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

The fund had a muted quarter in terms of performance, although year to date the return is now 8.5% This is slightly behind the quantitative benchmark, but well head of inflation for the period. The fund's broadly overweight positions in local equity and global equity have helped, but a low weighting to mainly offshore government bonds has detracted, as the property we held in its place has not yet performed.

It continues to be an extraordinary period in markets, as global leadership appears to be seriously adrift. In the US, the sitting president is browbeating the head of the central bank to cut interest rates, even as the economy hits record low levels of unemployment and maintains reasonable levels of economic growth. This, in turn, has once again spurred the search for yield and benefited emerging markets, where yields and currencies have rallied, despite the same US president fighting a trade war with all its trading partners, mainly emerging markets. European interest rates continue to plummet as the European Central Bank has turned equally dovish and negative yields across the yield curve are once again prevalent. Nationalism remains in ascendency in a large number of Western economies and is being increasingly accepted in emerging economies. This trend raises the stakes in trade wars and increasingly the prospect of real wars in the Middle East. Despite this backdrop, equity markets are generally hitting, or getting close to, all-time highs, while volatility (the market standard for measuring risk) is at all-time lows. What a recipe for a disruption! Bull markets in bonds, which imply low growth and low inflation, and bull markets in equities, which generally correlates with high growth and higher inflation, should not be coterminous. Yet, here we are again, with two major capital markets sending conflicting signals, and many pundits proclaiming which is right and which is wrong.

In our offshore exposure, we have generally been well positioned, with a high exposure to emerging markets. These markets have responded well to the decline in interest rates in developed markets and are again enjoying an inflow of money, resulting in strengthening currencies and improving ratings in their equity markets. The S&P in the US, and most European markets, have also done well this year, if not as well as the emerging markets. Where we have detracted over the quarter, is not having any allocation to global bonds. With yields at low levels, we felt it didn't offer sufficient return for the risk being taken (return-free risk). However, the yields have managed to move even lower, with the 10-year US Treasury below 2% again and the German yield curve printing solidly negative yields across most points. Despite these ultra-low rates, the market remains sceptical on property. We have been invested in several European and US retail real estate investment trusts (REITs) and the yield differentials have continued to widen as bond yields have tightened. With blue -chip European retail REITs trading on 8% yields, we believe that the value will ultimately emerge.

Our local equity portfolio has continued to perform ahead of the market, although the lack of exposure to Richemont, a large weighting in the FTSE/JSE Capped All Share Index, hurt us over this period. We have maintained a solid weighting to resources, which have continued to perform well, particularly more recently on the back of significant price increases in iron ore (which we think are unsustainable). Our very low exposure to Sasol has proved highly beneficial as the share price has collapsed on the disclosure that the Lake Charles Chemicals Project in Louisiana has gone even further over budget and is unlikely ever to make a decent return on the vast capital injected to date. With the share price now below R350, we think the risk-reward has moved in our favour and we are starting to add to our position.

The poor performance of the South African economy remains a very worrying trend and has resulted in us maintaining an overweight position in rand-hedge shares, as well as being exposed to mainly defensive South African businesses. The disappointing State of the Nation Address by the recently-reappointed president Cyril Ramaphosa has left the country directionless, with no policy certainty and no tangible plans on how state-owned enterprises and vast public debts will be managed. It has also further exacerbated the low confidence in the outlook from consumers as well as businesses. While share prices and earnings have collapsed in most sectors, the lack of identifiable growth opportunities leaves us extremely cautious on moving too quickly to invest in a local turnaround.

An area that does look compelling, is the real yields available in the local bond market. Our real yields of circa 4% are the highest globally and above a number of other emerging markets that are already rated sub investment grade. We think the concerns over the potential downgrade by Moody's are overdone, and we doubt that the markets would move much should this happen.

Our local property sector has largely missed the rerating that has occurred in bonds this year. Still weighed down by some of the shenanigans that have played out over the last few years, the market is sceptical of sustainable yields and valuations. Add to this the pressure that retailers are under as well as negative reversions in the office and, increasingly, the retail space, investors have not rewarded the sector with an improved rating. For the careful investor, we think this is an opportune time to pick up some of the better-quality property names on attractive yields, and we have been doing so in the fund.

Given the uncertainty alluded to in the opening paragraphs, I am sure that the second half of the year will be eventful. We will hopefully start to see some policy decisions in South Africa, the warm-up for the US presidential elections next year, and the choosing of the Democratic Party contender. Should the market start to see signs of a possible loss for President Trump, he will likely respond with more poorly thought-through rhetoric and policies, the impact of which could be significant. As always, a multi-asset fund such as this portfolio is the perfect vehicle for protecting and growing capital in these uncertain times.

Portfolio managers
Neville Chester and Nic Stein
as at 30 June 2019