



## Quarterly review

### Nedgroup Investments Core Guarded Fund

As at 30 September 2023

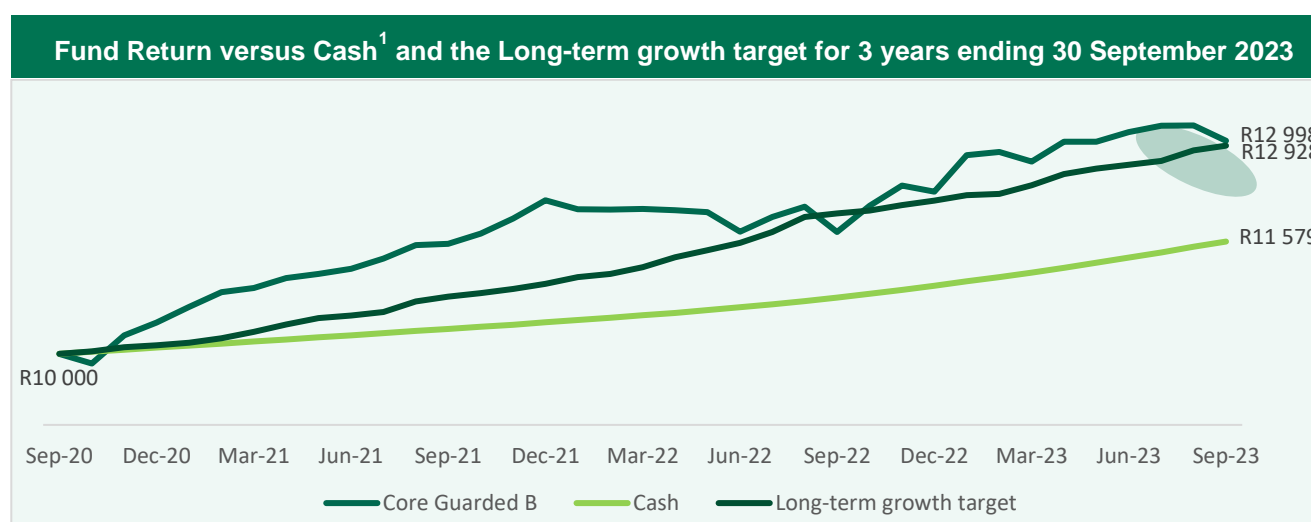


## Recession fears and central-bank tightening are driving market volatility

The path toward a more balanced economic state has impact on financial markets. In most developed regions, the excessive debt accumulation over the previous decades that created the large economic imbalance today has already begun to reverse. The combination of central banks raising interest rates, draining reserves and banks tightening lending standards, in addition to other fiscal policy conditions, has combined to reduce the flow of money to markets and economies - causing significant market volatility. After a positive first half, risk assets started to price for the more challenging backdrop in the third quarter. The Nedgroup Investments Core Guarded Fund decreased by -0.9% over the quarter.

The table below compares an investment in Nedgroup Investments Core Guarded Fund to bank deposits (cash) investment over various time periods. For every R10 000 invested in the Nedgroup Investments Core Guarded Fund three years ago, you would have R12 998 at the 30<sup>th</sup> of September 2023. This is lower than the R11 579 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 decline, which helps to contextualise the returns experienced over the past few years.

Value of R10,000 investment in Nedgroup Investment Core Guarded Fund versus Cash <sup>1</sup> and the Growth target						
	3 Months	1 Year	3 Years	5 Years	7 Years	Inception 29 January 2010
Growth of fund (after fees) (Growth in %)	R9 910 -0.9%	R11 096 11.0%	R12 998 9.1% p.a.	R14 291 7.4% p.a.	R16 110 7.1% p.a.	R32 773 9.1% p.a.
Growth of cash (Growth in %)	R10 201 2.0%	R10 732 7.3%	R11 579 5.0% p.a.	R13 001 5.4% p.a.	R14 824 5.8% p.a.	R21 292 5.7% p.a.
Growth target (inflation+3%) (Growth in %)	R10 213 2.1%	R10 795 8.0%	R12 928 8.9% p.a.	R14 753 8.1% p.a.	R17 208 8.1% p.a.	R29 985 8.4% p.a.



The Nedgroup Investment Core Guarded Fund has a growth target of 3% above inflation (around 8% per year) over 3-year periods. The Fund has almost reached its target over the last 3 years. However, history<sup>2</sup> demonstrates that one-third of the time, a fund such as the Nedgroup Investments Core Guarded Fund, would have underperformed its long-term growth target over any 3-year period. The other two-thirds of the time it would have achieved or exceeded its long-term target.

<sup>1</sup> We used the STeFI call deposit rate for cash returns



After a strong start to the quarter in July, equity markets fell in August and September. Investors grew cautious as the reality of 'higher for longer' interest rates became apparent. Bond yields rose throughout the quarter with US 10-year yields hitting a 16-year high on the first day of the fourth quarter. Q3 global bond market losses have come as the 10-year Treasury yield - the benchmark for world borrowing costs - has surged roughly 75 basis points to just above 4.6 percent. That is the largest quarterly jump in a year and one which hoists it back to its long-term average for the first time since 2007.

Today, we are faced with significant levels of imbalance in developed market economies that are difficult to resolve; most notable is the divergence between demand (nominal spending) and supply (economic output). Current high levels of nominal spending were triggered by the unprecedented liquidity injection and fiscal debt build-up during the COVID-19 pandemic, which have outstripped the ability of developed market economies to produce more, leading to an inflationary overshoot. Unsurprisingly, policy makers are left with no appetite to inject more stimulus into the economy and are now forced to engineer a broad economic slowdown to rein in demand.

In an effort to combat historically high levels of inflation, the Federal Reserve has implemented an unprecedented Fed Funds rate hiking cycle of 525 bps in a brief span of 16 months. This has shifted monetary policy from accommodative to restrictive, reflected in long-term real interest rates that have risen to 2 percent, a level not seen since the GFC. This restrictive monetary policy position (which includes so-called "Quantitative Tightening"), coupled with softening inflation suggest to us that we are nearing the end of Fed rate hikes. The key questions going forward for the market are how long will the Fed hold this restrictive policy and when will they need to pivot? While the market ponders these two questions, market pricing is entering an inflection point where real yields are cyclically high and high yield spreads are cyclically tight, a market pricing environment that has historically been unsustainable.

While growth stocks have been under pressure, this round of higher interest rates has had more of an impact on two specific groups of stocks: dividend stocks and stocks exposed to consumer spending. The moderation in US inflation had seemed broad-based during the first half of the year but was certainly aided by a lack of energy price inflation. The equation for financial markets over the last few months has been both simple and painful: A near 30 percent surge in oil prices + a steep rise in borrowing costs = a clattering for global stocks and bonds. Equity bulls have also been biffed. The S&P 500 lost 3.3 percent over the third quarter, while declines across Europe and Asia were more meaningful.

In the month of September, the South African Reserve Bank's (SARB) Monetary Policy Committee (MPC) decided to leave the repo rate unchanged at 8.25 percent. The decision to pause was not unanimous, with three members of the MPC voting in favour of this outcome, while two other members preferred a 25 basis points (bps) increase.

Views around inflation have remained contentious over the last 18 months, however two prevailing arguments have since resolved the long-standing dispute. The first is that peak inflation is now firmly behind us. The second is that inflation in many countries is starting to fall towards target.

While the second argument may be true, the pace in price moderation is somewhat sticky, requiring higher for longer policy rates. The Forward Rate Agreement (FRA) market seems to concur, and now pricing-in another 25-bps increase in November 2023 before interest rates start to retreat in the second half of 2024.

The market's latest policy outlook is largely informed by reduced global oil inventory levels, as well as the impact thereof on future fuel price inflation. According to Stats SA, the annual consumer price inflation (CPI) index rose from 4.7 percent in July to 4.8 percent in August. Notwithstanding the reversal of low base effects, it is our view that a moderating economic backdrop is unlikely to maintain elevated inflationary pressures.

In the SA money market, the 3-month JIBAR rate fell by 2.5-bps to 8.333, while the 12-month JIBAR rate increased by 32.5-bps to 9.275 versus the previous month. In the last 12 months, the 3-month, and the 12-month JIBAR rates increased by 187-bps and 68-bps, respectively. These elevated JIBAR rates imply that

money market funds are likely to generate a return of between 9 percent and 10 percent over the next 12 months with no (or limited) risk of capital loss.



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