Kagiso Islamic High Yield Fund

December 2021

The fund was up 2.5% this quarter, outperforming its benchmark (Short-term Fixed Interest Index) (up 1.0%). It is up 8.3% over the last two years, ahead of the peer group average (up 4.6% pa). Since its inception in 2019, the fund has returned 7.8% pa.

Economic backdrop

Although the global economy has largely recovered from the COVID-19 pandemic shock, the recovery is very uneven across countries and sectors. Despite high vaccine efficacy, new virus variant waves continue to impede a full recovery due to government containment measures. The pandemic has severely impacted manufactured goods supply chains and this is contributing to supply shortages and to higher inflation rates. Enduring economic trends may be visible only when fiscal support and monetary stimulus tapers off more meaningfully and when supply chains are functioning more normally.

Developed economies are growing above pre-crisis trend rates for now, despite the supply chain disruptions and even as fiscal stimulus benefits rapidly wane. This is due to healthy consumer spending stemming from robust labour markets, accumulated savings from lockdown periods and surging wealth levels.

Chinese economic growth has now slowed due to its property market excesses unwinding following regulatory interventions, energy shortages, supply constraints and isolated hard lockdowns. Chinese government interventions in many areas of its economy, which are aligned with its longer-term planning (and congruent with sustainably high longer-term growth) are proving very 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 medium-term outlook for emerging economies is extremely varied at present, with differing exposures to global supply chain bottlenecks, volatile energy and agricultural prices (importers versus exporters), strong mining commodity prices, a moribund tourism industry and differing impacts from the stewardship of the pandemic crisis and efficacy of vaccine rollouts. Due to recovering domestic demand and signs of increased inflation, policy interest rates have continued normalising higher from extraordinarily low crisis levels.

Although economic growth has rebounded as expected, the South African economy will continue to produce only moderate expansion from here, despite notable strengthening of the primary sectors (mining and agriculture). Scarring from years of state mismanagement and the pandemic lockdowns is highly evident in consumer spending, manufacturing capacity and fixed investment. There is a risk that future less buoyant commodity prices (particularly platinum group metals, iron ore and coal), which are currently strongly supporting the economy, will result in an even weaker outlook. In addition, South Africa continues to battle burgeoning unemployment, a large and unskilled population, unstable and inadequate electricity supply, underinvestment in key transport infrastructure, weakened and revenue-hungry municipalities and 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 are still hampered by political unwillingness to take unpopular but necessary actions. Recent actions to liberalise private sector electricity production and early steps towards enabling private sector access to freight rail network are modest moves in the right direction. In addition, actions to rebuild crime fighting and tax collection capabilities continue to bear fruit, albeit at a slow pace due to capacity challenges.

Market review

Global markets were strongly positive in the final quarter (up 7.9% in US dollars), with the USA (up 11.0%) and France (up 8.1%) outperforming and Hong Kong (down 4.8%) and Japan (down 5.3%) underperforming. Emerging markets were again weak in the fourth quarter (down 1.2%), with particularly poor performances from Russia (down 9.0%), China (down 6.1%) and Turkey (down 11.1%). 2021 was a very strong year for global equity markets (up 22.3% overall).

In rand terms, the local equity market was up significantly in the quarter (up 15.1%). Resources stocks were very positive (up 22.2%), with RBPlats (up 110.6%), Gold Fields (up 41.3%) and Anglo Platinum (up 39.3%) outperforming, while Sasol (down 9.3%) and Exxaro (down 5.1%) underperformed.

Industrials were also positive (up 16.8%), with standout positive performers being Richemont (up 55.2%), Telkom (up 22.5%), MTN (up 20.8%), Dis-chem (up 19.9%) and Shoprite (up 16.9%). Aspen (down 17.2%), Woolworths (down 12.2%) and Pick n Pay (down 7.3%) all lagged.

Financials underperformed (up 2.2%), with listed property (up 8.4%), banks (up 3.2%) and life insurance (down 4.8%). Investec (up 37.6%), Fortress B (up 27.5%) and RMI Holdings (up 20.7%) outperformed, while Momentum (down 9.3%), Old Mutual (down 7.6%) and Sanlam (down 7.1%) underperformed.

The local market was positive for the year (up 29.2%). Resources were up 32.4%, financials were up 27.4% and industrials were up 24.7%.

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KAGISO Asset Management

Fund performance and positioning

The fund's domestic equity holdings were the biggest contributor to fund performance in quarter 4 with the fund's holdings in RB Platinum and MTN contributing strongly to performance. RB Platinum appreciated by 110% in the quarter after Impala and Northam both made bids for the company. The funds' holding in select property stocks also contributed positively to performance with notable contributions from Hyprop and Equites property.

The fund has a prudent allocation to property with our preferred property exposure concentrated in holdings in Equites and Resilient Properties.

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