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Gold or base metals?

2020Q4 Newsletter

Please note that our offices are operational for the lockdown period.

We will however not meet any clients at our offices, as a safety precaution.

Dear Investor,

We are re-assessing our call on gold shares based on the following observations:

Global growth has seemingly bottomed, which is being reflected in the US 10 year government bond yield. Rising yields are indicative of increasing growth and inflation expectations, which favours base metals over precious metals.

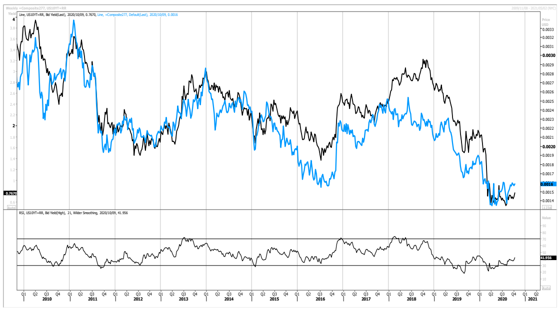


Figure 1 – US 10 year bond yield (black) and copper/gold ratio (blue)

The research of Cross Border Capital highligts that the US 10 year bond can rise to 2% from 0.76% currently, which will result in a substantial underperformance of gold.

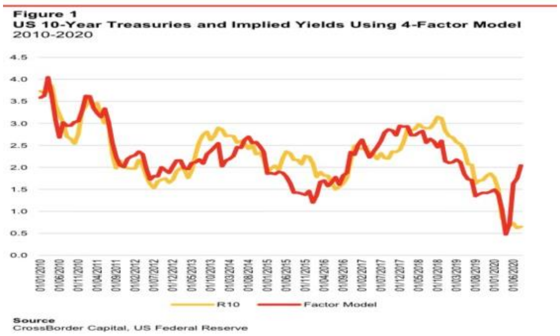


Figure 2 – US 10 year bond yield set to rise on increased economic activity

We therefore recommend that investors start positioning them for this recovery by overweighting base metal stocks (AGL, BHP, GLN, S32) and underweight gold in their portfolios.

SA Inc. equities

The increase in economic activity has historically favoured emerging markets, and especially commodity producing economies. We therefore remain positive on a recovery on the Rand, especially given the recent relative good news of the Ramaphosa administration taking a firmer stance on corruption.

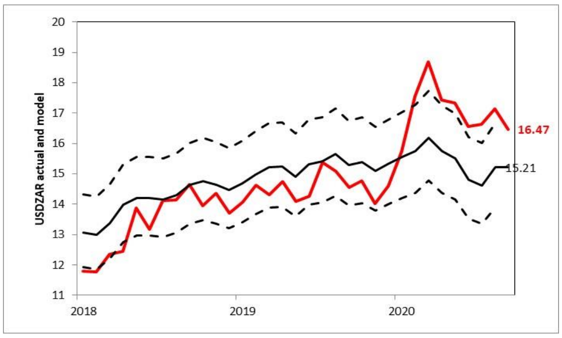


Figure 3 – USDZAR and fair value model

Any investment into SA Inc shares needs to be based on a gradual earnings recovery. The bulk of bad news has been priced into stocks, as well as the very low probability of a recovery in dividend payments over the next 12 months.

The figure below highlights the dividend yield based on the past 5 years average DPS, divided by the current share price. The assumption is that as the economy normalises, and stocks resume their dividend payments, the current share prices offer very attractive entry points.

LEWIS, REUNERT, MTN, NEDBANK, LIBERTY LIFE and ABSA rank high on this methodology.

We highlight LEWIS where management commentary was very bullish, with a debt-free balance sheet and which paid a dividend recently.

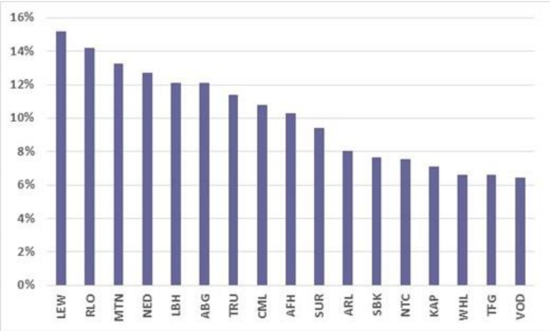


Figure 4 - SA Inc, DY based on past 5 years average DPS

Emerging market equities

The surge in global liquidity tends to favour emerging market equities. With the MSCI EM trading at a 25% discount to the MSCI World index, we believe that the attractive valuation, superior growth prospects and global liquidity should favour the asset class.

Figure 5 – MSCI EM trading a 25% discount to MSCI World

Investors can get exposure via the STXEMG ETF and for country-specific exposure we would allocate some cash to the STXCHN (SATRIX CHINA ETF).

Income Assets

We highlight the potential high dividend yielding stocks in Figure 4, with the associate company specific risks.

For income investors deposit rates have never been this low, as the Reserve Bank aggressively cut interest rates to stimulate the economy. The FRA curves are currently discounting a 50% probability of another 25bps cut, but more importantly that interest rates will gradually start increasing in 15 to 18 months' time.

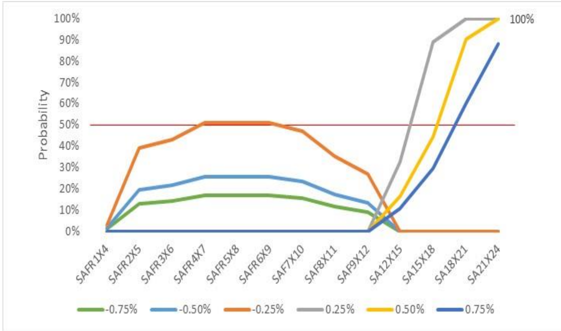


Figure 5 – FRA curves implying slow uptick in interest rates

The preference share index is both undervalued and most likely offering secure dividend payments. We have only seen one default on a dividend payment in the recent cycle, being the SASFIN Preference share.

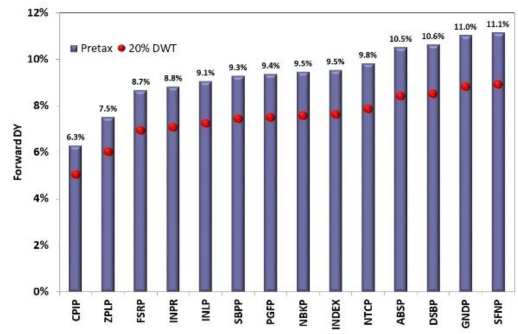


Figure 6 – JSE Preference shares offer value

From a valuation and quality perspective our top picks are the Discovery Preference share (DSBP, FDY = 10.6%) and the ABSA Preference share (ABSP, FDY = 10.5%).

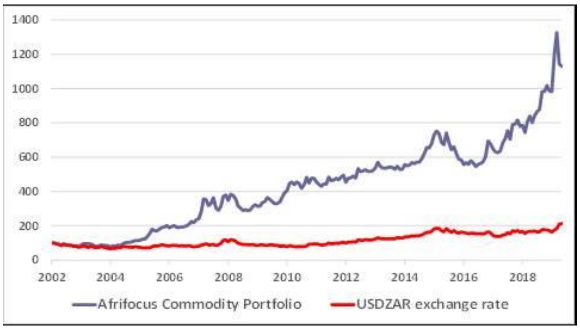
Afrifocus Commodity Portfolio

We have seen interest in our new Commodity Portfolio – a rules-based allocation model that allows for dynamic management of a physical commodity account, using JSE-listed ETFs and ETNs. The performance benchmark is the movement in the USDZAR exchange rate.

We believe that the model has been robustly developed and back-tested, resulting in average returns of 14% per annum after costs and fees. Speak to your Afrifocus Portfolio Manager to invest in this portfolio, with a minimum investment of R100 000.

The investment is

- High risk
- Suitable for investor who want to invest in an alternative real asset class, with a low correlation to traditional assets
- Carries counterparty risk



		Strategy	Benchmark
MaxDrawDown		-27%	-35%
Sharpe		0.51	
AnnReturn		14.9%	4.2%
Volatility		21.0%	17.0%
Rolling 12m	Min	-26%	
	Max	92%	

Figure 10 – Afrifocus Commodity Portfolio – superior risk-adjusted performance

Communicate with your Portfolio Manager on

- Full discretionary and advisory portfolio management across various risk profiles and asset classes
- Tax-free Savings Accounts
- Offshore investments using your annual offshore allowance
- Wealth management via unit trusts on the Alan Gray platform

Regards

Afrifocus Personal Wealth

Table 1 - Forecast returns for JSE Sectors

09 Oct 2020	INDEX	FPE	FDY	FORECAST GROWTH EPS	FORECAST GROWTH REVISIONS	FORECAST GROWTH DPS	TARGET	RETURN
ALSI	54555	11.3	3.6%	24%		19%	67624	28%
FINANCIALS	25519	9.5	5.4%	24%		27%	32202	32%
BANKS	5425	10.7	4.1%	14%		30%	6531	24%
LIFE INSURERS	27384	10.2	5.9%	28%		17%	36465	39%
FINANCIAL SERVICES	2397	7.9	3.3%	83%		22%	2778	19%
SA PROPERTY	227	6.1	13.7%	21%		33%	352	69%
INDUSTRIALS	26884	10.7	3.4%	44%		44%	32917	26%
CONSTRUCTION & MATERIALS	12	8.7	1.9%	50%		355%	15	26%
GENERAL INDUSTRIALS	99	12.3	3.5%	40%		33%	122	27%
INDUSTRIAL TRANSPORT	105	7.6	3.1%	53%		63%	124	21%
CONSUMER GOODS	57591	22.1	3.2%	10%		7%	56661	2%
FOOD PRODUCERS	6093	13.7	4.7%	15%		16%	6107	5%
BEVERAGES	160	65.0	1.3%	-14%		-13%	158	0%
PERSONAL GOODS	1119	40.0	2.0%	10%		4%	1026	-6%
TOBACCO	7493	7.9	8.1%	13%		9%	9456	34%
HEALTHCARE	3669	11.8	3.1%	14%		164%	4303	20%
HEALTHCARE EQUIP & SERVICES	4572	15.3	3.4%	31%		146%	5342	20%
PHARMACEUTICALS & BIOTECH	11626	8.8	2.6%	1%		266%	13710	21%
CONSUMER SERVICES	17946	19.9	2.6%	21%		22%	19245	10%
GENERAL RETAILERS	3954	23.0	1.3%	17%		29%	4162	7%
FOOD & DRUG RETAILERS	10324	19.6	2.7%	17%		20%	11099	10%
MEDIA	759	13.7	5.3%	62%		12%	820	13%
TRAVEL & LEISURE	1397	-8.2	-1.4%	5%		n/a	2010	42%
TELECOMMUNICATIONS	3662	8.2	7.2%	12%		11%	4977	43%
FIXED LINE TELECOMMUNICATIONS	867	5.7	0.0%	33%		-100%	1271	47%
MOBILE TELECOMMUNICATIONS	121	8.4	7.5%	10%		12%	164	43%
TECHNOLOGY	39710	21.5	0.2%	44%		28%	60864	54%
BASIC MATERIALS	38358	8.0	5.1%	22%		16%	44957	22%
GENERAL MINING	12358	9.1	6.1%	5%		5%	14376	22%
PLATINUM MINING	73	4.9	5.8%	35%		53%	91	30%
GOLD MINING	5117	6.5	3.3%	53%		57%	6256	26%
CHEMICALS	7194	12.3	0.7%	n/a		1132%	9011	26%
FORESTRY & PAPER	54297	14.2	3.1%	18%		33%	53037	1%
INDUSTRIAL METALS	23867	9.0	9.6%	-12%		-16%	21083	-2%