Discovery Equity Fund

Market background

September was a brutal month for global equity markets, with the US S&P 500 Index down 9.3%. The continued global equity correction means the MSCI World Index has been down in seven of the nine months this year. The negative themes in Q3 remained the strong US dollar (USD) and lower revisions to global growth forecasts. The euro area continues to see the biggest economic growth downgrades as energy concerns take their toll. Meanwhile, fiscal policy missteps in the UK (unfunded tax cuts) saw the pound plunge to all-time lows, while gilts shot up significantly (yields rise as prices fall). In the aftermath, the Bank of England (BoE) intervened in the gilt market, to prevent calamities in the UK pension market. In commodities, oil marched lower with Brent crude down to US$86.2/bbl, the lowest level since the Russo-Ukraine war started. Hard commodities also dropped in September with the LME Metals Index down -5.3% and Copper down -3.0%, respectively, but Palladium gained US$78 to US$2166/oz at quarter end.

Emerging markets (EM) underperformed Global markets over the quarter. The MSCI EM Index decreased by 11.4% while developed market stocks (MSCI World Index) fell 6.6%. On a year-to-date basis, emerging markets are underperforming their developed markets peers, with the MSCI EM down 28.9% (-26.3% ex-Russia) compared to the MSCI World return of 25.4%.

Locally, equity markets were not spared, with the JSE All Share Index ending the quarter down 1.4% after dropping 4.2% in September. The Capped Swix ended the quarter down 2.4% leading to a year-to-date decline of 7.0%. The rand was one of the worst performing currencies relative to the dollar in Q3 after declining by 8.8% amid sustained pressure on risk assets. This was despite the 75bps interest rate hikes by the South African Reserve Bank (SARB) in July and September. Several SA corporates reported results in Q3. The general theme from domestic companies was that the economy continues to hold up better than expected but that the outlook is worsening.

Performance review

For the quarter, the Fund outperformed the benchmark.

The local component was the biggest driver of portfolio returns over the period. In particular, the underweight position in Capitec Bank helped relative performance as the share price came under pressure following a decent set of results, but the market was caught unaware by undisclosed one-off savings. The underweight in petrochemicals firm Sasol also added to relative performance amid oil price weakness. More negatively, underweight positions in Woolworths and AngloGold Ashanti dragged on relative performance.

The offshore component of the Fund also added positively to returns, and this was further boosted by a weaker local currency over the period.

Significant purchases over the period included FirstRand and Naspers, while significant sales included Richemont and MTN Group.

Outlook and strategy

The portfolio's investment philosophy and process aim to deliver consistent returns for investors. We follow a multi-style investment approach which is dynamically adjusted to ensure that relative risk is actively managed throughout the business cycle. We prefer shares that are trading at a discount relative to the market.

Some of the portfolio's largest overweight positions include Exxaro Resources and MultiChoice Group, while its significant underweight holdings include Standard Bank Group and Anglo American. Exxaro displays strong relative earnings revisions, MultiChoice exhibits strong relative quality attributes. In contrast, Standard Bank is showing weak relative quality attributes, while Naspers displays weak relative momentum.