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

The Fund returned 2.1% for the quarter, resulting in a return of 25.5% over the last year. The long-term performance of the Fund remains pleasing, delivering an annualised return of 10.9% and alpha of 1.4% per annum since inception.

Global equity markets were stronger over the quarter, with the MSCI All Country World Index up 6.7% in USD (+18.5% over 12 months). Within this, developed markets outperformed emerging markets on the back of higher Covid-19 vaccination rates leading to a further easing of economic restrictions. The discovery of the highly contagious Omicron variant in December of last year threatened to derail, or at least slow, this recovery. Many countries re-introduced travel bans, focused primarily on countries in southern Africa (where the variant was first detected) and accelerated the rollout of booster shots to contain the spread of this variant but, adversely, impacting economic activity (particularly international tourism) over the crucial December holiday period. While there is early evidence pointing to the Omicron variant causing less severe disease, the threat of further variants remains a global concern, particularly where mutations result in lower vaccine efficacy.

On the back of the supply and demand imbalances arising from the pandemic, the upside risks to inflation have increased significantly. Supply chains remain constrained, commodity prices are high, and the labour shortages in the US and parts of Europe are all contributing to elevated levels of inflation at a time when economies are re-opening and seeing pent-up demand from consumers. This has brought forward the need for central banks to tighten monetary policy. In the US, the Federal Reserve Board (the Fed) left interest rates unchanged but brought forward the tapering of its bond purchases at the December Monetary Policy Committee (MPC) meeting. Furthermore, the Fed now expects three 25 basis points (bps) rate hikes to be implemented in 2022 to counter upward price pressure. In the UK, the Bank of England raised its policy rate by 15bps to 0.25% and maintained the size and pace of its asset purchases, while in the euro area, the European Central Bank left rates unchanged but announced that it will reduce the pace of its asset purchases under the Pandemic Emergency Purchase Programme and wind down the programme in March 2022. In South Africa, despite some evidence of weak economic activity during the fourth quarter of 2021, the outlook for interest rates remains for a steady normalisation of the repo rate.

The financial sector performance for the quarter was driven by strong returns from banks (3.2%) and the non-life insurance sector (10.3%), while the life insurance sector (-4.8%) lagged. Throughout 2021, the financial results from the banks showed a faster-than-expected recovery in earnings as bad debts expenses normalised lower and economic activity returned. The provisions raised in 2020 by the banking sector in anticipation of losses incurred because of the Covid-19 pandemic appear to have been conservative. The life sector also raised reserves for anticipated losses from higher Covid-19-related mortality risk, but as more Covid-19 waves came through, they needed to bolster these reserves. The earnings recovery for the life sector has therefore lagged banks as a result, but we believe the sector remains sufficiently capitalised to ride out the Covid-19 challenges.

Contributors to performance for the quarter included underweight positions in Old Mutual and overweight holdings in RMI Holdings, Ninety One and EPE Capital Partners. Detractors to quarterly performance included underweight positions in Investec, Capitec Bank and Absa and overweight positions in FirstRand as well as Momentum Metropolitan Holdings.

In our previous quarterly commentary, we discussed the announcement by RMI to unlock shareholder value by unbundling their holdings in MMI and Discovery to shareholders and create a focused company whose main asset is short-term insurer OUTsurance. During the quarter, RMI enhanced this restructuring by disposing of its holding in Hastings at a very attractive valuation, ahead of our assessment of the Hastings intrinsic value. In addition to achieving a full price, this sale improves shareholder returns by removing the need for RMI to do a rights issue to reduce debt. The sale also enables RMI to move to a dividend policy that returns 100% of free cash flows (FCF), versus the previous 50% of FCF. While these actions have been instrumental in unlocking some shareholder value, we remain optimistic about the long-term prospects of OUTsurance and retain a meaningful holding in RMI in the Fund.

Actions in the Fund this quarter included purchases of Remgro and additions to holdings in Nedbank, FirstRand, Momentum Metropolitan Holdings and PSG, with funding coming from the sale of Absa, Investec, Old Mutual, Coronation Fund Managers and EPE Capital Partners. PSG is a holding company trading at a discount to the value of its underlying holdings. This discount widened significantly over the course of 2020 and presented an attractive investment opportunity. We like the underlying businesses and management have proved to be good capital allocators over the long term, buying back shares at points of significant undervaluation and investing fresh capital into fast growth opportunities in the portfolio. It was pleasing to see the discount narrowing over this quarter in acknowledgement of both the portfolio quality and prudent capital allocation. As with PSG, Remgro trades at a discount to the value of its underlying portfolio of attractive businesses.

The Covid-19 pandemic has disrupted economies and industries significantly over the last two years. Out of this disruption, we have seen opportunities emerge and the strong businesses are taking advantage of these opportunities to bolster their businesses. Some business models have been severely challenged and will emerge weaker out of the pandemic. We are continuously positioning the Fund to own those companies which we see emerging as winners over the long term.

Portfolio managers
Neill Young and Godwill Chahwahwa
as at 31 December 2021