Quarterly commentary

Kagiso Global Equity Feeder Fund
March 2021

KAGISO Asset Management

The fund was up 11.9% this quarter, meaningfully outperforming other Global general equity funds (up 4.2% on average) and is up 43.3% over 1 year (outperforming the 25.3% competitor average).

With the pandemic market shock now a year behind us, we are pleased with the extent of our fund's rebound and its continued outperformance of the market. The shock was unexpected and materially changed the economic outlook and the prospects for the companies and economies in which we invest. At the time of the shock, we raised a little extra cash, assessed the new prospects for our holdings and other potential options and pivoted the portfolio accordingly. In particular at this juncture, we took a very conservative stance on balance sheet risk, focused on cashflow generation and favoured the better management teams. As always, we are guided by the price the market offers us relative to future company cashflow prospects.

Economic backdrop

Rapid rollout programs of very effective vaccines are underway in the USA, the UK and Israel, with other rich countries accelerating after slow starts. This increases the probability of a faster return to more normal activity in those regions, limiting further scarring in services sectors (particularly tourism and leisure). Unfortunately, several less wealthy nations are enduring another Covid-19 surge, accompanied by very slow vaccine rollout programs. This is delaying their economic recoveries. It appears that the rate of vaccine rollouts is insufficient to quell the virus worldwide and, with mutations arising where the virus is raging, it's likely that negative economic effects are likely to endure for an extended period. Uncertainty remains high.

Positively, the global economy entered the crisis in a strong position, with healthy consumer dynamics in most developed markets and a moderating, but still strongly growing, Chinese economy. Developed market consumer and corporate health appears to have been largely preserved through extensive and ongoing fiscal and monetary support. In the USA, the level of fiscal support has increased further this year and will be a positive and enduring boost for the global economy. Consumers have fared better than initially expected and increased cumulative savings (from less spend during lockdowns and direct forms of fiscal stimulus) bodes well for future consumption under more normal conditions. Nevertheless, enduring economic conditions may be visible only when fiscal support and monetary stimulus tapers off and the reality of permanent job losses manifests.

Following a rapid resumption of economic activity back to pre-crisis levels, the Chinese economy is once again growing strongly. This is largely due to the successful early containment of the pandemic, government stimulus (which boosted infrastructure investment in particular) and surprisingly strong exports and manufacturing (buoyed by temporary Covid-19-related goods demand). This is despite continued lackluster consumer confidence and spending. However, pre-crisis risks remain: a disruptive moderation and rebalancing of economic growth (away from fixed asset investments and towards consumption) and potential further deterioration in geopolitical relations.

Due to relatively moderate lockdown restrictions the local South African economic recovery was not meaningfully derailed by the strong second wave of Covid-19 infections. Nevertheless, a much more effective vaccine rollout will be needed to continue the recovery in services sectors. Positively, continued high commodity prices (particularly platinum group metals and iron ore) are significantly supporting economic outcomes and the agricultural sector is very buoyant. The economy shows signs of permanent economic damage (scarring) from years of state mismanagement (particularly, a very depressed labour market, unstable electricity supply, weakened and tax-hungry municipalities and chronically low business and investment confidence) and the restrictions of the lockdowns.

While economic revival plans are well articulated, they still rely too heavily on implementation from weakened state institutions and do not draw sufficiently on private sector co-operation. Although on a strong recovery path from very low levels, it is clear that a full post-crisis economic recovery will take meaningfully longer than the rest of the world due to the inherent structural weaknesses of the South African economy, with increased risk due to unsustainably high sovereign debt. Economic growth prospects, under more normal medium-term conditions (household consumption in particular) have weakened substantially relative to before the crisis.

The medium-term outlook for emerging economies is extremely varied at present, with differing exposures to volatile energy prices (importers vs exporters), strong commodity prices, the decimated tourism industry and differing impacts from the management of the pandemic and efficacy of vaccine rollouts. Due to recovering domestic demand and some signs of increased inflation, policy interest rates are beginning to normalize higher from extraordinarily low crisis levels.

Market review

Global markets were strong again this quarter (up 5.0% in US dollars), with the USA up 6.2%, France up 5.3% and the UK up 6.1%. Within emerging markets (up 2.3% in dollar terms), South Africa (up 12.3%) and Russia (up 5.0%) outperformed, while Turkey (down 20.2%) and Brazil (down 10.6%) lagged. Over the last twelve months global equity markets have recovered very strongly from the March 2020 lows (up 54.8% overall).

Extremely high developed market fiscal and monetary stimulus, which are being sustained (and in the case of the USA increased) into the recovery phase, are providing a powerful support for financial markets and have led to dramatic increases in general asset prices. We expect increased volatility when fiscal stimulus inevitably wanes, if inflation emerges at last and when interest rates rise from their extremely low levels.

Kagiso Global Equity Feeder Fund

March 2021

Fund performance and positioning

The underlying fund's significant outperformance of the FTSE World Index over the first quarter of 2021 was due to the strong performance of our Energy, Industrials, Materials and Financial holdings.

We saw positive contributions from Inpex and Kinder Morgan in the Energy sector, while Prudential and M&G were also notable contributors in our Financial holdings. Our quality Industrial and Material stocks had another strong quarter, with Johnson Matthey, Siemens, Dupont and SKF all significant contributors. Ontex and Aroundtown were the main detractors in the quarter.

The fund maintained significant underweight positions in the Communication Services, Consumer Discretionary, Information Technology and Utilities sectors in the past 3 months. The sectors where the fund had overweight exposure are in the Energy (Kinder Morgan and Inpex), Materials (DuPont, Evonik, Corteva and Johnson Matthey), Industrial (SKF, Bodycote, Siemens, Timken and Nisshinbo) and Real Estate (Aroundtown, Unibail-Rodamco-Westfield and Grand City) sectors.

Our fund is mainly positioned in companies listed in developed markets, with exposure to a broad range of diversified sectors. Some examples of the global structural themes underpinning some of our holdings include an ageing population (hospitals, pharmaceuticals, financial services), tomorrow's workforce (automation and robotics), food security (crop protection, farm efficiency, seeds and aquaculture), future mobility (energy storage, components and consumables) and the transition to greener forms of energy (wind and hydrogen power).

Despite the continued strong performance in several of our holdings during the quarter, we have maintained our positioning in high quality cyclical companies as we believe that share price levels are still low relative to their long-term prospects and they should provide very attractive forward-looking returns.

Disclaimer

The Kagiso unit trust fund range is offered by Kagiso Collective Investments (RF) Limited (Kagiso), registration number 2010/009289/06. Kagiso is a subsidiary of Kagiso Asset Management (Pty) Limited [a licensed financial services provider (FSP No. 784)], the investment manager of the unit trust funds. Kagiso is a member of the Association for Savings and Investment SA (ASISA) and is a registered management company in terms of the Collective Investment Schemes Control Act, No 45 of 2002.

Unit trusts are generally medium to long-term investments. The value of units will fluctuate and past performance should not be used as a guide for future performance. Kagiso does not provide any guarantee either with respect to the capital or the return of the portfolio(s). Foreign securities may be included in the portfolio(s) and may result in potential constraints on liquidity and the repatriation of funds. In addition, macroeconomic, political, foreign exchange, tax and settlement risks may apply. However, our robust investment process takes these factors into account. Unit trusts are traded at ruling prices and can engage in scrip lending and borrowing. Exchange rate movements, where applicable, may affect the value of underlying investments. Different classes of units may apply and are subject to different fees and charges. A feeder fund is a portfolio that invests in a single portfolio of a collective investment scheme, which levies its own charges and which could result in a higher fee structure for the feeder fund. A schedule of the maximum fees, charges and commissions is available upon request. Commission and incentives may be paid, and if so, would be included in the overall costs. Kagiso has the right to close the portfolio to new investors in order to manage it more effectively in accordance with its mandate. Additional information is available free of charge on our website or from Client Service.