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

**Performance and fund positioning**

The Fund returned 0.52% in April, bringing its 12-month total return to 9.82%, ahead of cash (8.22%) and its benchmark (9.07%) over the same year. We continue to believe that current positioning offers the best probability of achieving the Fund's cash + 2% objective over the medium to longer term.

Local 'bonds' performance in April was uninspiring. The FTSE/JSE All Bond Index (ALBI) delivered 1.37%, with the long end of the curve (12+ years) posting the best returns, up 2.31%. The belly of the curve (7-12 years) closed 1.27% higher, while medium-term bonds (3-7 years) returned 0.56%. Short-term bonds (1-3 years) were up 0.41%, while cash was up 0.65%, and inflation-linked bonds (ILBs) were up 0.26%.

April dataflow was dominated by first-quarter 2024 (Q1-24) economic growth readings, with the US, China and the euro area showing soft but positive quarter-on-quarter (q/q) growth. Inflation readings remained steady, marginally easing from the previous month, with food prices declining but core inflation broadly sticky. Better-than-expected growth with persistent inflation remains a prevailing theme.

In the US, the economy grew by 1.6% q/q in Q1-24 from 3.4% q/q in the fourth quarter of 2023 (Q4-23). Growth was supported by strong consumer spending, increases in fixed asset investment, and government spending at the state and local levels. Subdued private inventory investment and an increase in imports detracted from the overall growth rate.

At the Federal Open Market Committee (FOMC) meeting in early May, the Federal Reserve Board (Fed) left the Fed funds rate unchanged at the 5.25%-5.50% target range. The FOMC statement noted strong economic activity, resilient labour markets and the low unemployment rate in the US as conditions that supported their ongoing tight monetary policy settings. The FOMC also cautioned that inflation remains elevated, and there has been limited progress towards reaching the 2.0% inflation target. Headline inflation rose to 3.5% year on year (y/y) in March from 3.2% y/y in February, while core inflation remained unchanged at 3.8% y/y – both well in excess of the c. 2% long-term target. The increase in inflation was driven by a rise in energy costs, shelter, and apparel and was partly offset by the moderation in food prices.

In emerging markets, 'China's economy grew by 1.6% q/q in Q1-24 from a revised growth of 1.2% q/q in Q4-23 and 5.3% y/y. The growth was mainly due to government spending on infrastructure and an export-driven recovery in manufacturing. Retail sales were also up, as wage growth remains positive. However, the property market remains weak and will remain a drag on overall activity.

The rand ended the month at R18.79/US$1. 'SA's idiosyncratic problems and the turn in global risk sentiment continued to weigh on the ZAR. Offshore credit assets and certain developed market bonds continue to flag as relatively attractive. The Fund has utilised a significant part of its offshore allowance to invest in these assets. When valuations are stretched, the Fund will hedge/unhedge portions of its exposure back into rands/dollars by selling/buying JSE-traded currency futures (US dollars, UK pounds, and euros). These instruments are used to adjust the 'Fund's exposure synthetically, allowing it to maintain its core holdings in offshore assets.

In South Africa (SA), headline inflation eased to 5.3% y/y in March from 5.6% y/y in February, while core inflation slowed a little to 4.9% y/y from 5.0% y/y. The drop was driven by a moderation in food and fuel costs. Elsewhere, prices were generally soft, with modest gains in apparel, household services, restaurants, and hotels.

At the end of April, shorter-dated fixed-rate negotiable certificates of deposit (NCDs) traded at 9.43% (three-year) and 10.05% (five-year), higher compared to the end of the previous month. Our inflation expectations suggest that the current pricing of these instruments remains attractive due to their lower modified duration and, hence, high breakeven relative to cash. In addition, NCDs have the added benefit of being liquid, thus aligning the Fund's liquidity with the needs of its investors. The Fund continues to hold decent exposure to these instruments (fewer floating than fixed), but we will remain cautious and selective when increasing exposure.

The significant reduction in rate cut expectations over the last quarter has tainted the enthusiasm for risk assets. However, the monetary policy pivot still remains in play, and, as such, emerging markets should continue to see supportive flows into their markets. Idiosyncratic SA factors have led to further underperformance of SA assets relative to the peer group. Low growth, sticky inflation and burgeoning deficits will continue to weigh on the longer-term outlook for SA unless reform implementation is accelerated through increased private sector participation. 'SA's bond yields remain elevated but still provide an attractive alternative to cash, given their high embedded risk premium.

ILBs are securities designed to help protect investors against inflation. They are indexed to inflation so that the principal amount invested and, hence, the interest payments rise and fall with the inflation rate. ILBs have offered protection to investors since the start of the year. However, current breakeven inflation across the ILB curve averages between 5.5% and 6%, which is well above even our own expectations for inflation over the medium term. It is only the shorter-dated ILBs (I2029, six years to maturity and I2033, nine years to maturity) that flag as fairly valued from a valuation perspective. Risks on the inflation front still remain elevated, and these shorter-dated ILBs, due to their inherent inflation protection, warrant a decent allocation within portfolios.

The local listed property sector was down 0.48% over the month, bringing its 12-month return to 13.24%. Operational performance will remain in the spotlight as an indicator of the pace and depth of the 'sector's recovery. The current poor growth outlook, combined with an increase in cost base due to higher administered prices and second-round effects on loadshedding, will weigh on the 'sector's earnings in the coming year. We believe that one must remain cautious due to the high levels of uncertainty around the strength and durability of the local recovery.

We believe that allocating significant amounts of capital to the local credit market is unwise and would represent a substantial opportunity cost in the face of attractive valuations in other, more liquid asset classes. The current level of credit spreads on offer are at historically compressed levels despite SA being close its weakest economic position in its history. Corporate profitability and creditworthiness are inevitably tied to economic outcomes, with significant polarisation in performance. SA is a sub-investment grade economy and, thus, local credit should trade at high yield spreads. However, SA trades as an investment grade issuer. The only spreads that trade at the high yield equivalent are riskier issues coming from taxi financing, subordinated tranches of securitisations and bank debt. This also shows, how much better value there currently is in offshore credit, which offers higher credit quality and better diversity at much more attractive valuation levels.

The use of structured products, such as credit-linked notes (CLNs), have become ubiquitous within the local market. This sector of the market has grown exponentially over the last five years and has reached a market size of over R100 billion, but only a third of this market reprices, creating an inaccurate representation of asset volatility and pricing. 'CLN's mask the underlying/see-through credit risk as the issuing entity (predominantly local banks) is seen as the primary credit risk. The increased usage of CLNs has not expanded the pool of borrowers, rather it has only served to concentrate it. This is due to the ability to limit the volatility of these instruments through not marking them to market[1] based on the underlying asset price movements. This is why CLN repacks of SA government bonds have become so popular over the last five years. The combination of attractive yields and no volatility is an opportunity that not many would pass up, unless, of course, transparency of pricing is important to the underlying investor. As a result, there can be significant unseen risks within fixed income funds. Investors need to remain prudently focused on finding assets of which the valuations are correctly aligned to fundamentals and efficient market pricing.

**Outlook**

We remain vigilant of the risks from the dislocations between stretched valuations and the local economy's underlying fundamentals. However, we believe that the 'Fund's current positioning correctly reflects appropriate levels of caution. The 'Fund's yield of 10.3% (gross of fees) remains attractive relative to its duration risk. We continue to believe that this yield is an adequate proxy for expected Fund performance over the next 12 months. As is evident, we remain cautious in our management of the Fund. We continue to invest only in assets and instruments that we believe have the correct risk and term premium to limit investor downside and enhance yield.

**Portfolio managers**
**Nishan Maharaj and Mauro Longano**
as at 30 April 2024

[1] Valuations are not regularly adjusted to mirror their current value