NEDGROUP INVESTMENTS

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Quarterly review

Nedgroup Investments Core Global Fund

As at 31 March 2021

Progress against COVID-19 leading to optimism abouth the economic rebound

Despite the lockdown restrictions, the opening of economies and improved activity in 2021 are made more likely by approval and rollout of vaccines. These sentiments were echoed by the IMF and World Bank, both forecasting an expansion for the global economy for 2021 of 5.5%% and 4.0%, respectively. The OECD has now joined the ranks of entities that have lifted their economic growth forecasts to account for vaccine rollouts and greater US fiscal stimulus, now expecting global growth of 5.6% in 2021 (up from 4.2%). A historic rally saw the S&P 500, gain +56.4% over the year, supporting a +54.8% (in dollar terms) gain for the MSCI World Index.Overall, this was a volatile first quarter, with duration exposed assets in the crossfire with bond yields and earnings trending higher. Over the course of the quarter, the Nedgroup Investments Core Global Fund grew by +3.0%.

The table below compares an investment in the Nedgroup Investments Core Global Fund to US bank deposits (cash) and its growth target over various time periods. For every $10 000 invested in the Nedgroup Investments Core Global Fund at inception (16 November 2015), you would have $15 770 at the 31st of March 2021. This is better than the $10 710 you would have achieved had you invested your money in US bank deposits (cash) over the same period. The green circle in the chart below, highlights the recent market recovery, which helps to contextualise the returns experienced in the past few years.

	Value of R10,000 investment in Nedgroup Investments Core Global Fund versus US Cash[1]				
	3 Months	1 Year	3 Years	5 Years	Inception 16 November 2015
Growth of fund (after fees) ***(Growth in %)***	$10 300 *3.0%*	$13 632 *36.3%*	$12 984 *9.1% p.a.*	$15 262 *9.4% p.a.*	$15 770 *8.9% p.a.*
Growth of US Cash ***(Growth in %)***	$10 002 *0.0%*	$10 034 *0.3%*	$10 490 *1.6% p.a.*	$10 695 *1.4% p.a.*	$10 710 *1.3% p.a.*
Growth target (EAA Fund USD Aggressive Allocation) ***(Growth in %)***	$10 343 *3.4%*	$13 614 *36.1%*	$12 446 *7.6% p.a.*	$14 550 *7.8% p.a.*	$14 500 *7.2% p.a.*

Fund Return versus US Cash[1] from inception to 31 March 2021

Source: Morningstar

Since the inception of the Nedgroup Investments Core Global Fund, it has delivered returns in excess of US cash. However, it is to be expected that occasionally there will be periods where the Fund does not beat US cash over 5 years. Over the long term[2], a portfolio such as Nedgroup Investments Core Global Fund would have delivered a higher return than US cash approximately 64% of the time over any 5-year period.

1. We used the ICE Bank of America 3 month deposit rate for US cash returns
2. Based on Global market returns from 1997 to 2018 (source Morningstar) using the same long-term equity allocation and fees.

Economic and market performance – One step forward

By the end of March, 32% of the US population and 75% of adults over 65 years had received at least one dose of the vaccine. With approximately 3 million doses being administered each day in the US, and as this pace of vaccination continue, the prevailing expectation is that the economy will experience significant pickup in domestic and global economic activities. As vaccination continue to accelerate in large economies, providing a much-needed boost to the economic activities, slow vaccination rollout and extended lockdowns in countries with lack of access to the vaccine threatens the recovery. Hence, this has kept the pandemic at the forefront of everyone’s mind, most notably that of policy makers.

Stock markets enjoyed another positive quarter, the fourth in a row since last year’s March pull back, with the S&P 500 closing at a +6.2% gain over the quarter. Developed markets gained +4.0% over the quarter, meanwhile emerging markets only gained +2.3% against a stronger US Dollar and heightened volatility. Global Real Estate also saw a positive return over the quarter with the index gaining +6.2%. Global bond markets lost further ground on higher bond yields resulting in a -4.5% decline in the Barclays Global Aggregate Index. It is not unusual to see bonds loose value when stocks are doing well because generally high-quality bonds move in the opposite direction of equities.

The first quarter also saw the US President elect Joe Biden’s inauguration proceeding without incident given the lingering concerns that protests at the Capitol would be repeated. The new administration moved swiftly to reverse many of the previous administration’s decisions, which can now easily be done since the balance of power is in favour of the Democratic Party.

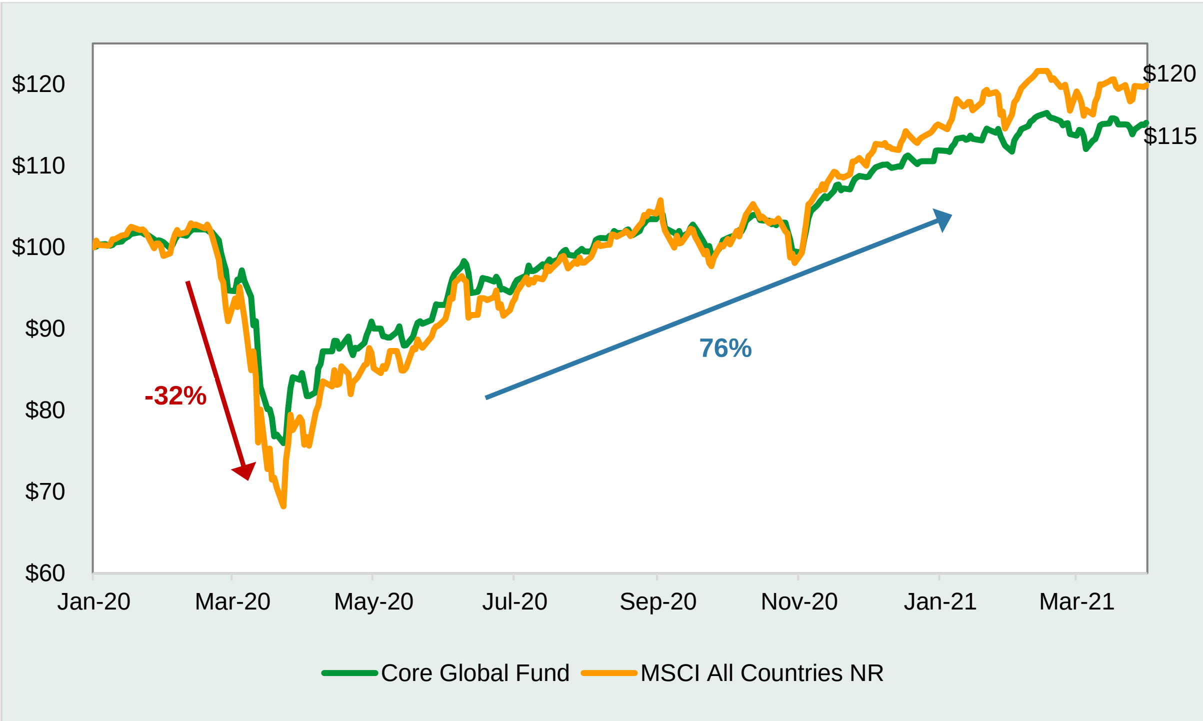
Global central banks have done all they can to communicate their preference to remain accommodative, especially given the uneven nature of vaccine rollouts and economic recovery to date. Bond markets are, however, already pricing a future of expansion in fiscal support, economic growth and potential for related inflation, as reflected in higher bond yields. The European Central Bank (ECB) kept monetary policy unchanged at its meeting in March. The Pandemic Emergency Purchase Programme (PEPP) was maintained at $1.85 trillion, although policymakers noted that the total amount might not be utilised unless inflationary pressures became risky. The short-term economic outlook remains uncertain; however, a moderate rebound in activity is expected sometime this year. The ECB views the current uptick in inflation as temporary. Time will tell whether markets will force policy makers to act, but for now, the tussle will continue to impact broader asset prices.

Investments lessons over the past year

A year on from the first global lockdown and related market rout, the world is still grappling with the pandemic, but is slowly on the mend. Expectations of a third wave of infections are prevalent, with a resurgence in cases already evidenced in Europe. Slow vaccination rollouts and extended lockdowns threaten the economic recovery in the region and highlights the risks faced by other countries with lack of access to vaccines or slow distribution.

Global market returns over the first quarter were up by around 5% while global bonds declined by 4% as bond yields trended higher. Over the past year Global equities delivered a staggering 55% and REITS 36% in USD. It is however important to contextualise these returns to the market events that took place at the beginning of the Covid19 crises. The chart below shows the returns of equity markets over that past 15 months.

Equity market returns over the past 15 months



Source: Morningstar

One can see that during the crises Global equities dropped by 32% before starting its recovery in April 2020. Since then we have seen growth of 76% to achieve a cumulative return of 20% over the full 15-month period. If an investor had panicked at the bottom of the market, they would have locked in the 32% loss and missed out on the recovery performance. This highlights the importance of staying invested for the long term as markets generally recover over time. In this case it was a quick recovery by historical standards as there has been periods where it took years to recover.

For that reason, diversification across global asset classes, regions and currencies is the most sensible strategy to deal with market uncertainty as it smooths out the investment journey. One can see that the Nedgroup Investments Core Global Fund experienced drawdown of 14% which it recovered from by late July 2020.

Is concentration risk on the rise?

The market has largely been dominated by the five most popular and top performing American technology companies are commonly referred to as FAANG stocks, which consist of Facebook, Apple, Amazon, Netflix and Google. These companies have a staggering combined value of over 4 trillion US dollars. This is more than the GDP of most countries, including India. This begs question: is concentration risk is on the rise?

To unpack this, let's begin with the basics, that is the weight of the top 10 stocks in the United States, the world and the Nedgroup Investments Core Global Fund as at 31 March 2021.

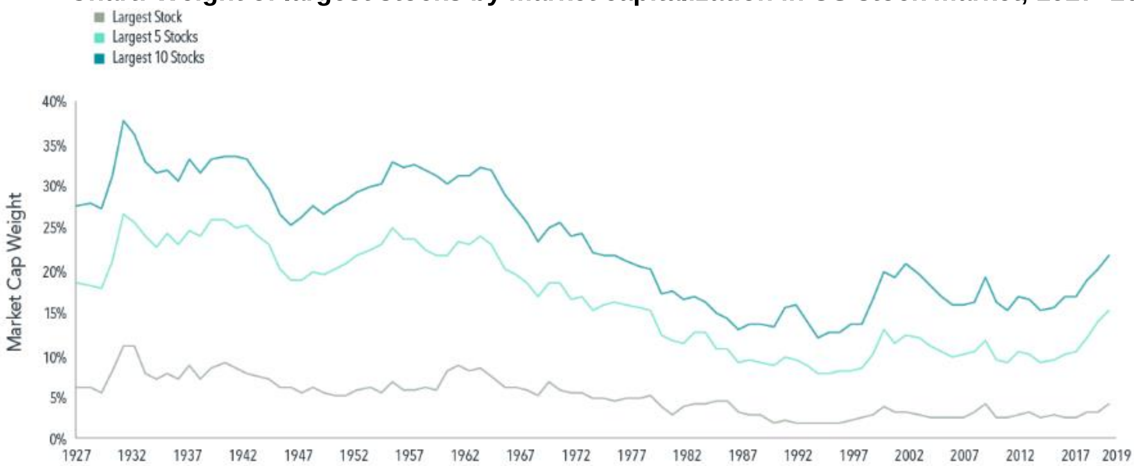
Top 10 shares	US (S&P500)	Top 10 shares	Global (ACWI)	Top 10 shares	Core Global Fund
APPLE INC	5.7%	APPLE INC	3.4%	APPLE INC	2.3%
MICROSOFT CORP	5.3%	MICROSOFT CORP	2.7%	MICROSOFT CORP	2.0%
AMAZON COM INC	3.9%	AMAZON COM INC	2.1%	AMAZON COM INC	1.5%
FACEBOOK CLASS A INC	2.1%	FACEBOOK CLASS A INC	1.1%	FACEBOOK CLASS A INC	0.8%
ALPHABET INC CLASS A	1.8%	ALPHABET INC CLASS A	1.0%	ALPHABET INC CLASS A	0.7%
ALPHABET INC CLASS C	1.8%	ALPHABET INC CLASS C	1.0%	ALPHABET INC CLASS C	0.7%
TESLA INC	1.5%	TAIWAN SEMICONDUCTOR	0.8%	TESLA INC	0.6%
BERKSHIRE HATHAWAY	1.5%	TESLA INC	0.8%	TAIWAN SEMICONDUCTOR	0.6%
JPMORGAN CHASE & CO	1.4%	JPMORGAN CHASE & CO	0.8%	JPMORGAN CHASE & CO	0.5%
JOHNSON & JOHNSON	1.3%	TENCENT HOLDINGS LTD	0.7%	JOHNSON & JOHNSON	0.5%
	26.3%		14.5%		10.3%

Source: Morningstar

In the table above, we represent the United States by the S&P 500 Index and global shares by the MSCI All Countries World Index (ACWI) which comprises both developing and developed countries. As we move from the US to global shares and finally to the Nedgroup Investments Core Global Fund, the concentration in the top 10 shares improves dramatically, dropping from 26% to 10%. This is a good illustration of the fact that investing in a diversified fund that comprises a variety of asset classes, invested across a range of geographies and holding thousands of individual securities provides a significant reduction in concentration risk.

Coming back to the original question, although there has been a trend of rising concentration risk in the US stock market in recent decades, this is not out of line with the concentration levels witnessed over the last century. The chart below illustrates that having a handful of stocks represent such a large percentage of the market is nothing new. This once again reiterates the importance of holding a well-diversified fund to help mitigate concentration risk.

Chart: Weight of largest stocks by market capitalization in US stock market, 1927–2019



Source: Dimensional Fund Advisors

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