Consider this

Consider this: Q3 2023 - CEO Letter

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Chief Executive

During the third quarter of 2023, global equities and bonds experienced a significant sell-off as a result of growing risk-off investor sentiment, especially in September. This was brought on largely by the increased likelihood of "higher for longer" interest rates and pessimism around global growth. South African financial markets followed suit, so that few local asset classes ended the quarter with positive returns, apart from inflation-linked bonds and shorter-term, cash-type investments. This left Income portfolios as the relative outperformers for the period. For more about market developments and our latest views, please read David Knee's Q3 Market Observations commentary.

Safety in cheap SA valuations

In such times, investor patience and nerves may be tested, but experience shows that it pays to stay invested in growth assets and wait for the cycle to turn. This is the topic of Pieter Hugo's Table Talk article in this edition of Consider this. Global interest rate hikes are nearing their end and inflation continues to ease in most economies, which should reduce current levels of investor pessimism. In South Africa we have seen evidence of this as the SARB has kept the repo rate steady since May and inflation has fallen within the 3-6% target range. Near-term growth forecasts have also been revised higher both in SA and abroad, even as prospects for 2024 have moderated somewhat. Still, we are optimistic that there is safety for investors in the very cheap valuations we're seeing in SA equities and bonds currently. While we recognise that local risks have risen, in our view SA assets are still overcompensating investors for the risks involved in holding them, and investors should be rewarded with above-market returns from them over the next three to five years.

M&G fund performance*

-The M&G Income and Enhanced Income Funds posted positive returns in Q3 2023, delivering 2.6% and 2.1%, respectively, and outperforming the average fund returns of their ASISA categories at 2.2% and 1.6%, respectively. The performances extended both funds' strong relative results over the past three years.

-The M&G equity funds produced returns of between -2% and -4% over the quarter, but the M&G Dividend Maximiser Fund, for example, has still produced 14.4% over the past 12 months and 16.6% p.a. for the three years to 30 September 2023.

-The M&G Balanced Fund was also in the red for the quarter, but it has given clients a 12.8% p.a. return over both the one- and three-year periods.

Exploiting market volatility

We capitalised on the turbulence in global bond markets in September by adding to our portfolios' exposure to long-dated US Treasuries, UK gilts and German bunds at the highest yield levels for over 15 years. These instruments also act as strong diversifiers for local equity risk. In South Africa, we have been selective in our purchases, ensuring we buy undervalued stocks that have pricing power and strong balance sheets and cashflows, for example adding to our holdings of British American Tobacco at an attractive valuation in the M&G Balanced and M&G Inflation Plus Funds during the quarter to take advantage of its defensive characteristics.

Reaching out to clients

Amid the uncertain conditions we believe it's particularly important to communicate with our clients to help them understand what we're thinking and doing to grow and protect their investments. During the quarter we spent considerable time interacting with our clients through many events hosted by ourselves and jointly with other investment managers. The highlight was our annual showcase event, Face to Face, hosted by our CIO David Knee, in which we shared our latest views in Johannesburg, Pretoria, Durban, Gqeberha, Cape Town and Windhoek. I'm very pleased that we were able to bring M&G's expert managers to so many of our clients and that, judging from the positive feedback, it was well received.

While Face to Face is tailored toward financial advisers and individuals, we have also been active in our interactions with institutional investors through our participation in events hosted by the Institute of Retirement Funds Africa (IRFA) and Batseta. Most recently M&G hosted a "Diversity and Inclusion"-themed breakfast exploring the role of investing in promoting diversity, and featuring Thembeka Stemela Dagbo, a London-based M&G Deputy Fund Manager focusing on a range of investment strategies aimed at delivering meaningful positive outcomes, while addressing societal and environmental challenges

A new CSI partnership

I'm also happy to report that we welcomed the Amoyo Foundation as a new partner in our Corporate Social Investment (CSI) programme in September. Focusing on the underprivileged communities of Imizamo Yethu and Hangberg in Hout Bay, Cape Town, they help build children's confidence and valuable life skills through teaching the performing arts. They offer daily after-school and holiday classes of a high quality in dance, musical drama, speech, singing and performance, among others, to children of all ages in a "spirit of appreciation" (which is the definition of "amoyo"). The emphasis is on life and communications skills, emotional intelligence, self-discipline and core values so that students can become highly employable and lead successful lives once they finish matric.

In conclusion, the past quarter's market performance was not a friendly one for investors. However, as mentioned above, we are now at a turning point in the interest rate cycle, from rising to steady – and eventually falling – interest rates. History has shown that periods of falling interest rates are of course positive for bonds and, ultimately, economic growth, and therefore also for equities and listed property. As I have noted before, patient investors should be rewarded for staying exposed to attractively valued growth assets and maintaining well-diversified portfolios over time. We are confident that our portfolios are well-positioned to take advantage of improving conditions and investor sentiment.

*All quoted returns are after fees. Source: Morningstar data to 30 September 2023.