

Discovery Equity Fund

Quarter ending 30 June 2024

Market background

It was a mixed second quarter (Q2) for global capital markets. In the US, the S&P 500 reached another all-time high, fuelled by big-tech euphoria and growing optimism over the possibility of a rate cut later this year. In Europe, gains for far-right parties in the European Parliamentary elections led French president Emmanuel Macron to call a snap election, putting equities under pressure. In Asia, Hong Kong and Chinese mainland stocks fell for the second consecutive month in June, with markets lethargic ahead of the July meeting of China's top leaders. Turning to South Africa, the national elections took centre stage as the prospect of a market-friendly outcome gained momentum, lifting domestic equities higher.

Performance review

For the quarter the portfolio underperformed the benchmark.

Among the largest detractors from relative performance was the portfolio's overweight position in Telkom. Our decision to hold an overweight position in the telecommunications company was influenced by strong earnings expectations and positive signals in the momentum and value categories. Within the value category, positive book yield and cash flow yield were the main drawcards. Also weighing on relative performance was the portfolio's underweight exposure to Anglo American. Our underweight allocation to the global mining company was influenced by poor earnings expectations, negative momentum indicators, and weak quality signals. Specifically, revenue growth factors were the main drawbacks within the quality category.

Contributing to relative performance over the period was the portfolio's overweight exposure to Mr Price Group. Our overweight position in the retailer was based on strong earnings expectations and positive signals in the quality category. Within the quality category, key characteristics included capital utilisation, revenue growth and low volatility. Also adding to relative performance over the period was the portfolio's overweight position in Momentum Metropolitan Holdings. Our overweight exposure to the financial services group was largely driven by strong signals in the quality and value categories. Within the value category, the company's cash flow yield and earnings yield stood out as the main positive characteristics; while in the quality category, low volatility and positive capital utilisation were the main contributing factors.

Outlook and strategy

The portfolio's investment philosophy and process aim to deliver consistent returns for investors. We follow a multi-style investment approach which is dynamically adjusted to ensure that relative risk is actively managed throughout the business cycle. We prefer shares that are trading at a discount relative to the market, with positive momentum, positive earnings expectations and low downside risk.

Some of the portfolio's largest overweight positions include Investec Plc and Momentum Metropolitan Holdings, while significant underweights include Bidcorp and Shoprite Holdings.

In our view, Investec Plc displays strong positive valuation, earnings expectations, and quality; while Momentum Metropolitan Holdings displays strong positive quality and valuation. Positive quality refers to good financial health, low volatility and downside risk, while positive value indicates that the stock is trading at an attractive value.

In terms of the portfolio's underweights, in our view, Bidcorp displays negative momentum, valuation, and quality signals; while Shoprite Holdings displays negative momentum and value.