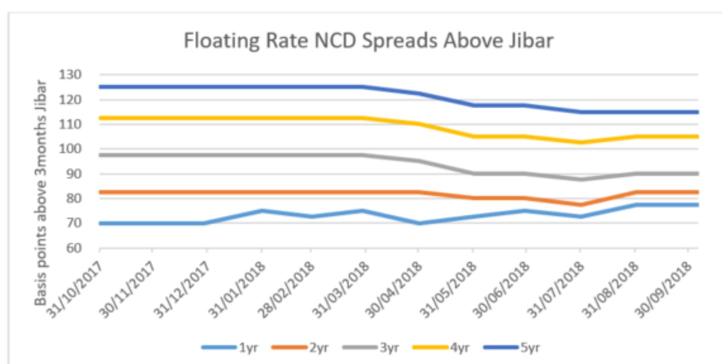
Please note that the commentary is for the retail class of the fund.

The fund generated a return (net of management fees) of 2.0% for the quarter and 8.1% over a rolling 12-month period, which is ahead of the 3-month STeFI benchmark return of 6.9%.

The South African Reserve Bank (SARB) Monetary Policy Committee (MPC) kept interest rates unchanged during the last quarter. Inflation continues to surprise to the downside, with a print of 4.9% y/y in August, falling from the previous level of 5.1% y/y. While there has been some isolated pressure from fuel prices and a weaker currency, food inflation remains low and the benefit of a stronger exchange rate earlier in the year continues to be a tailwind. In addition, the weak growth environment has capped any demand-induced pressure. What is worth noting, however, is that while the Monetary Policy Committee (MPC) left the repo rate unchanged, the vote was split at four votes to three. This does suggest that the MPC maintains a hawkish stance, which is currently being reflected in the market pricing just over two interest rate hikes over the next 12 months. Our current view remains that the MPC will be on hold over the next year, with no breaches in the inflation target band, based on our forecasts.

The 3-month Johannesburg Interbank Agreed Rate (Jibar) index, off which most of the floating rate instruments in the fund are priced, has increased to 7.0%. This compares to an average rate of 6.9% for the prior period. All the floating rate instruments in the fund reset to the prevailing 3-month Jibar rate every three months, post their initial investment date. As such, this increase in the Jibar rate should provide some marginal uplift to the fund yield over the next quarter, providing the current market expectations remain unchanged. As our view is that the repo rate remains constant over the next year, the current yield of the fund is expected to remain unchanged for the foreseeable future.

The last quarter has seen spreads on Negotiable Certificates of Deposit (NCDs) decrease further, continuing the trend which we have been witnessing for most of the year. While we have seen the yield on 12-month Treasury Bills increase to 8.0%, it has still made sense to place excess liquidity with banks, where one can purchase a 1-year NCD at above 8.2%. The contraction in NCD credit spreads continues to be positive for the fund, although the benefit is only received when an NCD is sold back to the issuing bank. As such, there is no immediate yield uplift, but the benefit should materialise over time as the fund routinely creates liquidity by trading in these instruments. Going forward, we continue to see the risks to NCD spreads as being broadly balanced, with the fund being well placed to handle adverse market moves.



Source: Bloomberg

Credit issuance in the primary market remains limited, which is partly a function of the low growth environment. The weakness in GDP growth remains particularly concerning for credit markets from an overall supply perspective. For the eight months ending August 2018, issuance from banks was down 38% with corporate issuance being down 18%. This weakness has been broad based, as evidenced by recent weak asset growth numbers from the banking sector and subdued credit extension.

What further remains challenging is that we continue to see primary issuance come at spreads which are significantly below our fair-value levels. This spread compression seems irrational to us, being driven more by limited supply rather than credit fundamentals. All our credit purchases need to meet our stringent fair-value criteria in order to receive approval from our credit committee.

Our current GDP growth expectations are for 1.8% in 2019 and similar for 2020. However, this is largely predicated on an improvement in consumption expenditure rather than increased fixed capital formation. This does not bode well for issuance levels. Nonetheless, we remain cautious and continue to only invest in instruments which are attractively priced relative to their underlying risk profile. Capital preservation and liquidity remain our key focus areas.

Portfolio managers

Nishan Maharaj, Mauro Longano and Sinovuyo Ndaleni

as at 30 September 2018