



Our Weekly Paid Newsletter

Richard Cluver Predicts

In our 34th year of service to the investing public of South Africa



Volume: 34

27 August 2021

Two major economic events will, in retrospect have dominated this week, but both will likely go completely un-noticed by the majority of citizens.

Locally, the release of new GDP statistics have significantly lowered South Africa's gross debt from 81.9 percent of GDP to 71.1% for 2020/2021 and lowered the 2021/2022 estimates to 73.5% from an earlier forecast of 81.9 percent of GDP; and taken down the 2023/2024 forecast to 78.4% (87.3%).

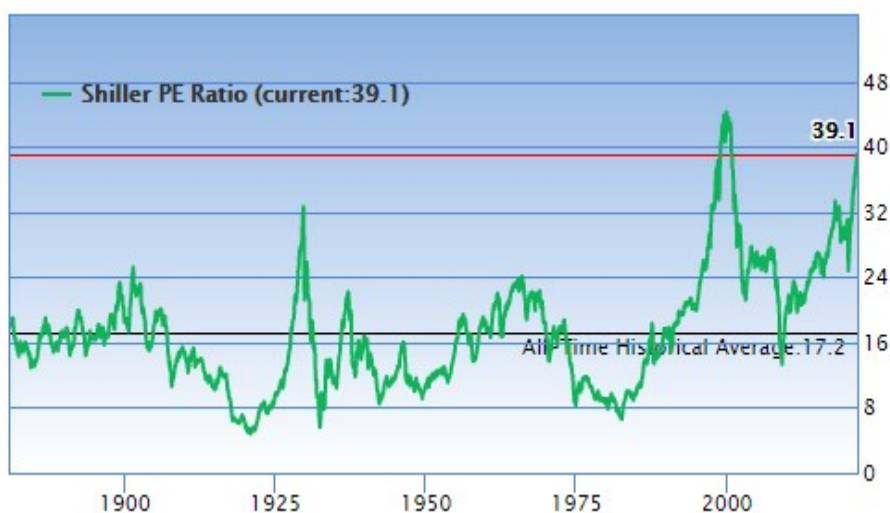
The revisions lower the budget deficit ratio to -12.4% of GDP from 14% for 2020/2021, all of which will make South Africa look far more attractive to foreign investors and, ultimately, make items like household bond costs and hire purchase charges affordable for longer. Its good news at a time when South Africa dearly needs every bit of good news it can get.

For the worldwide community, however, a meeting at Jackson Hole in the USA will today feature Federal Reserve Chairman Jerome Powell who will give his views on monetary policy. With US inflation on the rise, the Fed is under growing pressure to increase lending rates which, as I detailed in this month's issue of *The Investor*, could well precipitate another "Taper Tantrum" which could end Wall Street's long-running bull market.

So it is important to draw readers' attention once again to the oft-quoted Shiller Wall Street price earnings ratio. As I have so often explained, the ratio is an inflation corrected graph based upon the Standard and Poors 500 index of the New York Stock Exchange. Currently at 39.1, it is at its highest level since its peak of 43.8 attained in July 1999 just ahead of the "Dot Com Tech Bubble" burst which *Fortune Magazine* described as, "A frenzy so unhinged that it took 13 years for investors who bought at the peak to break even."

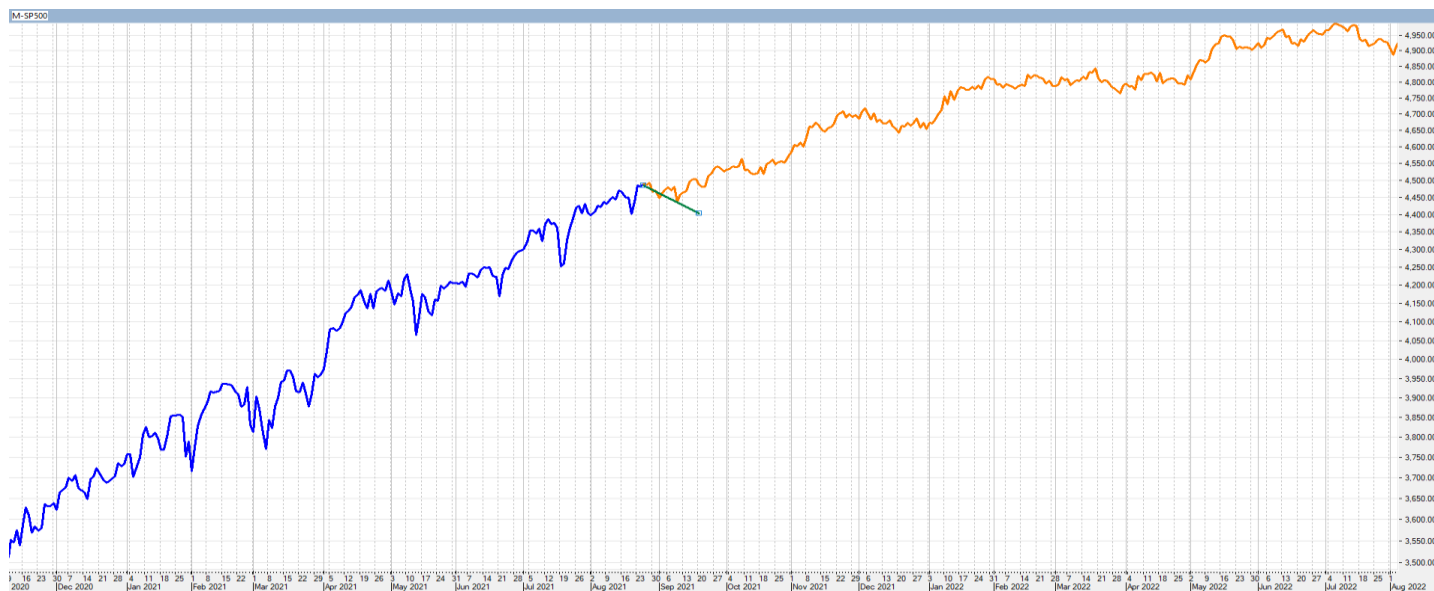
Developed by [Yale economist and Nobel laureate Robert Shiller](#), the CAPE ratio is signalling that stocks are at their most expensive level as compared with any time in the past 150 years other than just ahead of the dotcom bubble.

Because earnings are highly volatile, a temporary spike can make P/E multiples look artificially cheap, while a short-lived fall can make S&P valuations seem inflated. To correct for that problem, Shiller deploys a 10-year average of earnings per share, adjusted for inflation. Using that formula for smoothing the peaks and valleys makes the CAPE ratio a reliable predictor of the returns shareholders can expect in the years to come. Starting at an ultrahigh CAPE ratio portends poor to mediocre performance for shares bought now for five to ten years hence.

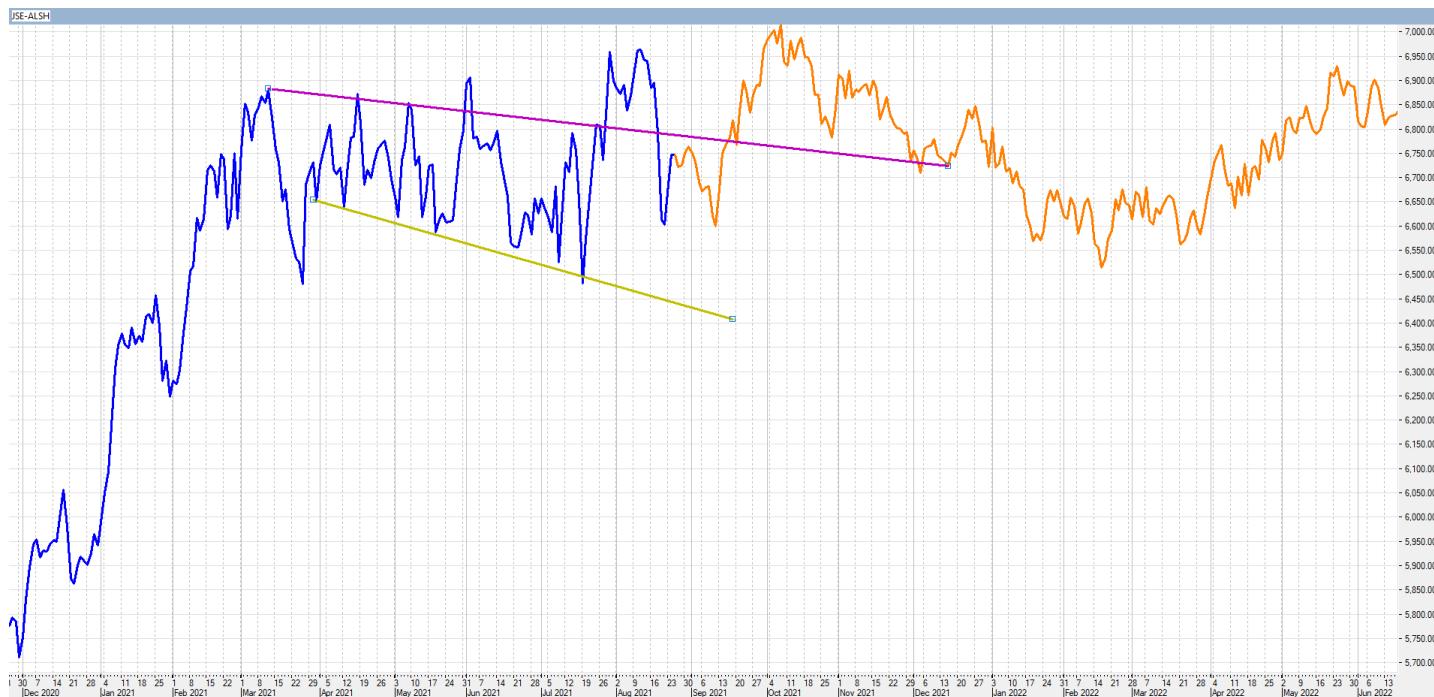


So what does ShareFinder make of the current situation? For over a year now it has been predicting quite a severe market drop starting about now. However, as most readers understand, ShareFinder's artificial intelligence-powered forward projection system is exponentially weighted. What that means is that the latest data has a far greater influence upon current events than the regularly-recurring market cycles of the past. The consequence has been that as new data has arrived, ShareFinder has steadily moderated the extent of the drop which it saw beginning today until it has become a mere interlude lasting from today until September 9 before markets continue their unabated climb into the stratosphere.

To even make it visible to readers I have had to draw in a green trend line on the graph below:



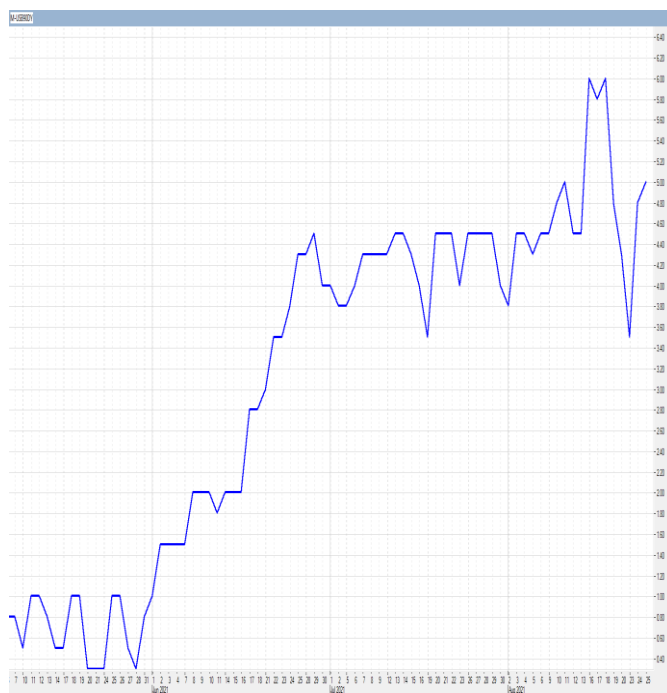
Moreover, ShareFinder does not see any significant market reaction in the immediate future...at least until October 7 when it senses a mini bear market until mid-February. And of course, most of you will anyway have been distracted by the daily rise in your portfolio value which in the middle of this month saw us attain the highest level the JSE All Share Index has ever reached.... that was until the Chinese government began rattling the Tencent/Naspers golden cage.



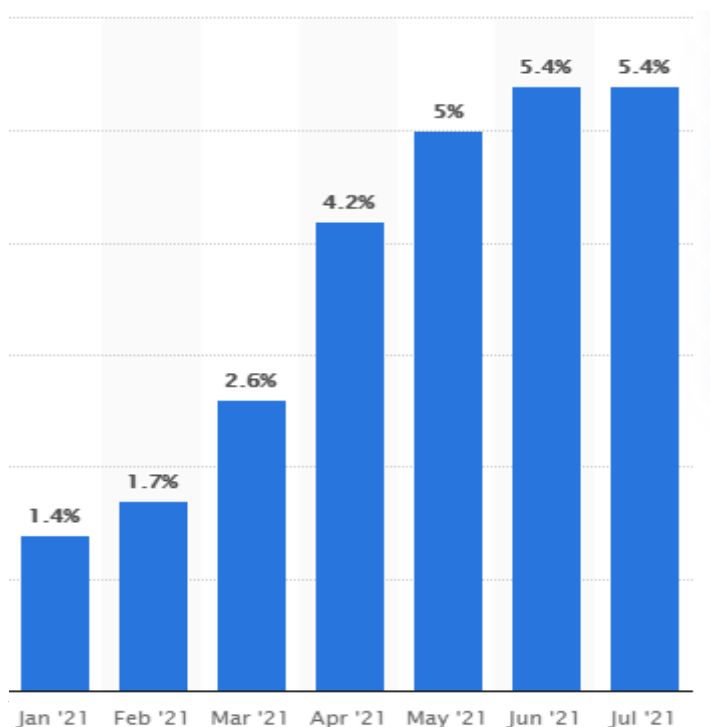
For those who are worried about Naspers, which at its worst this week was down 40 percent on its February peak valuation, ShareFinder predicts a recovery from here on well into the New Year though it is unlikely to reclaim the previous peak for some time while the dust of the matter settles! Note the ShareFinder graph below:



So what does the money market make of the potential for another Taper Tantrum in the US? The most sensitive barometer is the 90-day borrowing rate which, my graph on the right illustrates, has moved from 0.3 percent in May to a peak of 6 percent on August 18. It fell briefly to a low of 3.5 percent on Monday but by yesterday was back up to five percent.



What should materially affect the Fed's decision on lending rates will be clear on the morning of Tuesday September 14 - 8.30 am US eastern time - or 2.30 pm SA time. The bar graph below tells the recent US inflation story:



The moral of all of this is that this is NOT a time to take your eyes off the ball. A better than expected inflation outcome will likely be VERY positive for markets worldwide. And of course the opposite outcome also holds.

I have created cash in my portfolios in order to be able to react and I trust those of you who regularly read this column have done the same. We live in hope but prepare for the worst!

Do enjoy your weekend!

The month ahead:

New York's SP500: I correctly anticipated a brief up-tick. Now I see weakness until the second week of September and I still see the low on the 9th.

Nasdaq: I was correct in suggesting an upward was under way. Now I expect weakness from August 30 until mid-September ahead of a recovery until April.

London's Footsie: I correctly predicted a decline which I continue to expect to last until mid-October.

Germany's Dax: I correctly predicted that weakness would continue with a brief gaining trend until the end of August within an overall long-term decline lasting well into the New Year.

France's Cac 40: I correctly predicted the declines that have begun and should last well into the New Year.

Hong Kong's Hangsen: I correctly predicted a volatile recovery which I expect to last.

Japan's Nikkei: I correctly predicted a few months of upward trend until the end of October before a long decline sets in. There is a strong likelihood of some reverses for the next fortnight however.

Australia's All Ordinaries: I correctly predicted an end to the gains around the 17th followed by declines until mid-October.

JSE Top 40 Index: I correctly predicted the interim recovery was temporarily. Now I see gains until early October ahead of five months of weakness.

ShareFinder JSE Blue Chip Index: I correctly forecast a brief recovery which I believed was over with weakness now likely until mid-September when a month-long further recovery seems likely. But after that I see a long decline.

Rand/Dollar: I correctly predicted the start of about six weeks of gains before weakness re-asserts itself in late-October through to February.

Rand/Euro: I correctly sensed a period of gains until mid-September but weakness thereafter well into the New Year.

Bitcoin: I correctly predicted gains from this week brief losses likely until about September 11 when another bout of weakness seems likely.

The Predicts accuracy rate on a running average basis since January 2001 has been 86.34 percent. For the past 12 months it has been 93.2 percent.

Naspers/Prosus share buybacks: More than R20bn of shareholder value destroyed

by Justin Rowe-Roberts writing for Biznews

The Naspers/Prosus ('Naspers stable') share buyback programme was initiated at the latter end of 2020 with the intention of returning value to shareholders. Unfortunately, as has been the case with a number of the Naspers stable's corporate actions in the last few years, it has failed miserably. In theory, the buybacks make a lot of sense. Both Naspers and Prosus trade at large discounts to its stake in Chinese internet giant Tencent, without including the other technology businesses within its portfolio. The share buybacks are a mechanism used to close this discount. However, when the share price continues to fall (as it has), it means that shareholders would've been better off with management allocating that capital in a different manner (ie in the form of dividends).

Taking the Naspers and Prosus closing price on Friday the 20th of August, which was c.R2,400 and c.R1,227 respectively, the share buybacks – which have spanned over a period of more than six months, have shed c.R20.7bn in shareholder value. In total, the original value of the Naspers buyback was c.\$3.6bn and the Prosus buyback was c.\$1.4bn. The calculations were done using the figures below.

Since the commencement of the programme on 23 November 2020:

- A total of 11 874 493 Prosus ordinary shares N were purchased (representing c. 0.7309% of the issued Prosus ordinary shares N) for a total consideration of US\$1.37bn excluding transaction costs, which represents an average cost of EUR94.97 per Prosus ordinary share N.
- A total of 15 992 042 Naspers N ordinary shares were purchased (representing c. 3.672% of the issued Naspers N ordinary shares) for a total consideration of US\$3.63bn excluding transaction costs, which represents an average cost of ZAR3 317.96 per Naspers N ordinary share

The timing could not have been worse for both counters, with Naspers and Prosus down around 40% since its highs in February. The Chinese government have been ruthless in their approach, hammering down on many of the country's most powerful and innovative businesses. Apart from Tencent, other Chinese giants which been subject to the regulatory crackdown include Jack Ma's Alibaba, Baidu and the JD Group. The MSCI Golden Dragon Index (listed on the Nasdaq), which captures the equity market performance of large and mid-cap Chinese securities, is down almost 50% in the last six months alone. The Chinese Communist Party is out for blood and no one knows when or if this theme will stop.

These capital allocation mishaps have left Bob Van Dijk and his management team under severe pressure. Apart from the share buybacks, the Naspers/Prosus share swap – which was another form of corporate action used by management to unlock value for shareholders – has been a setback. A number of South Africa's top asset management firms formed a collaborative engagement in a stance of activism against the transaction as market participants reached boiling point over years of perceived mismanagement. The argument is that despite Naspers phenomenal share price performance over the past few years, it's been driven by the outperformance in Tencent rather than management's doing.

Of even more concern to Naspers stable shareholders, the aggressive buybacks of the last six months would've artificially kept the share price higher than if the buybacks had not been implemented. Interestingly, Prosus has announced a further share buyback of \$5bn.

This comes at a time where the most bullish, pro-China analysts are starting to have doubts around the sustainability on the likes of Tencent's earnings going forward. All this uncertainty will lead market participants to apply lower multiples on Chinese companies such as Tencent, lowering its valuation and ultimately lowering the valuation of the Naspers stable. Although the Naspers stable is starting to grow a sizeable tech-centric portfolio outside of Tencent, the value of the Chinese tech titan ultimately determines the value of Naspers and Prosus due to its sheer size.

Tencent is one of the best businesses on the planet. However, the concerns surrounding the Chinese government and regulatory authorities cannot be understated. Especially given China's history. As with any stock, there's a risk vs reward trade-off. The risks in Tencent have escalated tenfold.

A concern for many South African pensioners.