Discovery Target Retirement Date Funds

Market background

April was reasonably calm for global financial markets. Just one month after narrowly avoiding a potential global banking crisis following the collapse of Silicon Valley Bank, investors were met with the news that First Republic Bank was on the brink of collapse and that JPMorgan Chase & Co. would take over the bank's remaining assets. Fortunately, much of the fallout was contained, and by one measure (the VIX index), April marked the least volatile month since the pandemic.

Returns across global financial markets were fairly subdued but broadly positive for the month, as investors weighed the prospect of a slowdown in global economic growth and stubbornly high inflation against a potential economic resurgence in China. For April, global equities as measured by the MSCI All Country World Index returned +1.4%. Developed markets outperformed emerging markets, with the MSCI World Index returning +1.8%, while the MSCI Emerging Markets Index ended the month down by 1.1%.

Global bonds (Bloomberg Barclays Aggregate Bond Index) delivered a modest +0.4% for the month, largely on the back of positive gains across credit markets.

All returns are quoted in US dollars.

Local equities closed the month broadly firmer, in line with international markets. For April, the Capped SWIX gained 3.4%. Resources advanced 4.0%, led by gains in precious metals and mining sectors (+14.6%). Industrials added 3.1%, supported by stronger tobacco (+7.2%) and personal goods (+6.4%) sectors. Financials closed 3.4% higher, with real estate investment and services (+8.8%) the standout performer. The FTSE/JSE All Property Index gained 5.8% for the month, while the JSE All Bond Index fell by 1.1%. Cash, as measured by the STeFI Composite Index, delivered +0.6%. In currencies, the rand closed the month weaker against the US dollar, euro and pound sterling.

Performance review

For the month, the portfolio delivered a positive absolute return.

Key positive contributions:

- In a mildly positive backdrop for local and global equities:
  - Within the SA equity component, AngloGold, FirstRand and the platinum-group metals (PGM) miners (Northam Platinum & Impala Platinum) were strong contributors to returns. Exposure to SA hospitals (Life Healthcare & Netcare) also added to returns.
  - The offshore equity component notably benefitted from holdings in Microsoft, Rentokil, BP, and Bank Rakyat.
- The rand weakness over the month was a tailwind for the portfolio's offshore earnings.

Key negative contributions:

- Within the mildly positive backdrop for SA and global equities over the month, notable positions that detracted from returns are:
  - Diversified miners (Anglo American and BHP Group) and our allocation to the Naspers-Prosus stable detracted from returns for the month in the local equity component.
  - The offshore equity's allocation to Alibaba, JD.com and Universal Music Group were notable detractors over the month.

SA Bonds detracted from absolute returns for the month. Our exposure to South Korean and Australian bonds also held back returns.

Portfolio activity

Within the SA equity allocation, we increased positions in holdings Anheuser-Busch InBev and Richemont, at the expense of SA cyclicals (exiting our position in Nedbank Group and trimming Capitec Bank) as we allocate capital to areas with stronger conviction on earnings revisions profiles. We were net sellers of SA equity over the month and retain cash proceeds as dry powder to take advantage of availing opportunities in the coming months, given expected market volatility.

Outlook and strategy

The credit growth outlook for the US is rapidly weakening given the weakness in the regional banking system and is evident in the recent lending surveys. This is likely to pressure growth in the months ahead and confirm our base case for a weak growth outlook in the second half of the year. In addition, global liquidity tailwinds from recent months are turning into headwinds in the months ahead. Furthermore, China's reopening is proving to be an uneven recovery, given bottlenecks and no further strong stimulus measures by authorities. This will likely result in a slower recovery than seen in other economies following their COVID reopening.

The market is also starting to downgrade growth expectations for the SA economy, as we are unfortunately grappling with electricity concerns and what may turn out to be a tricky winter period to navigate. In addition, SA CPI surprised to the upside and made the South African Reserve Bank (SARB's) decision to hike by a surprise 50bps at the end of March, when the market was expecting 25bps, particularly clairvoyant. We will continue to look for opportunities to lower our bond exposure as well as rotate into shorter-duration SA bond assets. This will likely result in continued volatility in risk assets in the period ahead.

We expect continued volatility in risk assets in the period ahead and therefore have a lighter overall equity exposure with a preference for, albeit reduced position, in SA Equity over offshore equity. We continue to believe the valuation support (SA did not enjoy the multiple expansion seen in developed markets), coupled with strong earnings revisions profiles across our holdings, has tilted the portfolio to the domestic market. The earnings revisions have prompted us to increase positions in defensive exposure at the expense of SA cyclicals within the local equity component. Developed market equities (after the recent rally) are now fully valued and do not yet reflect the high likelihood of earnings downside risk to due record margins and sales levels in the goods side of the economy as it declines towards trend. The offshore stock selection continues to favour a position in Asia ex-Japan equities, to benefit from the expected consumption tailwinds from China, while developed market exposures are tilted to more defensive sectors (healthcare, utilities and real estate), given the earnings risk in cyclical sectors such as consumer discretionary and industrials.

As we near the end of the global hiking cycle, our position in defensive government bonds focused on high-grade nations with leverage and housing imbalances (Australia, New Zealand, South Korea, Canada and Sweden) should enhance returns of the overall portfolio.

