SPEKTRA FINANCIAL SERVICES

MARKETS OUTPERFORM EXPECTATIONS IN H1 2023

SUMMARY

- Despite the wave of negative sentiment, both local and global markets have experienced a robust first half of 2023.
- Local Balanced Funds have generated double-digit returns over the last twelve months on the back of strong equity and bond returns.
- Offshore, investor interest is expected to shift from Inflation and Interest Rates, to Growth and Earnings.
- Investors should temper expectations as returns over the next twelve months are unlikely to be as elevated as the previous twelve.

GLOBAL MARKETS

Global Equity Markets have enjoyed a robust first half of 2023, with Developed Markets (as measured by the MSCI World Index) up 15.4% in dollar terms at the end of June (a whopping 26.9% when measured in rand terms). Markets responded positively to the dissipating risks faced by the global banking sector, following the collapse of Silicon Valley Bank in March. Subsequently, the political debate around raising the US debt ceiling (to prevent the US from defaulting on its debt) drove uncertainty, with several market commentators signalling an imminent US Recession. Consequently, the deal was passed to the relief of market participants and the US Equity Market continued its upward trajectory.

Mega-cap, US-listed tech stocks remain a key driver of equity market returns (benefitting from the hype surrounding artificial intelligence [AI]), with the share prices of Nvidia, Meta and Tesla more than doubling YTD and impressive gains from Amazon, Apple, Microsoft and Alphabet, respectively.

These seven stocks, dubbed “The Magnificent 7”, have grown to a combined market cap of $11.34 trillion, and account for roughly 30% of the total S&P 500. A recent Moneyweb Article[1] detailing the meteoric rise of the Magnificent 7 said the following; “To put this into context, just looking at the largest of the seven, Apple, they have a market cap of $3 trillion which is larger than Frances’s total GDP ($2.78 trillion in 2022) and more than seven times that of South Africa ($406 billion in 2022). If we include the other six into the fold, which are Microsoft, Alphabet, Amazon, Meta, Nvidia, and Tesla, cumulatively, they are 3.5 times larger than the entire GDP of the African continent and have an equivalent market cap of 66% of the European Union GDP ($16.64 trillion as of 2022).”

Overall, US equity markets performed well as a rally in growth stocks, an upbeat earnings season, and hopes of the US Federal Reserve (Fed) ending its aggressive monetary tightening sooner rather than later buoyed the leading US indices and lifted investor sentiment. Recent US economic data have reflected a resilient economy despite the higher interest rate environment, soothing investor fears of a possible recession triggered by the Fed’s aggressive rate hikes.

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[1] Source: Moneyweb, The Magnificent 7: How AI is lifting the S&P 500, 19 July 2023

LOCAL MARKETS

Despite the slew of negative news flow and sentiment regarding loadshedding, Greylisting, and political instability leading up to the 2024 General Elections, to name a few, the South African equity market has proved to be fairly resilient, posting a year-to-date return of 5.9% to the end of June. Over the last 12 months our local market is up a staggering 19.6%, while our local bond market (as measured by the SA All Bond Index) is up a very respectable 8.2%.

Encouragingly, the Analytics Model Portfolios have taken advantage of the positive market returns, both locally and globally, with the entire local range of Analytics Core Models outperforming their respective peer groups over the last twelve months. Furthermore, the Stable, Balanced, Flexible, and TFSA Flexible Model Portfolios all generated first-quartile performance relative to peers over the last year.

Despite the continued struggle surrounding electricity generation and transmission locally, there have been several positive developments. Leading up to the winter season many commentators were forecasting our worst bout of loadshedding on record, with expectations for the country to be plunged into stage 8 loadshedding, equating to 12 hours a day without electricity. In June, instead of increased power outages, the country experienced reduced loadshedding, owing to decreased unplanned maintenance and a greater contribution from renewable energy sources, amongst other factors.

Economically, there have also been encouraging signs with a better-than-expected Q1 current account deficit and easing inflation, which helped mitigate the currency's depreciation, standing at 11% year to date, at end June.

OUTLOOK

The last twelve months has seen the average Low Equity Fund in South Africa return 11.5%, while the average High Equity Fund has returned 14.7%; elevated returns in any market environment. As we move deeper into 2023, consensus suggests that the global economy is slowing. As such, investors should manage their expectations, as the next twelve months are unlikely to bring the same buoyant returns as the previous twelve.

Global inflation continues to pose a significant challenge, persisting at elevated levels beyond initial expectations. In June, the US Federal Reserve held its interest rates steady for the first time in ten consecutive rate hikes. These rate increases have had noticeable repercussions, particularly in the US banking sector over recent months. Now, the focus is shifting away from inflation and interest rates, towards concerns about economic growth and earnings. As the economic outlook faces mounting pressures, earnings growth is expected to moderate.

The prospects for the South African economy remain worrisome. Despite the improvement in loadshedding during the early stages of winter, the issue remains a significant impediment to growth.

Additionally, the South African fiscus is under severe strain, with the government expected to borrow billions in the upcoming years. Unfortunately, there are no quick fixes to these challenges. The country is anxiously awaiting the implementation of reform measures rather than mere discussions, as a crucial step towards addressing these issues effectively.

However, as the last twelve months has reminded investors, the political landscape and the economic environment do not move in tandem, with local balanced funds giving double-digit returns despite the negative sentiment. As such, listening to sound investment advice and staying the course will most often lead to the best investment outcome