MARKETS IN A NUTSHELL

	WORLD	SOUTH AFRICA
EQUITIES	Developed market bourses were sharply lower as central banks executed synchronised monetary tightening as inflation soared — emerging markets underperformed as Chinese stocks fell on economic headwinds	Rand weakness helped to buoy JSE Limited indices, which declined by low single-digit percentage points — helped by resources stocks that were market leaders, while financials and listed property lagged
BONDS	Developed market bond yields continued to rise as financial conditions tightened — on higher inflation, rising short-term interest rates and central bank quantitative tightening	Bond yields tracked global yields higher — but the All Bond Index provided some safety and eked out a positive return
CURRENCIES	The US dollar rallied further on relative US economic strength and rising interest rate differentials — and buoyed by its safe-haven appeal during periods of heightened volatility	The rand weakened sharply on the global risk off sentiment, surging US dollar and foreign net selling of South African financial assets — compounded by deteriorating terms of trade
COMMODITIES	Industrial commodity prices fell sharply from their June all-time highs on falling economic growth expectations and fading base effects — energy prices are lower but should remain well bid for now, while rising real yields and dollar strength will pressure the gold price	
ECONOMY	Global economic growth expectations continued to deteriorate, with a 2023 US recession becoming increasingly likely — while Europe confronts an energy crisis and China endures its COVID-zero policy and troubled property sector	Quarter-on-quarter GDP growth turned negative as the base effects of the post-pandemic recovery faded — while Eskom unleashed the worst bout of loadshedding ever
MONETARY AND FISCAL POLICY	The US Federal Reserve hiked rates by a third consecutive 75 basis point increase for a cumulative 3% since March — marking the fastest pace of tightening since the summer of 1980	The SA Reserve Bank hawkishly followed the US Federal Reserve by raising rates 75 basis points twice in the quarter — to combat high inflation, which is at risk of staying higher for longer

EMERGING MARKETS — AT THE MERCY OF THE MIGHTY DOLLAR

LINDA EEDES
Investment Executive

In September, the rand broke through R18 to the US dollar for the first time since the COVID-19 crisis. Investment executive LINDA EEDES writes that the rand's recent slump is less about the rand and more about what is finding favour with the world's investors: the US dollar.

Nearly every major currency has lost ground against the greenback this year. Even the so-called hard currencies have cracked under pressure. In July, the euro breached parity with the dollar for the first time in 20 years, while, in September, the British pound reached an all-time low perilously close to dollar parity. The rand is in good company at least.

What's behind this dollar strength? The answer is rate hikes and risk aversion. With the US economy in relatively good shape, the US Federal Reserve has raised interest rates faster than any other advanced economy to combat inflation. Investors have also sought out the dollar's safe-haven appeal amidst rising geopolitical tension and market turmoil. The combination of increasingly attractive yields and perceived safety has caused an irresistible pull towards the mighty dollar.

Dollar strength is negative for emerging economies for two main reasons. Firstly, most commodities are priced in dollars, so vital imports become more expensive — countries can inadvertently import inflation along with their wheat and fuel. Secondly, many emerging market governments borrow in dollars, so their borrowing costs increase when the dollar strengthens — crowding out other government spending.

South Africa has also suffered the knock-on effect of rising food and energy costs. However, its position as one of the world's largest exporters of commodities, such as platinum group metals, has helped to offset imported inflation. Fortunately for us, South Africa's debt is mostly rand-denominated.

While the Fed is fighting inflation, emerging market central banks must fight the twin perils of inflation and dollar strength. They can only do this by also rapidly raising interest rates, even if this tips their economies into recession before the US. The SA Reserve Bank has therefore had no option but to follow the Fed's lead in aggressively hiking the local repo rate.

> *"Nearly every major currency has lost ground against the greenback this year."*

Countries such as South Africa, with structurally higher inflation and interest rates, should experience steady currency depreciation over time. This in turn fuels inflationary pressures, which we must manage if we are to meet our primary investment objective of achieving meaningful inflation-beating returns for our investors over time.

For portfolios which permit offshore investment, investing abroad achieves the dual outcomes of currency hedging and better diversification from the wide global opportunity set outside of South Africa. Nevertheless, it is worthwhile noting that more than half of the revenues generated by companies listed on the JSE Limited is earned in foreign currencies. This provides a useful hedge against rand weakness for investors in portfolios focused only on the SA market.

FUND RANGE

BEST INVESTMENT VIEW FUNDS

FOORD FLEXIBLE	FOR INVESTORS
Exploiting the benefits of global diversification, the fund aims to provide investors with an after-fee return of 5% per annum above the South African inflation rate.	• With a moderate risk profile • Seeking long-term inflation-beating returns over periods exceeding five years • Requiring a balanced exposure to South African and global investments.

FOORD INTERNATIONAL (US$)	FOR INVESTORS
The fund aims to achieve meaningful inflation-beating US$ returns over rolling five-year periods from a conservatively managed portfolio of global investments reflecting Foord's prevailing best investment view.	• With a moderate risk profile • Requiring diversification through investments not available in South Africa • Seeking to hedge rand depreciation.

REGULATION 28 FUNDS

FOORD BALANCED	FOR INVESTORS
Managed to comply with the statutory investment limits set for retirement funds in South Africa, the fund aims to grow retirement savings by meaningful, inflation-beating returns over the long term.	• With a moderate risk profile • Seeking long-term, inflation-beating returns over periods exceeding five years • From an SA retirement fund investment product (Reg 28).

FOORD CONSERVATIVE	FOR INVESTORS
Managed to comply with the statutory investment limits set for retirement funds in South Africa, the fund aims to provide conservative, medium-term investors with inflation-beating returns over rolling three-year periods.	• With a conservative risk profile • Close to or in retirement • Seeking medium-term, inflation-beating returns over periods of three to five years • From an SA retirement fund investment product (Reg 28).

SPECIALIST EQUITY FUNDS

FOORD EQUITY	FOR INVESTORS
The fund aims to outperform the FTSE/JSE Capped All Share Index over the long term, with lower risk of loss.	• With a higher risk profile • Seeking long-term growth over periods exceeding five years • From a portfolio of JSE-listed equity, commodity and property stocks • And able to withstand investment volatility in the short to medium term.

FOORD GLOBAL EQUITY (US$)	FOR INVESTORS
The fund aims to outperform the MSCI All Country World Net Total Return Index from an actively managed portfolio of global equities, without assuming greater risk.	• With a higher risk profile • Requiring diversification through investments not available in South Africa • Seeking to hedge rand depreciation • And able to withstand investment volatility in the short to medium term.

A MEMBER OF THE ASSOCIATION FOR SAVINGS & INVESTMENT SA PLEASE REFER TO THE FACT SHEETS CARRIED ON WWW.FOORD.CO.ZA FOR MORE DETAILED INFORMATION.

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F40REWORD

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DID YOU KNOW? FOORD UNIT TRUSTS TURNS 20

The Foord Equity and Foord Balanced Funds launched on 1 September 2002. Previously, Foord had tried unsuccessfully to obtain a unit trust license for decades. One was finally awarded to the early empowerment joint venture between Foord Asset Management and AMB (African Merchant Bank) Holdings, known as AMB Foord Asset Management and AMB Foord Unit Trusts. The funds were called AMB Foord Equity Fund and AMB Foord Balanced Fund. Foord later bought out the AMB shareholding and on 30 September 2003 the names changed to Foord Unit Trusts, Foord Equity Fund and Foord Balanced Fund.

At launch, general equity funds dominated the unit trust universe in South Africa. We expected that Foord Equity Fund would grow quickly to become many times the size of Foord Balanced Fund, which was offered in Regulation 28-compliant form (complying with SA retirement fund asset spreading rules). However, financial advice risk was fast becoming prominent after the Financial Advisory and Intermediary Services (FAIS) Act became fully operational on 1 October 2004. Financial advisors and asset consultants started allocating monies to multi-asset funds, especially the so-called balanced funds.

Equity unit trust funds have not attracted much money in the last 15 years, but they seem to have grown in value mainly due to their legacy popularity and market growth. Multi-asset funds, notably the high-equity balanced funds and later the low-equity stable funds, became the behemoths of the investment industry.

WE'D RATHER BE MOSTLY RIGHT THAN PRECISELY WRONG

NICK CURTIN
Investment Executive

The famous British economist, Sir John Maynard Keynes, reportedly said that 'it is better to be approximately right than precisely wrong'[1]. Investment executive NICK CURTIN discusses how Foord embraces this philosophy in building safety-first investment portfolios.

In the early twentieth century, Keynes pioneered economic theory that advocated for government fiscal and monetary interventions to mitigate against adversities thrown up by the normal business cycle. The theory made a dramatic resurgence after the Global Financial Crisis of 2008/9 (which was itself blamed, to a large extent, on the competing economic theory of monetarism). Massive Keynesian 'free money' stimulus measures were also employed in unprecedented quantities during the COVID-19 pandemic crisis.

Yet it now appears that this stimulus (unsurprisingly) is core to the market malaise currently playing out. First, exceedingly low interest rates and, more latterly, unprecedented levels of fiscal support culminated in severe distortions to global capital markets as we headed into 2022. We have talked much in these pages over the last two years about our growing concerns for the rising global risks, so I won't belabour the point here. Suffice it to say that the macro-economic chickens are now coming home to roost.

The concept of precision is psychologically very comforting — our human minds are hardwired to find precision, even where none exists. There are of course certain endeavours in life where precision is not only essential but also completely possible, and increasingly so as mankind continues to develop the technologies with which to do them: they are typically found in the science and engineering realms. Precision was non-negotiable for NASA scientists trying to put man on the moon in the 1960s, or Elon Musk's Space-X geeks who created a rocket ship that can land itself on a square meter patch back on earth after delivering its payload to orbit.

> *Mathematically, we don't have to be always right — just more right than wrong.*

Even a less ambitious activity like making the *perfect* souffle requires a precise combination of *perfectly* whipped egg whites, *just right* oven temperature and exact baking time to come out *just right*. Or at least it should — for some reason it requires almost as much art as science — as lovers of the Great British Bake-off will already know.

But for systems as intricate and exceedingly complex as the global economy and its associated financial markets, the idea of precision becomes a fallacy — and trying to find it soon becomes a fool's errand. In the world of investing we are dealing with the future. Unlike the hard sciences, it is a future that is not confined to a predetermined set of physics and chemical elements whose behaviour under certain conditions we can know with certainty. We simply cannot predict, with full accuracy and without risk, market tops or troughs, or those of individual securities either.

> *Foord's investment philosophy is focused not on point forecasts, but on getting the big calls right.*

But with investments, precision is quite simply not needed. It is precisely for this reason that Foord's investment philosophy is focused not on point forecasts, but on getting the big calls right. We also diversify the investment positions in such a way that we can deliver a reasonable investment outcome even if our base case scenario does not eventuate. Mathematically, we don't have to be always right — just more right than wrong, and as consistently as possible. Then, if we are patient, the mathematical wonder of compounding will work its magic.

The range of possible economic, political, environmental or investment outcomes is ordinarily wider than our human minds can probably comprehend. The current elevated levels of risk and uncertainty make this range of possibilities even wider. We must therefore resist the temptation for precision even more than usual because the consequences of being precisely wrong are that much worse.

This is the thinking that informs our cautious fund positioning, which is neither fully invested in risk assets hoping for a rebound, nor fully in cash awaiting a market bottom. Rather, we have a balanced exposure to asset classes. We focus on specific investments where the range of possible outcomes is as narrow as possible, rather than trying to load the bases on the elusive all-out winner — this is not the time for taking that kind of risk (it hardly ever is).

We therefore have a meaningful investment in foreign assets with a preference for quality companies with pricing power. These investments are best placed to protect capital from persistent inflation in the coming years. But portfolio hedges and cautious stock selection are important to protect capital in the short term.

We also have a reasonable investment in South African companies that are attractively valued and supported by relatively defensive (predictable) earnings prospects. South African bonds also comprise a portion of the funds, but at moderate levels, given the country's worrying fiscal and political risks. Listed property is constrained to a low weighting, given poor fundamentals for the asset class. Liquidity levels across the funds are also higher than normal, so that we can exploit the opportunities that market inflection points inevitably deliver.

So caution is the byword — we are not trying to be the fastest car in the race. We are more interested in making sure that we reach the destination, or at least the next waypoint on the map. In the current world, speed is less important than the ability to persevere and survive. We'd rather be mostly right than precisely wrong.

[1] *The quote actually appeared decades earlier in a book on logic and reasoning by nineteenth-century philosopher, Carveth Read.*

M.I.C.E. UPDATED

RASHAAD TAYOB
Portfolio Manager

We've written previously about the M.I.C.E. framework that Foord uses as a temperature gauge for share markets. With global bourses now in bear market territory, portfolio manager RASHAAD TAYOB revisits the framework to test current market levels.

Foord uses a high-level four-factor framework called 'M.I.C.E.' to gauge market levels and assess where they might be headed. As a macro strategist new to Foord, I quite like the simplicity of the framework. It focuses on four key factors and excludes a lot of subsidiary variables and noise. M.I.C.E. stands for Money for the Markets, Interest Rates, Confidence and Earnings.

Money for the Markets describes the quantum of liquidity that is available to buy into share markets. Liquidity is heavily influenced by central bank policy, specifically the volume of quantitative easing or tightening. Central banks pumped record amounts of money into the global economy during the height of the COVID-19 lockdowns. This money is now gradually being withdrawn, but slower than expected in some areas. This is a headwind to asset price recovery.

Interest rates are key drivers of market levels because they set the cost of borrowing. Rapid and globally synchronised rising interest rates this year means less money will flow into financial assets. Markets are expecting the benchmark federal funds rate to near its mid-2000s peak of 5% by year end. More importantly, the 10-year US Treasury *real* yield — the yield after deducting inflation — is now above 1% after languishing at -1% for two years. This level resulted in big market selloffs in 2013 and 2018. Further interest rate rises will be very negative for share markets.

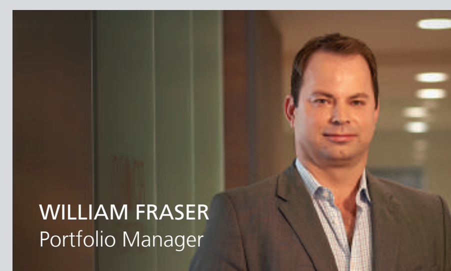
Confidence describes risk sentiment or the animal spirits of the market — it determines how much companies and consumers are willing to borrow, spend and invest. A glance at the daily financial news suggests that there is no shortage of things to worry about. We can see this in the portfolio positing of global fund managers: more fund managers are underweight shares than was the case during the 2008/9 Global Financial Crisis. Confidence is low, but investors are not yet panicked.

> *M.I.C.E. stands for Money for the Markets, Interest Rates, Confidence and Earnings.*

The fourth factor is earnings. In our view, earnings are the most important driver of long-term equity returns. We need to understand where we are in the economic cycle and assess where we are still headed. Corporate earnings collapsed during the pandemic but rebounded rapidly on government handouts. Earnings are now above their long-term growth trend. The withdrawal of government stimulus, rising interest rates increasing the cost of borrowing, and rising inflation putting pressure on margins are all headwinds to corporate earnings.

We are therefore still cautious, even after the significant market falls this year. We remain invested in quality companies with a low weight to cyclical sectors. We expect there to be some good buying opportunities in the months ahead.

ADIEU WILLIAM FRASER


WILLIAM FRASER
Portfolio Manager

Our colleague and friend William Fraser retired from Foord at the end of August. He is only 48 but was with the firm and in the hot seat for 17 years. He has courageously left his portfolio manager day job at the peak of his career to focus more on himself and his family. Managing director PAUL CLUER applauds him for making this very difficult decision at a very difficult time.

William joined Foord on 1 October 2005 from the country's largest multi-manager, Investment Solutions (now Alexander Forbes Investments). He worked at its Johannesburg head office with Eldria Wagenaar, whom he later married. They decided jointly to relocate to Cape Town and both aspired to work at investment boutiques. William and Eldria agreed that for demographic reasons it was William who ought to secure employment first.

I believe that William made only one call on the job-search front — to veteran fund manager, Dave Foord. Foord Asset Management had managed portfolios for Alexander Forbes Investments since 2002 and through this account William had had exposure to Foord's investment management style (actually, from even before this when he was with actuarial asset consultants Ginsburg Malan & Carsons, but that goes far back into the annals).

Foord was a tiny boutique back then, but this was where William wanted to work. Thankfully for us, we felt there were synergies, especially in the fixed income, macro strategy and institutional account management space with then managing director Chris Greyling soon to retire. Eldria Fraser subsequently found a home at Cape Town-based fixed income specialist Prescient Investment Managers.

I would like to mark William's retirement with a note of thanks for his herculean contribution to the firm. William is one of the modern-day bastions of the business and a true stalwart. He has a trove of industry insights and organisational memory that is not easily replicated. Thankfully, we will still be able to access this knowledge, given his agreement to remain a non-executive director at Foord.

Within the investment team he is somewhat of an enigma to the 'share people,' who came to rely heavily on his different perspective of the markets. He has also always been very good at translating the prevailing investment thesis into something that is consumable and relevant to professional and lay investors alike. Technically very smart, his contribution has not only been to the investment team — he's equally at home on the operational and business development fronts.

William was an invaluable resource to me personally and I have relied deeply on his judgment. We will (and already do) miss his physical presence in the office. A peaceful and quiet person, William is a true gentleman with unquestionable ethics. He retires on the best of terms and in true friendship.