

Discovery Global Equity Feeder Fund

30 September 2024

Market context

The third quarter (Q3) of 2024 proved to be a strong one for global equity markets. This was primarily driven by several central banks, including the US Federal Reserve (Fed) and the European Central Bank, cutting interest rates, while US economic data proved to be more resilient than initially feared.

Emerging markets outperformed developed markets, supported by China unveiling its most substantial stimulus package since the pandemic to boost its ailing economy. This helped the country post its best quarterly equity performance since 2009. US, European and UK equities also advanced.

South African equities also had a strong run, closing Q3 firmly in positive territory. Key drivers included 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 in the form of China's stimulus programme, 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.

Performance

For the quarter, the Fund underperformed the benchmark.

Market rotation meant that the sectors that had contributed most to performance in the previous quarter — information technology and communication services — now became the leading detractors. Social creation website **Pinterest** suffered after disappointing numbers, and semiconductor giant **Nvidia** saw profit-taking, not helped by the delay of a new product. Profit-taking also afflicted South Korean semiconductor businesses **Samsung Electronics** and **SK Hynix**, compounded by growing concerns that the memory chip cycle may be peaking. An uncharacteristic narrowing of top-line guidance, flat quarter-on-quarter order-book progression, and broader skittishness regarding AI beneficiaries and the semiconductor cycle all resulted in **Synopsys** lagging the market. Internet giant **Amazon** also saw profit-taking as a step-up in stock-based compensation, seller fee reductions for specific categories, and strategic investments raised question marks over the prior restructuring thesis. In addition, Amazon Web Services reported mildly disappointing results.

Conversely, stock selection in the industrial sector proved successful during the period. Australian logistics business **Brambles** was boosted by a favourable reaction to its increased dividend payout ratio target, along with the share buyback announced with full-year results. Credit rating business **Transunion** reported strong results and increased full-year guidance, helped by a growing share of data breach remediation activity. Chinese financial **Ping An Insurance** rallied with the rebound in Chinese stocks, reporting strong results ahead of analyst expectations.



US online real estate business **Zillow** outperformed following the cut in US interest rates which was viewed as a positive catalyst for housing market transaction volumes. In Europe, Spanish utility **Iberdrola** rose after highlighting its growing position in data centres, and German online retailer **Zalando** benefited from expectations of improving sales and profitability.

Outlook

We expect higher, more volatile inflation through the cycle, driving greater swings in interest rate expectations, resulting in the sort of market volatility we have seen in the last quarter. Currently, reasonable economic growth persists, bolstered by lower inflation and interest rate cuts. The first 50 basis point US rate cut of the cycle has already occurred, with the bond yield curve steepening and early-cycle sectors like housebuilders performing well.

Inflationary pressures remain sticky, particularly in commodities, as the recent Chinese stimulus revives metal prices, and the latest developments in the Middle East have halted the prior slide in oil prices. The market now expects another 50 basis point cut in the US, with an additional 100 basis points in 2025. Europe has seen two ECB rate cuts, while Switzerland and Canada also eased policy.

China's recovery remains sluggish, though recent monetary and fiscal stimulus sparked a sharp rally in its markets. Low valuations and improving momentum could offer opportunities, especially compared to expensive Indian and developed markets. However, as most of the planned initiatives are monetary in nature, in our view, they are likely to prove insufficient to address China's structural issues, even if they are a step in the right direction. For the positive momentum to sustain, we will probably need to see improved economic data points emerging and more policy support to continue, particularly those that address structural challenges such as local government financing and fiscal reform. Meanwhile, in Japan, yen strength, rising wages, and shareholder activism create potential investment opportunities.

Geopolitical risks, including the Russia-Ukraine crisis and Middle Eastern tensions, present ongoing challenges. Elections in key regions, including the US, add to uncertainty. However, market fundamentals, not political outcomes, remain central to our strategy. The US election result could impact policy, particularly around tariffs and corporate lobbying, but sector performance has historically been unrelated to party affiliation. Consumer discretionary and technology were the best and second-best performing sectors during the Obama administration, and they were the second-best and best-performing sectors during the Trump years. Despite widely disparate views regarding the sector, energy was the worst-performing sector under both presidents.

Given the complex macroeconomic landscape, we advocate a balanced, multi-factor approach with a focus on stock selection and flexibility. Resources, notably materials, remain attractive for diversification, while climate-related investments offer growth potential in electric vehicles and infrastructure. Our tech holdings have driven recent outperformance, particularly in AI and data centres, though we are cognisant of valuations and potential market volatility.