# Onshore Global ETF Portfolio

## Q2 2023

## Investment Objective

The portfolio aims to improve the long-term wealth of investors by holding investments which deliver both capital growth and income, while maintaining a medium risk profile. The investments are extensively researched to assess their intrinsic value over the longer term.

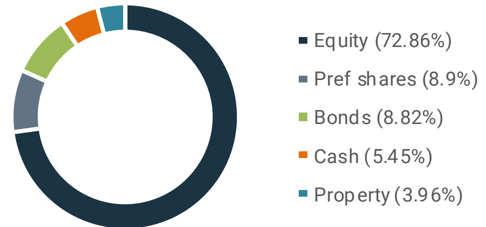
## Risk Rating

## Portfolio Description

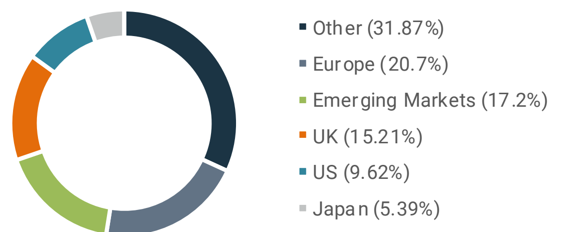
This actively managed share portfolio aims to provide a balanced investment solution across asset classes. The underlying investments include a well-diversified mix of equities, bonds, preference shares, real estate and cash. Total equity exposure is unlikely to exceed 70% of the portfolio. The portfolio predominantly comprises local index tracking exchange traded funds (ETF's) with an underlying exposure to offshore markets.

The portfolio is flexible, providing an indirect exposure to a broad range of geographies, industries, economic sectors, and currencies. The base currency is South African Rands.

## Asset Allocation (see through basis)




## Global Allocation (see through basis)




## Investor Criteria

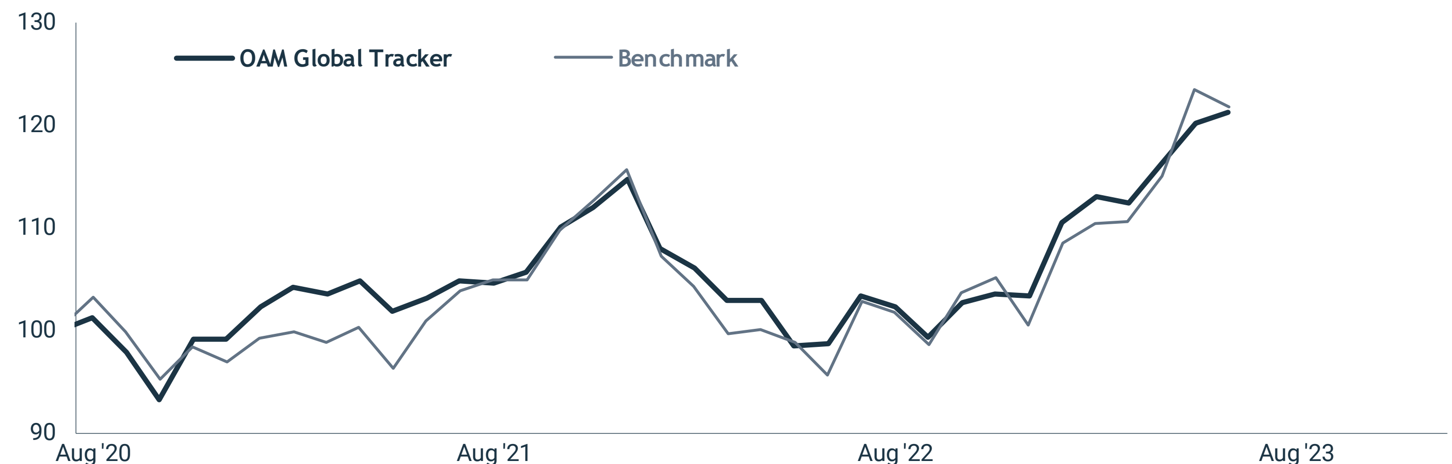
- Seek meaningful long-term capital growth and income.
- Recognise the benefits of indirect offshore exposure.
- Are comfortable with a medium level of risk and short-term market fluctuations.
- Typically aim to invest for a period of 5 years or longer.

## Performance

| Growth | OAM* | Benchmark** |
|---|---|---|
| Annualised (%) | ZAR | ZAR |
| Inception 2020 | 6.80 | 6.97 |
| 2 years | 8.37 | 9.91 |
| 1 year | 22.76 | 27.29 |
| YTD | 17.21 | 21.25 |

*Performance figures are based on a typical portfolio.
***Performance figures are net of all fees** (including asset management, platform, trading and advisor fees).
** The Benchmark is comprised of 60% MSCI ACWI, 40% WorldBIG index (in ZAR terms)

## Top 3 Holdings

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overberg
asset management

*beyond wealth.*

## Local Market Review and Strategy Outlook for the quarter ended June 2023

South African equities were relatively stable during the second quarter despite chronic loadshedding, a diplomatic rift with the US, further monetary tightening and worsening structural impediments to growth. The deteriorating outlook caused the rand to fall another 5.8% versus the US dollar in the second quarter (Q2) ending at R/$18.85, a 10.8% depreciation for the year-to-date (YTD). The JSE All Share index held onto a 4.1% YTD gain following a mild decline of 0.1% in Q2. Dual listed multinational companies like Naspers, Prosus and Richemont helped the Industrial 25 index post the best gains, up 3.4% in Q2 and 17.8% YTD. After showing nil return in Q1, the Financial 15 index fared better in Q2 with a 3.6% return as fears of a global banking crisis receded, cementing a 3.4% YTD appreciation. The Resources 20 index lagged with Q2 and YTD losses of 6.5% and 12.4%, as the global manufacturing slowdown and disappointment over China's post-Covid rebound impacted metals prices. The weakening rand coincided with government bond losses, which saw the 10-year government bond yield rising over the quarter from 9.83% to 10.51% compared with 10.18% at the end of 2022. The All-Bond Total Return index has a shorter maturity but still lost 1.53% in Q2, trimming its YTD gain to just 1.84% as the South African Reserve Bank (SARB) dealt a blow to bond prices with continued interest rate hikes over the quarter.

Despite the significant deterioration in electricity availability the economy narrowly escaped recession. GDP grew in Q1 by 0.4% quarter-on quarter, an improvement on the 1.1% contraction in Q4 2022. Growth would have been stronger had it not been for the 12.3% q/q decline in agricultural output, which should be temporary. Besides agriculture and utility output, which was also negative, the other ten industries monitored for GDP data posted gains over the quarter, led by manufacturing, up 1.5% q/q. An improved trade surplus helped narrow the current account deficit to 1.0% of GDP from 2.3% the prior quarter. However, electricity supply constraints will continue to act as a handbrake on economic activity. The SARB estimated that loadshedding will subtract 2% from GDP growth in 2023. Despite the reprieve in Q1, the IMF forecasts GDP growth will decelerate this year to just 0.1%, primarily due to the intensity of power cuts. Business and consumer confidence continued to decline due to loadshedding and other structural impediments, including deteriorating municipal delivery, organised crime syndicates, FATF grey listing, potential trade friction with the US, and collapsing State-Owned Enterprises. Transnet is estimated to be costing the economy as much as loadshedding, at an estimated R1 billion per day.

The RMB/BER business confidence index declined for a fifth consecutive quarter in Q2, dropping to 27 points from 46 points in Q1 2022 while the consumer confidence index fell in Q2 for a sixth consecutive quarter, dropping to -25 compared with -9 in Q4 2021. The SARB's leading business cycle indicator has been on a steady decline since June 2022 when it registered 121.2 points, falling steadily to 110.3 points in April. The South Africa Chamber of Commerce and Industry business confidence index shows a similar pattern, falling continuously since December last year from a reading of 117.3 to 106.9 in May. The manufacturing purchasing managers' index (PMI) dropped further below the critical 50 threshold that signals contraction, from 49.2 in May to 47.6 in June, its lowest since July 2021 when the economy was rocked by widespread social unrest. The survey is forward-looking, signalling further declines in output over the coming months. The five main PMI sub-components were all below 50 for the first time since 2018. The only silver lining is that the future conditions index recovered from 43.7 in May to 52.4 in June signalling an improvement in outlook, perhaps attributed to an easing in power outages in June. The same may have been behind the improvement in the economy wide S&P PMI from 47.9 in May to 48.7 in June.

Loadshedding intensity eased during June as the "energy availability factor" improved to about 60% from a low point of around 50% in May. The improvement is attributed to a reduction in unplanned outages and a rise in renewable energy supply. The registration of private-generation projects has increased and Eskom reports that rooftop solar capacity has almost doubled over the past year, from 2,260MW in July 2022 to 4,040MW in May. It is hoped that loadshedding will lessen in early 2024 as more capacity is added at Medupi, Kusile and Koeberg power stations but even if it is less intense than it has been over the past year, business and consumer confidence are likely to remain depressed.

Consumer price inflation (CPI) eased in May to 6.3% year-on-year from 6.8% the previous month, providing some relief to consumers. Producer price inflation (PPI) also eased by more than expected to 7.3% from 8.6% the previous month, offering hope that the SARB's interest rate hike on 26th May will be the last. The SARB lifted the repo rate by 0.5% to 8.25%, a cumulative increase of 4.75% since November 2021. At the policy meeting the SARB upped its forecasts for headline inflation for 2023 and 2024, only expecting a moderation back to the midpoint of its target range of 3%-6% by the end of 2025. The SARB judged risks to the inflation outlook as still tilted to the upside and quantified the impact of loadshedding on price inflation at 0.5% for 2023. While the economy is teetering on the edge of recession, the SARB has made it clear that inflation

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will continue to be the key driver of its interest rate decisions. The SARB's next policy meeting is on 20th July, the day after the June CPI data is published but there is a strong likelihood the SARB will tighten again regardless of the inflation reading if the Federal Reserve remains in tightening mode, which is now the consensus forecast.

The SARB is acutely aware of the structural impediments to South Africa's economy. In its Financial Stability Review published on 29th May, it highlighted several risks to the country's financial stability. Besides the FATF grey listing, the SARB warned that government's perceived siding with Russia could have severe consequences: "the SA financial system will not be able to function if its is not able to make international payments in US dollars. It could lead to a sudden stop to capital inflows and increased outflows." The SARB also cited the increasingly detrimental and widespread ramifications of an insufficient and unreliable electricity supply and the deteriorating port and rail infrastructure. The Durban-Joburg container corridor is operating at just 25% capacity mainly due to sabotage, theft and corruption. The SARB also cited the burgeoning level of State-Owned Enterprise debt, expressing its alarm at the dwindling foreign appetite for new issuances of government debt.

Certain high impact albeit low probability risks face South Africa's economy and financial markets, including grid collapse, mass social unrest, US sanctions, and an ANC-EFF coalition following the 2024 election. Although there is a low probability of these risks materialising, as South Africa has somehow always muddled through in the past, the scenarios are becoming increasingly plausible given government's lack of structural reform, and therefore increasingly affecting investor sentiment. The JSE All Share index is now valued at a price-earnings multiple of just 9.5x, down from 11.2x at the end of Q1, and a 35% discount to its long-term average. Yet, there seems to be no economic or political catalyst on the horizon that could ignite a market re-rating. SARB governor has repeatedly stated that there is little the central bank can do to revive growth given that the culprits are structural factors. For the foreseeable future investors are faced with the double burden of weak domestic earnings and elevated interest rates. In this environment, fixed income, rand hedge and overseas exposure should protect clients' portfolios and provide better investment returns.

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