplored the outbreak of hostilities and "respected the territorial integrity of all countries". FT.

Ukraine War Leads to More Global Business Disruption

Russia's invasion of Ukraine, and a blistering volley of Western sanctions in response, unleashed another day of global business upheaval - prompting Apple Inc. to cut off Russian sales of iPhones and threatening to shut down Volkswagen AG's flagship car plant later this month. The wide-ranging disruptions reflected several different dynamics that have played out since Russian President Vladimir Putin invaded Ukraine last week. Key parts and commodities that typically flow out of Ukraine, a major agricultural exporter and an auto-parts supplier, have been bottled up inside the country.

Biden chides Putin in State of the Union, says his top priority is getting prices under control

President Biden delivered his first State of the Union address Tuesday (Politico). First part of the speech focused on Russia, confirmed US closing American airspace to all Russian flights and announced DOJ will assemble task force to go after crimes of Russian oligarchs. Said while Putin may make gains on battlefield, he will pay a continuing high price over long run. On domestic front, Biden rehashed first year legislative achievements such as Covid-19 relief program and mounted another argument for his Build Back Better proposals. Top priority is getting prices under control, focused on strengthening domestic supply chains and boosting local production of cars and semiconductors. Aims to ease inflation by lowering cost of prescription drugs, cutting energy costs by providing green investment tax credits, and reduce cost of childcare.

Outlined efforts to reduce deficit, including closing tax loopholes for ultra-wealthy.
Advocated raising minimum wage to $15 an hour and extending child tax credit.

Moscow intensifies attack on Ukraine, more sanctions announced as companies pull out of Russia

Russia's attack on Ukraine intensifying as Moscow escalates its attack on civilian areas and attempts to encircle Kyiv in a bid to demoralize Ukrainian resistance (Washington Post, WSJ, NY Times, Bloomberg). Comes as US defence officials say Russian troops making slower than expected progress amid food and fuel shortages. Western countries continue to put restrictions on Russia with UK announcing new sanctions against its central bank and its largest commercial bank, Sberbank. EU blocked seven other Russian banks from SWIFT. US expected to announce ban of Russian flights from its airspace. Companies in a range of industries with sales and JVs in Russia also under mounting pressure to cut ties. Apple (AAPL-US) the latest to halt product sales to Russia while Exxon Mobil (XOM-US) to shut down production there by exiting its Sakhalin JV and making no new investments in the country.

Bonds rallying as markets assess impact on growth, inflation and policy from Russian invasion

Global bonds continue to rally strongly amid heightened geopolitical tensions with global pile of negative yielding debt rising by $3T in two days (Bloomberg). While Ukraine crisis is not expected to alter plans by Fed and other central banks to raise rates in March, markets have pared back tightening expectations with a 50 bp move by the Fed all-but ruled out. Futures now pricing in less than five Fed rate hikes in 2022 vs six previously and have dialled back rate hike bets at other central banks.

Markets also predicting a shallower peak in fed funds rate of 1.7%, down more than 20 bp from earlier expectations (Bloomberg). Indicative of competing dynamics as central banks look to tame surging inflation while global economy faces more uncertainties. Real rates have fallen sharply with 5Y TIPS yield down to -1.7% from below -1% few weeks ago.

Russia's invasion of Ukraine may pressure already strained supply chains, driving up costs

Russia's invasion of Ukraine driving discussions about additional supply chains strains that could drive up costs for businesses and worsen inflation pressures (Bloomberg, NY Times). On Tuesday, world's biggest container carriers Mediterranean Shipping and Maersk halted bookings for Russian freight, squeezing Russian exports and imports of containerized goods. Ships struggling to access Ukrainian ports amid the fighting, while airspace restrictions risk lengthening Asia-Europe cargo travel times, prolonging deliveries and adding to freight costs. Meanwhile, sanctions have prompted banks to suspend financing for Russian commodity trades, potentially impacting supplies of energy, crops, and metals. Leaves auto manufacturers vulnerable to parts shortages, chip manufacturers wary of inputs like xenon and palladium, and food manufacturers potentially facing reduced supply of wheat and sunflower oil.

References: PMK Investment committee, exchange4 free, Momentum Investment consulting, Momentum securities, RMB Global markets Swissquote, eToro, Currency Partners

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Path of least resistance still lower

Market dealing with a lot of uncertainty right now. Russian invasion of Ukraine remains the big headline risk, particularly amid concerns the most destructive part of the offensive is still to come. Also scepticism about the potential for any meaningful breakthroughs at the next round of peace talks. Accompanying commodity rally providing support for some pockets of the market (energy, metals, solar), but also plays into the high-profile inflation concerns that have driven the hawkish shift in Fed policy. While geopolitical tensions may make it easier for Fed to opt for a 25 bp liftoff in March, not expected to put a dent in the near-term tightening path. Reopening trades under scrutiny despite Covid improvement and better economic data. Rate rally may be somewhat of a factor, with some growthier/riskier pockets of the market faring better as of late. At the same time, extent of the move lower in yields may be a function of one-way positioning (short duration).

Financials, materials worst performers while energy only sector higher

Sectors mostly lower in Tuesday trading and fairly mixed with value and growth in line despite big Treasury move. Banks hit hard again on rates, with both money centres and regionals sharply lower. Rate-sensitive insurance and credit cards also weaker. Chemicals and paper/packaging sharply lower again. Transports lower across the board, with airlines hit particularly hard on today's oil rally. Other travel and leisure groups also seeing sharp selloffs, including OTAs, cruise lines, hotels, and gaming. Semis, tech hardware and IT equipment, building materials, restaurants, autos, apparel, drug stores, cosmetics, HPC, beverages also weaker. Pockets of retail higher including discounters on big TGT-US earnings tailwind, while dollar stores and housing-related retail also better. Protein names higher on HRL-US earnings. Cybersecurity and A&D among groups better again amid geopolitical tensions. Commodity trade seeing big gains on higher underlying prices. Industrial metals stronger though steel mixed and off best levels. Precious metals miners higher, while energy the standout on today's big crude rally.

WTI finishes above $100 for first time since July 2014

WTI and Brent finished above $100 on Tuesday amid the latest ramp in geopolitical tensions, impact on western sanctions on Russia. While US Treasury announced yesterday energy payments through Central Bank of Russia can continue until 24-Jun under a waiver (Platts), Reuters reported that Russian oil buyers have already faced more difficulties with payments and availability of vessels after sanctions were announced this week. No relief from agreement by IEA members to release 60M barrels of oil stocks, including around 30M from the US (Reuters). OPEC+ is also unlikely to add additional barrels beyond standard 400K bpd monthly increase at tomorrow's meeting after last week it maintained assessment that there would be a global surplus in Q1. Bloomberg also reported that Saudi Arabia is expected to raise the price of its main oil grade to a record for April shipments to Asia.

References: PMK Investment committee, exchange4 free, Momentum Investment consulting, Momentum securities, RMB Global markets Swissquote, eToro, Currency Partners

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February ISM manufacturing beats, reversing January decline

February ISM manufacturing index up 1.0 points m/m to 58.6, ahead of estimates for 58.0. New orders index up 3.8 points m/m to 61.7, highest since September. Production index, supplier deliveries index, also higher. Prices index down 0.5 points to 75.6, though backlog of orders index up 8.6 points to 65. Report said manufacturing improved as omicron impact dissipated, with new orders and backlogs indicating strong growth. Employment index down 1.6 points to 52.9, though respondents overwhelmingly indicated increasing head counts. Commentary continued to flag impact of supply chain challenges though still-strong demand backdrop. Early economist reads noted that the ISM survey, along with the February PMI, indicated that the worst of supply chain pressures may be over, which could help ease core goods inflation in the coming months. Today's final February IHS Markit Manufacturing PMI revised up 0.1 to 57.6, up one point from January.

Market sees near-zero chance of Fed 50 bp March rate hike, fewer total hikes this year

Amid ramp in geopolitical tensions, the market has essentially zeroed-out the odds of a 50 bp March rate hike. According to the CME FedWatch, there is a less than 2% chance of an outsized 50 bp hike in March, down from over 90% following the hotter than expected January CPI print.

Markets have also marked down full-year rate path expectations, pricing in an 80% chance of five or fewer hikes this year, up from only 17% a week ago. Sell-side economists have noted near-term effects of the Russia-Ukraine crisis appear to be inflationary, though impact may be somewhat offset by the hit to growth.

Some also noted that geopolitical tensions give Fed cover to proceed cautiously on tightening, as there will likely be less political pressure to combat inflation amid conflict. Reuters noted that Chair Powell set to testify to Congress and is expected to continue to message that the Fed is focused on combating inflation while also downplaying 50 bp hike.

South Africa

Zondo 3 largely about Bosasa

Just in case we forgot, the State Capture Part 3 report, which focuses exclusively on the late Gavin Watson’s company, describes how the essential business model was based on corruption which was possible on an industrial scale because of the wide range of contacts. It also deals with evidence uncovering how Bosasa companies got contracts and the inner workings of State Capture design including after-hours planning meetings at Zuma's residences-who was present and what was discussed. Agrizzi's evidence shows that between 2000 and 2016 Bosasa companies got contracts around R2.3 bn including R75m in bribes.

The report also recommends that ANC leaders including former Gauteng premier Nomvula Mokonyane, Gwede Mantashe and Zuma be investigated in this connection. DM.

References: PMK Investment committee, exchange4 free, Momentum Investment consulting, Momentum securities, RMB Global markets Swissquote, eToro, Currency Partners

Whistle-blower Athol Williams tells of Bain & Co's corruption

In his book Deep Collusion Williams says reported his employer Bain & Co for withholding information on their complicity in State Capture, he had no idea how far-reaching their collusion had been. Drawing on his testimony before the Zondo Commission, Williams reveals Bain withhold information and witnesses from the authorities and also tried to buy Williams's silence and block his Zondo testimony. Williams uncovers the inner workings of State Capture design and takes us into the evidence revealing the after-hours planning meetings at Zuma's residences – who was present and what was discussed. DM

Social Compact countdown begins

Yacoob Aba Omar of the Mapungubwe Institute says the 100 day countdown set in the Sona has begun and gives some clarity around what to many is a woolly concept. Social compacts are "collective agreements between important social partners in society about how to address major issues requiring their collective contribution." Ramaphosa has said a lot about this in his various Sonas and has pointed out that it is not just business and labour but "citizens and patriots" as well. Omar says "South Africans should start monitoring the 100 day countdown : this is one of the last few remaining hopes for lifting our country out of the nightmarish scenarios we are descending into." BD.

Exchange rate

Latest Rates	Spot	Move
USD/ZAR	15.76	^
GBP/ZAR	20.55	^
EUR/ZAR	17.17	^
CHF/ZAR	16.63	^

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Backdrop

Archimedes' principle can be useful to markets. When a large object drops into a pool, it will displace a lot of liquid that must subsequently go somewhere. The Greek mathematician and physicist discovered this by getting into a bathtub.

The principle is also at work in world financial markets: what started off as a buoyant week for the Rand following the Budget Speech from the finance minister, was later followed by strong selling pressure as Russia pulled the figurative trigger - launching an all-out invasion of Ukraine.

After weeks of taunting, threatening, and trolling, Russian president Vladimir Putin gave the go-ahead to invade Ukraine, causing the global financial markets to drown in a sea of red ink – at least temporarily. The leading benchmark indexes sank, commodities soared, and currencies took a hiding. The conflagration in Ukraine has had economists ripping up their forecasts and sent them back to the drawing board. Predictions were already battered by the uncertainties brought on by the Covid-19 pandemic and subsequent supply-chain bottlenecks.

It's probably safe to say that the economic threats are akin to tossing a stone in a pond: a big splash at the centre, with ripples that diminish in size as they get further and further away. The threat to the Ukrainian economy is pretty obvious, and potentially severe. Russia faces a serious cost of economic sanctions against it by major Western trading partners, never mind the potentially great expense of waging a war (which the country's predecessor, the Soviet Union, learned the hard way in invading Afghanistan four decades ago). But how big a splash the invasion makes, and how disruptive and far-reaching the ripples, depends on how long and involved this conflict becomes – which is very difficult for anyone to predict.

Coming Up

- European stocks are set for another down day as the war in Ukraine continues to dominate headlines.
- It's a busy day for Federal Reserve watchers today ahead of the central bank's meeting later this month:
- Chair Jerome Powell is slated to deliver his semi-annual testimony before U.S. lawmakers in the House,
- Chicago and St. Louis presidents speak at events. Investors will be looking for hints to the size of the expected rate hike amid soaring commodity prices and inflation.
- The ECB's chief economist Philip Lane also speaks.
- In earnings, Snowflake, SoftBank-backed Coupang and Dollar Tree report in the U.S.
- in Europe, Aviva, Sberbank and Just Eat Takeaway are among the highlights.

http://pmkgroup.co.za

References: PMK Investment committee, exchange4 free, Momentum Investment consulting, Momentum securities, RMB Global markets Swissquote, eToro, Currency Partners