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

The Fund returned 2.4% for the quarter, resulting in a return of 23.5% over the last year. Performance benefited from recovering markets, asset allocation decisions and alpha in the domestic and global equity building blocks. The Fund has performed well against its peer group over all meaningful time periods.

The global recovery continued, supported by high vaccination rates in developed markets and easing economic restrictions. Markets were weaker, reflecting fears that growth would not live up to the high expectations priced in. The MSCI All Country World Index declined -1% in US dollars for the quarter (27% over 12 months). As discussed previously, the Fund has reduced its exposure to global equities, given the high market levels. We do continue to see opportunities for stock picking.

Developed markets (MSCI World Index 0%) were broadly flat, although they fell in September (-4%) as concerns about growth increased. Emerging markets underperformed their developed market counterparts (MSCI Emerging Markets [EM] -8%). Brazil (Bovespa -20%) and China (MSCI China -18%) both had a particularly weak quarter.

Investor confidence in China was shaken by a raft of new regulations across multiple sectors that were invoked swiftly and largely without consultation. While China's authoritarian political system has always posed a risk, recent actions have heightened this. The remit of government interventions widened to include a drive for common prosperity and wealth redistribution, as well as social engineering. These policies are in direct conflict with the economic opening that has taken place over the past few decades. The role that foreign capital will be permitted to play is less certain. Evidence of slower Chinese growth also emerged after a very rapid recovery earlier in the pandemic.

Rapidly increasing global demand put strain on supply chains, resulting in stock shortages and rising input prices. The oil price (Brent crude) rose 5% for the quarter and is now up 92% over 12 months. Higher prices prompted fears that inflation may be less transitory than initially hoped. Labour markets remain tight but may ease as Covid-19 wage subsidies subside. The strong recovery in demand also opens the door to rising interest rates and a tapering of asset support. Indeed, hawkish central bank comments alluded to the latter. High levels of sovereign indebtedness and insufficient yields keep us cautious on global bonds. For the quarter, the Barclays Global Aggregate Bond Index declined -1% in US dollars.

South African (SA) investor confidence was dealt a blow early in the quarter, with the rioting and looting in KwaZulu-Natal. Social inequality and high unemployment (worsened by the pandemic and associated economic restrictions) remain a major concern. An additional Basic Income Grant has been extended to those most in need. The additional grant, ongoing support of state-owned enterprises (SOEs) and a higher-than-anticipated public sector wage agreement further strained the fiscus. SA needs sustained economic growth to heal its fiscal woes. The decline in prices of some of SA's key export commodities (iron ore -28% in Q3-21 in US dollar and PGMs) is a threat to the current account surpluses that have supported the rand. The local currency declined -5% against the US dollar for the quarter. While the quarter heralded a disappointing number of setbacks to the fiscal outlook, the government remains committed to fiscal discipline. The new Minister of Finance is not expected to make any major changes. The All Bond index delivered 0% for the quarter. The Fund has meaningful exposure to SA bonds, with the long end of the curve offering very attractive yields in both absolute terms and relative to other emerging markets and alternatives such as cash.

SA's vaccine rollout has been slow to ramp up, with 20% of the adult population now fully vaccinated. Easing Covid-19 infection numbers have supported a lowering of restrictions, with the country moving to level 1 at the end of the quarter. The risk of further waves remains given low levels of vaccination.

The Fund's exposure to SA equities is sitting at a decade high, given the breadth of value across many sectors, including resources, locally-listed global stocks and domestic shares. For the quarter, the JSE Capped SWIX Index delivered 3% in rands. The financials index returned 12% as banking earnings continued to improve, fuelled by a faster than expected recovery in bad debts. Industrials declined -4%, as major constituent Naspers (-17%) dragged down the index return. The resource index also declined (-4%) as global growth concerns and commodity price pressures weighed on a number of stocks.

The Fund has long had considerable exposure to a number of global businesses that are listed in SA. Major holdings include Naspers (-17%)/Prosus (-15%), Aspen (69%), Bidcorp (4%), British American Tobacco (-1%), Quilter (-0%) and Textainer (13%). All are attractive for stock-specific reasons.

Naspers came under considerable pressure during the quarter as regulatory intervention in China intensified. Within the technology sector, much of the regulation is consistent with what is seen elsewhere, including those governing fintech, antitrust, competition law, data security, protection of personal information and gig employee labour protection. More specifically, for Tencent, government attempts to protect minors means increasing restrictions on time spent gaming. Thus far, none of the restrictions is expected to change Tencent's prospects meaningfully. However, the breadth and depth of Chinese regulatory intervention and the amplified threat to foreign capital have increased the risk of any Chinese investment. Valuations now look extremely attractive, with Chinese technology businesses trading at considerable discounts to their developed market peers. Tencent is a formidable company that generates good free cash flows, has a very engaged user base, and is growing businesses across multiple verticals. At the Naspers/ Prosus level, investors benefit from an undervalued rump where management has been achieving good returns on recent portfolio actions.

Aspen delivered strong returns for the quarter (+69%), bringing 12-month returns to 130%. While organic delivery has been pleasing, the more recent share price performance stems from two specific opportunities. Aspen is under cautionary related to the potential disposal of its API business, which is expected to be accretive. More materially, Aspen could potentially benefit from a vaccine licensing deal from J&J, which would materially increase its revenues.

Domestic companies continued to report results ahead of our expectations due to more resilient economic activity and stringent cost-cutting. We are concerned about the secondary effects of this cost-cutting and the ongoing weak employment numbers.

Like many holding companies, RMI (+20%) has seen the discount (at which it trades to the value of its underlying parts) widen over the last few years. We believe this undervalues some of the attractive assets it owns, including OUTsurance, an unlisted short-term insurer with a strong history of delivering earnings growth while achieving high levels of cash flow conversion. We have had many engagements with RMI management over the years about how this value could be unlocked and were pleased to note the restructuring announced in September. RMI intends to unbundle its holdings in Metropolitan Momentum and Discovery to shareholders leaving a smaller, more focused company with its major holdings in short-term insurance (OUTsurance and Hastings). RMI has also committed to paying out 50% free cash flow to shareholders. Although a capital raise in the form of a rights issue will be required to achieve this, the restructuring and higher pay-out are undoubtedly positive. We hope that these are the first steps on a journey to further improve shareholder returns by passing through more of the underlying dividends.

The portfolio has a small overweight in resource shares, which comes from the holdings in the diversified miners. Holdings in Glencore and Anglo American have contributed strongly to performance over the past few years, but we believe they continue to offer good value. They trade on low multiples with solid free cash flow generation and attractive upside. We are not bullish on all commodities but expect an accelerating global drive to decarbonise to create increasing demand and tight markets in commodities like copper, cobalt and nickel. Glencore is particularly well exposed.

The portfolio has continued to increase its holding in gold equities, which offer upside and reasonably priced protection against stretched sovereign balance sheets and high global market levels. Both AngloGold and Goldfields have improved their production profiles and geographic diversification. We anticipate a period of increased returns to shareholders under their new leadership teams. These positions have been funded by taking profits in the PGM shares.

The portfolio has moderate property exposure, preferring to use its risk budget in equities and bonds. Holdings are predominantly in the A shares, with some exposure to logistics assets. The medium-term outlook remains subdued as a weak economy and a structural shift in demand from increasing digital engagement and work-from-home trends undermine rental tension. Several sector balance sheets remain undercapitalised.

Markets are ever-changing. The significant disturbance wrought on the world by Covid-19 has accelerated disruption in many industries while placing significant pressure on sovereign balance sheets. The sweeping changes effected by the pandemic has created opportunities where longer-term consequences are being mispriced. We constantly challenge our beliefs to enable us to take advantage of these opportunities.

Portfolio managers
Karl Leinberger and Sarah-Jane Alexander
as at 30 September 2021