COMMENT ON

UPDATE: Considering the investment implications of a Ramaphosa departure

7 December 2022

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South Africa's political future suddenly became much more uncertain on 1 December with the independent Parliamentary panel's findings of "prima facie" evidence that President Cyril Ramaphosa had committed impeachable offenses related to the Phala Phala scandal. We are very concerned about these developments and are keeping a close eye on the unfolding news, while also studying different future scenarios that could result. Importantly, we have considered whether this merits changes to our client portfolios and how best to position them as a result.

As our clients know, we do not pretend to know the future, and will not invest on the basis of forecasting uncertain outcomes, since the risk of being wrong is high. There are several possible scenarios as to who might become President of South Africa going forward, including Ramaphosa himself -- the President's ANC supporters have rallied behind him. One thing we can be certain of, however, is that markets intensely dislike uncertainty, and South African asset prices were punished on the back of the announcement of the report's findings and rumours that Ramaphosa was set to resign immediately.

The rand, government bonds and domestically focused stocks were hit hard, as investors considered the implications of Ramaphosa being replaced by various alternative ANC leaders, all of whom are much less well-known, and well-liked, by the markets. Even if Ramaphosa continues in his role, there is the risk his standing in the ANC is diminished, and his ability to continue driving a reform agenda through the NPA, SARS, the SIU, and Operation Vulindlela, to name a few initiatives, may be impaired.

The fact is that the long-scheduled ANC leadership elections taking place on 16-20 December now take centre stage. With different ANC factions split on many issues, there is sure to be aggressive bargaining for votes behind the scenes.

None of the potential replacements for Ramaphosa offer comfort to investors, largely being unknown quantities to global audiences. As such, we would expect elevated levels of uncertainty to keep our markets volatile and vulnerable to further losses as the situation develops. Any new President would need to make known his (or her) policy positions in order to ease investor concerns.

Despite these uncertainties, as of the time of writing, the rand and government bonds had recovered some of their losses of 1 December, but remain at weaker levels, implying that there has been a rise in the short-term risk premium applied to these assets, as well as to domestically focussed equities. Historically, taking Nenegate as one example, such spikes in risk-aversion tend to be short-lived, and consequently can present buying opportunities for us as valuation-based investment managers.

Our process remains deliberately focused on the medium-term outlook. To the extent that new facts present themselves that cause us to view that outlook as impaired, we would reflect that in client positioning. At present, there are almost no facts beyond the sell-off in asset prices on which to base a change in our outlook. Consequently, our general approach would be to back the valuation signals, which remain in favour of South

African assets in terms of their expected real returns over the medium term.

Our client portfolios have already been carefully positioned to weather the exceptional global market volatility of the past year given the deteriorating growth, rising inflation and interest rates and global equity and bond weakness we have experienced. They have been well diversified across global and South African markets, and we have added assets at attractive valuations to help cushion market downturns. In equities, we have chosen companies that are price-makers in their sectors to help safeguard their margins in the current high-inflation environment, as well as those with strong balance sheets that can avoid expensive debt costs and deploy cash when necessary. These defensive characteristics can help our portfolio performance through this period of uncertainty.

In fixed income, we are overweight government bonds on the basis of prospective real returns of over 6.0% on longer-maturity securities, and remain comfortable with this view. Should yields remain at more elevated levels, if anything, our process would identify this as a potential opportunity to add exposure. Looking beyond the immediate horizon remains central to our investment process and has served our clients and their portfolios well for more than 25 years. The notable events of 1 December will not change this approach. □

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