Cytonn 2020 Markets Outlook

Global Markets Outlook

The year 2019 was characterized by a slow-down in global growth, which was weighed down by the negative effects of the trade conflicts among the major economies. These include: (i) the on-going trade dispute between the US and China, (ii) uncertainty in Britain over its exit from the European Union ("Brexit"), (iii) geopolitical tension between the US and Iran, disrupting the mid-stream and down-stream oil supply channel, and (iv) overall slowing global trade, which, according to the World Trade Organization, is estimated to have grown by 1.2% in 2019. According to the World Bank, global GDP growth in 2020 is expected to come in at 2.5%, a marginal increase from the estimated 2.4% in 2019, driven by the expectations that policy actions put in place, in an effort to ease trade tensions, will lead to a reduction in policy uncertainty.

Following the economic growth experienced in 2019, we look at the three key themes that we believe will shape the global markets in 2020:

i. ***Global Trade to Pick-Up…***

A sharp slowdown in the manufacturing sector, majorly experienced in advanced economies, has continued to weigh down on global trade. The poor performance in the manufacturing sector can be attributed to weakening demand in Europe and Asia, particularly for trade-intensive automobiles and technology products. Similarly, trade tensions between the US and China have escalated for the most part of 2019, and have resulted in significant aggregate losses for world trade. Despite this, the recent negotiations have led to a Phase One agreement, signaling a notable de-escalation of trade tensions. This will ultimately reduce the cost of international trade.

Similarly, trade policies will be the drivers of global trade and help promote it in the year 2020. For example, the Africa Continental Free Trade Agreement which was ratified in 2019, will establish the largest free trade area in the world, according to the United Nations Conference on Trade and Development (UNCTAD). It will cover 1.2 billion people and over USD 3.0 trillion in GDP. The agreement seeks to increase intra-African trade by cutting tariffs by 90.0% and harmonizing trading rules at a regional and continental level. Our expectation is that global trade is set to pick up during the year, pegged on how well the policies put in place will be implemented.

ii. ***Monetary Policy Easing…***

Monetary policy stances are expected to ease in advanced economies. The US Federal Open Market Committee (FOMC) is expected to continue on the path towards spurring growth through the easing of monetary policy, and expected to maintain the Federal Funds Rate at between 1.50% - 1.75% in 2020, despite elections in 2020. The European Central Bank (ECB) is expected to maintain its benchmark interest rates for the main refinancing operations, marginal lending facility and the deposit facility at 0.0%, 0.25% and -0.50%, respectively, through the year, having considered that the overall fiscal position of the Euro Area is expected to be roughly balanced amongst the member countries, and ultimately providing little additional support to activity.

iii. ***Falling Commodity Prices…***

Most global commodities registered declines in 2019, with agriculture, non-energy commodities, metals & minerals and Brent oil registering declines of 4.6%, 4.7%, 6.0%, and 11.8%, respectively, while energy was the biggest decliner falling by 14.9%, according to the World Bank Commodity Prices Index. Oil prices closed at USD 61.1 per barrel, having averaged USD 61.0 per barrel in 2019, and are projected to decline slightly to an average of USD 59.0 per barrel in 2020 and 2021, according to the World Bank. This performance was driven by production cuts by OPEC and its partners, coupled with constrained production in the Islamic Republic of Iran and Venezuela. These factors were however mitigated by the weakening oil demand. In 2020, the World Bank expects oil prices to decline slightly. Oil supply from the US is expected to continue increasing as a new pipeline capacity comes on stream, with the main downside risk being the further deterioration in growth and the geopolitical tensions between the US and Iran.

Having considered the two key factors that will drive Global Markets in 2020, we now look at specific economic regions and expectations for their GDP performance in 2020:

World GDP Growth Rates

	Region	**2016**	**2017**	**2018**	**2019e**	**2020f**
1.	China	6.7%	6.8%	6.6%	6.1%	5.9%
2.	India	7.1%	7.2%	6.8%	5.0%	5.8%
3.	Sub-Saharan Africa*	1.3%	2.7%	2.6%	2.4%	2.9%
4.	Middle East, North Africa	5.1%	1.1%	0.8%	0.1%	2.4%
5.	Brazil	(3.3%)	1.3%	1.3%	1.1%	2.0%
6.	United States	1.6%	2.4%	2.9%	2.3%	1.8%
7.	Euro Area	1.9%	2.5%	1.9%	1.1%	1.0%
8.	South Africa (SA)	0.6%	1.4%	0.8%	0.4%	0.9%
9.	Japan	0.6%	1.9%	0.8%	1.1%	0.7%
	Global Growth Rate	**2.4%**	**3.2%**	**3.0%**	**2.4%**	**2.5%**
	***including South Africa*					

Source: World Bank

United States:

The US economy is expected to grow by 1.8% in 2020, 0.5% points slower than the estimated 2.3% growth in 2019. In mid-October 2019, the US Government started talks over the Phase One trade deal with China, which includes a partial rollback of tariffs which has since de-escalated trade tensions. Market expectations are for the Federal Reserve to maintain the Federal Funds Rate at the current banded range of 1.50% - 1.75%, a more accommodative policy given that 2020 is an electioneering year and the softening global economic prospects.

In 2020, the stock market is expected to be bearish, driven by the political uncertainty brought about by President Trump’s impeachment and the elections set for 2020. The recent agreement between the US and China, which has resulted in the de-escalation of trade tensions, will help mitigate this effect. According to Bloomberg, investors are set to earn much less in 2020 than they did in 2019, this they attribute to the downside risks associated with the electioneering period and fears of a global recession in 2020.

Eurozone:

The Eurozone is expected to grow by 1.0% in 2020, 0.1% points lower than the estimated 1.1% growth in 2019. This is mainly informed by weaknesses seen in several economies such as in Germany, where the industrial sector has been struggling with falling demand from Asia and disruptions in car production. The uncertainty around the Brexit also contributed to the slow growth. The ECB managed to restart quantitative easing by pushing its policy rate deeper into the negative territory, ultimately providing cheap credit to banks for onward lending.

The Stoxx 600 index gained by 24.6% in 2019. The P/E ratio currently at 15.0x, is 23.1% below the historical average of 19.5x, indicating markets are currently trading at relatively cheaper valuations. In 2020, the stock market is expected to be bullish, supported by reduced geopolitical tensions, following Britain’s General elections which have reduced uncertainty on Britain’s withdrawal from the EU (“Brexit”), coupled with the de-escalation of the US-China trade war achieved through the Phase One agreement.

China:

The Chinese economy is expected to grow by 5.9% in 2020, slower than the 6.1% expected growth in 2019, owing to cooling domestic demand and the existing trade tensions. Higher trade tariffs and trade policy uncertainty have weighed down on investor sentiment for the better part of 2019. Trade tensions between the US and China have escalated for the most part of 2019, and have resulted in significant aggregate losses for world trade. The recent negotiations have however resulted in a Phase One agreement signaling a notable de-escalation of trade tensions.

The Shanghai Composite index gained 25.2% during the year 2019. The gains were mainly supported by expectations of a positive outcome following the resumption of trade talks with the United States, coupled with increased capital injection by the government, which improved investor confidence. The P/E ratio currently at 14.7x, is 0.2% above the historical average of 14.5x, indicating that the market is currently trading at slightly more expensive valuations. In 2020, the stock market is expected to be bullishly supported by the renewed hope from the Phase One trade deal with the US, which had helped in de-escalating the trade tensions between the two countries.
