Discovery Balanced, Moderate Balanced, Cautious Balanced Funds

31 October 2024

Market background

October was a volatile month for markets, with global equities moving lower after a sell-off at the end of the month. Global growth risks remained the primary concern for investors, who were spooked by some underwhelming earnings releases. Uncertainty was also heightened by the impending US election and the potential policy implications. Emerging market equities – particularly Chinese stocks – underperformed developed markets. That said, US equities fell for the first time in six months, partly due to the 'Magnificent 7' earnings updates disappointing investors.
In Europe, sentiment was subdued, and equities lagged other developed markets. Japanese equities, however, gained on the back of a weaker yen amid political uncertainty, with the ruling LDP losing its parliamentary majority. Chinese stocks, having started the month strongly, gave up their gains as markets were disappointed by the lack of significant new fiscal spending announcements from Beijing, and speculative positioning eased.

Yields across government bond markets rose in October, resulting in negative total returns in fixed-income markets. This was most pronounced in the US and UK.

In South Africa, equities delivered their first negative performance since the formation of the Government of National Unity (GNU) earlier this year. Global dynamics contributed to investor caution, including the upcoming US presidential election, uncertainty relating to the implementation of China's latest round of stimulus measures and rising geopolitical tensions in the Middle East. Investors also kept a close eye on US economic data for signs that could influence the pace of the US Federal Reserve's (Fed's) interest rate cuts.

Gold continued its march upwards, in the face of geopolitical tensions and rate cut expectations, ending the month up 4% at US$2,744.

Performance review

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

Key contributors:

- Global equities delivered positive returns in rand terms (but not in USD)
- Discovery, Capitec, and Truworths International performed well
- Gold and platinum shares: Gold Fields, Agnico Eagle, AngloGold Ashanti and Impala Platinum
- Semiconductor holdings: Nvidia, TSMC
- Visa and Mastercard, after posting good results
- AECom and General Motors, bucked the global risk-off trend, performing well
- Weaker rand benefitted the offshore holdings in the portfolio

Key detractors

- China stocks saw profit-taking in the month, as no further stimulus measures were announced
- Microsoft: lost momentum following its results, which exceeded expectations but guidance for its cloud business disappointed due to supply constraints
- 'SA Inc.' shares sold off in line with SA bonds sold

We made several changes to the portfolio during the month. We reduced our German bund holdings earlier in the month to take profits after a strong rally and similarly trimmed our SA bond holdings. We reduced our positions in Gold Fields and Harmony Gold due to price strength and did the same with Shoprite. Bidcorp was sold to lock in profits, as our analyst expectations no longer exceeded market expectations. We fully exited Zalando following a strong trading update and took some profits on US retailer Tapestry after the FSCA blocked the deal. Additionally, we trimmed Richemont as our growth expectations have diminished.

On the other hand, we increased our holding in the London Stock Exchange on a price pullback. We also added to our 'SA Inc.' positions, including Discovery, Sanlam, and Standard Bank, and invested in Anheuser-Busch InBev, anticipating a bottom in earnings.

Outlook and strategy

The market has shifted its outlook from anticipating an aggressive rate-cutting cycle to pricing in expectations for a more moderate approach, as recent data suggests slowing progress on inflation alongside a resilient labor market.

Our base case remains slowing growth leading to a soft landing. On a positive note, we expect market volatility to ease after the US election, as certainty returns and hedges are unwound. Additionally, the seasonal uplift typical of November and December should support equity markets. However, this may shift in the new year as the incoming US administration rolls out its policies.

Volatility is likely to impact the rand, with mixed US economic data creating uncertainty around the direction of the US policy. Locally, sentiment is positive as inflation slows and the 'Government of National Unity' marked its first 100 days power. The consumer is benefitting from the lower oil price, Two-pot money flowing, and some relief from lower interest rates. This is benefitting our retail holdings and has been confirmed in recent trading updates and results.

In China, a series of stimulus measures sparked a rally in Chinese equities in September. Further stimulus was announced which underwhelmed the market. However, it did signal the government's clear intent to provide additional support as and when needed.

The portfolio maintains a modest cash balance, offering an attractive risk-free return. At month-end, the portfolio had a healthy allocation to equities, but we intend to increase it gradually as the volatility provides opportunities to adjust positions during market pullbacks. Our equity portfolio favors companies with robust earnings fundamentals at reasonable valuations, currently weighted toward South African equities. However, global equities remain in focus, with expected US market volatility potentially offering buying opportunities among our preferred stocks. We remain cautious about increasing our exposure to Chinese equities until we gain more confidence in their growth prospects.