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

Performance

The Fund had a strong finish to the year, returning 14.4% in the fourth quarter (Q4-22), which was slightly behind an even better benchmark performance of 15.7%. For 2022 as a whole, the Fund outperformed the benchmark by 4.4%, which contributed positively to its longer-term track record relative to the benchmark.

Persistent hawkishness from the US Federal Reserve continued to play a key part in the pricing of equities (and other financial assets) in the quarter, as more interest rate hikes were put through. Added to this, was the rising probability of recession in many parts of the world.

China was the other key driver of local market performance, given the sizeable contribution the country makes to the fortunes of two of the largest industrial companies in the benchmark (Naspers/Prosus and Richemont). President Xi Jinping secured a third term at the governing party's national congress in October, which allowed the government more room to turn its attention back to economic growth. This included providing a bit more clarity on recent regulatory changes and substantially unwinding the restrictive zero-Covid policy (which was having a meaningful stifling effect in this regard). A very strong November performance from the abovementioned shares drove the bulk of benchmark returns in Q4-22.

Here in South Africa, a surprisingly strong Q3 GDP print gave way to the underlying headwinds faced by the local economy. Slowing growth and an escalation in the amount and severity of load shedding, which was made worse by the impending loss of two senior officials – COO and CEO. The ANC also hosted its elective conference in December, where against consensus expectations, Cyril Ramaphosa comprehensively retained presidency of the party, with an executive that has a strong representation by his allies.

What worked well for the Fund during the quarter, was our underweight positioning in a number of SA retail names – Clicks, Shoprite and Mr Price. While all high-quality companies within their sectors, they are also very highly rated versus peers and the benchmark. As domestic industrials broadly underperformed during Q4-22, this basket of stocks added more than 1% of outperformance for the Fund. Another notable contributor was the Fund's underweight position in paper company Mondi, which added 0.4%.

On the detractors side, three overweight positions featured strongly. Taken together, these stocks were responsible for more than 1% underperformance during the quarter. UK software licencing reseller Bytes, SA ICT business Altron, and food retailer Spar, all reported results during the period – in all three cases the market took a dim view either of the result itself, or the prospective outlook (both operational and strategic). Post results we continue to believe the earnings power of these businesses remains intact, and the shares are trading on undemanding forward PE multiples (Spar and Altron both under 10 times; Bytes trades on a 19 times, but is growing earnings in excess of 20%). Our underweight in luxury goods company Richemont also hurt.

Fund positioning

Incidentally, the Fund's biggest buy in Q4-22, was Richemont. After delivering strong revenue growth for the full year to May, earnings came in below expectations. The share reacted poorly to these numbers and continued to languish for much of 2022. We then took the view that the strong revenue trends could continue into their new financial year, while the earnings would be more resilient than what was being priced in. When the H1 results were released in November, we were pleased to see a strong share price reaction. We also added to our position in telecommunications company MTN, whose share price remained depressed. Anheuser-Busch InBev also deserves a mention in the buy column.

Sells during the quarter largely came from the rand hedge stocks. These included Naspers, British American Tobacco, and Richemont (post the share price jump). We also sold some Barloworld, which had done well from levels we had bought it at.

Outlook

With the new year having begun, industrial shares have, pleasingly, had a good start to the year. Despite the challenges that are out there, both locally and globally, we are excited about both the current positioning of the Fund and the return potential from its holdings.

Portfolio managers
Tumisho Motlanthe and Nicholas Hops
as at 31 December 2022