Discovery Balanced, Moderate Balanced, Cautious Balanced Funds

Market background

Global equities had a strong quarter, with several markets reaching all-time highs. That was driven by growing hopes for a soft economic landing, or even a 'no landing' in the US, along with ongoing optimism around artificial intelligence (AI). The S&P 500 Index posted consecutive double-digit gains for the first time in over a decade, while in Japan, the Nikkei saw its strongest performance since the global financial crisis.

Chinese equities were lower over the quarter, but there was a sharp positive momentum swing in February, just before the Lunar New Year holiday, when the Chinese authorities decided to intervene to help stabilise sentiment towards an equity market which had declined to five-year lows.

Within defensive assets, US treasury yields rose across the curve, while in Europe, 10-year yields climbed, notably in Germany and France, with yields in the UK also rising. Emerging market bond returns were marginally positive over the period.

In SA, despite equities performing better in March, declines earlier in the year saw equities close the first quarter in negative territory. Weighing on performance were financials and resources, while industrials managed to eke out a positive return. Encouragingly, a sharp rise in precious metal prices in March lifted the broad index, largely supported by platinum group metals (PGM) miners and gold miners.
Gold ended the quarter 8% higher.

To read more, please click here or visit the Insights section of www.ninetyone.com.

Performance review

The portfolio delivered a positive absolute return in March and over the quarter.

Key positive contributions:

We note the following contributors to performance over the last quarter:

- Global equities were strong with standout performers:
    - Semi-conductor holdings TSMC, KLA and ASML as well as big tech Microsoft
    - Energy stocks: ExxonMobil, BP
    - Industrials: Trane Technologies, Schneider Electric
    - Financials: JP Morgan, Mastercard and Bank Rakyat
- SA-listed property decoupled from SA bonds, delivering a positive contribution to returns
- Naspers, Prosus and Richemont performed well in a negative local equity market backdrop as China sentiment improved, while BidCorp performed well after solid results. Our holding in Gold Fields also had a strong quarter
- The rand weakened, supporting returns of the offshore holdings

Key negative contributions:

- SA bonds and global bonds
- 'SA Inc.' stocks which fell out of favour
- Defensive holdings: global property, utilities such as Iberdrola and Enel Spa
- Diversified miners: despite the uptick in China following the National People's Congress, investors remained cautious about the economic recovery.

Activity

In response to market volatility, we continue to make strategic adjustments to our equity holdings. During the quarter, we initiated a position in Constellation Brands, Canadian National Railway and Siemens. We also
topped up our positions in Google, KLA, and Samsung, capitalising on a temporary dip in their share prices while maintaining confidence in their fundamentals. Additionally, we bolstered our investments in select South African retailers and banks, where we have strong conviction in their earnings potential. Finally, we took advantage of a pullback in gold stocks earlier in the quarter and added to our positions in this sector.
Conversely, after a strong performance, we sold **Waste Management** and **Bank Rakyat** and trimmed our position in Mastercard. Overall, our net equity position has increased slightly.

We increased duration on **SA bonds** taking the position to neutral on the back of news that the SA government planned to tap GFERCA funds to help reduce the country's debt burden. The portfolio is now neutral duration versus the benchmark. We continue to hold our position in **European bonds** which we believe will add value as evidence of the economic slowdown in the eurozone continues to build, which we believe will force the European Central Bank's (ECB) hand to cut rates. We did, however, decrease duration on German bunds, and took profits here. We sold our South Korean bonds to zero earlier in the quarter following a strong run and sold some Australian bonds on strong performance. The result was a net decrease in our global bond holdings.

The portfolio has a healthy cash balance, which continues to yield an attractive risk-free return. This dry powder in cash puts us in a better position to take advantage of future opportunities.

Outlook and strategy

The quarter ahead has two very key events:

- Globally – will we start to see the first rate cuts in developed markets? We believe there is stronger evidence on weak growth and inflation for the ECB to cut in June, while inflation data over the next two months in the US will determine whether the Federal Reserve (Fed) can also cut rates this quarter. This matters for emerging market risk assets as they tend to do well when the Fed is easing.
- The South African elections, scheduled for 29 May will likely elevate noise and therefore increase volatility. While we do not position the portfolio into election outcomes, we pay attention to results, which inevitably create new risks and opportunities.

Currently, the market has shifted into a reflation regime on the back of two of the largest economies' (US and China) manufacturing data pointing to being in expansion territory again after an extended period of contraction.

- In the **US**, we continue to see a two-speed economy: while manufacturing data is showing early signs of green shoots, the services sector is slowing, but still in expansionary territory. The labour market remains strong, and incomes continue to grow, ensuring that the economy remains resilient.
- In **China** economic data is improving; consumer spending has trended upward over the holiday season, surpassing 2019 levels. In addition, manufacturing PMI's have turned positive. While there is the risk of a stop-start recovery, the Chinese government's focus on strategic sectors such as renewables, technology and infrastructure is likely to remain, and will be supportive of commodities. The recent policy conference confirmed that while the property sector is not a focus area for growth, it is a core focus area for authorities to stabilise and bring confidence back to the consumer. This is the area that is causing the stop-start recovery as they do need to boost confidence to get the wheels turning more smoothly going forward.

As a result of this reflation regime, various commodities have been rallying in recent weeks. This is supportive of our positions in the resources sector. If this continues at the current pace, it does pose a risk to the inflation trajectory in the US in the second half of the year. This is something that we are watching closely.

Over the quarter, opportunities were presenting themselves from a bottom-up perspective as earnings bases reset and/or share prices pulled back. We deployed some of our dry powder into stocks on our 'buy' list and will continue to do so in the months ahead. Our equity mix remains tilted towards companies with strong earnings fundamentals at a reasonable valuation. Our allocation to SA bonds is supported by a strong yield underpin. We expect our global bond allocation, which has a large proportion allocated to European bonds, to add value to the portfolio in the coming months as the ECB cuts interest rates. In addition, we do have cash reserves in hand and will take advantage as opportunities present themselves.

DISCLAIMER:

Discovery Life Investment Services Pty (Ltd): Registration number 2007/005969/07, branded as Discovery Invest, is an authorised financial services provider. Product rules and terms and conditions apply.

The views and opinions expressed in this article are for information purposes only and should not be seen as advice as defined in the Financial Advisory and Intermediary Services Act. Discovery shall not be liable for any actions taken by any person based on the correctness of this information. For full details on the products, benefits and any conditions, please refer to the relevant fact file. For tailored financial advice, please contact your financial adviser.

For the full CIS disclosure and risk statement, go to:
CIS disclosure:
http://www.discovery.co.za/assets/discoverycoza/corporate/cis-disclosure.pdf
Risk disclosure:
http://www.discovery.co.za/assets/discoverycoza/corporate/risk-disclosure.pdf