MENTENOVA

HOUSEVIEW TACTICAL ASSET ALLOCATION

21 November 2024

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We have maintained a moderately overweight position in SA bonds, funding the positions with SA cash. We have reduced our allocation to SA equities from moderately overweight to neutral and increased our offshore cash position from moderately underweight to neutral.

Figure 1: Houseview Tactical Asset Allocation

Asset Class	--	-	Neutral	+	++
SA Cash					
SA Bonds					
SA Inflation-Linked Bonds					
SA Listed Property					
SA Equity					
Foreign Cash					
Foreign Bonds					
Foreign Equity					
Foreign Property					

Synopsis

Here is our investment case for December 2024 and January 2025:

- We have maintained a moderately overweight position in SA nominal bonds, preferring it over local cash, supported by valuations and the continuing rate-cutting cycle, although the latter could be a shallower one than previously expected.
- We have moved from moderately overweight in SA equities to neutral, on the basis of attractive valuations, improving domestic political and macro landscapes, China and trade war exposures, and the SARB looking to become more cautious in its rate-cutting policy.
- We have moved from moderately underweight to neutral in foreign cash as Trump's policy stances appear to be reflationary, and together with a strong US economy and unsteady Chinese economic recovery, we expect the USD may remain strong in the near term.

Monthly Market Overview – October 2024

Market overview	October was a month characterised by much turbulence, with various markets experiencing uncertainty ahead of the United States presidential election. These elections were expected to shape policy decisions, particularly regarding inflation and interest rates, and their potential implications. As the election approached, the appetite for risk assets diminished, resulting in most asset classes closing the month in negative territory. Global equities declined, with the S&P 500 down 0.9%, largely due to an increase in global growth risks and mixed earnings results, particularly from the tech giants such as Alphabet, Apple and Meta (to name a few). Looking at style performance, growth stocks outperformed value stocks, even though they ended in the negative territories of -1.8% and -2.1% respectively. Developed markets experienced a momentum drawback and recorded negative gains, with the MSCI World Index down 2% for the month leading up to the US election. However, performance reversed in the first half of November, with the index showing a healthy gain of 3%. Its counterpart, the MSCI EM Index, lagged and was down 4.3%, pressured by a strong US dollar

and rising global bond yields. The biggest detractor was India, with the Nifty 50 Index down 6.1%, reversing gains made in previous months due to weaker earnings results and the reallocation of capital by investors to other markets, like China. It continued to decline into November with the MTD at -2.7%. Chinese equities were down 3.0% followed by Brazil at -1.6%. In contrast to its peers, Taiwan was the only emerging market to deliver a positive gain of 2.7%, driven by ongoing support and curiosity about artificial intelligence.

The local equity market was not immune to global pressures, with the FTSE/JSE All Share Index declining 0.9% for the month, underpinned by sectoral performance. The resources sector saw a positive gain of 2.7%, largely driven by an uptick in commodity prices, particularly palladium and gold, which investors turned to as safe havens amidst heightened geopolitical tensions. The largest detractors in equity performance were the industrials and property sectors. Financials also faced downward pressure, reflecting a broader risk-off sentiment and elevated concerns about fiscal policy. The government's Medium-Term Budget Policy Statement, which was the first budget speech under the newly formed coalition government, forecast a wider deficit and higher debt levels for the coming years, despite improved expected growth due to enhanced energy supply stability.

The bond market also experienced significant volatility, with yields increasing across the entire US treasury yield curve, resulting in negative returns for the month with the WGBI down 3.5%. This was largely driven by the US labour market and consumer confidence data, leading to market expectations of fewer rate cuts and a dialling back of US recession expectations. Comments from some Fed members suggesting a more cautious approach to rate cutting put further pressure on the US treasury market. The Bloomberg US Aggregate Bond Index fell 2.5% in October, reducing its year-to-date return to 1.9%. SA bonds also faced pressure, with the ALBI down 2.2%.

Ongoing tensions in the Middle East and the potential for sanctions on Russian palladium and titanium boosted commodities such as oil. Palladium was the top performer for the month, up 11.6%, bringing its 3-month performance to 20.6%. Gold followed (up 4.2%), maintaining its position as a top performer and delivering a year-to-date performance of 33%. The decision to impose sanctions on Russian palladium and titanium could create challenges, as Russia accounts for about 40% of the global supply. Crude oil prices were volatile, particularly after Iran launched a missile strike against Israel. Although tensions subsided as the month progressed, fears persisted, with Brent crude oil seeing a moderate gain of 1.9% by month end. Weakness in the Chinese economy, particularly in industrial activities and property development, weighed on demand for base metals such as copper and iron ore. Iron ore was down 6.3% and copper was down 3.3% for the month. Nickel experienced significant volatility over the year, with solid price momentum in the first half of the year benefiting from improved investor sentiment. However, these price highs were short-lived as nickel supply and demand fundamentals led to steep declines, making it the biggest underperformer for the month, with a 10.4% drop.

The property market also experienced declines locally and globally, with the SAPY Total Return down 2.8% and the S&P Global Property Total Return down 5% for the month of October.

Looking at currency performance, the US dollar appreciated significantly, with the dollar spot index up 3.2%, buoyed by robust domestic economic data, particularly strong consumer spending and labour figures. Expectations of continued monetary policy tightening by the Federal

Reserve further supported the dollar. This strengthening put pressure on emerging market currencies, including the South African rand, which depreciated by 1.9% against the dollar. However, the rand strengthened against other major currencies. It appreciated by 3.8% against the Japanese yen, benefiting from the Bank of Japan's ongoing monetary easing, which reduced demand for safe-haven currencies. The rand also showed relative strength against the British pound and the euro, up 1.7% and 0.3% respectively, due to weaker inflation data in the UK and continued dovish monetary policies in Europe, which made these currencies less attractive.

Figure 2: Major market indices' performance in local currency

31 October 2024 (Local Currency)	1M	3M	YTD	1 Year	3 Year (annualised)	5 Year (annualised)	10 Year (annualised)	MTD 14 November 2024
FTSE/JSE ALSI Total Return	-0.9%	4.5%	14.8%	27.2%	12.5%	12.8%	9.2%	-1.8%
FTSE/JSE Capped SWIX Total Return	-0.9%	4.3%	14.8%	28.0%	11.0%	10.9%	7.2%	-1.8%
S&P 500 Total Return	-0.9%	3.7%	21.0%	38.0%	9.1%	15.3%	13.0%	4.3%
STOXX 600 Total Return	-3.3%	-2.1%	8.1%	19.7%	4.7%	7.5%	6.9%	0.4%
Nikkei 225 Total Return	3.1%	0.7%	18.7%	28.9%	12.9%	13.4%	11.2%	-1.4%
MSCI World Total Return	-2.0%	2.5%	16.9%	34.3%	6.9%	12.6%	10.4%	3.0%
MSCI ACWI Total Return	-2.2%	2.7%	16.4%	33.4%	6.0%	11.6%	9.6%	2.3%
MSCI EM Total Return	-4.3%	3.8%	12.2%	25.9%	-1.0%	4.3%	3.8%	-3.1%
MSCI World Value Index	-2.1%	2.5%	14.6%	29.8%	7.6%	9.4%	7.7%	1.6%
MSCI World Growth Index	-1.8%	2.6%	19.3%	38.6%	5.6%	15.1%	12.7%	4.3%
MSCI World Small Cap Index	-2.7%	-0.3%	8.4%	30.0%	0.6%	8.3%	8.1%	2.8%
FTSE UK Series FTSE All Share TR	-1.6%	-2.5%	8.1%	16.3%	6.2%	5.7%	6.2%	-0.1%
MSCI AC Asia Ex. Japan Index	-4.5%	5.7%	16.1%	28.6%	-1.0%	5.0%	5.0%	-3.2%
MSCI Europe Excluding United Kingdom Index	-3.4%	-2.0%	7.9%	20.4%	5.0%	8.6%	8.2%	0.1%
Shanghai Shenzhen CSI 300 Index	-3.0%	13.6%	16.7%	12.2%	-5.1%	2.3%	6.8%	3.9%
Korea Stock Exchange KOSPI Index	-1.4%	-7.5%	-2.5%	14.5%	-2.8%	6.4%	4.7%	-5.4%
Taiwan Stock Exchange Weighted Index	2.7%	3.3%	30.3%	46.2%	14.3%	18.8%	13.8%	-0.5%
NSE Nifty 50 Index	-6.1%	-2.7%	12.7%	28.6%	12.6%	16.9%	12.8%	-2.7%
Ibovespa Brasil Sao Paulo Stock Exchange Index	-1.6%	1.6%	-3.3%	14.6%	7.8%	3.9%	9.0%	-1.5%
Nasdaq-100 Index	-0.8%	2.9%	19.0%	39.2%	8.8%	20.7%	18.1%	5.1%
Bloomberg Magnificent 7 Total Return Index	-0.4%	5.6%	43.8%	66.9%	19.3%	44.2%		8.7%
Bloomberg US Large Cap ex Magnificent 7 Total Return Index	-1.1%	3.7%	15.6%	32.3%	6.0%	11.3%		3.6%
Dow Jones Industrial Average TR	-1.3%	2.7%	12.5%	28.9%	7.4%	11.4%	11.7%	4.8%
STEFI	0.7%	2.1%	7.1%	8.5%	7.0%	6.1%	6.6%	0.3%
ALBI	-2.2%	4.0%	14.1%	21.3%	10.5%	9.4%	8.4%	1.0%
IGOV	-1.1%	1.9%	5.7%	13.4%	7.2%	7.1%	5.1%	-0.5%
WGBI	-3.5%	0.4%	-0.8%	8.4%	-5.4%	-2.8%	-0.5%	-1.5%
Bloomberg Global Inflation-Linked Total Return Index	-3.5%	-0.3%	-0.5%	9.2%	-6.7%	-1.3%	0.4%	-1.6%
Bloomberg US Agg Total Return	-2.5%	0.2%	1.9%	10.5%	-2.2%	-0.2%	1.5%	-0.5%
Bloomberg EuroAgg Total Return Index	-0.7%	0.9%	1.7%	8.0%	-3.3%	-2.1%	0.4%	0.6%
Bloomberg Global Agg Corporate Total Return Index	-2.7%	1.0%	2.5%	13.0%	-2.3%	0.2%	1.7%	-0.7%
Bloomberg US Corporate High Yield Total Return Index	-0.5%	2.7%	7.4%	16.5%	3.0%	4.5%	4.9%	0.6%
Bloomberg Pan-European High Yield Total Return Index	0.5%	2.8%	7.5%	13.9%	2.7%	3.2%	3.8%	0.5%
J.P. Morgan EMBI Global Core Hedged EUR	-2.2%	1.9%	5.0%	16.4%	-3.6%	-1.7%	0.8%	0.0%
SAPY Total Return	-2.8%	10.5%	26.4%	51.6%	15.5%	4.4%	3.3%	-1.4%
MSCI US REIT Total Return	-2.9%	6.1%	12.5%	36.5%	1.4%	4.6%	6.4%	0.2%
S&P Global Property Total Return	-5.0%	4.4%	8.0%	29.9%	-1.8%	0.9%	3.9%	-1.3%
STOXX 600 Real Estate Total Return	-7.8%	-0.1%	0.8%	28.1%	-9.1%	-3.9%	1.1%	-1.2%
FTSE EPRA Nareit Global REITs TR Index	-4.5%	4.6%	7.7%	30.7%	-1.2%	1.3%	4.3%	-0.8%
Crude Oil	1.9%	-9.4%	-5.0%	-16.3%	-4.6%	4.0%	-1.6%	-0.8%
Aluminium	0.2%	14.3%	9.8%	16.3%	-1.2%	8.3%	2.5%	-3.9%
Copper	-3.3%	3.0%	11.1%	17.2%	0.0%	10.4%	3.6%	-5.4%
Gold	4.2%	12.1%	33.0%	38.3%	15.4%	12.6%	8.9%	-6.5%
Platinum	1.3%	1.6%	0.3%	6.1%	-0.9%	1.3%	-2.2%	-5.4%
Nickel	-10.4%	-5.4%	-5.6%	-13.5%	-7.4%	-1.5%	-0.1%	-0.8%
Palladium	11.6%	20.6%	1.8%	-0.3%	-17.6%	-9.0%	3.5%	-15.7%
Iron Ore	-6.3%	1.1%	-26.8%	-18.7%	-4.4%	2.6%	2.2%	-2.9%
Bloomberg Commodity Index Total Return	-1.9%	3.0%	3.9%	-1.2%	2.1%	7.0%	-0.1%	-2.0%
USDZAR	1.9%	-3.3%	-4.1%	-5.6%	4.9%	3.1%	4.8%	3.8%
GBPZAR	-1.7%	-3.0%	-2.5%	0.2%	2.9%	3.1%	2.5%	2.0%
EURZAR	-0.3%	-2.7%	-4.9%	-2.7%	2.9%	2.6%	3.3%	0.5%
JPYZAR	-3.8%	-4.6%	-10.9%	-5.9%	-4.7%	-3.7%	1.6%	1.1%
Dollar Index Spot	3.2%	-0.1%	2.6%	-2.5%	3.4%	1.3%	1.8%	2.6%

Source: Bloomberg

TAA overview

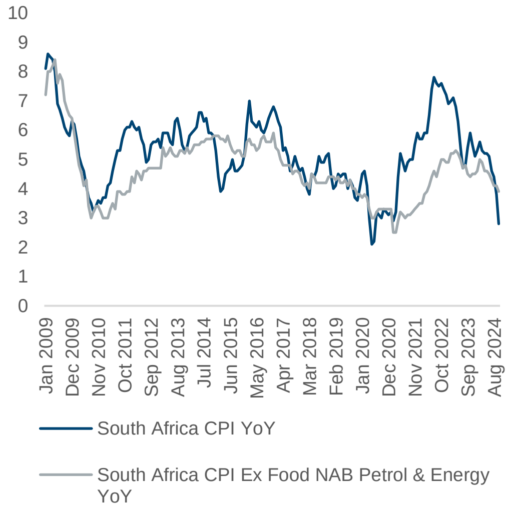
SA bonds

The global macro landscape into Q4 can be described as one of steady growth, with strong services sectors and manufacturing remaining in slight contraction; cooling inflation driven by a softer oil price, reasonable food price inflation and healthy supply chain pressure; and most major central banks have embarked on rate-cutting cycles, albeit shallower ones than previously expected. This backdrop is largely pro-growth and supportive of the risk-on sentiment. However, Trump's decisive victory in the 2024 US election in early November does create uncertainty in the global economy as the impact of some of his policy plans play out. While some plans are seemingly pro-US growth, such as tax cuts and deregulation, some could upend the global order, such as heightened protectionism (imposing tariffs or additional tariffs on major trading partners such as China), deportation pledges (especially in the face of a tight labour market) and hardened geopolitical stances. The overall impact of these policy plans on the US and the global economy may be mixed, as it depends on implementation and the extent of the changes. In addition, these policy plans are reflationary, which can complicate the Fed's interest-rate decisions and put additional strain on the US fiscal debt challenge. Our base case during last month's TAA on the US election was a constrained Trump victory as the race was too tight to call, resulting in more watered-down policy changes. With the Trump sweep, the impact will be more positive for global equities over global bonds, especially US domestically oriented equities and bullish for the USD, underpinned by US fiscal easing and tighter monetary policy in the short term.

For SA bonds, Trump trades have negatively impacted the flows to emerging market assets due to strong US economic growth over emerging markets, as shown in the economic surprise indices below. In addition, the Trump trade policy stance on China remains a major risk, especially for South Africa as a commodity-exporting country.

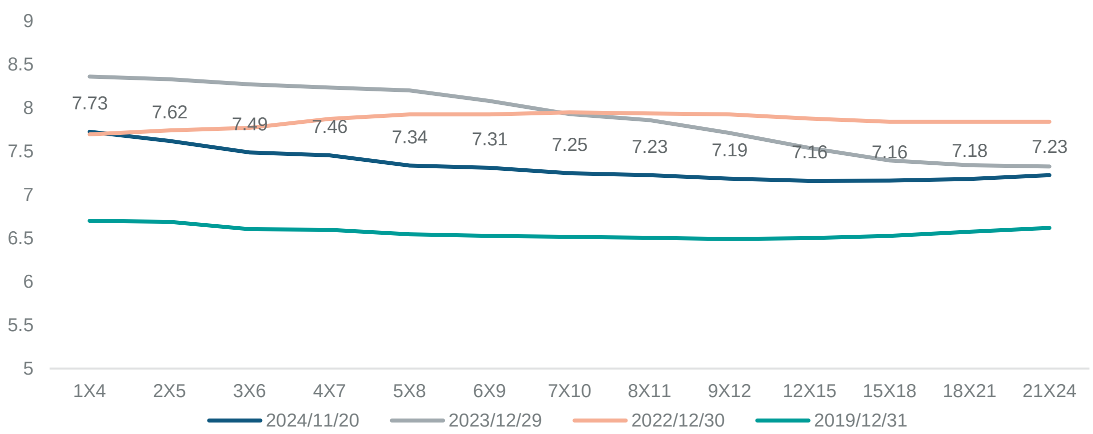
Figure 3: Citi Economic Surprise Indices

Figure 4: SA CPI and core CPI



Source: Bloomberg

Figure 5: SA FRAs



Source: Bloomberg

While SA bonds seem fully valued from an SA–US 10-year yield gap perspective, they still offer attractive real yield, hedged yield and trading at a discount to their implied yield. Despite elevated currency volatility and prudent or cautious rate decisions by the SARB in the short term, with S&P also recently revising its SA outlook from stable to neutral, and with falling inflation and a reasonable expectation of rate cuts for next year priced in by the market, we prefer this asset class over local cash and have hence maintained our moderately overweight position in SA bonds.

SA equities

While we still prefer SA equities for their attractive valuation, as there is potential for further relative re-rating of SA equities vs the S&P 500 on an improving SA sentiment and growth outlook (implementation remains key), a strong USD and the exposure to China remain two key headwinds. Historical data, from the 2018 trade war, showed that emerging market equities were vulnerable.

Figure 6: Cumulative performance in USD

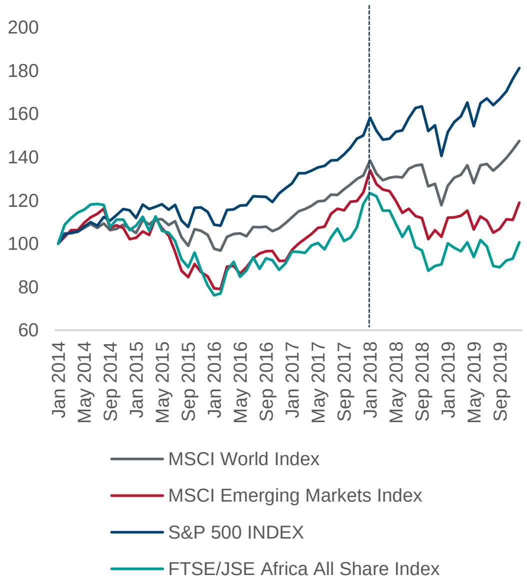
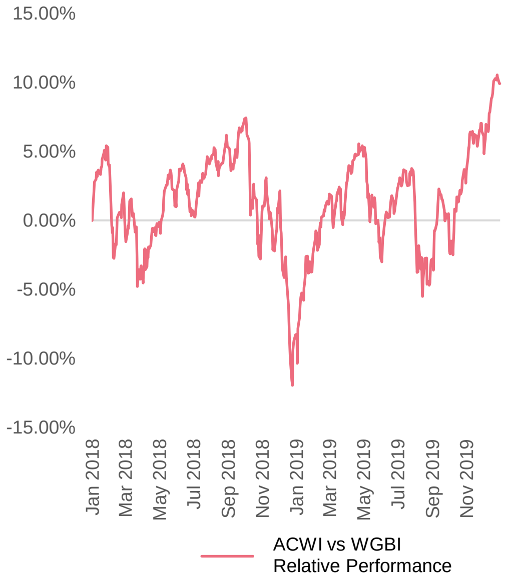


Figure 7: MSCI ACWI vs WGBI cumulative relative performance

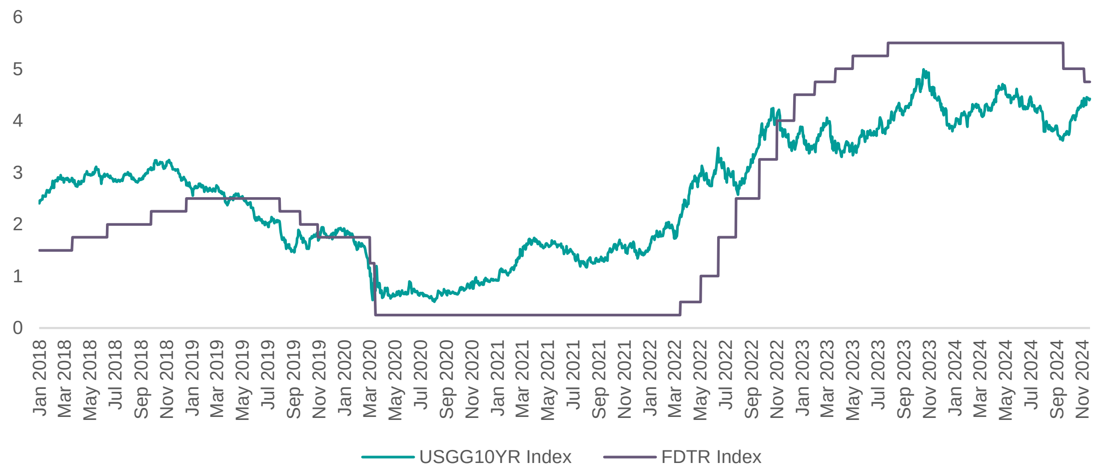


Source: Bloomberg

However, this time it is different as during the 2018 trade war, S&P 500 was derated from 21x of PE to 15x on the back of rate hikes. Now there is a bit of a cushion due to the rate-cutting cycle, despite an upside inflation risk and higher valuation of US equities with PE of 25x and positive growth prospects priced in. SA equities are not immune to trade wars, however. They are now trading at a much lower PE ratio of 14x, vs 19x in 2018, which should also result in a limited downside. There is still much uncertainty surrounding Trump's policy implementation. While the current environment is pro-risk assets, trade wars can negatively impact growth, as shown in the relative underperformance of MSCI ACWI vs WGBI in early 2018 and later that year into 2019.

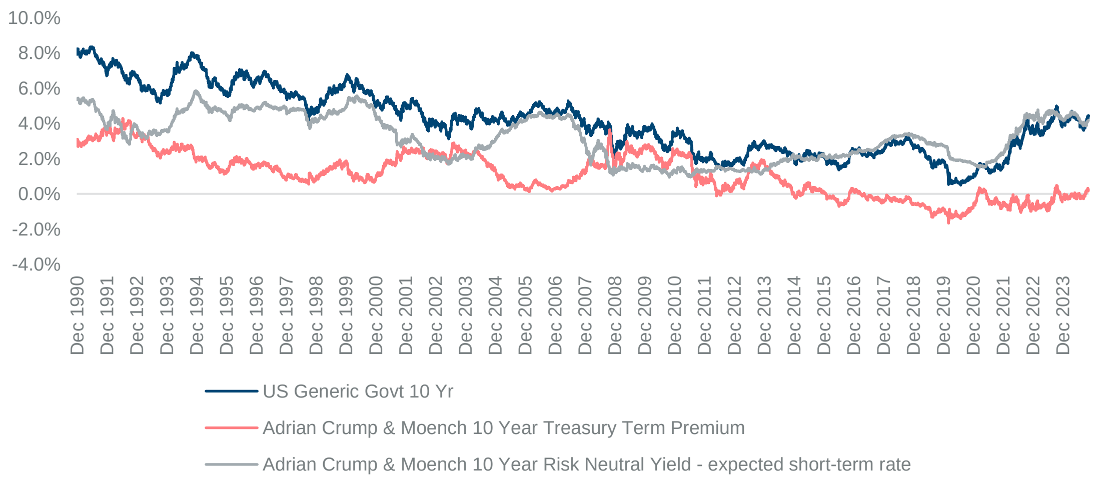
Another factor that could limit the upside equity potential is elevated bond yields. The Fed has cut rates by 75bps so far and yet the 10-year US treasury yield climbed, with markets concerned about US deficit spending driving up real interest rates and demanding higher-term premiums. On the balance of valuations and risks, we have therefore chosen to be neutral in SA equities.

Figure 8: US 10-year bond yield and Federal funds target rate



Source: Bloomberg

Figure 9: US 10-year bond yield disaggregation



Source: Bloomberg

Foreign cash

On the currency side, there is still the probability of the ZAR strengthening but the underlying dynamics have shifted from a month ago. Now there is less upside potential and a greater likelihood of the USD remaining strong in the face of US economic resilience and China's unsteady economic recovery, with more stimulus pending on Trump's trade policies and an upside inflation risk which could pause the rate cuts. We have therefore chosen to be neutral in foreign cash.

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