overberg asset management

LOCAL PERFORMANCE FACTSHEET

# OAM Local Defensive Portfolio

## Technical Details

2022 Q3

- 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 all fees and expenses (including asset management and financial advisor fees)

| Annualised Growth (%) | OAM | Benchmark |
|---|---|---|
| Inception 2009 | 5.63 | 8.47 |
| 7 years | 0.69 | 7.55 |
| 5 years | 0.14 | 6.27 |
| 3 years | -0.02 | 4.52 |
| 2022 YTD | -5.43 | -4.84 |

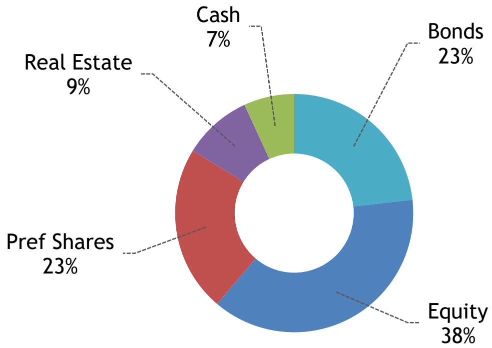
| | |
|---|---|
| Annualised Income Yield | 4.92% |

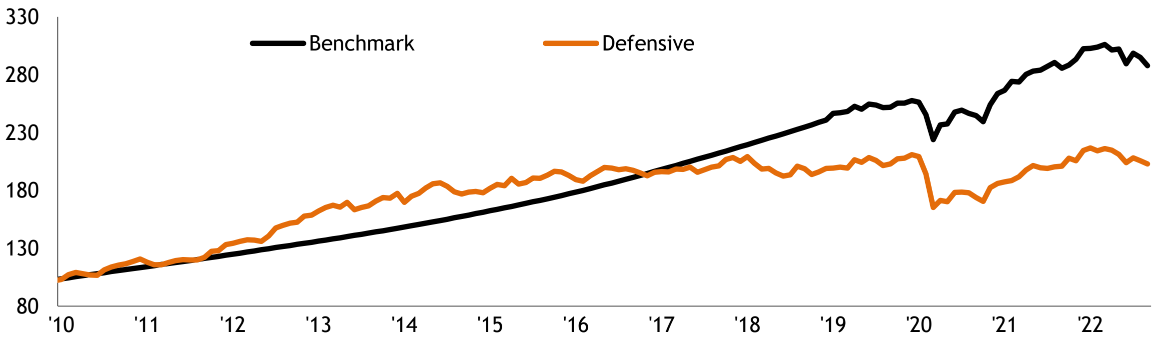
## Investment Objective

- Conservative growth
- Consistent annual returns
- Low volatility

| Top 5 Holdings | |
|---|---|
| NEWFUNDS TRACI 3-M ETF | |
| STOR-AGE PROP REIT LTD | |
| STANDARD BANK GROUP PREF | |
| INVESTEC LTD PREF | |
| REINET INVESTMENTS S.CA | |
| Total number of holdings | 21 |

**ASSET ALLOCATION**
(see through basis)



## Local Market Review and Strategy Outlook for the quarter ended September 2022

Despite reasonable earnings growth, local equities suffered a second consecutive quarter of declines in the third quarter (Q3). Sentiment was affected by rising inflation and interest rates, excessive load shedding and weakening global markets. The JSE All Share index dropped 3.8% in Q3 and 13.5% year-to-date (YTD). The Resources 20, Financial 15 and Industrial 25 indices all succumbed with quarterly losses of 5.5%, 6.1% and 2.5% widening their YTD declines to 15.1%, 6.8% and 18.9%. The surging US dollar and rising global bond yields impacted the rand and local bond returns. The rand lost 10.9% versus the dollar over the quarter and 12.9% YTD, ending at R/$ 17.99 at the end of September compared with R/$ 15.93 at the end of 2021. The All-Bond Total Return index eked out a slight 1.1% gain in Q3 but was down by 0.8% YTD. Inflation, rising interest rates and rate expectations caused the longer dated 10-year government bond yield to increase over the quarter from 10.55% to 10.89%, substantially above its closing level of 9.35% at the end of 2021. Impacted by the strong dollar, the dollar gold price ended the quarter at $1660.7 reflecting quarterly and YTD falls of 8.1% and 8.8%.

The devastating floods in KwaZulu-Natal and loadshedding contributed to GDP declining in Q2 by 0.7% quarter-on-quarter, a disappointment after the 1.7% growth recorded in Q1. After recovering to its pre-pandemic level in the first quarter, GDP slipped back below it in the second. Manufacturing was the biggest detractor declining 5.9% on the quarter and subtracting 0.7% from the headline GDP figure. Agriculture, mining, and trade also shrank, each subtracting 0.2% from Q2 GDP growth. Construction remains furthest from regaining its pre-pandemic output, lying 21.6% below its Q1 2020 level.

Despite further deterioration in load shedding and weakening external markets, the high frequency economic data point to a return to positive growth in Q3. Vehicle sales, which account for 12% of South Africa's GDP, grew strongly. Domestic sales increased in July, August and September by 30.9%, 14.2% and 10.8% year-on-year, respectively. Export sales grew over the same months by 177.7%, 57% and 104.6%. Despite rising interest rates and inflation's impact on household disposable income, retail sales grew in August by 8.6% on the year. However, mining production fell in July by 8.4% on the year due to ebbing commodity prices, and rail and port bottlenecks, and while manufacturing grew by 3.7%, the Absa manufacturing purchasing managers' index (PMI) dipped back into contractionary territory again in September, from 52.1 to 48.2, signalling continued output declines for the sector.

Other survey data were more encouraging. The S&P Global South Africa economy-wide PMI stayed above the neutral 50-mark at 52.7 in July and 51.7 in August. The SACCI Business Confidence index gained in July from 108.5 to 110.3 and the FNB/BER consumer confidence index increased between Q2 and Q3 from -25 to -20. Credit extension has been picking up steadily, driven by loan growth in the economy. Annual growth in private sector credit extension accelerated from 7.06% in July to 7.86% in August, maintaining its steady improvement from just 3.12% in January.

The South African Reserve Bank cut its GDP growth projection for 2022 from 2% to 1.9% but raised it for 2023 from 1.3% to 1.4% and for 2024 from 1.5% to 1.7%. Inflation remains a threat but less so than in most developed economies due to sluggish domestic demand. Annual consumer price inflation (CPI) eased in August from 7.8% to 7.6% and core inflation, excluding food and energy prices, dipped from 4.6% to 4.4%. On a monthly basis, headline CPI rose by just 0.2%, the least in 7 months, indicating that the peak in inflation may be past. Transport inflation fell from 25% to 21.2% and a further cut in the fuel price is tabled for October. The SARB forecast CPI will reduce to 6.5% by the end of 2022 and decline to 5.3% by end 2023, lower than its previous 5.7% forecast. The medicine of repo rate hikes appears to be taking effect. The repo rate was hiked by another 75 basis points to 6.25% in September, marking the 6th consecutive rate hike since policy normalisation began in November 2021. The repo rate is expected to top out at between 7.0 – 7.5%, indicating another two sizeable hikes.

Unfortunately, external demand is slowing which caused a narrowing in the trade surplus to just R7.2 billion in August, compared with R24.8 billion in July. The declining trade balance contributed to the current account losing its surplus status. It moved from a surplus of 2.4% of GDP in Q1 to a deficit of 1.3% of GDP in Q2, making the rand more vulnerable. Credit rating agency Fitch affirmed the country's foreign currency rating, but concerns abound over the country's fiscal deficit and debt burden, given the financial distress of state-owned enterprises, the slow pace of reform and socio-political pressures. The unemployment rate dropped marginally from 34.5% in Q1 to 33.9% in Q2, but the number of unemployed people still climbed by 132,000 to 7.994 million. The expanded definition of unemployment, including people who have stopped looking for work, is at 44.1%, placing growing demands on the Basic Income Grant to be made permanent.

The Eskom load shedding crisis is getting worse. Ageing plants, corruption and sabotage have led to a further increase in power outages. Fortunately, the crisis has prompted greater urgency from government. On 26th August, the government determined that an additional 14,491 MW of solar, wind and storage capacity, 1,000 MW from biomass and landfill projects, and 3,000 MW from gas would be procured, on top of the 6,000 MW already in various stages of development. Most of the financing will come from the private sector and concessional funding. Investment of more than R1.2 trillion is envisaged by 2030. Some analysts believe the expenditure, as well as alleviating the country's energy constraints, could be a significant catalyst for job growth and investment. Since the August announcement, Anglo American has pledged to deliver 5,000 MW of renewable energy by 2030, for the grid as well as its own needs.

The National Prosecuting Authority made progress in the fight against corruption and state capture, with high profile arrests of former Transnet directors, including CEO Brian Molefe and CFO Anoj Singh. The Hawks confirmed that 22,000 cases valued at R1.5 trillion, are under investigation and together with the NPA had concluded 4,447 convictions over the past 4 years. This may be the tip of the iceberg, but the announcements will hopefully earn South Africa a reprieve from being grey listed by the Financial Action task Force (FATF). A final decision will be made by April 2023. Grey listing would result in more red-tape, transaction costs and reduced foreign investment. Sam Tshabalala said the effect would be worse than a sovereign credit downgrade.

There is unlikely to be significant policy change ahead of the ANC elective conference in December, but the rising likelihood of losing its majority in the 2024 national election and the dire state of power, rail and port infrastructure and service delivery is leading to a thawing out in policy reform paralysis. Meanwhile, South Africa's attractively priced government bonds, relatively modest inflation pressures, healthy trade and current account balances, and fiscal conservatism, combine to make South Africa's investments attractive in a global context. Unfortunately, episodes of rising US treasury bond yields coupled with a strengthening dollar tend to be negative for emerging market capital flows. South African financial markets are suffering from the global retreat in risk appetite. However, the Federal Reserve is close to peak hawkishness and once it pivots towards a neutral monetary policy outlook, emerging markets and the JSE are likely to perform strongly.