

Discovery Balanced, Moderate Balanced, Cautious Balanced Funds

30 September 2024

Market background

Despite significant volatility at the start of August, the third quarter of 2024 proved to be a strong one for global markets, across both equities and fixed income. This was driven by several central banks, including the US Federal Reserve (Fed) and the European Central Bank (ECB), cutting interest rates, while US economic data proved to be more resilient than feared. An exception to the trend was oil markets, which saw prices fall over the period.

Emerging markets outperformed developed market as China unveiled its most substantial stimulus package since the pandemic to boost its ailing economy. This helped the country's equity market post its best quarterly performance since 2009. US, European and UK equities also advanced. Japanese equities, however, were the exception as they fell back for a second quarter following the Bank of Japan's rate hike.

Q3 was notable for its rotation away from tech stocks. Real estate and utilities were the top-performing sectors within the MSCI ACWI, while industrials and financials also outperformed. By contrast, IT and communication services lagged after some disappointing earnings numbers called into question the elevated valuations. Energy was the weakest performer amid the sluggish economic growth outlook.

Developed market sovereign bonds had a strong quarter as investors priced in more aggressive cuts.

South African equities had a strong run, closing Q3 firmly in positive territory. Key was the prospect — and subsequent realisation — of policy easing in both the US and South Africa, as well as progress towards the implementation of market-friendly reforms in South Africa. Further tailwinds came towards the end of September after China unveiled stimulus measures to support its ailing economy, prompting renewed impetus towards risk assets globally.

On the currency front, the rand continued its momentum over the quarter, supported by a combination of a weaker US dollar and a positive shift in sentiment towards the South African economy. Gold prices continued to rally to new record highs.

Performance review

Over the quarter and the month the portfolio delivered a positive absolute return.

Key contributors:

- SA property led gains, followed by SA bonds and SA equity
- 'SA Inc.' stocks, including SA banks, insurers and retailers
- Naspers, Prosus and direct China equity holdings, including Hong Kong Exchanges and Clearing, insurer AIA Group and appliance manufacturer Midea. Chinese stocks rallied following the stimulus announcement
- Gold holdings: Agnico Eagle, Barrick Gold



Key detractors:

- A stronger rand was a headwind for our global bond and global equity returns
- Technology stocks: Amazon, Google, Nvidia as well as semiconductor exposure as investors rotated into defensive stocks
- Diversified miners: a rally towards the end of the quarter was not sufficient to reverse the losses caused by weak commodity prices

Early in the quarter, we took profits on some of our **big-tech** (Alphabet, Microsoft and Amazon) and semiconductor (ASML, KLA) holdings as well as selling positions in **Trane Technologies** and **InterContinental Exchange**. Later in the quarter, we also trimmed **Visa** and **Mastercard**, taking profits on price strength. In August we redeployed some cash during the pullback, buying back into **JPMorgan Chase** and increasing holdings in **Barclays, Apple** and **American Tower**. Towards the latter part of the quarter, we added to industrial cyclicals, including Siemens, Schneider Electric, and infrastructure firm **AECOM**, while also initiating a new position in US retailer, Tapestry.

Locally, we also took profits on **British American Tobacco, Bidcorp** and **Shoptite** and used the proceeds to increase exposure to SA banks (**FirstRand** and **Standard Bank**) on price weakness, particularly viewing FirstRand's forward guidance as conservative.

We took profits on our New Zealand and Australian bonds, following a strong rally in the quarter.

Outlook and strategy

The market was gratified by the Fed's 50bps rate cut, which exceeded expectations by 25bps and outpaced earlier cuts by the ECB and Bank of England. Attention now shifts to duration and scale of the rate-cutting cycle.

While this supports global equity performance, volatility is likely to remain elevated for the remainder of the year. Our base case remains a slowdown in growth leading to a soft landing. However, uncertainty around the upcoming **US election** in November and the evolving Middle East crisis will likely amplify volatility.

Locally, sentiment is **positive** as inflation eases and business confidence improves, supported by an energised Government of National Unity. Investors will keep a wary eye on policy development, and more importantly, on the execution of necessary structural reforms.

In **China**, a raft of stimulus measures have sparked an equity rally, but the focus is now on the scale and deployment of fiscal support. Until there is clarity on these measures, we are hesitant to add to our Chinese exposure, particularly given ongoing concerns about the unresolved property sector debt crisis. These factors could stall or halt the rally.

The portfolio maintains some cash. We plan to increase equity exposure in the coming months and will adjust positions during market pullbacks. Our equity mix remains tilted towards companies with strong earnings fundamentals at reasonable valuations, with a current tilt towards South African equities. However, **global equities** remain on our radar as anticipated volatility could present buying opportunities among our preferred stocks. China's recovery remains uneven, and we are cautious about rebuilding our positions until we have more conviction in growth opportunities. We maintain our marginal duration overweight in SA bonds given the yield underpin but hold no exposure to global bonds following recent strong performance.