overberg
asset management

LOCAL PERFORMANCE FACTSHEET

OAM Local Defensive Portfolio

Technical Details

2021 Q2

- Base currency: **South African Rands**
- Benchmark: **Prime Interest Rate (2009 - 2018); 25% JSE All Share, 25% ALBI (1-3y 2019-Sept'20), 15% SAPY, 35% JSET (2019-)**
- Asset Allocation: **Flexible mix of equities, real estate holdings, preference loan stock, government bonds and cash**
- Individual portfolio representing Local Real Return investment style
- All performance figures include income and are net of fees and expenses

Annualised Growth (%)	OAM	Benchmark
Inception 2009	**6.10**	**9.29**
7 years	0.95	9.14
5 years	0.01	8.78
3 years	1.23	7.43
2021 YTD	7.16	7.66

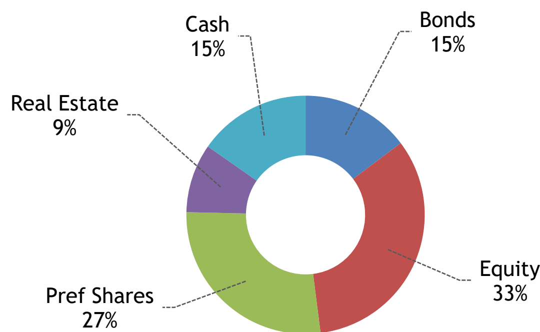
Annualised Income Yield	5.26%

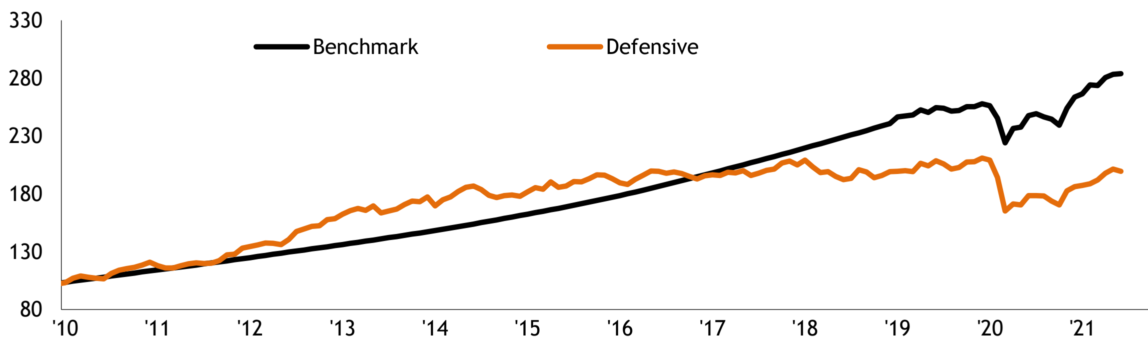
Investment Objective

- Conservative growth
- Consistent annual returns
- Low volatility

Top 5 Holdings	
STOR-AGE PROP REIT LTD	
SASFIN HLDGS LTD PREF	
REINET INVESTMENTS S.C.A	
ANGLO AMERICAN PLC	
STANDARD BANK GROUP PREF	
Total number of holdings	23

ASSET ALLOCATION
(see through basis)





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Local Market Review and Strategy Outlook for the quarter ended June 2021

Emerging markets gave up some of their stellar first quarter (Q1) gains in Q2. As one of the most liquid emerging markets, this process also affected South Africa. Despite a steady economic recovery, the JSE All-Share index consolidated its recent gains with a modest 0.4% pullback in Q2 although still posting a solid 11.5% year-to-date return. The culprits were profit taking in mining resources shares, causing the Resources 20 index to fall 5.5% in the quarter although still up 9.8% YTD, and profit taking in Prosus and Naspers due to a rotation from technology shares into cyclical shares, which caused the Industrial 25 index to drop 2.5% in the quarter although it leads with a YTD return of 12.0%. However, the sector rotation benefitted banks and financials, which tend to perform best during a cyclical economic rebound. The Financial 15 index gained 7.7% over the quarter and by 8.6% YTD. The rand firmed, helped by foreign demand for domestic bonds and a greatly improved trade performance and current account balance. Despite a recent appreciation in the trade weighted dollar index, the rand firmed versus the US dollar by 2.4% over the quarter and by 2.9% YTD to R/$ 14.27. The All-Bond Total Return index increased by 6.9% in Q2 and 5.0% YTD. Consolidation in commodity markets saw the platinum price fall 7.7% in the quarter to $1095 per once reducing its gain for the year to 2.4%. Gold recovered some of its recent losses with a quarterly increase of 4.2% but at $1778 per once is still lower for the year by 6.1%.

There is no doubt that the economy is recovering. In Q1, GDP beat expectations with growth of 4.6% quarter-on-quarter annualised, slowing from 5.8% in Q4 2020 but far better than the Reserve Bank's 2.7% forecast. Forward-looking survey data, coupled with strong export performance, driven by the mining sector and vehicle sales, point to economic momentum being maintained in Q2. The RMB/BER Business Confidence Index jumped from 15 to 50 in Q2. The number of survey respondents satisfied with business conditions now equals those that are not satisfied, an outcome we have not seen in years. The RMB/BER Retail Survey Index surged from 37 to 54, with confidence in the durable goods sectors especially strong, helped by record low interest rates. New vehicle dealer confidence increased from 35 to 63. The Absa manufacturing purchasing managers' index (PMI) increased to 57.8 in May, consistent with strong manufacturing activity over coming months. The IHS Markit PMI, measuring activity across the entire economy, is also well above the expansionary 50-level, printing 53.2 in May.

The South African Reserve Bank lifted its 2021 GDP growth forecast from 3.8% to 4.2%. Some economists believe growth of up to 5% could be achieved, but most question the sustainability of these upbeat growth rates. According to the SARB's longer-term forecasts, GDP growth will slow to 2.3% in 2022 and 2.4% in 2023. The current growth spurt is cyclical rather than structural, attributed to the restocking of inventories, which were depleted during the height of the Covid pandemic, and to the surge in global trade and commodity prices. The SARB's latest composite leading business cycle indicator recorded a new multi-year high of 125.8, registering a year-on-year increase of 31.4%%. Yet beside the obvious base effect of rock bottom comparative figures last year, the biggest contributor to this sizeable increase was the gain in the leading indicators of South Africa's trading partners. The US dollar-denominated export commodity price index also played a role. These represent external influences. Domestically focused measures such as money supply growth and the interest rate spread were negative contributors.

Our recent economic success stems predominantly from the "V" shaped recovery in the global economy, not from any structural improvements of our own. The trade surplus is surging, measuring R202.6 billion in the year to end May. In the same period last year, the trade balance showed a surplus of just R10.6 billion. The figures contributed to a R69 billion widening in the current account surplus in Q1 to R267 billion, rising from 3.7% of GDP to 5%. This is impressive and certainly the unexpected boost to our fiscus from commodity exports is a relief. Thanks in large part to a windfall from strong commodity exports, South Africa's main budget deficit for the last fiscal year came in at 11.2% of GDP, much lower than the earlier projection of 14%. We cannot escape the fact though that the surging trade surplus is also testament to acute weakness in domestic demand. Despite the strong headline GDP figure, gross

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fixed capital formation contracted in Q1. Household consumption expenditure strengthened by 4.7% but it is hard to envisage positive momentum amid shrinking private sector credit extension and a chronically depressed jobs market. Credit extension contracted year-on-year in April for a third straight month.

The unemployment situation is dire. The official unemployment rate increased to 32.6% in Q1 from 32.5% the prior quarter. The broader definition of unemployment, which includes those who are discouraged and given up looking for work, increased from 42.6% to 43.2%. The official unemployment rate among younger South Africans between the ages of 15-34 is an astonishing 46.3%, presenting an enormous risk to social stability. The risk is compounded by the rapid deterioration in public service provision and the financial stability of municipalities. In a worrying report, Ratings Afrika published a further decline to new record lows in the financial stability of the country's municipalities and metros, which on average are well below the deemed level of financial viability.

The credit rating agencies have kept South Africa's sovereign debt at three levels below investment grade. While listing the country's strengths, which include a credible central bank, a flexible exchange rate, actively traded currency and deep capital markets, the rating agencies cited the lack of structural economic reforms as a key risk. The good news is that President Ramaphosa, through Operation Vulindlela, a joint operation between the Presidency and the National Treasury, is finally taking action. In the space of two days, coinciding with Ramaphosa's attendance at the G7 meeting in the UK, the government announced that the licensing threshold for private sector electricity generation would be raised from 1 megawatt to 100 megawatts, and that South African Airways would be partly privatised with the sale of a 51% stake to the Takatso Consortium. These moves caught the public by surprise, which understandably has become increasingly cynical about Rampahosa's promised "new dawn", but the president has increased his authority within governing circles. He has driven the opposing "Radical Economic Transformation" factions further into touch following the ANC's formal suspension of Secretary General Ace Magashule. We are hopeful that these recent initiatives will be the start of a concerted structural reform drive rather than ad hoc measures taken out of desperation. As the proverb goes "One swallow does not a summer make."

Inflation has picked up. Consumer price inflation (CPI) accelerated in April to 5.2% year-on-year but with an absence of demand pressure and enormous slack in the economy and labour markets, there is not the same fear of rising inflation expectations as exists in the rest of the world. On a month-on-month basis, CPI increased by a very mild 0.1%. The SARB has reduced its 2021 CPI forecast from 4.3% to 4.2%, leaving it unchanged for 2022 and 2023 at 4.4% and 4.5%, comfortably tracking the midpoint of its 3-6% target range. With a strong and stable rand, underpinned by buoyant commodity prices and robust terms of trade, coupled with high long-term interest rates (amongst the highest bond yields in the world), any SARB interest rate hikes are likely to be gradual and mild.

Notwithstanding the 14-day adjusted Level 4 lockdown imposed on 27th June, the short-to medium-term outlook is positive. Low interest rates, a stable rand and an ultra-accommodative monetary policy at the Federal Reserve and other major central banks, are a constructive combination for outperformance by emerging markets. The JSE, with its heavy weighting in resource stocks, is no exception and should continue to perform well on a 12-month horizon, helped by expectations of a strong cyclical recovery over the period. However, over the longer-term, portfolios should maintain a healthy exposure to rand hedge investments and overseas markets, until there is more definitive evidence that the summer of structural economic reform has indeed arrived.

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