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NEDGROUP INVESTMENTS RAINMAKER FUND

Quarter Two, 2024

Nedgroup Investments Rainmaker Fund

Performance to 30 June 2024	Nedgroup Investments Rainmaker Fund[1]	ASISA category average	FTSE/JSE ALSI
3 months	2.9%	7.4%	8.2%
12 months	5.9%	9.8%	9.1%

Positive momentum continues in global markets, with major indices like the S&P 500 at all-time highs, despite concerns that the Fed might hold rates higher for longer. During the first half of 2024, MSCI World Markets returned +12.0% in US dollars while MSCI EM gained +7.7%.

Gold has also continued its steady climb - up approximately 13% for the year to date — driven by strong demand from central banks, rising geopolitical tensions and what looks like Chinese retail investor activity. In some respects, it is puzzling that gold has rallied against traditional headwinds of a strong US dollar and high real interest rates. However, the underlying strength has been reinforced by structural support - namely, the uptrend in economic and geopolitical risks. This is best illustrated by the appetite for gold by central banks, whose pace of purchases increased rapidly soon after the Russian invasion of Ukraine. The geopolitical motivation for many central banks to accumulate gold is likely to persist given a desire to guard against the risk of forex reserve confiscation, or to reduce the US dollar's role in their financial system. Equally important as the intent to raise gold holdings is the capacity to do so. As of Q124, China and India have 5% and 9% of their official reserves in gold, respectively, in contrast to gold representing 71% and 53% of official reserves for the United States and Euro area; illustrating that there is ample room for some central banks to acquire more gold in the coming years.

2024 continues to be the year of elections, with the South African election a key focal point over the last quarter and source of market volatility given the various outcomes that could have emerged. South Africa's ruling African National Congress party (ANC) lost its majority for the first time in 30 years, marking the biggest political shift in the country since the end of apartheid. The ANC suffered a heavy blow at the polls with support dropping to c40%, from the 57.5% it received in the last election in 2019. The blow to the ANC comes after years of corruption scandals and economic mismanagement. We are encouraged that this dramatic loss of political control by an African liberation party was effected through an open and fair democratic process without violence or voter intimidation and accepted gracefully. The previous official opposition party, the Democratic Alliance (DA), received c22% of the vote and former President Jacob Zuma's newly formed uMkhonto weSizwe Party (MK) won nearly 15% of the vote with this outcome driven largely by their regional success in Kwazulu Natal. Following the election outcome the ANC has negotiated a coalition government of several parties – preferring to partner with mostly moderate organisations seen as pragmatic and more business friendly. Encouragingly the 'nightmare' outcome of an ANC / EFF coalition was avoided and the eventual confirmation of a Government of National Unity (GNU), that excluded MK and EFF political parties, was well received by the market.

While we are not naïve about the inevitable challenges of actually operating a coalition government (new territory in South Africa) and the likelihood of political differences of perspective causing points of argument, a positive outcome has emerged with the GNU raising the prospect for more market friendly reform, stronger economic growth, faster fiscal consolidation and employment creation.

[1] Net return for the Nedgroup Investments Rainmaker Fund, A class. Source: Morningstar (monthly data series).

Portfolio Commentary

In the second quarter of 2024, the JSE All Share Index (ALSI) recovered strongly (+8.2%), offsetting the weak Q1 performance (-2.2%). The market-friendly outcome of the Government of National Unity spurred a market rally in June (ALSI +4.1%) which underpinned the quarterly outcome. The strength was driven by SA Financials (+15.9% for Q2), with SA Industrials (+5.2%) and SA Resources (+3.6%) lagging.

In comparison, the Nedgroup Investments Rainmaker Fund returned +2.9% for the quarter. While delivering a reasonable return, the fund lagged the JSE All Share return on account of the fund's global diversification with its offshore holdings not performing as strongly as South African domestic shares that were buoyed by the positive election outcome. Year to date, the fund (+6.1%) has outperformed the ALSI (+5.8%).

The top contributors to the fund's performance in Q2 were dominated by our domestic holdings, especially our domestic financials – namely, FirstRand (+24.6%), Sanlam (+22.4%) and Capitec (+27.0%). Anglo American (+23.9%) was the single largest positive contributor with the share price lifting on the back of BHP's offer for the business – subsequently withdrawn. In addition, our exposure to Naspers and Tencent also enhanced performance with Tencent reporting very strong earnings growth for Q124.

The top detractors for the quarter were several offshore holdings, namely Trex, Moncler and Eagle Materials.

Q2 Top contributors	Average weight	Performance contribution	Q2 Top detractors	Average weight	Performance contribution
Anglo American	5.5%	1.1%	Trex	1.7%	-0.6
FirstRand	4.7%	1.1%	Moncler	1.9%	-0.4
Alphabet	3.6%	0.6%	Eagle Materials	1.4%	-0.4
Sanlam	2.5%	0.6%	Samsonite	1.3%	-0.3
Naspers	5.8%	0.5%	Visa	3.0%	-0.3
Total		**+3.9%**	Total		**-2.0%**

Current positioning and outlook

Domestic SA Equity

The operating environment remained challenging during the first half of 2024.

Inflation, prolonged high interest rates, muted GDP growth and high unemployment continue to place local consumers under pressure. However, as we have communicated in recent reports, we have argued that due simply to base effects the outlook for domestic activity was improving, driven by the non-recurrence of negative factors such as the reduction in the intensity of load-shedding as privately installed solar and alternative energy sources relieved the pressure on Eskom. In reality, Eskom is performing better than we had expected. Lower inflation and interest rate cuts anticipated later this year are additional factors likely to boost consumption in SA and from September we will start to see the once off boost to be expected from the 2-pot retirement scheme relaxation which will allow households partial access to their retirement savings. These factors inform our domestic retail holdings, with key picks being Shoprite, Pepkor and Woolworths.

The fund also has substantial exposure to the South African banks, expressed chiefly through FirstRand and Capitec. During the quarter FirstRand released a positive trading update for their 2024 financial year, indicating robust revenue growth and a better operating and credit cost performance. Despite the challenging economic landscape and increased competition, Capitec has consistently outperformed its peers on key metrics (HEPS growth, ROE), and we expect this trend to continue over the medium-term. Capitec's transactional franchise has transformed the quality of the business, and in our view, a premium valuation is justified, given its excess capital, higher returns, best-in-class efficiency and new growth initiatives.

Anglo American is our largest resource holding (>5% weight) and was subject to a takeover proposal by BHP during the quarter. BHP's offer was rejected by the Anglos board twice and they countered with their own break-up strategy which they argue is expected to unlock greater value for shareholders. Anglos has set out a pathway to accelerate delivery of its strategy to make Anglos a simpler business focussed on Copper, Iron Ore (Kumba and Minas Rio) and Crop Nutrients (Woodsmith). Other divisions, including Anglo Platinum, De Beers, and their coal assets will be demerged or divested. We have owned Anglos as we felt that the firm's market cap did not reflect the full value of all its component assets. BHP's offer demonstrates this underappreciated value and we think over time a simpler, more focussed business (with >50% copper exposure) will be a very attractive investment for our clients (and possible future suitors). In addition to the restructuring, the combination of lower policy rates around the world, strengthening global growth and a weaker US dollar could lead to a lift in commodity prices later this year underpinning the near-term investment case.

Despite the recent lift in domestic equities fuelled by the positive election outcome, the SA market continues to trade at attractive levels relative to other comparable markets. While we expect bumps in the road of coalition government the GNU certainly raises the prospect for this to occur and we are in a better position to possibly succeed than at any time since 2008!.

Global Equity

After a very strong start to the year, stock performances varied materially in Q2, leaving the global portion of the Rainmaker Fund down for the quarter, despite some very strong contributors. This was no different to the US market where the S&P500 index had one of its most dispersed performances on record – 7 stocks delivered 66% of the index return and 100% of its earnings growth!

The consensus expectations of central bank rate cuts (following much reduced inflation), elevated but manageable geopolitical tension and the recovery of consumer spending in China got pushed back once again. The Ukrainian war and Middle Eastern conflict continue with slim hopes of imminent, peaceful resolutions. Elections across the world have caused much uncertainty as nationalism seems to be the only common denominator; be it the rise of the far right in France or the rising odds of Trump being elected again – this does not bode well for integrated global supply chains and trade.

The US consumer, strong out of the blocks post Covid, seem to have finally run out of excess savings (they were never big savers, but did build up ~$3trillion during Covid – now only about $480bn is left) at the same time as a double blow of two years of high inflation and higher-for-longer interest rates are having a very real impact on consumer wallets. The lowest pending new home sales and highest continuing jobless claims in 25 years attest to this.

In China consumer confidence remained frustratingly low – the combined toll of very strict Covid lockdowns, lower economic growth, increased unemployment amongst the younger population, the still bleak housing market, absence of a post-retirement social safety net and increasing trade tensions with the USA all conspire to result in little appetite to go out and spend. This is despite a record $19trillion of consumer savings having been built up (contrast this to the US excess savings total of just $480bn). There are green shoots of growth, but it remains anemic and not enough to cause general optimism in the stock market for consumer and related stocks. More recent initiatives from central government to resolve the housing crisis have delivered some early wins (Shanghai secondhand home sales in June increased 41% month on month). We remain convinced that the Chinese consumer will spend again – with current spending levels and expectations so low, even a modest recovery will be very positive.

Against the above relatively bleak backdrop, the +2.9% (in US$) performance of the MSCI All World Index is somewhat surprising. That is, until one looks at the contributors to this performance; US stocks make up about 65% of the index, with the "magnificent 7" (Nvidia, Microsoft, Google, Amazon, Meta, Eli Lilly and Apple) about 1/3 of the S&P500 index weight – or about 18% of the All Country World Index (which has 2,372 constituents). In the S&P500, these 7 stocks alone delivered 2/3's of the index performance and provided all the earnings growth (Eli Lilly replaced Tesla). 75% of the stocks in the S&P500 underperformed the index, the worst performance in over 30 years.

The Rainmaker Fund indeed owns Microsoft, Google and Amazon which did make a meaningful contribution to performance in Q2. Pleasingly, the fund's more diversified nature means that the likes of Tencent (+23%), Shell (+8%), and Intercos (+13%) also made very positive contributions to the fund's return. Unfortunately, the 10 worst performers in the fund negated these positive contributions by some margin. The weak US home sales number materially impacted Trex (-26%), Eagle Materials (-20%) and Moncler (-18%) declined on poor luxury goods sentiment. Amongst the Chinese holdings, Tongcheng Travel (-25%) and Samsonite (-22%) fared the worst as the weak Chinese consumer confidence numbers impacted the ratings of these travel related companies.

During the quarter, the fund added to Rheinmetall, the German defense business, more specifically after the stock retreated on (short lived) expectations of peace in Ukraine. We reiterate that peace deals in Ukraine and the Middle East, however positive that would be for the victims and general sentiment, will not detract from the long-term growth prospects for Rheinmetall. These conflicts, and the much-elevated global geopolitical tensions, starkly exposed the general underinvestment/spending on defense in much of Europe (and other countries). We are therefore expecting a multi-year stockpiling/rearmament of defense and related goods which will materially benefit the likes of Rheinmetall.

The fund initiated a new position in Proya Cosmetics, a leading Chinese cosmetics/skincare company. The Chinese cosmetics/skincare market is growing strongly, as seen elsewhere in the world. The sector benefits from consumers trading up as they use more expensive dermatological products, whilst the entry level continues to recruit new consumers as this is seen as an aspirational, feel-good and affordable product. Even during challenging times, the so called "lipstick effect" (feel-good smaller purchases) contributes to the sector. Proya is well placed with a range of products and brands that serve the consumer across income levels and preferences. Their flagship product category makes up 25% of sales and profits, but more importantly, help create a halo effect for the overall brand whilst also catering for the more aspirational and wealthier consumer. It has doubled its market share in China in the last 3 years, yet they only have about 3% share – this still makes them one of the largest local Chinese brands. Over the last year, imported cosmetics have declined by about 20%, whilst the local brands have grown. As a domestic and predominantly online retailer, they have managed to avoid the daigou dilemna (a sub-market where individuals buy large quantities of products in duty free zones to on sell again back in China) as the government has clamped down on this practice and hence caused significant declines in some international brands' sales to the duty-free territories. Proya brands have been the number one seller on a range of online channels (Tmall/Douyin/PDD) during the last year's special selling periods (e.g. singles day, 618, etc.).

Proya is expected to grow earnings at 23% compounded for the next 3 years, it has about 10% of its market capitalization in cash on the balance sheet, generates good cashflow, yet trades on 24X one year forward earnings and a current dividend yield of 1.2% (it pays out 30% of earnings – not common for Chinese stocks).

This PE ratio is well down on prior years as the company has increased earnings very strongly – we therefore believe this to be a good entry point for a business with much potential in an attractive and very large consumer sector. As they sell close to 100% of their product in China, they are shielded from geopolitical tensions (in fact, they would benefit if international brands withdraw).

The downside of Rand strength and a recovering SA equity market for Rainmaker is that the offshore positions were marked down. As much as we appreciate and invest in the local opportunities which we think is currently (and likely to remain) very favorable, we remain convinced of the benefit of offshore diversification; not just to hedge the currency, but more so for the significantly larger and more diversified investment opportunity set that it offers. It allows us to build a better, more diversified and balanced portfolio for the long run. In addition we have and will continue to hedge the currency impact of part (and even all) of the foreign positions back into Rand when we see cost effective opportunities to do so. This is another benefit of working in a multi-asset team where all of these alternatives are constantly being evaluated and considered.

Elevated geopolitical tensions, nationalistic rhetoric, disrupted supply chains, global warming and decarbonizing the energy complex all remain challenges for equity markets. This will make global stock picking more complex and will require more diversification across sectors and regions. Adversity and geopolitics do not curb investment opportunities, it just shifts them. The fund remains relatively conservatively invested and will continue to do detailed, fundamental research before investing. We remain confident that over the medium term the earnings growth of our shares should translate to attractive returns for investors.

Responsible Investment

Since the Paris Agreement in 2015, governments and societies have sought to accelerate the transition from fossil fuel-based to renewable-based energy systems to reduce carbon emissions. However, higher interest rates, elevated debt levels, inflation and complex geopolitics have limited the capacity of governments to fund the transition. Unfortunately, the world remains well off track to meet the Paris Agreement Goal of keeping global warming below 2°C above pre-industrial levels. In its assessment of progress towards 2030 targets, the Climate Action Tracker finds only 1 indicator of 42 is on track at the pace required. Assuming current policies and action, the world is on track for around 2.7°C of global warming by 2100.

In the face of the above data, it is of some concern to us that we have observed a growing anti-ESG rhetoric, particularly in the US, and which will likely be worsened by the possibility of a Republican presidency later this year. Even in South Africa, Eskom has recently been granted relief on emissions limits at some of its older coal-fired power stations.

After a flurry of interest and strong growth in 2020, dedicated ESG funds have experienced substantial outflows in the last 18 months. Partly, disappointingly, as a result of funds that were opportunistically launched into the fad and subsequently found by regulators and clients to have been fraudulently marketed and not managed in line with the fund's ESG mandate. But also due to poor performance. This illustrates the cold reality of the investment world – you must be able to produce returns acceptable to clients while at the same time consistently applying your ESG principles!

Abax is committed to investing in businesses that are proactively managing their interactions with society and the environment as well as taking steps to decarbonize their operations. This is turn will help protect our client portfolios from the systemic risks posed by climate change.

At Abax, we actively engage with companies and other stakeholders to address ESG issues. Notable ESG engagements during the second quarter of 2024 include:

- Absa: Engaged with Absa's treasury team on relevant regulatory changes for the banking sector (e.g. Basel IV, deposit insurance, etc).

- British American Tobacco: Engaged with company management with a specific focus on various regulatory issues.
- Anglo American: Participated in an ESG round table discussion with company management.
- Absa: Participated in an independent Stakeholder Engagement Survey.
- Raubex: Engaged with Board regarding adjustments to their remuneration incentive structure.
- Absa: Engaged with the Chairman of the Board and Head of Remuneration. The main discussion points included money laundering allegations, diversity & inclusion, data / cyber security and remuneration practices (including links to sustainability targets).
- Nedbank: Engaged with the Chairman of the Board and Lead Independent Director regarding varies ESG matters including IT oversight, climate change and progress towards net-zero, diversity, and financial inclusion.
- Woolworths: Participated in the Woolworths Stakeholder Perception Survey. The survey measures, trust, reputation, and the quality of their engagement with stakeholders.
- JSE: Engaged with the JSE as a member of the JSE Buy Side Council. Issues addressed included policy & regulation, market trends and key JSE initiatives.
- Woolworths: Engaged with Woolworths management regarding allegations of harassment and inappropriate behaviour in the workplace within the CRG Group (Australia).
- JSE: Engaged with management regarding the need from relevant authorities across jurisdictions to adopt the ISSB standards – IFRS S1 and IFRS S2 (ESG disclosure) – on an economy-wide basis by 2025.

Conclusion

Although the global macro-economic environment remains challenging, a new global monetary easing cycle has begun which should lead to firmer global economic growth and stimulate the run in global equity markets. The European Central Bank cut rates for the first time in nearly five years, joining the rate cutting cycle that has begun in a number of emerging markets and smaller developed markets (Sweden and Switzerland). Financial conditions are forecast to loosen further once US rate cuts come into focus – we expect in the next quarter.

Election (political) risk has been a big market theme in 2024, which will shift to developed countries in the second half of the year (French, UK and US elections). Recent election outcomes have been decidedly anti-establishment and during the second quarter we witnessed surprises in Mexico and even popular governments like Modi’s in India underperformed expectations. With respect to the US elections, the odds of a Joe Biden victory have collapsed to new lows following a poor showing at the head-to-head debate with former President Trump last month, while Trump’s odds increased to a new high of 59% (according to PredictIt). The prospect of a second Trump presidency amongst all the legal controversy he continues to face with the expected erratic statements and behaviour is not one markets will relish. Although his historic pro-US business and protectionist views towards the US economy, open hostility to some trade partners and demands regarding NATO defence spending will be favourable to many of the fund’s positions.

China’s growth has been erratic this year, and it has been unbalanced with exports growing strongly and domestic demand sluggish. The real estate market remains the biggest drag and while new policy initiatives to reduce housing inventory are steps in the right direction, the pace and implementation has so far been insufficient to address the problem fully. Trade tensions with the US remain, with Biden recently raising tariffs on Chinese imports of EVs, solar panels, batteries and more - the tariff hike is a reminder that negative China-related headlines is an ongoing risk in a US election year. We believe the collapse in P/E ratings of Chinese equities adequately reflects the heightened geopolitical and domestic risks.

Investors have been (understandably) incredibly negative on the prospects for genuine reform and economic growth in South Africa for over a decade. The economy has gone backward, evidenced by electricity shortages, the collapse of transport networks, rising unemployment, corruption and a fall in living standards, exacerbated by the Covid-19 pandemic. According to the World Bank, GDP per capita has fallen from a peak in 2011, leaving the average South African 23% poorer. Furthermore, public sector debt as a share of GDP has increased dramatically, with debt servicing costs consuming an ever-rising share of tax revenue – now >20%! Encouragingly, with the recent political landscape shift, there is for the first time since 2008 a realistic chance of economic reforms to drive growth and we see substantial further room for SA domestic equities to rally. Even after the initial rerating, we believe our banks, retailers and specifically some of the midcap industrial companies remain attractively valued in absolute and relative terms. In addition, there are multiple unrelated catalysts anticipated in the second half of 2024 which are growth positive including moderating inflation, lower interest rates, reduced loadshedding, improving Transnet performance and the boost to consumer spending as the 2-pot retirement saving system becomes accessible. Given the above-mentioned factors, together with the fact that our equity market is trading at a significant discount to emerging market peers, we are more optimistic about the prospects for the country's equities during the balance of the year.

Thank you for your ongoing trust in us - we remain committed to the delivery of superior long-term investment returns while fulfilling our role as an active and responsible investor.

Disclaimer

WHO WE ARE
Nedgroup Collective Investments (RF) Proprietary Limited is an authorised Collective Investment Scheme and the representative of Nedgroup Investments Funds PLC in terms of the Collective Investment Schemes Control Act. It is a member of the Association of Savings & Investment South Africa (ASISA)..

OUR TRUSTEE
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HOW ARE OUR FUNDS PRICED
Funds are valued daily at 15:00. Instructions must reach us before 14:00 (12:00 for Nedgroup Money Market Fund) to ensure same day value. Prices are published daily on our website and in selected major newspapers.

FEES
A schedule of fees and charges is available on request from Nedgroup Investments. One can also obtain additional information on Nedgroup Investments products on our website.

DISCLAIMER

Unit trusts are generally medium to long-term investments. The value of your investment may go down as well as up. Past performance is not necessarily a guide to future performance. Nedgroup Investments does not guarantee the performance of your investment and even if forecasts about the expected future performance are included you will carry the investment and market risk, which includes the possibility of losing capital. Our funds are traded at ruling prices and can engage in borrowing and scrip lending.

Some funds may hold foreign securities including foreign CIS funds. As a result, the fund may face material risks, which could include foreign exchange risks, market conditions and macro-economic and political conditions.

A fund of funds may only invest in other funds, and a feeder fund may only invest in another single fund, both will have funds that levy their own charges, which could result in a higher fee structure.

The Nedgroup Investments Money Market Fund offering aims to maintain a constant price of 100 cents per unit. A money market fund is not a bank deposit. The total return to the investor is made up of interest received and any gain or loss made on any particular instrument held. In most cases the return will merely have the effect of increasing or decreasing the daily yield, but in an extreme case it can have the effect of a capital loss. Excessive withdrawals from the fund may place the fund under liquidity pressures and that in such circumstances a process of ring-fencing of withdrawal instructions and managed pay-outs over time may be followed. The yield is calculated using an annualised seven day rolling average as at the relevant dates provided for in the fund fact sheet. Nedgroup Investments has the right to close its funds to new investors in order to manage it more efficiently.

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