Discovery Balanced, Moderate Balanced, Cautious Balanced Funds

Market background

Risk-off sentiment and volatility persisted throughout the month, but in the final week risk markets pared back some of the losses suffered earlier in the month as China eased some COVID-19 restrictions, allowing some key economic hubs to reopen, while in the US, the tone of central bank meeting minutes was judged to be somewhat on the softer side, providing a short-lived shot in the arm for risk sentiment.

Developed market equities (MSCI World Index) returned to positive territory, up 0.2% for the month, but were somewhat outdone by their emerging market peers (MSCI Emerging Markets Index), which posted gains of 0.5%. Regionally, the benchmark US S&P 500 Index snapped its string of weekly losses, eking out 0.2%, as investors appeared to unwind some of their short positions/bets against the market. Across the Atlantic, the pan-European Stoxx 600 Index enjoyed a positive spell to end the month up 1.1% as investors 'buying the dip' piled into European shares at attractive entry levels. In Asia we saw Japan's Topix close up a healthy 2.6% for the month, while China's blue-chip CSI 300 Index closed 1.1% higher.

In fixed income, investors sought refuge in bonds as the focus shifted from (problematic) inflation to (weaker) growth. Government bond yields edged lower (yields fall as prices rise) amid growing concerns that aggressive quantitative tightening (QT) by central banks could tip economies into a recession. The bond market rally saw the global benchmark (US 10-year Treasury) yield settle back down from its three-year high of 3.20% earlier in the month to 2.84% at the time of writing. The Bloomberg Barclays Global Aggregate Bond Index ended the month up 0.3%.
All returns are quoted in US dollars.
South African stocks ended the month flat, with the FTSE/JSE All Share Index recording a third straight month of losses, down 0.4%, while the Capped SWIX eked out +0.5% for the month. At a super-sector level, financials gained 3.0%, while resources (-0.4%) and industrials (-2.2%) ended in the red. Among yield-oriented assets, South African government bonds held the upper hand on their equity peers, with the JSE All Bond Index registering a 1.0% gain over the month, despite foreigners being net sellers over

the period and auction activity reflecting weakening demand from local investors. Listed property extended losses, down 0.3%. Cash, as measured by the STeFI Composite Index, returned 0.39% over the period. In currencies, rand volatility persisted, with the local unit losing ground against the euro, but firming against sterling and the greenback.

Performance review

For the month, the portfolio delivered positive absolute returns.

Key positive contributions:

- The allocation to South African Government Bonds added to performance over the month.
- Within local equities, allocation to South African banks and diversified miners (Anglo American, BHP Group and Glencore) contributed strongly to returns over the month. Returns were further enhanced by our holdings in British American Tobacco as well as Naspers and Prosus.
- Within offshore equity, exposure to oil and semi-conductor companies enhanced returns over the month. Geographically, the allocation to Chinese equities also added value.

Key negative contributions:

- Holdings in Life Healthcare, Gold Fields and Sibanye-Stillwater detracted from returns within the local equity component.
- In the offshore leg of the portfolio, the allocation to Intercontinental Exchange, United Health Group, Aon and Moncler detracted from returns over the month.
- ZAR strength over the month detracted from the offshore exposure.

Portfolio activity

Within the local equity component, we took some profits by trimming our holdings in South African banks (Standard Bank Group, Capitec Bank and Investec) and paper and pulp maker Sappi, following recent strength. We also continued to trim exposure to Quilter, as the risk of negative earnings revisions has increased amid prevailing weak market conditions. Some of the proceeds were used to add to our existing position in British American Tobacco (BTI), Anglo American and Shoprite on share price weakness, where we continue to believe the earnings revisions, cycle is supportive with reasonable valuations. We also allocated some capital to a new position in Bid Corp on weakness as the business is benefitting from lockdown reopenings in various regions and increased market share due to its continuous investment in the business through the COVID-disrupted periods.

Outlook and strategy

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Looking forward, we will continue to monitor the data points feeding into inflation in the US as this will have an impact on the extent of policy adjustment to be taken by the US Federal Reserve post the well telegraphed further two 50bps hikes at the upcoming meetings.

To navigate the current backdrop, in recent months, we have moderated our exposure to pro-cyclical assets in favour of more defensive assets and we continue to move to a more neutral overall equity exposure. We still, however, maintain a preference for South African equity over offshore equity. In the context of a rising interest rate environment and QT, one cannot rely on the expansion of valuations to contribute to returns. Earnings and dividends will drive the bulk of the return for investors in such an environment. The South African equity market has more valuation support as it did not enjoy the multiple expansion seen in developed markets. This, coupled with strong earnings revisions profiles across our holdings, has tilted the portfolio to the domestic market.

Regionally, in our offshore equity allocation, we continue to have a positive skew towards Asia as Chinese markets continue to exhibit reasonable valuations after the high-risk premium embedded in the stocks post the regulatory crackdown in 2021, while earnings have upside over the medium term, in our view. And as the reopening of the economy takes hold post the lockdowns and China's government policy is on an easing path.

The local equity composition is well diversified. Our defensive exposure is in the Naspers-Prosus stable, where earnings revisions appear to be troughing and sentiment is weak. We also continue to hold the position in BTI – we believe that the earnings revisions profile is at an inflection point as the loss making businesses start to improve, as well as the business doing share buybacks. This sits alongside an allocation to global cyclical stocks (diversified miners, Sappi, Mondi, Sasol) continuing to exhibit favourable earnings revisions profiles. Most of the exposures in this bucket are benefitting from tight commodity markets and low inventory levels, in our view. We also continue to have a healthy allocation to South African banks, where earnings revisions are strongly positive, and valuations are attractive. This sits alongside our exposure to select apparel retailers which display good earnings revisions profiles, trading at reasonable valuations. Our exposure to local defensive businesses has increased steadily over the past 12 months. This is mainly due to our holdings in MTN Group, Life Healthcare and Shoprite.

We maintain the material allocation to local sovereign bonds, especially within the context of the global fixed income universe. Within fixed income, we believe that the high income from South African sovereign bonds will continue to buffer the asset class through the volatility being experienced in global fixed income markets.

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