Abax SA Income Prescient Fund Commentary

Prescient

Q4 2023 Commentary

Returns (%, annualised)(Inception date 13-02-2020)

	1 m	3 m	1 Yr	Incep.
Abax SA Income Prescient A1	1.0	3.3	9.7	7.0
STeFI Call Deposit ZAR	0.7	2.0	7.8	5.1

* All performance shown is net of fees

Best and worst periods (%)

Best 12-months	6.8
Worst 12-months	5.2

The fund saw a strong fourth quarter (+3.4%), as asset classes across the board rallied and contributed positively to the portfolio's return. The fund managed to outperform its cash benchmark (STEFI Call) by 1.4% for the quarter.

Over the longer term the Abax SA Income Prescient Fund aims to outperform cash with a predictable and low risk return profile. The fund is managed with the philosophy of investing in a diversified range of fixed income asset classes, avoiding expensive asset classes and focusing on high credit quality.

The fourth quarter of 2023 saw stronger markets as lower inflation, slowing economic indicators and a dialing back of various developed central bank's hawkish stances took place.

The S&P 500 returned an incredible 11.7% for the quarter, with the MSCI World index close behind, returning 11.5%. Emerging markets also performed well, but not
quite to the same extent seen in the developed world, with the MSCI EM Index returning 7.8%. On the bond side, US Treasuries (+5.7%), US Corporate bonds (+8.5%),
EU Government bonds (+7.0%) and UK Government bonds (+8.6%) all generated exceptionally strong positive returns. EM bonds also performed well off the back of global risk-free rates rallying, with the EM USD bond index returning 8.1% for the quarter.

After aggressive interest rate increases by the Federal Reserve, ECB and BOE in 2023, markets are betting that interest rates hikes are coming to an end across the board
in 2024, as falling inflation and economic pressures are building. All three have put their tightening programs on hold, and the Federal Reserve in particular
communicated a more dovish stance in its December meeting, showing projections by officials for rates to be 75pts lower by the end of 2024. Additionally, Powell mentioned that discussions around rate cuts have begun and communicated the risks of keeping policy rates tight for too long. The ECB and BOE continue to present a more hawkish tone to the market, saying it was too early to discuss rate cuts, but that has not stopped the market from pricing in rate cuts in March/April 2024 for all
three central banks.

While inflation is coming down, it is worth noting that these numbers are not yet at (or even near) target and it is possible that the market is getting ahead of itself in the pace at which it is pricing rate cuts. US core inflation for example is still at 4% and a rally in market prices, as we have seen now in Q4, could further stoke the problem. Additionally, as the US continues to run loose fiscal policy, we are seeing high interest rates on large amounts of government debt resulting in even bigger runaway
deficits. These ballooning interest rate payments ironically push more money into the economy, making this environment, in our opinion, an incredibly difficult one to tame inflation permanently.

On the local front, markets experienced a similar rally off the back of lowered global interest rate expectations. The equity market (FTSE/JSE All Share index) saw more meagre returns of 6.9%, but interest rate sensitive asset classes such as bonds (ALBI) and property returned an exceptional 8.1% and 16.4% for the quarter respectively.

The November MPC kept rates unchanged unanimously and it seems likely that rate hikes are done. The MPC, however, remains cautious around inflation, particularly around the possibility that higher food and fuel prices might fuel wage inflation. While the market is pricing cuts in the first half of 2024, a lot will also depend on the
pace of developed market central banks, and the 2024 fiscal budget and national election (as these risks ultimately determine neutral rates).

Market Commentary (Cont..)

The last quarter of 2023 also saw finance minister Godongwana deliver the MTBPS, which pleasingly seemed to demonstrate prudence and some commitment to fiscal consolidation. While the downward projections in revenues were expected (due to corporate income tax revenues disappointing, largely because of lower commodity prices), the positive surprise came from the expenditure side. Aggressive expenditure cuts have accommodated the extension of the social relief of distress grant, higher wage compensation and debt service costs, to the extent that outer year's non-interest expenditure slightly reduced over the coming 2 years. Embedded in these assumptions, however, are conservative wage bill increases, without SOE assistance. Given the predicament Transnet is in, as well as the fact that we are in an election year, this does, however, seem unlikely and the market is left questioning the practicality of the budget. Despite the optimistic assumptions, two strong positive points from the budget was Treasury's commitment to limit nominal bond issuance increases and the other is them trying to implement a fiscal anchor into law (where some headway has been made with cabinet). Time will tell how serious these actions are, but in the absence of reforms, the market will continue to price large credit risk premia into government bonds.

Summary and Conclusion

The fourth quarter of 2023 saw stronger markets as lower inflation, slowing economic indicators and a dialing back of various developed central bank's hawkish stances took place. After aggressive interest rate increases by the Federal Reserve, ECB and BOE in 2023, markets are betting that interest rates hikes are coming to an end across the board in 2024. While inflation is coming down, these numbers are not yet at (or even near) target and it is possible that the market is getting ahead of itself in the pace at which it is pricing rate cuts. Additionally, a rally in market prices (as we have seen now in Q4), loose fiscal policy and ballooning interest rate payments that push more money into the economy, could potentially further stoke the inflation problem.

On the local front the MPC kept rates unchanged, and it seems that hikes are done, but they remain cautious around inflation and are dovish with communication. While the market is pricing cuts in the first half of 2024, a lot will depend on the pace of developed market central banks, and the 2024 fiscal budget and national election. Should the numbers projected in the MTBPS pan out, it will be positive for SA rates, but election pressures and failing SOE's will likely continue to place pressure on the SA fiscus.

Important Information

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Annualised performance shows longer term performance rescaled to a 1-year period. Annualised performance is the average return per year over the period. Actual annual figures are available to the investor on request. Highest and lowest is returns for any 1 year over the period since inception have been shown. NAV is the net asset value represents the assets of a Fund less its liabilities.

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*The forecasts are based on reasonable assumptions, are not guaranteed to occur and are provided for illustrative purposes only.

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