



Quarterly review

Nedgroup Investments Core Bond Fund

As at 30 June 2023



Current inflation is likely to be transitory

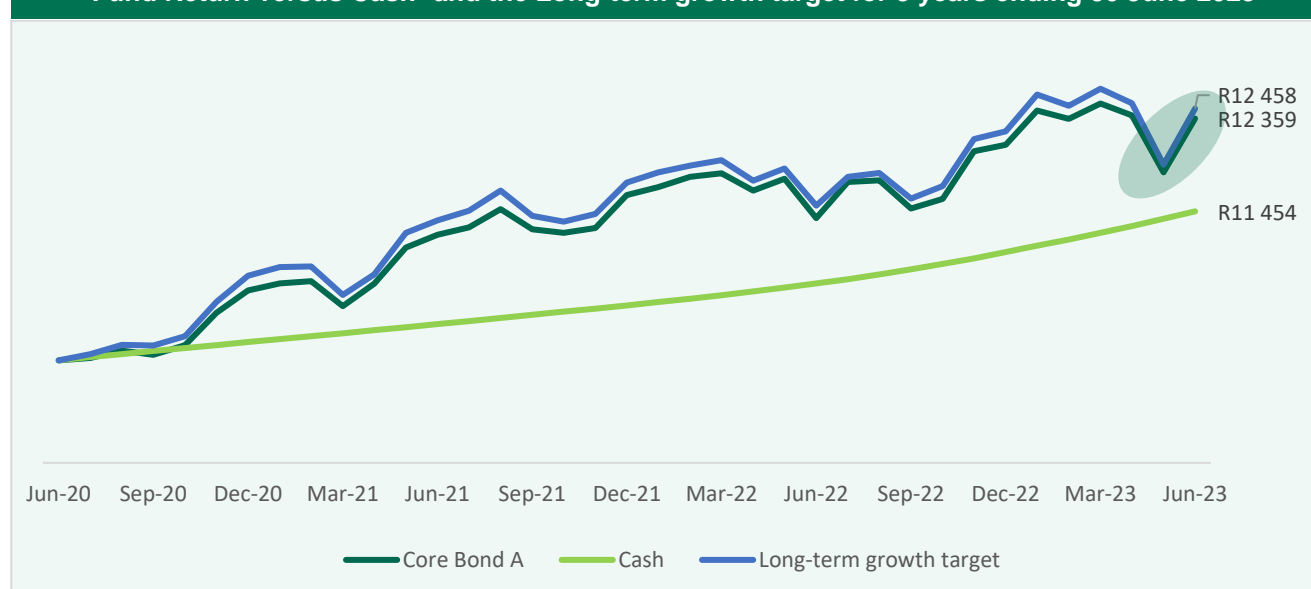
In 2022 investors were dealt with very disappointing results in both stocks and bonds. What we have seen in 2023 so far is a complete reversal of that. When one looks at 60% stocks and 40% bonds portfolio, it is off to its best start in 10 years. Investors are looking beyond what we have seen as very weak economic growth, likely recession this year, even the banking crises that occurred in the first quarter of 2023 and focusing on the fact that the federal reserve may be close to being done on the aggressive tightening cycle. This easing inflationary pressure helped lift markets in the first quarter. This easing inflationary pressure helped lift markets in the first quarter. Over the quarter, the Nedgroup Investments Core Bond Fund declined by -1.2%.

The table below compares an investment in the Nedgroup Investments Core Bond Fund to bank deposits (cash) over various time periods. This illustrates that over longer periods, investors have been rewarded for taking on interest rate risk. For every R10 000 invested in the Nedgroup Investments Core Bond Fund three years ago, you would have R12 359 at the 30th of June 2023. This is greater than the R12 458 you would have achieved had you invested your money in 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 Bond Fund versus Cash¹ and the Growth target

	3 Months	1 Year	3 Years	5 Years	7 Years	10 Years
Growth of fund (after fees) (Growth in %)	R9 882 -1.2%	R10 852 8.5%	R12 359 7.3% p.a.	R14 447 7.6% p.a.	R17 270 8.1% p.a.	R20 752 7.6% p.a.
Growth of cash (Growth in %)	R10 187 1.9%	R10 655 6.6%	R11 454 4.6% p.a.	R12 948 5.3% p.a.	R14 781 5.7% p.a.	R17 433 5.7% p.a.
Growth target (Beassa ALBI) (Growth in %)	R9 847 -1.5%	R10 823 8.2%	R12 458 7.6% p.a.	R14 286 7.4% p.a.	R16 989 7.9% p.a.	R20 407 7.4% p.a.

Fund Return versus Cash¹ and the Long-term growth target for 3 years ending 30 June 2023



Over most periods, the Nedgroup Investments Core Bond Fund has done significantly better than bank deposits (cash) as the Fund benefited from the yield enhancement from investing in longer dated bond instruments. Over the past ten years it has delivered more than 1.9% of additional return per annum, or R3 3181 for every R10 000 invested.

¹ We used the STeFI call deposit rate for cash returns



Economic and market review

Despite the threat of recession, interest rate hikes and inflation concerns, global shares have provided a surprising overall return of 13.9% in the first half of the year (in USD). The United States, which is by far has the largest weight in global equity indices, once again delivered higher returns than the rest of the world with the S&P500 returning 16.9% (in USD). Tech stocks made a comeback to their former glory, driving overall US market returns, after their fall from glory in 2022 where they tumbled over 30%. Even global bonds did well to provide relatively flat returns in spite of rapidly rising global interest rates (in USD).

South African share performance was unfortunately muted with a return of 3.6% for the first half of the year and South African property continued to disappoint investors with a decline of 10.9%.

The table below displays the returns of various asset classes for the first and second quarter of the year, as well as the year to date returns to the end of June 2023. Most asset classes earned similar returns in both quarters. The Rand depreciation of almost 10% year to date, further buoyed already good global equity returns.

Table: Returns in Rands

Asset class	Index	Q1	Q2	YTD to Jun 23
SA equity	FTSE/JSE Capped Shareholder Weighted Index	2.4%	1.2%	3.6%
SA property	FTSE/JSE REIT Index	-8.5%	-2.6%	-10.9%
SA nominal bond	SA All-Bond Index	3.4%	-1.5%	1.8%
SA inflation-linked bond	SA Inflation-linked Bond Index	0.9%	-0.8%	0.0%
SA cash	STeFI Composite Index	1.7%	1.9%	3.6%
Global equity	MSCI All Country World Index	11.9%	13.1%	26.5%
Global property	FTSE EPRA/NAREIT Developed (Net)	5.4%	7.1%	12.8%
Global nominal bond	Bloomberg Global Aggregate Bond Index	7.4%	4.8%	12.6%
Global inflation-linked bond	Bloomberg Global Inflation-linked Bond Index	8.9%	4.6%	13.9%
Global cash	Composite USD/GBP/EUR Libor 3-month	5.4%	7.8%	13.6%
ZAR/USD exchange rate	ZAR/USD exchange rate	4.7%	5.0%	9.9%

These exuberant global equity returns somewhat mask the shifting landscape. Since the global financial crisis, the world has enjoyed high money supply, low inflation and low interest rates which have driven up valuations of asset classes. However, this is rapidly changing, and the new regime seems to signal the end of easy money.

The chart below illustrates the European and US money supply since 1965, demonstrating the extremely high money supply we have enjoyed of late, followed by a sharp decline beginning in 2021. In essence, this decline implies that there is less money available in the economy helping to cool down the economy thereby reducing inflation and tightening lending conditions (although other factors such as the speed by which money changes hands in the economy can offset this).

Figure 1: Money Supply



Source: Macrobond, State Street Global Advisors Economics, Federal Reserve Board. Data as of 25 April 2023.

Most global economic forecasts project poor economic growth. But all is not doom and gloom; surprisingly the Federal Reserve have changed their stance on their prediction of a US recession and instead expect a soft landing due to their decision to hold off on a rate hike in June.

In such a rapidly changing environment, it's even more difficult to forecast the future. In such times, it is critical not to make emotionally driven investment decisions. The Core range funds all have very well diversified investments across a range of geographies, asset classes and sectors helping to reduce risk and volatility.



Interest rates and how the debt-ceiling agreement will impact the economy

The great debt-ceiling debate/negotiation ended in something of an anti-climax. While debates about who “won” and “lost” will probably continue for years in both parties, there was at least one clear winner - the United States (and by extension, the global economy). Of course, this episode raises questions on the US Treasury's ability to repay debt in the future when Congress will have to raise the debt ceiling again. However, for now, a breach of the debt ceiling - with the potential for throwing global financial markets into chaos - is off the table for the next two years. The US government shutdown - with the potential for throwing the economy into a recession - is lot less likely.

The agreement reduces the trajectory of Federal spending by a small amount, small enough to have little impact on the economic outlook. This success does not pave the way for a perfect economy. The Deloitte forecast still shows the economy slowing substantially in the second half of 2023. This slowdown is not, however, a recession. There's too much positive news, particularly in the labour market.

Have authorities successfully prevented rising interest rates from creating a financial crisis? The failure of three regional US banks and one large Swiss bank certainly got the attention of central banks, including the Fed and regulators including the Federal Deposit Insurance Corporation. So far, the economic impact looks to be modest. But the problems that showed up in March demonstrate that the economy is currently fragile, and that a financial disturbance could easily throw it into a recession.

The Federal Reserve reacted quickly to try to reassure depositors in other banks that these issues were isolated, and that there was no need to be concerned about the safety of deposits. And, in fact, the Fed's efforts appear

to have worked. But there will be some modest damage to the economy. As of late May 2023, deposits at small banks had stabilized (resuming the slow but controllable declining trend before March), indicating that depositors were satisfied with the safety of their deposits. Bank lending remains under the microscope because a pullback in lending could have a significant impact on economic activity.

In the medium term, the key question is whether long-term interest rates will once again settle in at a relatively low level, or whether they will return to levels consistent with the experience before the global financial crisis. Those arguing that interest rates will return to low levels point to fundamentals such as demographics (the aging global population). Those arguing that interest rates will return to previous behaviour point to the slowing of savings growth from China and the need for large investments (whether public or private) to reduce the impact of climate change. Of course, interest rates are always the least certain part of any forecast: Any significant news could—and will—alter interest rates significantly.



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