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

Performance

The Fund returned 5.4% for the quarter and 6.7% for the full year. The Fund's long-term performance remains pleasing against the peer group and benchmark.

Fund positioning

The top contributors to relative performance in the final quarter of the year were Quilter and Dis-Chem as both stocks rose strongly. Detractors were Sasol, which we own, and Gold Fields, which we do not own. Over the full year, Standard Bank was the top contributor to the Fund.

After a few soft months when markets were pricing in "higher for longer" interest rates, global equity markets had a strong end to the year in November and December because of a sharp reversal in interest rate expectations, which fuelled equity market returns for the quarter. US 10-year borrowing costs peaked at just north of 5% and dropped by ~120 basis points to end the quarter below 4%.

We meaningfully altered our resources exposure within the Fund this quarter, with BHP Billiton (BHP) and Glencore being sold to zero. African Rainbow Minerals (ARM) is a new entry to the Fund as we took advantage of a ~50% drawdown in the stock price since earlier in the 2023 calendar year. In addition, we added to several of the core industrial holdings with the balance of the BHP and Glencore proceeds. BHP and Glencore were sold after strong rallies in both names and a diminished margin of safety. When it comes to commodity companies held in the portfolio, we demand a higher margin of safety compared to other companies.

The Fund has not owned ARM since 2014, and its share price at present is very close to its 2014 levels. ARM is a South African miner with just over half of its fair value represented by its iron ore exposure. Platinum Group Metals (PGMs) make up just under one quarter of fair value, and manganese, coal and gold make up the remainder. From an earnings perspective, the rally in the iron ore price has been offset by the decline in PGM prices and we expect ARM earnings to be stable in 2024 and grow from that base as volume growth contributes across the business.

From a sentiment perspective, ARM is currently suffering due to its investment in the Bokoni PGM asset and its exposure to PGMs overall. Having bought it at the top of the PGM cycle, ARM is now facing an inflated capital bill and likely higher operating costs when it ramps up compared to its initial estimates. We carry Bokoni at *minus* R4 billion in our valuation and still find ARM attractive. ARM is trading on ~4 times earnings, and with 35% of its market cap in cash, it is defensively positioned. Having been a consistent dividend payer historically we are more confident that shareholders will receive their share of cash profits from ARM than most of its mining peers. In conclusion, we believe that ARM owns several reasonable quality assets, trades with a large margin of safety and an attractive dividend yield on a growing earnings profile.

Quilter enjoyed a strong run in the quarter and finished the year 28% higher than where it started. While Quilter has been a strong contributor over the last year, it has detracted from performance over longer time horizons. We have not reduced our position size in this rally as we believe the business remains one of the cheapest in the market. In buying Quilter one gets exposure to an industry with multi-decade tailwinds as the UK shifts from defined benefit savings to defined contribution savings and pushes more of the onus onto the consumer. Quilter's new CEO is driving strong operational change. With UK assets not being in favour (Brexit, tough macro), one can buy Quilter on a PE ratio of 12 times and dividend yield of >5%, which we see as attractive for a hard currency earnings stream with strong growth prospects.

Standard Bank was the top contributor to relative performance in the year and was complemented by Nedbank as interest rates drove banking sector earnings back to pre-Covid levels. Due to business mix and hedging policies, Standard Bank and Nedbank are the most sensitive of the Big Four banks to the interest rate cycle, and this came through well in the period. Standard Bank produced excellent interim results in August, coming in ahead of expectations. Their long-term investment into building a business in the rest of Africa has added significant value for shareholders as the region contributed 44% of earnings in the six-months reporting period. Having built a broad-based African business, we expect this franchise to continue growing ahead of the South African business, a unique differentiator compared to its peers. Despite Standard Bank's strong rally, it still trades on a 7% dividend yield, amongst the highest in the market, and should be able to grow real earnings off this base. It remains a key position in the Fund.

Lastly, we increased our Spar weighting in the quarter as the share price remained soft, and our fair value assessment remained more than 100% above spot levels. With a new CEO emboldened by a strong Chairman, we have seen decisive action from the business in 2023, which should deliver value for shareholders in the long term. A decision was made to exit the loss-making Polish business, the cost base is being addressed in South Africa and their online delivery division is gaining traction. Spar is trading on nine times what we believe is a very depressed earnings base, with the potential for earnings to grow at a compounded growth rate of 15% over the next five years.

Outlook

We believe the Fund offers attractive upside in absolute and relative terms, with a high hurdle being set by expected domestic equity returns.

Portfolio managers
Neville Chester and Nicholas Stein
as at 31 December 2023