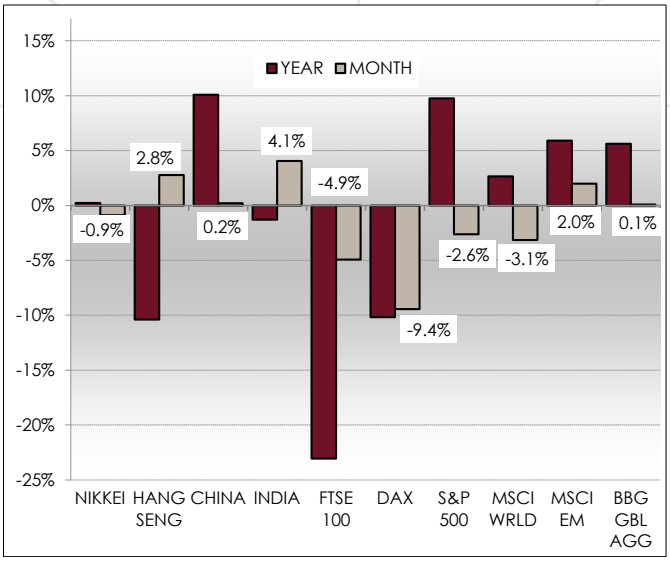
October in perspective – global markets

Investment markets continue to intrigue and fascinate; October was no exception. After a period of robust developed market returns, it was the turn of emerging markets to produce strong returns during the past month. Developed equity markets lost ground in absolute and relative returns: the US equity market lost 2.6%, the UK market lost 4.9% (bringing its year-to-date return to -26.1%) and the German equity market lost all of 9.4%. Even the defensive Swiss equity market lost 5.9% in October. In contrast, the Indian equity market rose 4.1%, and China 0.2%, the net result being that the MSCI World index lost 3.1% (bringing the year-to-date return to -2.8%) while MSCI Emerging market index gained 2.0% (year-to-date return of -1.0%).

It was noteworthy that mid and small-sized companies outperformed their larger peers. The S&P Mid and Small Cap indices *rose* 2.1% and 2.5% respectively, versus the 2.6% *decline* of US large caps, although the year-to-date returns are heavily skewed in favour of large caps.

Chart 1: Global returns to 31 Oct 2020



Emerging market currencies were firm during the month, as the dollar came under pressure. Strangely though, the DXY dollar index actually rose 0.2% on the month. Within the commodity price complex, precious metals were a bit weak but base metals and soft commodity prices were firm. The oil price lost 10.2% as a result of concerns about oversupply and slowing demand. The Bloomberg Global Aggregate Bond index was flat, posting a return of 0.1%.

Polar bear near Svalbard

Source: @fernando_ofarrill

What's on our radar screen?

Here is a summary of the things we have been keeping an eye on:

- *The SA economy:* The most important event during October was the Medium Term Budget Policy Statement (MTBPS), the purpose of which is to provide a medium to long-term view of government's plans and

"To achieve great things, two things are needed; a plan, and not quite enough time."
- Leonard Bernstein

how it intends to implement and finance them. However, given the Covid-19 pandemic and the emergency budget tabled after the official one in February, all eyes were on the MTBPS to obtain an update on how it was going to manage its finances during, and specifically after, the pandemic, given the emergency spending it tried to roll out in order to mitigate the devastating effects of the lockdown. Our expectations were not high.

A photo from "The Iceberg II" series

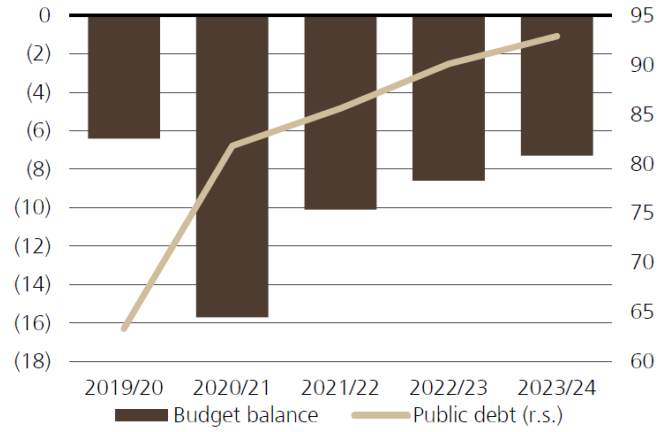
Source: @tomhegen.de

When it came, the news was not good: debt levels have escalated beyond reasonable levels with nothing more than vague promises to address them in the future. The MTBPS contained unconscionable plans like trimming the education and police budgets in order to throw another R10bn down the throat of a failed national airline – this after South African Airways has already consumed R40bn over the past few years with nothing to show for it! How can you actually take a government seriously when they act in this manner?

For the record, Treasury estimate the SA economy will shrink 7.8% this year, before growing by 3.3% and 1.7% in 2021 and 22 respectively. We think these forecasts are overly optimistic. Debt is forecast to peak at 95.3% of GDP before "stabilizing" at 86.4% in the 2025/26 fiscal year. Once again, these forecasts are overly optimistic. The bulk of the savings will come from government cutbacks, in particular on the civil servants' wage bill – and we all know how successful those attempts have been in the past. Government just doesn't have the political will to implement its forecast changes, and for that reason we think the SA economy will land up in a much worse position than government thinks.

Chart 2: Budget balance and public debt

As % of GDP



Source: Deutsche Bank

Treasury forecasts have rarely been accurate – they are always too optimistic – which leads us to further doubt the tabled

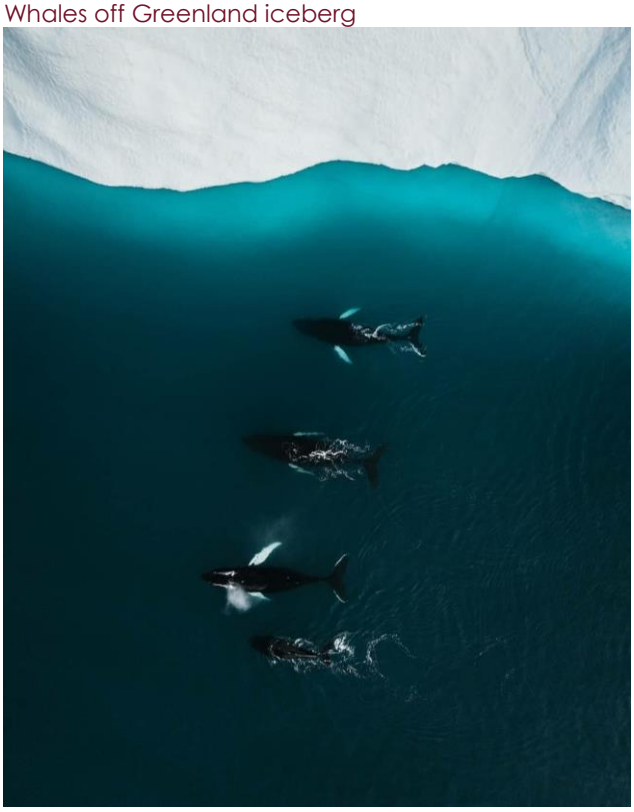
plans. Government has underestimated the loss in revenue due to the pandemic, further undermining its already over-indebtedness. All in all, our concerns about the future of the SA economy remain in place. The road ahead looks dire, to say the least, and we are not even talking about all the bankrupt State-owned Enterprise (which with the exception of SAA were largely ignored in the MTBPS), the systemically corrupt governing machine, the broken state delivery ability, and many other problematic areas of government.

Moving on from the MTBPS, the SA Reserve Bank (SARB) left interest rates unchanged at 3.5% at their November meeting. Three members of the Monetary Policy Committee (MPC) voted to keep rates unchanged while two members voted for a 0.25% rate cut. The SARB revised its 2020 inflation rate forecast to 3.2% and for 2021 to 3.9%. Reasons given for the inflation revisions included local food inflation, the temporary reduction in medical insurance price inflation, and a low pass-through from currency movements. The SARB also sees potential inflationary risks arising from exchange rate risks due to heightened fiscal risks, and electricity and other administered prices.

Finally, global credit rating agencies Fitch and Moody's have just downgraded South Africa's credit rating further which, given the current state of the economy as well as its prospects, is hardly surprising. The downgrade passed as a complete non-event.

A photo from "The Iceberg II" series

Whales off Greenland iceberg



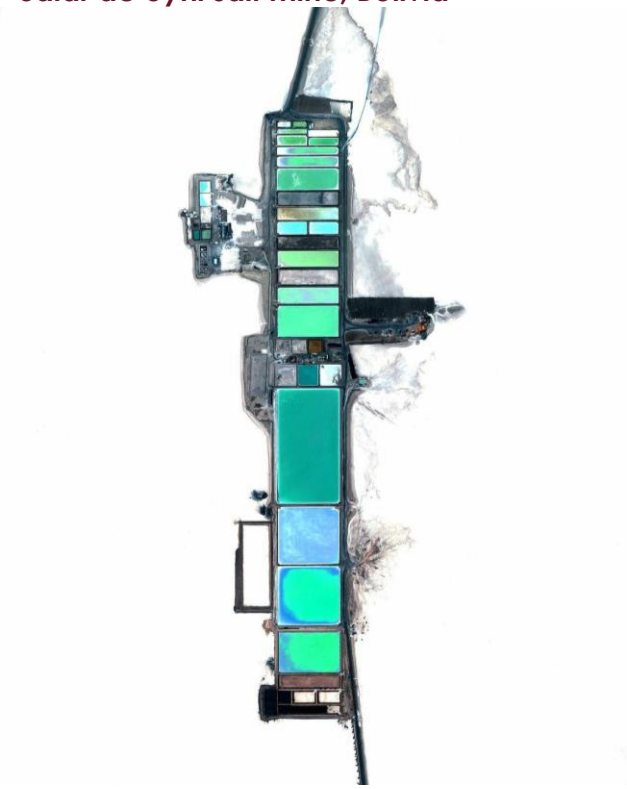
Source: @ tomhegen.de

- *The US economy*: We have seen significant recoveries across most economies, as they bounce back from the second quarter (Q2) lockdowns. The data is impressive, but it must be seen in the context of the unprecedented losses experienced during Q2, remembering always that a 50% gain after a 50% decline doesn't exactly leave one at the initial starting point! Bear that in mind when reviewing the large economic "bounces" during Q3 across the world.

  The US economy expanded at a quarter-on-quarter, annualized rate of 33.1% during Q3, following its 31.4% contraction during Q2. Durable and non-durable goods consumption rose 5.2% and 4.1% respectively, while services consumption

(services were particularly hard hit during the lockdowns) rose 16.1%. This recovery occurred in the light of the $2.59tn fiscal support from government, equivalent to 11.8% of US GDP. The 7.4% un-annualised Q3 growth still leaves US GDP 3.5% below pre-Covid (Q4 2019) levels.

Salar de Uyni salt mine, Bolivia



Source: @overview

Of course, economic growth data is old and backward looking, even more so now that the second wave of Covid infections in forcing new lockdowns in so many parts of the US. So while the data is interesting, it is of limited use. Of greater relevance are the ISM (PMI) data, which showed that the economy continued to expand and recover in September and October, but once again it doesn't include any of the data since the "second wave" gained traction across the States. October's ISM Manufacturing reading reached a 2-year high of 59.3 while the ISM Non-manufacturing (services) reading declined slightly to 56.6. The US labour market continues to recover slowly, with the unemployment rate falling to 6.9% in October. However, the number of long-term (jobless for 27 weeks or more) unemployed people rose by 1.5m to 3.56m, the highest level since early 2014. Retail sales rose 0.3% in October, bringing the annual rate to 5.7%, which is probably more symptomatic of government support than real underlying consumer strength. Industrial production rose 1.1%.

- *Developed economies*: In Japan, the Q2 economic slowdown was lowered to 8.2% quarter-on-quarter, while the Q3 rebound came in at 5.0%. Private consumption and export growth contributed to higher output but business spending continued to contract. Full year 2020 economic growth is still forecast at -5.0% with a more modest recovery of about 2.5% in 2021. In the UK, Q3 showed an expansion of 15.5% after the contraction of 19.8% during Q2. This leaves the UK economy around 10% smaller than pre-Covid levels – of course the uncertainty around Brexit hasn't done it any favours and many stringent lockdowns are being imposed at the time of writing, so expect another sharp contraction, in excess of 10%, in Q4 and for 2020 as a whole. To put the UK economy's dire position into perspective, forecasts show that the economy will still not have regained its pre-crisis level by the end of 2022. Emergency spending of more than £200bn so far and the Bank of England's expanded quantitative easing level of £895bn will have to be ramped up again if the UK gets

hit by a no-deal at the end of the year. Turning to the Eurozone, that economy rose 12.6% in Q3, bringing the year-on-year contraction to 4.4%. Italy's economy rose 16.1%, France 18.2% and Germany 8.2%. As in many other countries though, the better-than-expected data was over-shadowed by news of further lockdowns and rising infections. Eurozone inflation fell at an annual rate of 0.3% in October, and the European Central Bank expects the rate of disinflation to increase. Eurozone retail sales fell 2.0% in September but are still 2.2% higher on the year. Moving south, the Reserve Bank of Australia (RBA) reduced its official interest rate to 0.1% although at the same time tried to dampen expectations of negative interest rates in the future.

Greenland iceberg

Source: @tomhegen.de

- *Emerging economies:* The Philippines economy expanded at a quarterly rate of 8.0% during Q3 but is still 11.5% lower than a year ago. During Q2 the economy shrank 14.9%, taking its annual contraction to 16.9%. The Philippine central bank cut rates to a record low of 2.0%. Wracked by the economic recession, together with a string of natural disasters which have caused massive flooding and agricultural damage, the unemployment rate remains high at 10.0% and the country continues to face significant challenges. The Bank of Indonesia (BI) cut its rates for the first time in four months to 3.75% as imports declined at an annual rate of 26.9%, due largely to very weak domestic demand. South Korea's economy grew at 1.9% quarter-on-quarter during Q3, after having declined 3.2% in Q2 and 1.3% in Q1. The economy contracted at an annual rate of 1.3% to end-September, an improvement on the 2.7% contraction to end-June.

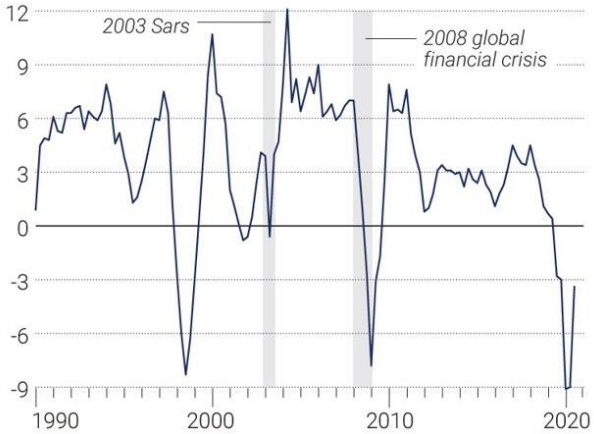
Turkey was in the news again, for all the "wrong" reasons as is so often the case. Turkey's October annual inflation rate was 11.9%, up from September's 11.75%. Turkey's economy is crumbling and their central bank was until a few days ago run by a member of President Erdogan's family. Under his leadership, the central bank refused to implement conventional monetary policy, the result of which was massive depreciation in the lira and sharply declining foreign exchange reserves. The lira rose to 8.53 to the dollar at one stage, although at the time of writing it had returned to a level of 7.63. Erdogan has repeatedly referred to what he calls the "the devil's triangle of interest and

exchange rates and inflation" but the un-conventional approach has not benefitted the economy at all. Consequently few were surprized when the central bank governor resigned and was replaced by a more competent and independent governor, who immediately hiked interest rates by 4.25% to 15.0% and promised to ensure that "tight monetary conditions remain in place until a permanent fall in inflation was achieved". China's annual inflation rate came in at 0.5% in October, while its producer price inflation was -2.1%. Exports rose at an annual rate of 11.4%, the highest rate of growth since March 2019, while imports great at an annual rate of 4.7%. The Hong Kong economy shrank at an annual rate of 3.5% during Q3, having now spent five consecutive quarters in recession – refer to Chart 3. The Q3 contraction was an improvement on the 9.1% and 9.0% annual contraction during Q1 and Q2 respectively. During Q3 private consumption declined by 7.7%, better than Q2's 14.2% decline, but government consumption grew at only 6.4%, less than its 9.7% increase during Q2. The Hong Kong government expects the economy to decline between 6% and 8% during 2020.

Finally, the Mexican economy rose 12.0% quarter-on-quarter during Q3, bringing the annual decline to 8.6%. The Mexican government has been slow to roll out any stimulus, having announced fiscal measures equivalent to only 1.2% of GDP, well below other peer countries who have on average spent between 8% and 12% of GDP on fiscal stimulus packages.

Chart 3: Hong Kong economic growth

Annual % change



Source: Hong Kong government

Obituary: Quino (1932 - 2020)

This is probably the first time you have ever read about, or heard of Quino – or Mafalda for that matter. Well, pardon my ignorance, but welcome to the club. However, when I read the Financial Times' obituary, I was not only intrigued by it, but his poignant contribution to the social debate seemed so relevant to South Africa, he could well have been a South African, writing for the prevailing times. I hope you find it interesting.

Source: FT.com

The day after the 1966 military coup in Argentina, a single picture of a forlorn girl with bushy black hair appeared in the newspaper El Mundo. The sparse comic strip was accompanied by the words: "So, what they taught me at school . . . "

Fortunately, that famously unfinished sentence — attentive readers understood its veiled criticism — went unnoticed by the generals. So did other irreverent observations by that enfant terrible Mafalda, a cartoon character who is an icon of Hispanic culture, as adored today as half a century ago. Her creator, Joaquín Salvador Lavado Tejón, better known as Quino, who has died at the age of 88, captured the spirit of a generation roiled by regional political and economic turmoil.

Today, the deliciously naughty six-year-old, who hated soup but loved The Beatles, remains as famous as Argentina's other beloved heroine, Evita Peron. Promoted by intellectual giants such as Umberto Eco, Julio Cortázar and Eric Hobsbawm, Latin America's best-selling and most widely-translated comic strip is "a phenomenon that exceeds anything to do with graphic humour," Quino's editor, Daniel Divinsky, said.

Source: thebogotapost.com

Influenced by Charles Schulz's North American comic strip Peanuts, Mafalda's precocious character combined childish innocence with adult themes in a way that transcended class, politics and age. She was ahead of her time as a feminist and an ecologist, and was an acerbic critic of consumerism, organized religion — and, especially, politics. One of her friends, Libertad, or Freedom, was drawn especially short "because freedom always seems small", as Quino once said. As for her famous dislike of soup: "It was really an allegory about . . . the governments one had to swallow daily, especially in the dictatorship era in Latin America." Mafalda's pet tortoise was meanwhile called Bureaucracy. When asked why, she replied that she needed more time to answer, but could not say how much.

"What makes him so great is his enormous critical capacity and his sharp observation on one hand, and his tenderness on the other. In Quino you have a wise old man and a 10-year-old child all in one," said Argentine cartoonist Juan Matías "Tute" Loiseau, describing him as "the father of modern graphic humour in Latin America".

Enigmatic and in later years a recluse, Quino was born in 1932 to Andalucían Republican immigrants in Guaymallén, a small town in the Andean winemaking province of Mendoza. His working-class parents died while he was a teenager, and he moved to Buenos Aires in 1950, dreaming of becoming a cartoonist — his uncle was an illustrator.

In 1960 he married Alicia Colombo, a chemist who became his agent, and Mafalda was conceived three years later for a domestic appliance advert that was never published. Her rebellious character was born as a comic strip in 1964. When the next military junta seized power in 1976, Quino fled to Milan, only returning when the dictatorship ended in 1983. "Had I kept drawing her, they would have shot me," Quino once recalled.

Mafalda allowed Quino to make uniquely Argentine jokes about economics that remain alarmingly relevant today. In one strip, Argentina's historical penchant for printing money is lampooned by a friend of Mafalda who expresses surprise at how "nicely ironed" the banknotes are. In another strip, when Mafalda hears about price controls, she quips: "And how much does good sense cost?"

"Quino said with humour what nobody dared to at the time, and in such a way that it could not be censored," said Cristina Fernández de Kirchner in 2014 — although Quino once said Mafalda "would not have liked" the former leftist Argentine president, who also printed money and imposed price controls while in power, because of her arrogance and pride. Sadly, Mafalda's great hope for world peace — she dreamt of becoming a UN translator — was never realized. Indeed, when Mr Divinsky last saw Quino in January, the illustrator told him he "was really worried because he thought that his worst fears were becoming reality".

Quino, whose wife died in 2017, divided his time between Buenos Aires, Madrid, Milan, Paris and Mendoza, and is survived by five nephews, one niece and, of course, his cartoons. Translated into 26 languages, including different dialects of Chinese, English was the last major language to hold out against Mafalda's charms. According to Mr Divinsky, that was because a US book agent complained she was "too sophisticated for North American children".

Articles worthy of sharing …

Ahead of the US election, the media and our research providers were full of fascinating and thought-provoking articles about the future, in particular after the US election. It is sometimes worthwhile revisiting these after the event, as they tend to carry more weight and insight – at least in some cases – than before the election outcome.

Even as the outcome of the US election remains contested at the time of writing, the following articles are worth bringing to your attention.

Polar vortex off Chicago, January 2019

Source: @europeanspaceagency

Irrespective … China wins

On 28 October *Julius Bär Chief Investment Officer Yves Bonzon* penned his weekly letter, which included the following extract:

"If there is one subject on which there is bipartisan consensus in Washington, it is the required stance in the face of China's rise to power. Whatever happens on the morning of 4 November, the US administration will maintain an aggressive attitude towards Beijing and its desire

to take its rightful place on the world stage. The form would improve in the event of a Biden administration, but the substance will remain unchanged.

"The same logic applies to the strategy of the Chinese under the leadership of President Xi Jinping. No change is therefore in sight regarding our secular outlook forecast of a bipolar world with a Chinese economic and financial cycle uncorrelated to its US counterpart and two technological ecosystems that might be unable to communicate with each other. The more time passes, the more reassured we are about the merits of our strategic allocations to renminbi bonds and Chinese equities.

Bonneville Salt flats, Utah, USA

Do you see the kayakers and paddle boarders?

Source: @mattcnewey

"The Chinese economy is poised to be 10% larger in 2021 compared to 2019, while other advanced economies will still operate below their 2019 GDP levels. Economic and financial reforms follow each other, and Beijing's recent signals for the 14th five-year plan point to an acceleration of the transition towards the internationalisation of the renminbi, paving the way for its future status as a reserve currency. For those of our readers who are rightly cautious about the topic of Chinese assets becoming a core asset class, we recommend the excellent article by Bridgewater founder Ray Dalio in the 23 October edition of the Financial Times. Investing successfully also means overcoming our preconceived ideas".

Don't be blind to China's rise in a changing world

Right on cue then, here is Ray Dalio's article. Ray Dalio is founder, co-chairman and co-chief investment officer of Bridgewater Associates. Incidentally, I can recommend his online series *The Changing World Order* to you which you can access by clicking here. In his article *Don't be blind to China's rise in a changing world,* he writes as follows:

"For as long as I can remember, people have said that China cannot succeed. Communism doesn't work. Authoritarianism doesn't work. The Chinese aren't creative. They have a big problem with bad debts and property speculation.

"Yet every day we see China succeeding in exceptional ways. It has achieved some of the world's lowest Covid-19 case rates. Over the past year, its economy grew at almost 5%, without monetising debt, while all major economies contracted. China produces more than it consumes and runs a balance of payments surplus, unlike the US and many western nations.

This year nearly half the world's initial public offerings will be in China, including Ant Financial's $30bn listing, the world's biggest ever. Even Tesla's best-selling Model 3 car may soon be made entirely in China.

"The world order is changing, yet many are missing this because of a persistent anti-China bias. China's extraordinary performance isn't new. In fact, apart from the 1839-1949 "Century of humiliation", it has historically been one of the world's most powerful countries and cultures. Just over the past four decades its economic changes have been remarkable. Whatever criticisms you may have about Chinese "state capitalism", you cannot say it hasn't worked, even if you strongly disagree with how Beijing has done it.

"When I first visited China 36 years ago, I would give $10 pocket calculators to high-ranking officials. They thought they were miracle devices. Now China rivals the US in advanced technologies and will probably take the lead in five years. Since 1984, per capita incomes have risen more than 30 times, life expectancy has increased by a decade and poverty rates have fallen nearly to zero.

"In 1990, China's first stock market was launched, designed by seven young patriots who I knew. Since then, it has become the second largest in the world. All this is to say that China's rise has giant political, economic and investment implications. Politically, China has become a major issue for both parties in the US, which fears its rise, spreading global influence, and rejects its authoritarian model and treatment of minorities such as the Uighur Muslims in Xinjiang. China's rejoinder is that a strong hand is needed to maintain order, what happens inside its borders is its business, and the US has its own human rights problems. Its sovereignty over Taiwan, Hong Kong and other areas are also big issues that are hotly disputed. Nobody knows how these tensions will pan out, but they will affect us all.

Polar bears adrift

Source: @PaulNicklen

"Meanwhile, China's economy is roughly the same size as the US's and expanding at a faster pace — so time is on China's side. It has a growing population of well-educated people, with around a third of the world's science and technology university majors, three times the US share. It also produces and collects vastly more data to process with artificial intelligence. For many in the west, this has a dark side in terms of state surveillance. But for many Chinese it reinforces positive social norms while also promising vast efficiencies. One way to look at China's relative power is that, with four times the US population, when its per capita income reaches half the US's in about 25 years, its economy will be twice as large.

"Last, there are the investment implications. As a global macro investor, I think a lot about how much I should invest where, looking at fundamentals and how others are positioned. China's fundamentals are strong, its assets relatively attractively priced, and the world is

underweight Chinese stocks and bonds. These currently account for 3% or less of foreign portfolio holdings; a neutral weighting would be closer to 15%. This discrepancy is at least in part due to anti-Chinese bias. I think it is about to change. Chinese markets are opening up to foreigners, who can now access at least 60% of them compared with 1% in 2015. Benchmark weights in major indices are rising. As a result, I expect China to enjoy favourable capital inflows that will support the currency, already at a two-year high, and financial markets too. All this argues for a China overweight in my portfolio. Of course things can go wrong in any country. Beijing may not stay its current course of economic reform, though I doubt that will happen. The US and China are also competing fiercely over trade, technology, geopolitics, capital markets and military power. No one can know how bad these wars will be, which country will win, or how. That is why I diversify and allocate money to both countries.

"In the long run, timeless and universal truths determine why countries succeed or fail. In brief, empires rise when they are productive, financially sound, earn more than they spend, and increase assets faster than their liabilities. This tends to happen when their people are well educated, work hard and behave civilly. Objectively compare China with the US on these measures, as I chronicle in an ongoing study, and the fundamentals clearly favour China. Prejudice and bias always blind people to opportunity.

"So, if you have been a China sceptic for reasons that don't square with what is happening there, I suggest you clear your mind. Likewise for events in the US and its place in the changing world. The eve of the US election is a good time to reflect on both".

Artic glaciers

Source: @PaulNicklen

China leads again

The last of the articles I would like to share is by Stephen Roach. Roach is a faculty member at Yale University and former Chairman of Morgan Stanley Asia. He is the author of *Unbalanced: The Co-dependency of America and China*. The article was written on 26 October.

"US President Donald Trump wears his recent experience with COVID-19 infection as some perverse badge of courage, rather than as a warning of what may lie ahead. And the adverse economic consequences of his administration's approach to the pandemic could not contrast more sharply with the robust recovery in China.

"Just as China led the world in economic recovery in the aftermath of the global financial crisis of 2008, it is playing a similar role today. Its post-COVID rebound is gathering momentum amid a developed world that remains on shaky ground. Unfortunately, this is a bitter pill for many to swallow – especially in the United States, where demonization of China has reached epic proportions.

Polar bear in Baffin, Nunavut, Canada

Source: @florian_ledoux_photographer

"The two crises are, of course, different. Wall Street was ground zero for the 2008 crisis, while the COVID-19 pandemic was spawned in the wet markets of Wuhan. But in both cases, China's crisis-response strategy was more effective than that deployed by the US. In the five years following the onset of the 2008 crisis, annual real GDP growth in China averaged 8.6% (on a purchasing power parity basis). While that was slower than the blistering (and unsustainable) 11.6% average pace of the five previous years, it was four times the US economy's anaemic 2.1% average annual growth over the post-crisis 2010-14 period.

"China's pandemic response hints at a comparable outcome in the years ahead. The GDP report for the third quarter of 2020 suggests a rapid return to the pre-COVID trend. The 4.9% year-on-year figure for real GDP growth does not convey a full sense of the self-sustaining recovery that is now emerging in China. Measuring economic growth on a sequential quarterly basis and converting those comparisons to annual rates – the preferred construct of US statisticians and policymakers – provides a much cleaner sense of real-time shifts in the underlying momentum of any economy. On that basis, China's real GDP rose at an 11% sequential annual rate in the third quarter, following a 55% post-lockdown surge in the second quarter.

"The comparison with the US is noteworthy. Both economies experienced comparable contractions during their respective lockdowns, which came one quarter later for the US. China's 33.8% sequential (annualized) plunge in the first quarter was almost identical to the 31.2% US contraction in the second quarter. Based on incoming high-frequency (monthly) data, the so-called *GDPNow* estimate of the Atlanta Federal Reserve puts third-quarter sequential real GDP growth in the US at around 35%. While that is a welcome and marked turnaround from the record decline during the lockdown, it is about 20 percentage points short of China's post-lockdown rebound and still leaves the US economy about 3% below its peak of late 2019.

"Post-lockdown rebounds are not the real story, however. They are akin to the snapback of a stretched rubber band – or in statistical terms, the arithmetical result of restarting an economy that has just been subjected to an unprecedented sudden stop. The true test comes after the snapback, and that's where China's strategy has its greatest advantage.

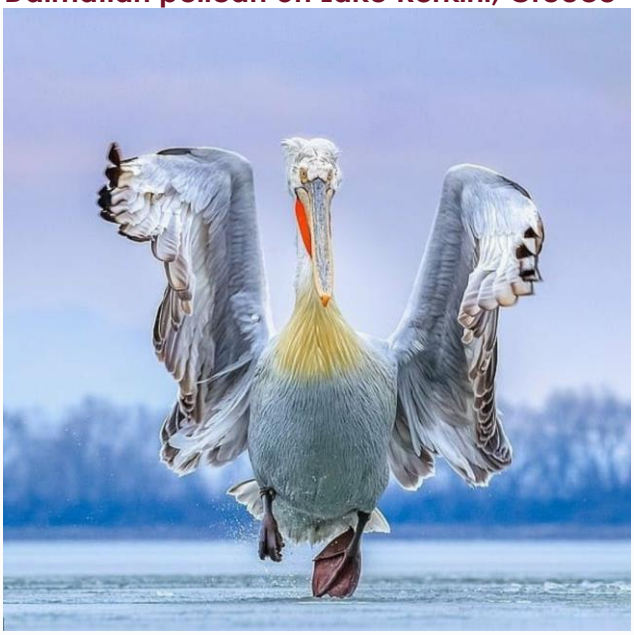
"China's response to COVID-19 borrowed a page from its 2008 playbook, when it ring-fenced its financial markets from the toxic fallout of the subprime crisis. The objective back then was crystal clear from the start: address the source of the shock itself, rather than the collateral damage the shock caused. The $596.4bn fiscal stimulus of 2008/9 worked only because China had taken strong actions to insulate its markets from a virulent financial contagion.

"China's approach today is similar: first, insulate its citizens from a virulent pathogenic contagion with draconian public-health measures aimed at containing and mitigating the spread of the disease, and then – and only then – make judicious use of monetary and fiscal policy to reinforce the post-lockdown snapback. This is very different from the approach taken in the US, where the post-lockdown debate is more about using monetary and fiscal policies as front-line instruments of economic liberation, rather than relying on disciplined public-health measures aimed at virus containment.

"This underscores the sharp contrast between China's COVID-first strategy and the America-first approach of US President Donald Trump's administration. In China, unlike the US, there is no political and public resistance to masks, social distancing, and aggressive testing as requisite norms of the COVID-19 era. Meanwhile, the US is in the midst of its third serious wave of infection while China continues to exercise prompt and effective control over new outbreaks. Earlier this autumn, for example, some 9m citizens in Qingdao were tested in just five days after a relatively small outbreak affecting fewer than 20 residents. By contrast, Trump wears his own experience with COVID-19 infection as some perverse badge of courage, rather than as a warning of what may lie ahead.

"In this context, China's impressive GDP results in the third quarter stand in even sharper contrast with the precarious post-lockdown state of the US economy. Ongoing distress in the US labour market (unemployment claims remained above 800 000 on a four-week moving average through mid-October and the 7.9% national unemployment rate in September was still more than double its pre-pandemic 3.5% level) leaves America's consumer-led economy vulnerable to a setback. The confluence of a new COVID-19 wave with the on-again, off-again political debate over another fiscal relief package has effectively neutralized the animal spirits that have long powered US economic recoveries.

Dalmatian pelican on Lake Kerkini, Greece



Source: @caronsteelephotography

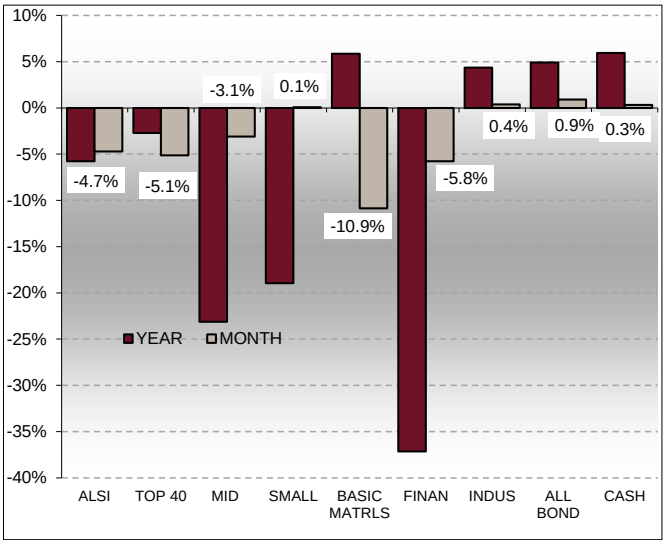
"While China's 11.2% sequential (annualized) growth in the third quarter of this year builds effectively on its post-lockdown snapback, some lingering signs of weakness are evident in several key segments of consumer services – namely travel, leisure, and entertainment. Human nature is the same everywhere, with fear and caution enduring, even in countries where aggressive containment measures are working. For those unwilling to focus on containment, like the US, the long shadow of COVID-19 speaks volumes to the ever-present perils of a double-dip recession. That is exactly what has happened in the aftermath of eight of the last 11 US recessions. The contrast with China's self-sustaining recovery couldn't be more striking".

"To achieve great things, two things are needed; a plan, and not quite enough time."
- Leonard Bernstein

October in perspective – local markets

Turning to the South African investment markets, weak global markets, the firm rand, and soft precious metal prices weighed on equity market returns. The Basic Material index lost 10.9% and the Financial index 5.8% although the Industrial index eked out a positive return of 0.4%. This all contributed to a *decline* of 4.7% in the All Share index, bringing its year-to-date return to -7.1% and its annual return to -5.8%. Whereas the Top40 (Large cap) index lost 5.1%, the Mid cap index lost "only" 3.1%. The Small cap index actually posted a positive return of 0.1%. The All Bond index rose 0.9%. In line with other emerging market currencies which were firm during October, the rand rose 2.7% relative to the dollar.

Chart 4: Local returns to 31 Oct 2020



We hope the period following the US election will bring calmer markets, but we know Donald Trump to be a bad loser, so expect that the recent period of uncertainty and volatility may not quite be over. That said, we remain positive on global equity markets and still prefer them over global bond markets. We are watching the second wave of lockdowns closely and hope that the economic effects they inevitably bring will not be as severe as the first time around.

Locally, the recent Medium Term Budget Policy Statement (MTBPS) was truly uninspiring. We remain of the view that government's talk is exactly that – talk, and no action. The country's finances are in a mess and deteriorating by the day, and the State-owned Enterprises are virtually all bankrupt. Government's recent decision to waste another R10bn on South African Airways, having plundered the Education and Policing budgets to secure the money, epitomizes their misdirected priorities, and lack of understanding of the devastating effects of their policies. We remain of the view that there is little hope for the country's economy, which is now well down the road to "Destination Zimbabwe", although it will take a few years to get there.

Artic wonder

Source: @xkarenhuynh

For the record

Table 1 lists the latest returns of the mutual and retirement funds under Maestro's care. Returns include income and are presented *after* fees have been charged. Fund Summaries for each respective fund listed in the table, as well as all the historic returns, are available on our website.

"To achieve great things, two things are needed; a plan, and not quite enough time."
- Leonard Bernstein

Table 1: The returns of funds in Maestro's care

	Period ended	Month	Year to date	Year
Maestro Equity Prescient Fund	**Oct**	**-3.5%**	**0.0%**	**-1.3%**
JSE All Share Index	*Oct*	*-4.7%*	*-7.1%*	*-5.8%*
Morningstar sector ave	*Oct*	*-3.5%*	*-10.1%*	*-9.0%*
Maestro Growth Fund	**Oct**	**-3.5%**	**8.1%**	**7.0%**
Fund Benchmark	*Oct*	*-3.1%*	*-1.2%*	*-0.2%*
Morningstar sector ave	*Oct*	*-2.8%*	*-3.2%*	*-2.8%*
Maestro Balanced Fund	**Oct**	**-3.2%**	**7.3%**	**6.6%**
Fund Benchmark	*Oct*	*-2.6%*	*0.0%*	*1.0%*
Morningstar sector ave	*Oct*	*-2.1%*	*-1.6%*	*-1.2%*
Maestro Cautious Fund	**Oct**	**-0.9%**	**3.6%**	**4.4%**
Fund Benchmark	*Oct*	*--1.0%*	*1.0%*	*2.6%*
Morningstar sector ave	*Oct*	*-1.3%*	*1.3%*	*0.4%*
Maestro Global Balanced Fund	**Oct**	**-6.1%**	**22.1%**	**20.4%**
Benchmark	*Oct*	*-4.4%*	*17.4%*	*12.6%*
*Sector average **	*Oct*	*-4.1%*	*12.9%*	*9.6%*

* Morningstar Global Multi Asset Flexible Category

Notwithstanding the returns listed in Table 1, we thought it would be appropriate to list our longer-term returns for our investment solutions, shown in the following tables. All returns are for periods to 31 October, and are taken from Morningstar's monthly unit trust survey. Returns are shown on a net basis i.e. after all fees have been deducted.

Table 2: The Maestro Equity Prescient Fund

Morningstar (ASISA) South Africa Equity General - October 2020						
	3 mths	6 mths	1 year	3 years	5 years	10 years
Maestro Equity Prescient Fund	***-3.0%***	***5.4%***	***-1.3%***	***-5.5%***	***-3.5%***	***4.7%***
Maestro Equity Fund benchmark	-4.8%	2.5%	-4.4%	-2.2%	1.5%	10.6%
SA Peer Group Average	-5.0%	3.0%	-9.0%	-3.9%	-0.3%	6.3%
Maestro position within Group	29	29	24	102	98	49
Number of participants	169	167	163	146	113	62
Quartile	1st	1st	1st	3rd	4th	4th

Table 3: The Maestro Growth Fund

Morningstar (ASISA) South Africa Multi-Asset High Equity - October 2020						
	3 mths	6 mths	1 year	3 years	5 years	10 years
Maestro Growth Fund	***-4.0%***	***2.1%***	***7.0%***	***2.2%***	***2.4%***	***7.2%***
Maestro Growth Fund benchmark	-4.0%	3.8%	-0.2%	2.9%	4.8%	9.1%
SA Peer Group Average	-3.5%	2.1%	-2.8%	0.1%	2.5%	7.4%
Maestro position within Group	129	101	7	23	69	30
Number of participants	202	201	194	133	126	54
Quartile	3rd	3rd	1st	1st	3rd	3rd

Table 4: The Maestro Balanced Fund

Morningstar (ASISA) South Africa Multi-Asset Medium Equity - October 2020						
	3 mths	6 mths	1 year	3 years	5 years	10 years
Maestro Balanced Fund	***-3.7%***	***2.1%***	***6.6%***	***1.5%***	***2.2%***	***6.8%***
Maestro Balanced Fund benchmark	-3.2%	3.7%	1.0%	3.7%	5.3%	8.8%
SA Peer Group Average	-2.7%	2.2%	-1.2%	1.4%	3.1%	7.0%
Maestro position within Group	77	51	1	43	55	20
Number of participants	96	95	94	83	66	35
Quartile	4th	3rd	1st	3rd	4th	3rd

Table 5: The Maestro Cautious Fund

Morningstar (ASISA) South African Multi-Asset Low Equity - October 2020						
	3 mths	6 mths	1 year	3 years	5 years	10 years
Maestro Cautious Fund	***-1.0%***	***1.3%***	***4.4%***	***4.3%***	***4.1%***	***7.6%***
Maestro Cautious Fund benchmark	-1.0%	4.7%	2.6%	5.2%	6.0%	7.7%
SA Peer Group Average	-1.4%	2.3%	0.4%	2.9%	4.3%	7.1%
Maestro position within Group	54	129	22	13	66	19
Number of participants	158	157	154	136	103	50
Quartile	2nd	4th	1st	1st	3rd	2nd

Table 6: Maestro Global Balanced Fund

Morningstar (ASISA) Global Multi-Asset Flexible - October 2020						
	3 mths	6 mths	1 Year	3 Years	5 Years	10 years
Maestro Global Balanced Fund	***-8.3%***	***-0.7%***	***20.4%***	***N/A****	***N/A****	***N/A****
Global Balanced Fund benchmark	-5.0%	-3.8%	12.6%	9.4%	8.8%	13.8%
SA Peer Group Average	-4.7%	-3.0%	9.6%	11.0%	7.7%	12.4%
Maestro position within Group	34	11	4	N/A	N/A	N/A
Number of participants	36	35	32	25	19	11
Quartile	4th	1st	1st	N/A	N/A	N/A

Table 7: Central Park Global Balanced Fund

Morningstar USD Moderate Allocation - October 2020						
	1 Year	3 Years	5 Years	7 years	10 years	15 years
Central Park Global Balanced Fund ($)	***13.4%***	***5.6%***	***5.7%***	***3.7%***	***2.1%***	***3.0%***
Central Park Glbl Balanced Fund benchmark	4.4%	4.5%	5.3%	4.3%	4.6%	4.4%
Global Sector Average	1.2%	1.9%	3.4%	2.6%	3.0%	N/A

Chinese bonds revisited

The advent of negative interest rates on most developed market bonds is an unattractive environment for investors. Consequently we have avoided investing in bonds in our global portfolios for some time now. It has been a frustrating time, having had one of the major means of diversification (away from equity markets) removed.

In recent weeks though we have begun investing in Chinese bonds though, as a source of income as well as a means of diversifying some of the equity market risk (although make no mistake, we are still positive on global equity markets). We thought we'd share some of our thinking with you in this regard.

"To achieve great things, two things are needed; a plan, and not quite enough time."
- Leonard Bernstein

The attraction of Chinese bonds is not only the level of income we secure in the process – 10-year Chinese bonds are currently trading on a yield of 3.33% compared to the US 10-year yield of 0.88% - but we are also of the view that the Chinese currency, the yuan (CNY), is likely to continue to strengthen in the years to come – it has already risen 8.5% against the dollar so far this year – refer to Chart 5 below.

Chart 5: The Chinese yuan in dollar terms

Source: FT.com

We are not alone in this view; one could even argue that we are "a bit late on this trade" but we think this theme will play out over many years and so are comfortable taking this position even though we would have benefitted had we taken it earlier.

On 23 October Julius Bär had the following to say: "The CNY had a strong rally earlier this week, up 1% in a week with the currency touching 6.65 per dollar on Wednesday, the strongest since July 2018. CNY strength is driven by strong inflows into China's onshore bond market. Overseas investors have bought more than $100bn worth of debt in the interbank market this year, roughly ten times the planned quota increase.

"Chinese government bonds' (CGB) strength is underpinned by China's strong economic and FTSE World Government Bond Index inclusion starting next year and its attractive interest rate differential of above 2.40% above the US Treasury when the rest of the developed world debt is paying investors nearly nothing for risk-free debt.

"Besides yield, one important argument for CGB is China's interest rate policy, that is both *neutral* (no excessive easing needed with the economy on a firmer footing) and *independent* (independent from the Federal Reserve and other major central banks). It is quite clear by now that the rest of the major central banks are focusing on containing the effects of the pandemic, which invariably leads to interest rate cuts to zero with saving jobs the priority. Under such an economic backdrop, investors are getting lower compensation yet higher risk from a deteriorating economic outlook. In contrast, having contained the coronavirus early, China's monetary policy has moved on to the next leg where it is doing less heavy lifting with a focus on fiscal spending. While staying accommodative, the central bank's focus is on inflation and curbing excessive speculation, which means the risk of an interest rate cut is not high.

"Investors investing in CGB are getting higher compensation amid an improving economic backdrop. The CNY has gained nearly 7% since the end of May. Large inflows before the index inclusion are likely to give China the confidence to allow more overseas investments in the coming months."

As a matter of interest, an indication of the extent to which the CNY may still "internationalize" in the coming years – and it will be a long and slow process – the CNY's share in global payments remains low. As of Q1 2020, the CNY accounted for 2.0% of global central banks' reserves, behind the dollar (62%), euro (20%), yen (6%) and sterling (4%).

Red sail

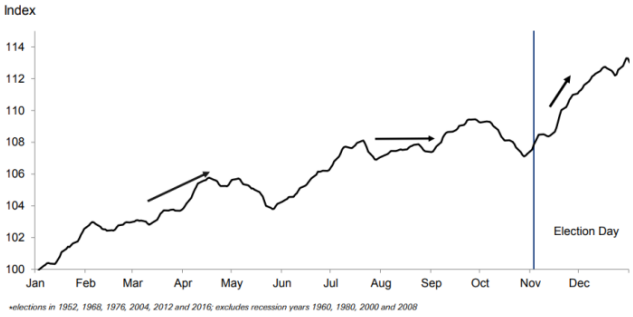
Source: @manikgroverphotography

Charts of the month

Seasonality in the market place – US elections

We touch on the matter of market seasonality in last month's *Intermezzo* but think it is appropriate to revisit it again briefly. Last month we showed how consistent seasonal patterns were in the US equity markets. More specifically, US markets are also relatively consistent in their movements when it comes to US Presidential elections, as seen in Chart 6. That was one of the reasons behind us increasing the equity weighting in Central Park Global Balanced Fund during the last week of October. In closely contested elections, such as the recent one, it rarely matters who wins – markets have historically risen regardless of who wins.

Chart 6: Close elections bode well for markets



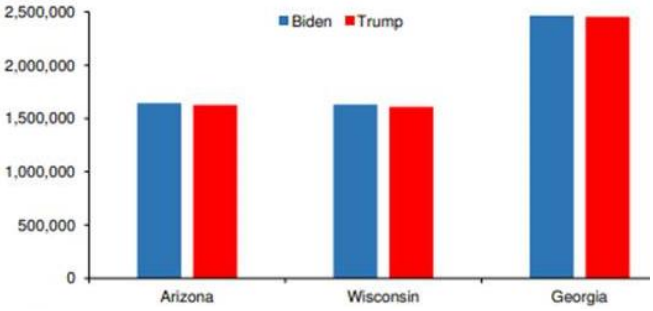
Source: Deutsche Bank

How close is close?

At the time of writing this, the US election results have not been officially finalized yet, but it is clear by now that Biden will be the next US President (I can hear millions of people around the world breathing a collective sigh of relief!) Just how close was the election result? *Deutsche Bank's Jim Reid* provided the following chart; it shows just how close the result actually was. No wonder The Donald is still sulking!!

Reid pointed out that if 25 000 voters i.e. 0.016% of all national voters had switched from Biden to Trump in three States (Arizona, Wisconsin, and Georgia), then Trump would likely have been on a path to retaining the Presidency! That's close!!

Chart 7: Close has never been this close



Source: Deutsche Bank

Ant Financial – now you see it, now you don't

I prepared a long section on Alibaba's financial technology (fintech) subsidiary, Ant Financial, for inclusion in this letter. However, much to my and millions of others' disappointment, four days before the listing, the company called off their Initial Public Offering (IPO). It will go down as one of the most dramatic times in economic history: the largest IPO of all times, an opportunity for China to showcase its world-leading technological prowess – especially in light of the tough stance the Trump administration had taken against it – and a perfect opportunity for China to take up its role as a global leader in the

"To achieve great things, two things are needed; a plan, and not quite enough time."
- Leonard Bernstein

arena of finance and technology (fintech) – the IPO had all the makings of a great moment in history. But just days before the listing, four regulators met with two of Ant Financial's executives and Alibaba founder Jack Ma, and hours later Ant called off the listing. It doesn't come more dramatic than that.

There is much to write about the drama surrounding the listing, and the reasons why it was called off, but I will leave that for another time. However, in the light of the enormity of the scale of the planned IPO, I thought I'd share a few aspects of the world's largest IPO that never happened:

- As a business, at the end of September Ant Financial had 731m monthly active users.
- The planned raising of $34.5bn would have been the world's largest ever IPO – refer to Chart 8. Ant was offering only 11% of its shares initially.
- The expected size of Ant Financial, at the offer price, was between $350bn and $450bn. To place that in perspective, the largest US bank, JP Morgan, has a market cap of $359bn. The entire Nigerian or Austrian economy is similar in size i.e. $350bn. JP Morgan traces its roots back to 1799 in New York – Ant is only 16 years old.
- At its planned IPO price Ant would be valued at 48 times its trailing 12-month net profit. PayPal, with a market cap (size) of $238bn, trades at 98 times its trailing 12-month net profits. Tencent, whose subsidiary WeChat competes with Ant's AliPay, trades at 51 times.
- Ant Financial was to be listed in Hong Kong and Shanghai. The Hong Kong offer was 389 times over-subscribed and the Shanghai offer 870 times over-subscribed. Together, retail investors deposited no less than $3tn (that's three trillion US dollars) with banks ahead of the planned listing, caused severe money supply distortions in Hong Kong capital markets.

Chart 8: The biggest IPOs of all time ($bn)

Global IPOs with most money raised

Source: statista

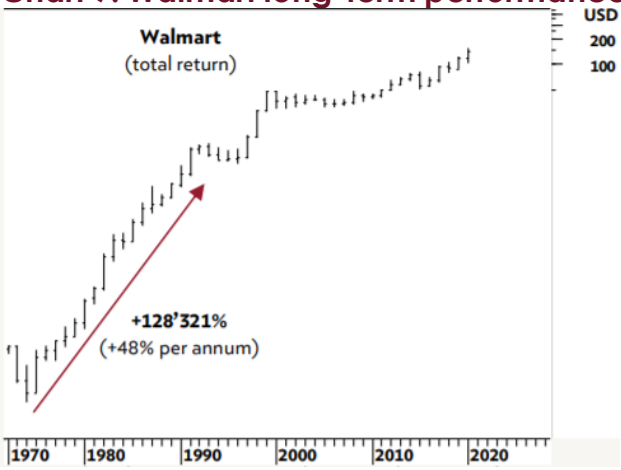
Much more can be written about the drama surrounding the world's most valuable privately owned company, but we will keep it for another day. To say the aborted IPO was a dis-appointment would be an understatement, bearing in mind that Alibaba is one of the largest holdings in our global portfolios (Alibaba owns an effective 33% of Ant). What the events do show is the extent to which the Chinese authorities will go to ensure that the appropriate – at least in their opinion – regulation is applied throughout the retail financial landscape in China. Ant has estimated that they will reconsider a listing in six months' time, if at all. We may yet write more about Ant Financial, but when we do it will be a very different company.

File 13: Information almost worth saving

Stick to stocks in long-term uptrends.

Here is more sage advice from *Mensur Pocinci, Head of Technical Analysis at Julius Bär*: "We have written many times about the fact that individual stocks are, first of all, risky and secondly, the majority of the stock market wealth creation comes from a handful of stocks. One example is Walmart. Of course, it is difficult to remember, but as seen on the chart, Walmart has been one of the biggest growth stocks of the past fifty years. It managed to rise by 48% per annum from 1973 to 1993. With the compounding effect, this means of course that the stock rose by a factor of 1,283. Thus, it remains elementary for investors to stay invested in long-term uptrends. One current example of course might be Amazon, which has risen by 39% per annum since the lows of 2001".

Chart 9: Walmart long-term performance



Source: Julius Bär

So what's with the pics?

The theme of this month's photographs – if there is one – is one of cold, of ice and snow. There is no particular reason for this theme, although it is perhaps an appropriate one with which to head into the end of what has been a remarkable year for all of this planet's citizens.

Greenland in the moonlight

Source: @joe_shutter

Time to bring 2020 to a close

The lateness of this edition of *Intermezzo* means that many of you may have left the (home) office and "closed shop" for the year. As we all know, it has been a tough year for many, including many in the broader "Maestro family". Many of our friends and even family have lost their jobs, and their lives have changed for good. Each day, within the Maestro team, we are conscious of how privileged we are, having retained our careers and professions, and having been able to make it through 2020 in relatively good health – physically and in other ways, including psychologically, financially and emotionally.

Despite the economic hardship and suffering around us, Maestro has had a good year. Most of our clients – certainly all those who gave Maestro full discretion in the management of

"To achieve great things, two things are needed; a plan, and not quite enough time."
- Leonard Bernstein

client portfolios – enjoyed more than respectable returns in absolute and relative terms, and in dollar and rand terms.

In "normal times" this would be most gratifying, but after a year such as 2020, this is nothing short of remarkable. Certainly we could never have imagined it towards the end of March this year, when global equity markets plunged into the fastest bear market in living history. How extraordinary is it then, to review many of the underlying companies in which we have invested, and see their share prices having more than doubled since then. We would and could never have imagined anything like this – we can but stand back and be humbled by the returns, yet immediately also express our gratitude to our clients who have placed their confidence – and their assets – in our small, humble team. Thank you so, so much.

It would be amiss of us to not also express our sincere gratitude to all our suppliers, without which Maestro would simply not be able to provide the service and returns which we have. From our auditors, to the administrators, to the providers of the most remarkable research and ideas, always presented in such a professional and exciting manner – we are so grateful to all of you. Thank you so much. Space simply precludes me listing them all here, but they know who they are – spread across the world, from Mauritius to the BVI, from Switzerland to the Cayman Islands – each with their own teams, spread far and wide across the world. The Covid-19 pandemic has affected them all, yet without exception they have continued to provide us – and our clients – with the most professional and impeccable service. Thank you again.

Greenland under the aurora

Source: @joe_shutter

As we reach the end of this year, may you experience a time of refreshment and renewal – to the fullest extent possible – during the traditional summer holidays here in South Africa. May you experience a sense of blessing and gratitude as we remember and consider those less fortunate than ourselves, who were not necessarily able to escape the physical and professional hardships of this year. Thank you for your support, your friendship, your kindness and your loyalty. We are looking forward to what 2021 holds, though we know it won't be an easy year. We also look forward to continuing to be of service to you through the year.

"Saluti", and God bless and keep you through the Festive Season and beyond.

"To achieve great things, two things are needed; a plan, and not quite enough time."
- Leonard Bernstein