NEDGROUP INVESTMENTS

UNIT TRUSTS | INTERNATIONAL | RETIREMENT FUNDS

see money differently

NEDGROUP INVESTMENTS RAINMAKER FUND

Quarter Three, 2024

Nedgroup Investments Rainmaker Fund

Stocks continued to rally in the third quarter of 2024. MSCI World markets returned +6.5% in US$, with MSCI Emerging Markets outperforming (+8.9%), lifted by a sharp rise from the Chinese market.

Monetary and fiscal measures announced by China in the last week of September had a galvanizing effect on financial and commodity markets. The PBoC unveiled its largest stimulus measures since the Covid pandemic to help the ailing property market and lift economic growth. This was followed by China's top leaders pledging fiscal support at the Politburo meeting held in September – the timing, a rare move for authorities, demonstrates an increased sense of urgency for China's policymakers. We believe that China's growth problems in recent years are primarily self-inflicted; thus, the decisive measures are expected to improve economic performance and the financial market outlook.

In September, the US central bank finally commenced cutting interest rates, with a larger than expected -50bps cut. Looking ahead, we see ongoing cuts by the Fed, the ECB, and other developed and emerging market central banks; however, there is still uncertainty regarding the timing and magnitude of these. The SA Reserve Bank also finally delivered a repo rate cut given the improved outlook for domestic inflation.

Sentiment around South Africa has improved since the coalition government was formed. This, together with improving domestic growth prospects has provided strong support to our equity market with the JSE ALSI appreciating >15% since the elections. The optimism is further evidenced by improving business confidence (rising to a 2-year high in Q3 – off a very low base it's important to add) as well as a strengthening currency (the rand is one of the biggest gainers against the US dollar year-to-date). The imminent Medium-Term Budget Policy Statement may add further support to sentiment by providing detail about policy reforms, particularly those related to infrastructure as well as possible solutions to state enterprise debt – notably at Transnet and Eskom.

Whilst global equity markets will be buoyed with central banks shifting policy to a more supportive stance, we do face a period of uncertainty over the next several months. The conflict in the Middle East has widened with possible implications for shipping (supply chains) as well as oil prices (inflation). In contrast to previous periods of conflict in the Middle East, diplomacy has failed to bring about any compromise. In addition, the outcome of the US election (in November) remains a key event with domestic and foreign policy implications (notably for China).

Encouragingly, South Africa remains a bright spot. With business-friendly policies, no load shedding, moderating inflation and monetary relief, the business environment has improved meaningfully – the combination is expected to improve earnings growth, cashflows, as well as dividends for domestic businesses and in turn should translate to attractive returns for shareholders.

Portfolio Commentary

In the third quarter of 2024, the JSE All Share Index (ALSI) returned a strong +9.6%. The strength was driven by SA Financials (+14.3% for Q3) and SA Industrials (+11.6%), with SA Resources (-1.5%) lagging. Positively, MSCI South Africa (+22.1% in US$), is among the best performing equity markets globally year-to-date. The SA rand appreciated by another +6% in Q3, to be up +6.1% against the US dollar year-to-date.

In comparison, the Nedgroup Investments Rainmaker Fund returned +5.2% 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 have been buoyed by the positive election outcome and the further impact of Rand strength versus US$.

The top contributors to the fund's performance in Q3 were dominated by our domestic holdings (Pepkor, FirstRand) as well as China exposed companies (Alibaba, Naspers). Pepkor (+29% in Q3) was the single largest positive contributor with the share price rising on the back of an improved outlook for discretionary consumer spending. Domestic prospects are more positive following the national election with consumption expected to lift over the medium-term given higher economic growth, easing inflation and lower interest rates.

In late September, Chinese authorities made clear the need for coordinated, decisive and effective monetary and fiscal stimulus to support the economy – this spurred an equity rally benefiting several of our holdings, most notably Naspers, Tencent, Alibaba and JD.COM. In addition, our exposure to British American Tobacco (+15% in Q3) also contributed meaningfully.

The top detractors for the quarter were several offshore holdings, namely Samsung, Alphabet and Microsoft. These companies are discussed in greater detail within the Global Equity section of this report.

Q3 Top contributors	Average weight	Performance contribution	Q3 Top detractors	Average weight	Performance contribution
Pepkor	3.4%	0.9%	Samsung	2.7%	-0.8
Naspers	4.8%	0.9%	Alphabet	3.1%	-0.5
British American Tobacco	4.2%	0.6%	Microsoft	3.2%	-0.3
Alibaba	1.2%	0.6%	Shell	2.1%	-0.3
FirstRand	5.8%	0.5%	Amazon	2.7%	-0.3
Total		**+3.4%**	Total		**-2.1%**

Current positioning and outlook

Domestic SA Equity

In the concluding paragraph of the Q2 2024 commentary, we expressed a very positive outlook for the local market for the balance of 2024. Given the subsequent performance of the local market during Q3 (already covered above) and notably in the Financial and Industrial sectors, many investors are likely to be asking themselves if they should be taking some profit on their domestic portfolios.

In the short-term this makes good logical sense and especially in the context of where in South Africa we have had false starts before – recall the Ramaphoria period and subsequent disappointment of late 2018, early 2019.

In addition we fully acknowledge that many of the structural problems that have caused the SA economy to stagnate continue to be present and as a quick reminder we would point to amongst others the following:

1. Failing state provision of crucial infrastructure in a country where private provision remains crowded out – power, transport (freight and passenger), municipal services and now also water and sanitation.
2. Unsupportive centrist state economic policies and inflexible labour regulation.
3. High and increasing levels of state indebtedness and rising levels of cost of borrowing.
4. A failing public education system and rising unemployment.
5. Neglect of fixed investment spending and a rising social welfare burden on a stagnant and over exploited tax base.

While all of the above are factually correct, in a 5 month post-GNU South Africa and judging by the following incremental data points we have the view that undeniably the SA economy and business and consumer environment look healthier than at any time since the 2008 GFC – and more importantly despite the price move of the last quarter, domestic equity valuations largely remain attractive.

1. We have now had 195 days of zero loadshedding, the electricity availability factor continues to improve but 2024 marks the highest capital spend of privately produced electricity infrastructure – and which will continue into 2025 and beyond. Transnet has a new management team and a plan with the direct involvement of the private sector to slowly increase rail freight volumes – although this is likely to take years and the balance sheet hurdle has not been addressed.
2. Operation Vulindlela continues to gather momentum and some failed municipalities have been taken over.
3. In the GNU several SACP members and strong anti-private sector opinion holders have been replaced – notably Ebrahim Patel, Pravin Gordhan and Blade Nzimande. In addition we have observed encouraging progress and more importantly embrace of the private sectors ability to fix problems in some portfolios – notably Home Affairs (tourism), Trade and Industry, Transport and Health (NHI now under constructive discussion).
4. Interest rates have started to decline and we expect more cuts imminently.
5. The 2 pot system has started to be accessed, boosting debt repayment and consumer spending.
6. The petrol price is 20% lower than 1 year ago – all released into the economy.
7. NPA prosecutions are continuing (although glacially slowly), the NPA is receiving greater resource funding and we have a reasonable chance of being rehabilitated from grey-listing status in 2025.
8. With the exhaustion of outflows from SA following the Reg 28 foreign investment limit relaxation in 2022 and the likely turn in consistent net outflow of foreign investor exposure to SA we feel the tide has “stopped going out”!

In this context of these points we conclude that the answer to the question posed above is no – this is not the time to sell or even reduce SA equity exposure.

Global Equity

In Q3, global markets continued to grind higher, although intra-month volatility increased amidst multiple layers of uncertainty.

Our previous quarterly comment bemoaned the global macro themes of elevated geopolitical tensions and rhetoric, divisive elections across the world, continued (and worsening) wars in Ukraine and the Middle East and the continued postponement of the imminent rate cut cycle in the US. Unfortunately, these themes worsened in Q3, except for the USA's Fed making their first, larger than expected, interest rate cut on September 18th. A week later the Chinese central government announced unexpectedly large stimulus measures to ease their housing crisis. Combined, these two events boosted stock markets, especially in China, where the Shanghai Composite Index bounced +21% in the last 5 days of September. China boosted the Emerging Market index performance from +4.1% to +8.9% in Q3, thereby outperforming the MSCI World Market's 6.5%.

During the quarter, the top global contributors were Eagle Materials (share price increase of +32%), Alibaba (+56%), JD.Com (+62%) and St James's Place (+33%). Detractors were Samsung Electronics (-21%), Google (-9%), Shell (-15%), Trex (-10%) and Heineken (-12%).

The dominance of Chinese stocks in the above contributor list is clear. It is pleasing to see our patience paying off. Our Chinese positions appeared very attractively valued coming out of material Covid lockdowns, but the resurgence in consumer expenditure just never materialized. Despite that, these companies continued to grow and generate cash, adding to the net cash balances on their balance sheets. The lack of consumer confidence because of the housing crisis has caused a material slump in consumer spending, despite an unprecedented $18 trillion of built up personal savings. Where Western monetary authorities stimulate their consumers/voters into loosening their purse strings, the Chinese government's preference has been to rather stimulate through the country's capital stock. They have built transport networks and factories that will employ and uplift more people than hand out cheques to fuel potentially unsustainable consumer expenditure. Their stimulus measures have focused more on reducing lending rates and deposit hurdles to kick-start the housing market, whilst also reducing various local and state housing ownership limitations. The size of this latest stimulus was more than expected and hence the positive market reaction. The real impact on economic activity and consumer expenditure will take longer to manifest. In addition, we've started to see more shareholder friendly actions by Chinese companies in the form of higher dividend payout ratio's and share buy-backs. Given the significant cash balances on many of the company's balance sheets, these actions are key to investor confidence. Alibaba, as an example, is now on a 6-8% yield ratio with their significant share buy-back and enhanced dividend.

St. James Place is another example of the fund taking advantage of a market dislocation to acquire a quality asset at a much-reduced price. St. James's has long been a large and very successful agency investment distribution business, focusing on the mass affluent market through their own salesforce and life company and unit trust group. After customer complaints over service failures and questionable fee calculations, a regulatory review was initiated. The immediate market concern was a significant reduction in their fee structure and calculations that would negatively impact their financial model and hence valuation. St James's acknowledged some shortcomings and incorrect fee calculations and provided against potential remedies, in turn giving comfort to investors fearing a loss of the client base and/or their advisor headcount. But during this period of uncertainty the share price dropped 75% from its peak. This created the opportunity for us to acquire a quality asset with excellent long-term value potential and which is now well on the road to recovery and in a healthier state.

The detractor list represents more idiosyncratic, company specific events. Samsung has been a disappointment (one could question whether this is a so-called value trap); despite good operational and financial performance in a technology sector that is in strong demand, the stock just did not grow with the earnings. Despite material capital investment (to stay ahead of the pack with their manufacturing expertise and capacity), Samsung continues to generate free cash, has ¼ of the market capitalization in net cash on the balance sheet and trades on a single digit forward PE multiple.

The very concentrated nature of the US stock market performance is of concern (year to date 5 stocks delivered half the performance, with 66% of stocks performing worse than the benchmark). The fund continued to lighten the holdings in long term winners Microsoft and Google (2 of the "magnificent 7") during the quarter. We continue to believe in the investment merits of these companies, but consider their valuations to be stretched.

The fund also reduced our holdings in Autozone and Eagle Materials after strong share price performance. Whilst the US car park continues to age (now averaging 13 years) and will thus require maintenance and spare parts, the US consumer has spent her excess savings post Covid and we believe will likely cutback on maintenance in the near future (as in previous economic cycles) adversely impacting Autozone in the short-term. In addition, we anticipate softness in building material demand, informing our decision to take some profit in Eagle Materials.

During the quarter the fund added to Alibaba and JD.Com as their valuations seemed to be at extreme low levels, yet they maintained their strong balance sheets and good operational and financial performance. The JD.Com addition was particularly pleasing as the stock appreciated +63% since. Even after the share price uplift, the business only trades on an 11X forward PE multiple with more than 40% of their market cap in net cash.

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

The availability and quality of ESG related disclosure within emerging markets (such as South Africa) requires improvement. As part of our engagement activities, we encourage companies to publish policies and sustainability reports as a framework for establishing goals for improvement and as a means of providing important information to investors. However, we still find that companies don't explain their social and environmental commitments in a comparable way. Consequently, we have endorsed and are a signatory to the PRI call for commitment from relevant authorities across jurisdictions to adopt the ISSB standards (IFRS S1 and IFRS S2) on an economy-wide basis by 2025. We have also engaged with the Johannesburg Stock Exchange regarding this matter. Regulators and policymakers have an essential role to play in addressing the gaps in sustainability-related data, through the introduction of requirements on the disclosure of key sustainability-related information. This will help analysts, fund managers and clients measure and manage social and environmental impacts and risks more effectively.

The regulatory backdrop continues to evolve and during the quarter President Ramaphosa signed the Climate Change Bill into law. The Climate Change Act will form the legislative foundation for South Africa's climate change mitigation and adaptation response. This will include a national greenhouse gas emissions trajectory as well as Sectoral Emissions Targets (SET) and an allocation of carbon budgets. Individual national government departments will be tasked with developing and implementing policies and measures to ensure emissions from within a sector or sub-sector remain within SET limits. Carbon budgets will put in place a maximum volume of emissions that companies will be allowed to emit over three rolling five-year periods. This is intended to drive mitigation in the private sector, and the penalty for not complying will be in the form of a carbon tax.

Notable ESG engagements during the third quarter of 2024 include:

- Shoprite: Engagement with the Group's Head of Sustainability about plastics, the circular economy, food waste and Sixty60 driver safety.
- Mr Price: Engagement with the CEO and senior management regarding ESG priorities, with a specific focus on supply chain strategies.
- WWF: Discussion with WWF (South Africa) regarding plastics and the circular economy.
- UNPRI: Attended a PRI signatory event with the PRI CEO to discuss the latest news from the PRI as well as initiatives to enhance the Responsible Investment agenda in South Africa.
- Vodacom: Engagement with the Chairman as well as various board subcommittees' chairs, covering ES and G matters. The discussion mostly centred around governance, specifically executive incentives (STI and LTI measurements) and our dissatisfaction regarding the lack of alignment between management remuneration versus shareholder returns.
- Bidvest: Engagement with management on water use and emission reduction strategies as well as new targets. In addition, data security was discussed, specifically the AI control of networks to detect misuse or potential cyber breaches.
- BHP: Engagement with senior executives regarding safety (given 3 recent fatalities), their Climate Transaction Action Plan as well as new technologies to reduce scope 3 emissions.

Conclusion

We have nothing more to add over and above that contained in the above and continue to feel that the prospects for the fund look very attractive.

The domestic portfolio is concentrated and offers compelling exposure to an ongoing local economic and consumer recovery with a mix between large cap and mid cap businesses. The global stock selections offer diversified exposure to high quality businesses that are not comparable to anything available in the SA market and offer exposure to attractive long term commercial opportunities.

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
The Standard Bank of South Africa Limited is the registered trustee.
Contact details: Standard Bank, Po Box 54, Cape Town 8000,
Trustee-compliance@standardbank.co.za, Tel 021 401 2002.

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.

NEDGROUP INVESTMENTS CONTACT DETAILS
Tel: 0860 123 263 (RSA only)
Tel: +27 21 416 6011 (Outside RSA)
Email: info@nedgroupinvestments.co.za
For further information on the fund please visit: www.nedgroupinvestments.co.za

OUR OFFICES ARE LOCATED AT
Nedbank Clocktower, Clocktower Precinct, V&A Waterfront, Cape Town, 8001
WRITE TO US
PO Box 1510, Cape Town, 8000

Issue Date: October 2024