ViewPoints

Summer Edition - January 2021

At a glance – our asset class views

Please be aware that there are risks in simply implementing these views into a portfolio without carefully considering the dynamic nature of the environment, how changes impact each asset class and the unique needs of each client.

While our long-term real return assumptions are derived assuming that markets are in equilibrium, we do not believe that is the case all the time. We therefore take views (tactically over/underweight) on relative asset class performance over three to twelve months, specifically ignoring shorter term noise, and not relying on long-term expectations i.e. we need to see the catalyst for the relative performance.

Domestic SA	**Comment**	–	°	+
Equities	Overweight – potential beneficiary of risk-on trade			+
Listed property	Underweight – weak economic fundamentals	–		
Bonds	Overweight – attractive real yield opportunities			+
Income*	Overweight – defensive characteristics			+
Money market	Underweight – default asset class	–		

Global	**Comment**	–	°	+
Equities	Overweight – support from central banks			+
Bonds	Underweight – low yields	–		
Money market	Underweight – default asset class	–		

**Floating rate instruments of maturity longer than one year*

***Views expressed for each asset class are subjective and are for the asset class as a whole. All views are as at 31 December 2020*

Domestic asset classes

Equities

- We started 2020 with an overweight position in SA equities as, at that point, valuations were supportive and US and China had agreed to a ceasefire. However, COVID-19 changed everything, introducing new risks to company earnings as global trade started plummeting. As it unfolded, we changed our positioning to an underweight, a decision that protected well in the March sell-off.
- Valuations became attractive post the sell-off, but we remained concerned as fundamentals were still poor and the likely impact of COVID-19 together with the resulting lockdowns on company earnings were yet unknown. The market looked past this and post the US election in November and as news of a possible vaccine took shape, we became more positive on risk assets and started buying domestic equities. While we are happy with valuations, we are only marginally overweight as we are concerned about the increasing rate of positive cases – the return of SA to lockdown level 3 limits sales for a number of companies.

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Listed property

- We took an underweight position in property in February which was maintained for the remainder of the year. Listed property continues to face major headwinds. The resurgence of tighter restrictions will likely lead to lower foot traffic in many of the retail outlets. Loan-to-value ratios remain elevated and many companies have cut their pay-out ratios.
- Valuations look optically attractive and companies have prioritised their balance sheets. For these reasons, we started adding to property towards the end of the year, however, our conviction is still low and hence, we remain underweight.

Bonds

- We started 2020 with an overweight position in SA bonds. We added to this position in the second quarter as yields became even more attractive, especially on longer dated bonds.
- SA bonds reached 12.4% at the height of the sell-off in March. We started adding to our position in May and bought more in July. Since then, yields have rallied all the way to 8.7%.
- Despite the rally, we remain happy with our overweight position. Inflation is likely to remain contained in the first half of 2021 due to further lockdown restrictions. As result, we expect short-term rates to remain low, making bonds more attractive for investors looking for positive real yields.

Income

- For similar reasons to bonds, we prefer income relative to cash. Having said that, income performed very well in 2020 and consequently, we have started taking some profits from this position.
- The 3x6 FRA still implies that the SARB could cut rates by another 25 basis points in the first half of 2021. However, even if this does not happen, inflation remains very low, which means short-term interest rates are likely to be anchored for a while longer.

Cash

- Default asset class. The SARB cut rates by 300 basis points in 2020 and on the back of this, the 3-month JIBAR is currently yielding 3.6%, which is significantly lower than the 7.0% yield of only two years ago. If rates remain at current levels – as we expect – cash will remain unattractive for the next few months.

Global asset classes

Equities

- We were marginally overweight global equities at the start of 2020, a position that we added to post March due to attractive valuations and the stimulus support from central banks. In September, we started to get concerned that equities were becoming expensive. At this point, the market was back to pre-COVID-19 levels and we started scaling back on the position.
- Equities are trading on a trailing PE of 32.0x compared to a historic average of 20.2x. This makes them expensive by historic standards. The dividend yield measure has come down to 1.8%, significantly lower than the long term average of 3.2%.
- Having said that, we are marginally overweight as efforts of finding a COVID-19 vaccine seem to be progressing well. Moreover, central banks remain committed to helping economies recover.

Bonds

- We remain underweight global bonds. When we compare the 0.91% offered by 10-year US treasuries to the 8.7% we can receive in SA, it is difficult to justify being overweight global bonds.
- We acknowledge that yields on global bonds can and have continued to fall. As a result, capital returns have been better and also understand the risks priced by higher yield markets such as SA.
- We still, however, prefer SA bonds to offshore bonds.

Cash

- Default asset class. We use global cash to increase/decrease offshore exposure and currently, we have reduced cash to an underweight position as we believe SA assets are more attractive relative to global assets.

STANLIB Multi-Manager Investment Team
www.stanlibmultimanager.com