STANLIB
MULTI-MANAGER

ViewPoints

Winter Edition - July 2022

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 this is the case all the time. We therefore take views (tactically over/underweight) on relative asset class performance over three to 12 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 – recent sell-off has improved valuations			+
Listed property	Overweight – cheap but facing several headwinds			+
Bonds	Overweight – the steeper yield curve is attractive			+
Income*	Neutral – the SARB is on a rate hiking cycle		°	
Money market	Underweight – short-term rates are too low	–		

Global	Comment	–	°	+
Equities	Overweight – valuations are starting to look attractive			+
Bonds	Underweight – the US Fed is on a rate hiking cycle	–		
Money market	Underweight – prefer local fixed income	–		

**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 30 June 2022.*

Domestic asset classes

Equities

- South African equities came under pressure in the second quarter, with the FTSE/JSE Capped SWIX Index losing 10.6% and 4.7% for the year to date. Expectations of slow economic growth, the war in Ukraine, higher US bond yields and problems in China sparked a risk-off environment.
- We are marginally overweight equities. In the first quarter we highlighted some of the risks that stood to threaten our view and while most of them remain, valuations are in favor of our view. The historic PE of 9.8x is considerably lower than the historic average of 17.0x. Dividend yield for the market is an attractive 4.6%, back at levels that we last saw in the March 2020 sell-off.
- We acknowledge that the market might not have bottomed as global inflation remains high but are now pondering on whether we should be using the dips to allocate more assets to equities.

Listed property

- The SA-listed property sector continues to face several issues and lost 12.1% in the quarter. Pressure from anchor tenants to reduce rentals and high office vacancy rates are just some of challenges the sector is facing. But it is not all doom and gloom – some office buildings are being repurposed to residential apartments and post Covid recovery, Europe is gaining momentum.
- Similar to SA equities, we are only marginally overweight property as we understand that some of the headwinds its is facing are likely to remain for some time. However, it is difficult to ignore the 6.7% forward yield and the increase in retail sales over the past eight months.

Bonds

- Yields on the 10-year bond yield rose from 9.96% in Q1 to 10.99% in June and the All Bond Index lost 3.7% in over the quarter. SA yields were impacted by the negative global fixed income environment but also by rising domestic inflation concerns. The latest inflation print of 6.5% was on the high side and the SARB responded accordingly.
- We have liked SA bonds for some time now – the high yields they offer are difficult to ignore. The yield curve shifted up in Q2 and in our view, remains attractive. Currently, the R2048 is yielding 11.88%, which is 5.4% higher than current inflation and looks even better when one assumes that future inflation is likely to come back into the SARB's 3% to 6% target band.

Income

- Short-dated bonds were flat in Q2 and are up 1.3% for the year, ahead of most asset classes.
- We reduced our overweight exposure to neutral in the first quarter. While we continue to like the spread to cash, which is 337 basis points at this point, we are concerned that short-dated bonds could sell off as the SARB continues to hike interest rates.

Money market

- This is our default asset class. The SARB continued to hike rates in Q2, surprising the market by a 50-basis point hike in its May meeting. Despite recent increases, cash rates remain very low by historic standards and hence we are maintaining our underweight for the time being.

Global asset classes

Equities

- Global stocks extended a bruising sell-off this quarter as investors fear that while the rate increases are needed, they could put the brakes on economic growth – company earnings – if the tightening of monetary policy becomes too aggressive. The MSCI All Country Index lost 15.5% in Q2 and is down 20.0% year to date.
- Like SA equities, we are marginally overweight global equities as the recent sell-off reduced frothiness in the market. The historic PE, one of the valuation measures we look at, is down to 15.5x. This is lower than the 20.3x historic average. However, the forward PE is only 14.4x, which signals that the market is not overly optimistic about future earnings.
- We are looking for better opportunities to allocate more to global equities but remain cautious as we think equities could continue to sell off.

Bonds

- Bonds – which are usually regarded as a safe haven when equities sell-off – are also losing money in this equity bear market. Rising inflation and interest rates have negatively impacted the price of bonds, sending the Bloomberg Multiverse Bond Index down 14.0% so far in 2022, not too far from equity markets. Tighter Fed policy has pushed bond yields up.
- The yield on the 10-year US Treasury note peaked at 3.47% in mid-June, above 2018 levels, when the Fed was reaching the end of its last tightening cycle; and far from the 0.6% it reached in April 2020. The June inflation print of 9.1% surprised on the upside and the market has now started pricing in a 100-basis point hike for the July meeting.
- We remain underweight global bonds as yields are not high enough to compensate for the risks.

Money market

- This is our default asset class and is used to increase/decrease our offshore exposure. At this point, we prefer domestic fixed income instruments to their offshore counterparts.

STANLIB Multi-Manager Investment Team
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