NAMIBIA ASSET MANAGEMENT

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CORONATION

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NAM CORONATION BALANCED PLUS FUND

QUARTERLY COMMENTARY Q2-23

Please note that the commentary is for the retail class of the Fund.

Performance

The Fund returned 6.9% for the quarter (Q2-23), benefiting from its meaningful exposure to equities (particularly global) built up during 2022. The Fund has performed well against its peer group over all meaningful time periods.

Fund positioning

Global markets have delivered a strong performance year to date (YTD), with the MSCI All Country World Index (ACWI) up 14% YTD (and 6% for the quarter). Fears of a US recession are receding in the face of robust employment data and resilient consumer demand. The S&P 500 rose 9% for the quarter (and is now up 17% YTD) to end the period at a level that is within 10% of its December 2021 high. We took full advantage of market weakness during 2022 to build a sizeable position in global equities. This position has benefited from market strength. The extent of the recovery means upside largely lies in stock-picking from here. The much-touted post-Covid Chinese recovery has disappointed. Weaker-than-expected Chinese growth has resulted in softer commodity prices. Oil too was lower despite OPEC's efforts to reduce supply.

Central banks continued to raise rates during the quarter given persistently high inflation. In June, the US Fed announced a pause in the rate hiking cycle (as inflation moderated), although further increases may yet be necessary. The Bloomberg Barclays Global Aggregate Bond Index declined -1.5% for the quarter (up 1.4% YTD). Bond yields are closer to normal levels, but still offer inadequate compensation for heavily indebted sovereign balance sheets. The Fund has no exposure to developed market sovereign bonds. This is consistent with its positioning for many years. Unlike the narrow credit spreads in Namibia and South Africa (SA), global credit bonds offer more attractive pricing. We have built up a basket of credit names trading on high single-digit hard currency yields.

The Namibian economy remains on an expansionary trajectory, largely attributable to foreign investment within the mineral space, investments in green hydrogen pilot projects, ongoing expansion of major roads across the country. Improved economic activity is however yet to translate into meaning employment, as youth unemployment remains one of the country's biggest challenges. Risks to local growth include a weaker external environment going forward, with the demand for commodities expected to slow down further.

Our exposure to Namibian Breweries bode well for performance during the quarter, following the market's appreciation of value of the domestic business once the dividend from the sale of Heineken South Africa was received.

The SA economy continues to face numerous headwinds as failing infrastructure (including power, water, and rail) and services undermine productivity and growth. These challenges alongside foreign policy missteps undermined the currency which weakened -6% against the USD for the quarter (-10% YTD). The sustainability of the improved energy availability in the last few weeks is uncertain as planned maintenance is running below what we believe is required. Challenging production, combined with falling prices of key metals (coal and PGMs), will weigh on export revenues in 2023. The fiscal situation has deteriorated in the face of revenue pressures, the rising costs of servicing debt, a higher public sector wage deal, and ongoing SOE support. The FTSE/JSE All Bond Index delivered a return of -2% for the quarter (+1% YTD). Despite high SA government bond yields, the Fund has a meaningful underweight position here. Part of the Fund's bond holding sits in inflation-linked bonds (ILBs) that offer protection against sticky domestic inflation (exacerbated by rising costs of production). Inflation concerns have resulted in ongoing rate hikes by the South African Reserve Bank despite the weak economy and mounting consumer stress. We believe growth assets (both global and local equities) offer better risk-adjusted returns.

In SA, the FTSE/JSE Capped Shareholder Weighted Index (SWIX) returned 1% for the quarter (4% YTD). The pricing of SA equities remains attractive with broad value across resources, global stocks listed on the JSE, and domestics.
Within the domestic universe, considered stock picking is required to identify businesses that can deliver real earnings growth despite the subdued growth outlook and rising costs of doing business. A slew of weak results across the retailers has illustrated the pains of costs growing faster than top line. We favour businesses with strong business models that can grow and pass on inflationary pressures to customers. ADvTECH is one such business where careful cost management is enabling management to contain fee increases at or below inflationary levels, and therefore grow enrolments strongly.

The financial sector rose 6% for the quarter (YTD 6%). The Fund has a reasonable holding in the banks given their low ratings and attractive high-single digit dividend yields supported by good capital positions. The banks are exposed to the tough consumer environment but conservative advances growth into this cycle and high levels of provisioning should mitigate credit losses. The endowment benefit brings further earnings support for unhedged banks like Standard Bank and Nedbank. Corporate lending is expected to bolster revenues.

The resource sector was down -6% for the quarter (-11% YTD). Slower global growth and weaker-than-expected Chinese demand have resulted in market imbalances and price declines across many commodities. The Fund meaningfully cut its resources exposure over the last two years as we exited PGMs and gold and trimmed diversified miners. The large underweight position in PGMs has benefited the Fund over this period while the more recent sell-down in gold names has hurt. The outlook for PGMs is deteriorating as EV (electric vehicle) adoption accelerates and local producers battle rising costs of production. We have no exposure to pure play PGM producers. Local gold producers have also battled rising production costs over time. AngloGold's recent operational performance was disappointing in this regard. Current ratings for the SA gold shares don't offer a sufficient margin of safety for the short life, high-cost nature of these assets. The bulk of the resource exposure sits in Glencore, Anglo American, and energy names. The diversified miners offer attractive free cash flow streams, even at more normal commodity prices and we have maintained a reasonable holding. We expect energy markets to be tight over the medium term as demand remains robust during the transition to lower carbon energy sources and the lack of investment in new capacity over the last few years constrains supply. We have diversified our energy holdings across a global basket of names to reduce company-specific risk.

The Industrials Index rose 3% for the quarter (+17% YTD), led by many of the global stocks listed in SA. Richemont, Aspen, Bidcorp and Anheuser-Busch InBev, are all meaningful holdings that have contributed to YTD performance. Naspers/Prosus remains a sizeable holding in the Fund. We were pleased by recent management actions which once again illustrated commitment to narrowing the discount and maximising shareholder value. As part of the recent results, Prosus management announced the simplification of the corporate structure which involves removing the previously created cross shareholdings. This cross shareholding created unnecessary complexity and most likely contributed to the persistent discount to net asset value. This simplification also removed any constraints to Naspers's ongoing share buyback programme which continues to create shareholder value daily at both Prosus and Naspers.

The portfolio has limited property exposure, preferring to use its risk budget in equities. The property sector has lagged equities (5-year -5% CAGR). A weak economy, nodal decay and chronic cost pressures undermine the medium-term outlook.

Portfolio managers

Karl Leinberger and Sarah-Jane Alexander
as at 30 June 2023