Quarterly commentary

Camissa Islamic Equity Fund

March 2022

The fund was up 2.9% in the quarter, underperforming the peer group average (up 4.1%). It is up 16.0% over the last three years, materially ahead of the peer group average (up 11.5% pa). Since its inception in 2009, the fund has returned 12.4% pa.

Economic backdrop

The Russian invasion of the Ukraine and the resultant united and coordinated response by Western governments to impose substantial economic sanctions on Russia has caused an acute global supply shockwave. We now have very high commodity prices, supply chain frictions (that were beginning to normalise after the severe pandemic impacts), inflation and a decline in business sector confidence. It is not possible to predict how this conflict is resolved and its ultimate duration.

Some of the important long-term impacts of the war include: structural changes to the European energy ecosystem (which is overly reliant on Russia), an acceleration of de-globalisation trends (shifts towards less efficient but more stable regionalised supply chains) and changes to China-USA economic and political relations.

Developed economies were growing at above pre-crisis trend rates until recently, despite waning fiscal stimulus, due to very healthy consumer spending stemming from robust labour markets, accumulated savings from lockdown periods and surging wealth levels. This initial strength together with some additional fiscal stimulus targeting consumer energy cost relief, means that positive growth should be maintained. European near-term economic growth has been most negatively impacted due to an exceedingly high gas price and a dampening of business and consumer sentiment.

Chinese economic growth has now slowed due to: property market activity rebasing to a lower level because of cyclical excesses unwinding following regulatory interventions, supply constraints and targeted urban COVID-19 lockdowns. Chinese government interventions in many areas of its economy - aligned with longer-term planning (and congruent with sustainably high longer-term growth) - are proving disruptive in the short term. These interventions are targeting more inclusive and less financially risky growth, corporate monopoly positions, carbon emission reduction and technological independence.

The outlook for emerging economies differs widely, with varied exposures to global supply chain bottlenecks, high energy and agricultural prices, strong mining commodity prices, a moribund tourism industry and differing impacts from the stewardship of the pandemic crisis and efficacy of vaccine rollouts. In particular, some poorer economies are facing extremely high current food and energy inflation, which is leading to increased socio-economic instability risks.

Enduring global economic trends may be visible only when fiscal support and monetary stimulus tapers off more meaningfully, when supply chains are functioning more normally, when the acute effects of the military conflict have receded and when the longer-term impact of the military conflict is clearer.

Although South African economic growth has rebounded as expected, the local economy will continue to produce only moderate expansion from here, despite continued strength in the primary sectors (mining and agriculture). Scarring from years of state mismanagement and the recent pandemic lockdowns is highly evident in consumer spending, manufacturing capacity and fixed investment. In addition, there is a risk that future less buoyant commodity prices (particularly platinum group metals, iron ore and coal) will result in an even weaker outlook.

South Africa continues to battle with very high unemployment and a large unskilled population, which increases social instability risks - particularly in the face of increasing inflation. Growth continues to be hampered by unstable and inadequate electricity supply, underperformance of key transport infrastructure, weakened and revenue-hungry municipalities, as well as chronically low business and investment confidence. For these reasons, coupled with the very large government debt burden, we remain pessimistic regarding the structural growth rate for the local economy.

While economic revival plans are well articulated, they still rely too heavily on implementation from weakened state institutions, do not draw sufficiently on private sector co-operation and remain hampered by political unwillingness to take unpopular but necessary actions. Recent actions to liberalise private sector electricity production, the conclusion of a long-delayed telecommunication spectrum auction and early steps towards enabling private sector access to freight rail network are modest moves in the right direction. Additionally, actions to rebuild crime fighting and tax collection capabilities continue to bear fruit - albeit at a slow pace as a result of capacity challenges.

Market review

Global markets were weak in the first quarter (down 5.0% in US dollars), with the UK (down 0.1%) outperforming, and Germany (down 11.1%) and France (down 9.2%) underperforming. Emerging markets were also weak in the quarter (down 1.2%) with highly varied performances: Russia (extreme weakness), China (down 14.2%) and South Korea (down 9%) were poor, whereas Brazil (up 34.8%) and South Africa (up 20.5%) performed relatively well.

In rand terms, the local equity market was up in the quarter (up 3.8%). Financials outperformed (up 20.2%), with banks up 25.2%, life insurers up 16.7% and listed property down 1.3%. Nedbank (up 33.2%), Standard Bank (up 30.1%) and First Rand (up 30.0%) outperformed, while Ninety One Plc (down 14.5%), Quilter (down 12.9%) and Coronation (down 11.8%) underperformed.

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Resources stocks were very strong again (up 19.0%), with Kumba (up 49.1%), Exxaro (up 44.9%) and Sasol (up 37.1%) outperforming. Despite being up, Impala Platinum (up 2.3%) and Northam Platinum (up 4.1%) underwhelmed.

Industrials underperformed (down 13.9%), with standout positive performers: The Foschini Group (up 20.3%), Bidvest (up 20.1%), Vodacom (up 18.9%) and Truworths (up 17.4%)). Very weak performances were delivered by Prosus (down 39.2%), Naspers (down 32.7%) and Richemont (down 21.6%).

Fund performance and positioning
Key positive contributors within local equities in the quarter included Omnia, Anglo Platinum, African Rainbow Minerals and Gold Fields. PPC Telkom, Wilson Bayely Holmes-Ovcon and Aspen, detracted.

Along with our global equity holdings, detractors included Johnson Electric, Bodycote, Bellway, Continental and Hochtief. Inpex, Bayer, Nutrien and Shell all contributed positively.

Our portfolios currently have high exposure to PGM miners, Prosus, Omnia and a diverse range of other mispriced stocks, including an array of deeply discounted local mid-cap stocks.

An example of a compelling mid-cap idea is Datatec, where we expect corporate restructuring to unlock substantial value. The company has three operating businesses. Logicalis is a global leader in information technology managed services, Westcon is a global information technology hardware distributor and Analysis Mason is a niche consultancy - now focused on the fast-growing 5G market. In 2017, Datatec sold its US and Latin American Westcon operations (roughly half of Westcon) for an attractive price. While the operating businesses are performing well, we believe the company trades at a large discount to the value of its underlying assets. To address this persistent discount, Datatec recently announced a broader strategic review, which in our view should unlock value through the sale of one or more of its businesses. The holding company has very high central costs and there is potential for outsized positive returns if the holding company structure is wound down. Management owns over 13% of the company and is therefore fully aligned with shareholders to pursue options that maximise value.

We maintain a high weighting in Prosus, which has both a strong balance sheet and a very bright, long-term future through its underlying exposure to online Chinese economic activity (via Hong Kong-listed Tencent). Tencent's prospects remain excellent, even as it navigates the current period of high and abnormally front-loaded regulatory interventions (many of which are sensible and will lead to healthier and more sustainable future growth). Very elevated levels of pessimism are currently priced into the Prosus share price resulting in extremely attractive upside.

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