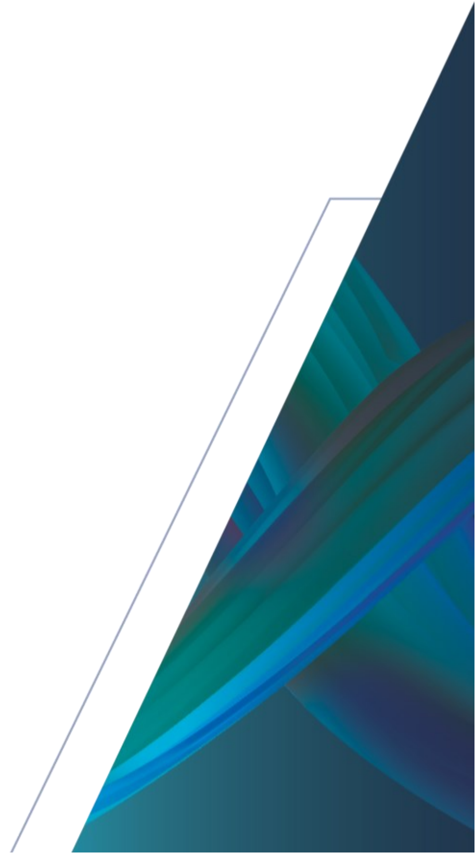
PORTFOLIOMETRIX

QUARTERLY COMMENTARY

GLOBAL PORTFOLIOS EDITION

SEPTEMBER 2021



QUARTERLY COMMENTARY

GLOBAL PORTFOLIOS EDITION SEPTEMBER 2021

ASSET CLASS RETURNS

Asset Class	Underlying Index	CCY / Price	Sep 2021	Q3 2021	1 Year	3 Years Annualised	5 Years Annualised
Global Asset Returns							
Global Equities	MSCI AC World	USD	-4.1%	-1.0%	27.9%	13.1%	13.7%
Global Bonds	Bloomberg Barclays Global Agg	USD	-1.8%	-0.9%	-0.9%	4.2%	2.0%
Global Property	FTSE EPRA NAREIT Developed Rental	USD	-6.2%	-0.5%	30.5%	6.7%	4.5%
Global Asset Classes	**Underlying Index**	**CCY / Price**	**Sep 2021**	**Q3 2021**	**1 Year**	**3 Years Annualised**	**5 Years Annualised**
Global Equities							
Developed Equity	MSCI World	USD	-4.1%	0.1%	29.4%	13.7%	14.3%
Emerging Market Equity	MSCI Emerging Markets	USD	-4.0%	-8.0%	18.5%	8.9%	9.6%
S&P 500	S&P 500 Index	USD	-4.7%	0.6%	30.0%	16.0%	16.9%
Dow Jones	Dow Jones Industrial Average	USD	-4.2%	-1.5%	24.2%	11.0%	15.7%
Nasdaq	NASDAQ Composite Index	USD	-5.3%	-0.2%	30.3%	22.7%	23.4%
FTSE 100	FTSE 100 Index	GBP	-0.2%	1.9%	25.3%	2.0%	4.6%
STOXX Europe 600	STOXX Europe 600 Price Index EUR	EUR	-3.3%	1.0%	29.6%	9.2%	9.3%
CAC	CAC 40 Index	EUR	-2.2%	0.4%	39.0%	8.8%	11.0%
DAX	Deutsche Boerse German Stock Index	EUR	-3.6%	-1.7%	19.6%	7.6%	7.7%
Hong Kong HSI	Hong Kong Hang Seng Index	HKD	-4.7%	-13.9%	7.5%	-0.9%	4.5%
Nikkei	Nikkei 225	JPY	5.4%	2.9%	29.0%	8.9%	14.5%
Shanghai SE	Shanghai Stock Exchange Comp Index	CNY	0.8%	0.4%	13.2%	10.6%	5.9%
SA ALSI	FTSE/JSE All Share - Return in USD	USD	-7.1%	-6.1%	36.0%	6.3%	5.8%
MSCI South Africa	MSCI South Africa Index USD	USD	-4.8%	-5.6%	27.5%	2.4%	2.1%
Currencies							
Rand/Dollar	ZAR/USD	15.07	-3.7%	-5.2%	11.1%	-2.1%	-1.9%
Rand/Pound	ZAR/GBP	20.31	-1.6%	-2.8%	6.5%	-3.2%	-2.6%
Rand/Euro	ZAR/EUR	17.46	-1.9%	-3.0%	12.6%	-2.0%	-2.4%
US Dollar Index	DXY	94.23	1.7%	1.9%	0.4%	-0.3%	-0.3%
Euro/Dollar	EUR/USD	1.16	-1.9%	-2.3%	-1.2%	-0.1%	0.6%
Dollar/Yen	USD/JPY	111.29	1.2%	0.2%	5.5%	-0.7%	1.9%
Pound/Dollar	GBP/USD	1.35	-2.0%	-2.6%	4.3%	1.1%	0.8%
Commodity Prices (USD)							
West Texas Oil	WTI Crude	$75.03	9.9%	5.8%	74.4%	6.3%	5.5%
Brent Crude Oil	Brent Crude	$78.52	7.6%	4.5%	91.7%	-1.7%	9.9%
Gold	Gold Spot $/Oz	$1,757	-3.1%	-0.7%	-6.8%	13.8%	6.0%
Platinum	Platinum Spot $/Oz	$967	-4.8%	-10.0%	8.3%	5.8%	-1.2%
Palladium	Palladium Spot $/Oz	$1,913	-22.6%	-31.3%	-17.2%	21.2%	21.6%
Copper	LME Copper Spot ($)	$8,945	-6.1%	-4.4%	34.1%	12.6%	13.0%
Iron Ore 62%	Generic 1st 'SCO' Future	$120	-24.9%	-44.2%	-3.5%	20.3%	16.1%

Towards the end of the third quarter of 2021, global equities saw their first sell-off in about a year as fears emerged that China's heavily indebted property developer Evergrande Group might lead to the collapse of China's systemically important real-estate market, as well as major central banks starting to indicate tighter monetary policy than markets expected. More generally, the quarter saw markets begin to worry more seriously about 'Stagflation', the worst of all worlds in the form of lower growth (stagnation) and rising prices (inflation). The previous narrative of reflation faltered as growth numbers softened, whilst reported inflation kept on rising.

Q3 DRIVERS

Evergrande and Chinese Property Developers

Regulatory changes coming out of China has been a source of angst for global markets for a large part of the year now. Most recently the fears of an Evergrande default and potential knock-on effects were a contributing factor to the selloff in markets in September. But what started this and why now?

After a meeting in August 2020, China imposed the three red lines guidance on selected developers. This was done at a time when Chinese property was experiencing significant increases in land prices, booming sales and growing debt levels. To control excessive leverage in the industry, regulators imposed certain criteria that, depending on their adherence to these criteria, would dictate the levels of borrowing they could take on (access to finance). The criteria were as follows:

1. Liability to asset ratio (excl. advance receipts) of less than 70%
2. Net gearing ratio of less than 100%
3. Cash to short-term debt ratio of more than 1x

If a developer met all criteria, they had greater access to debt than otherwise, as detailed below:

Color code	Number of red lines breached	Allowable annual growth in debt
Green	0	15%
Yellow	1	10%
Orange	2	5%
Red	3	0%

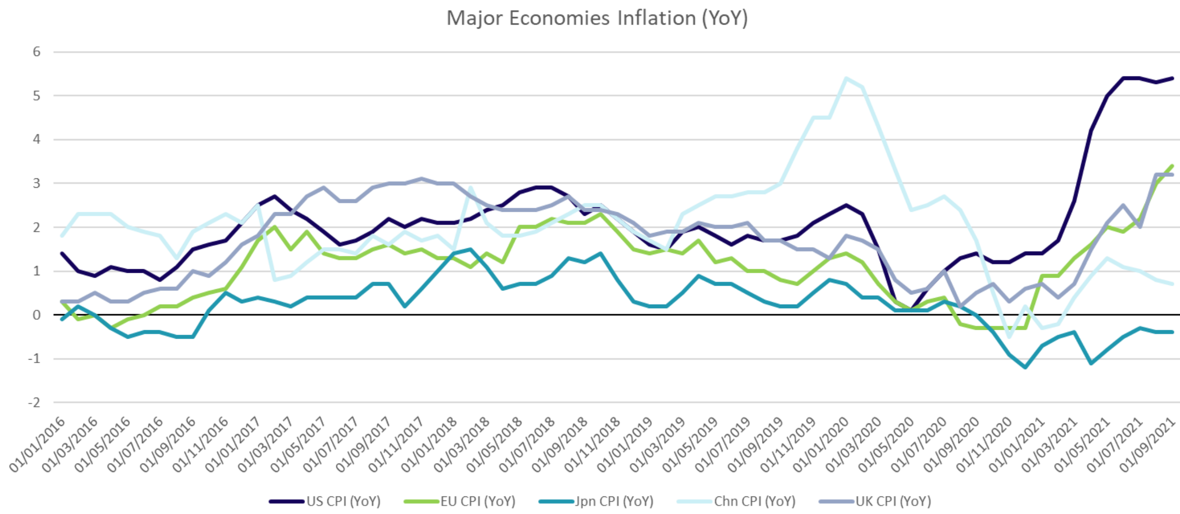
Source: UBS Asset Management

Evergrande's level of debt has been a concern for many years now and the implementation of the three red lines accelerated the decline for the company due to their poor debt metrics. The reason why it all came to a head in September was that debt repayments came due, and the company simply did not have the liquidity to honour these. It is an ongoing saga with restructuring required.

But should we be worried? As it relates directly to Evergrande we think that the Chinese government have sufficient resources to manage the crisis successfully. However, Chinese property is a big contributor to GDP growth and so the broader issues surrounding the sector certainly pose a growth risk to the country and hence global growth.

Stagflation Risks

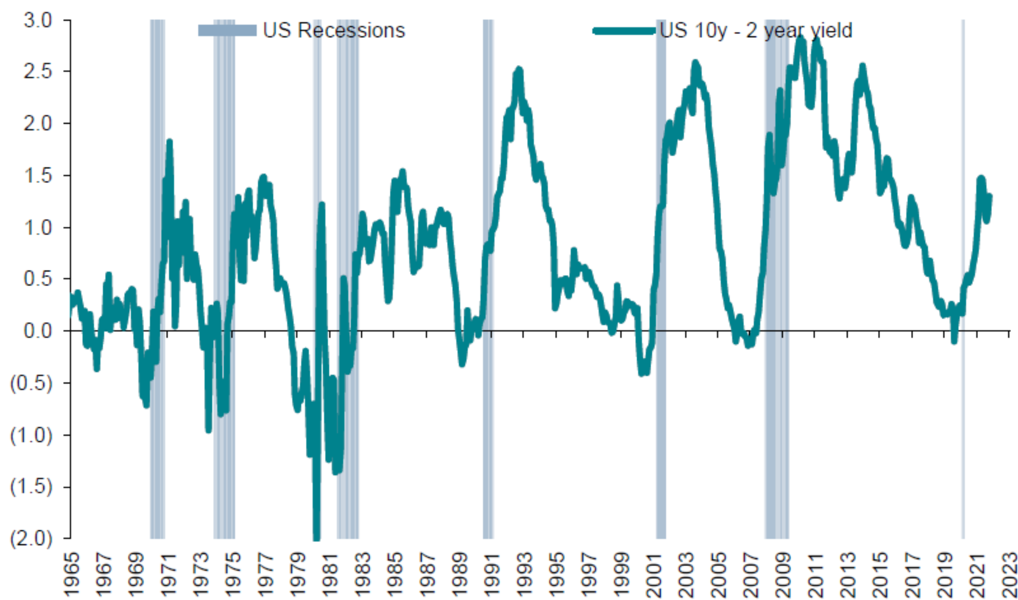
Inflation numbers across the globe are high and the most recent U.S. inflation figure is the highest read since 2008.



Source: Bloomberg and PortfolioMetrix

Contributing factors to global inflation have worsened and markets are concerned that higher inflation will be around for longer. Logjams at ports in the U.S. pose serious logistical issues that need to be addressed in the lead up to Christmas as demand for goods are likely to pick up.

Although stagflation risks have accelerated, these periods are typically precipitated by a yield curve flattening, and then inverting. However, over the last month the yield curve has steepened:



Source: Exane BNP Paribas estimates, DataStream

Growth forecasts globally remain robust. Deceleration is expected but growth figures remain healthy:

Bloomberg Consensus	2014-19 Avg.	2020	2021	2022	2023
Brazil	-0.3	-4.1	5.2	2.1	2.3
China	6.8	2.3	8.4	5.5	5.2
India	7.2	4.0		9.2	6.7
Japan	0.8	-4.7	2.4	2.5	1.3
Mexico	2.1	-8.2	6.0	3.0	2.3
Russia	0.9	-3.0	4.0	2.5	2.1
South Africa	1.0	-7.0	4.8	2.3	2.0
UK	1.9	-9.9	6.8	5.4	2.0
US	2.4	-3.4	5.9	4.2	2.4
Eurozone	1.9	-6.3	5.0	4.3	2.2

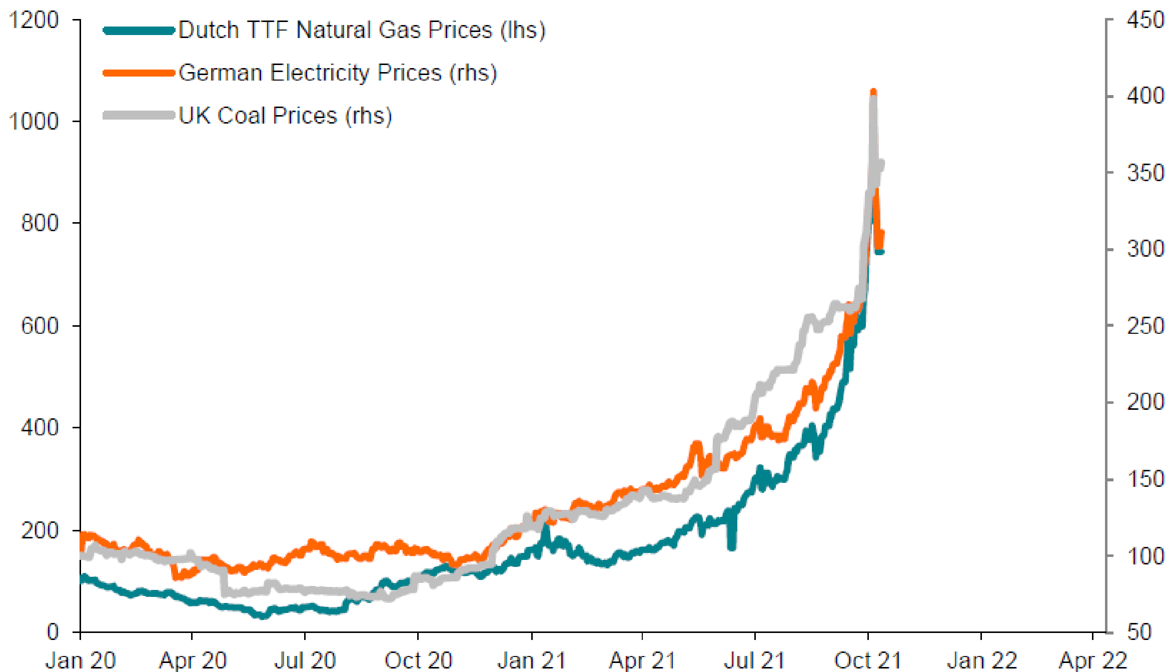
GS	2014-19 Avg.	2020	2021	2022	2023
Brazil	-0.3	-4.1	4.9	2.0	2.2
China	6.8	2.3	8.2	5.6	5.3
India	7.2	4.0		7.3	6.1
Japan	0.8	-4.7	2.6	2.9	1.2
Mexico	2.1	-8.2	6.0	2.5	2.1
Russia	0.9	-3.0	4.3	3.7	3.2
South Africa	1.0	-7.0	5.0	2.4	2.2
UK	1.9	-9.9	6.1	5.4	2.1
US	2.4	-3.4	5.8	4.5	2.0
Eurozone	1.9	-6.3	5.2	4.5	1.9

Below consensus
In line with consensus
Above consensus

Source: Goldman Sachs Asset Management

That said, risks to inflation are high as supply bottlenecks worsen and a recent energy price surge reminds us that growth needs energy. The fact that globally we are undertaking the greatest energy shift in history in a (justified) aggressive manner certainly means that it will not be plain sailing.

Figure 14: European gas and electricity prices have increased sharply



Source: Exane BNP Paribas estimates, DataStream

Although we still think that many of the factors driving up inflation right now are transitory this cannot be a static view held indefinitely. The global energy transition to greener sources have resulted in higher energy costs in Europe, power outages in China and the UK needing to fire up old coal-fired power stations to meet demand (and try to cushion price spikes). Currently, fossil fuels satisfy 83% of primary-energy demand and this needs to fall towards zero. With low inventories in fuel sources, the system is more vulnerable to shocks and the transition away from fossil fuels will be bumpy, if not carefully managed.

For now, the growth backdrop remains robust, inflationary pressures are expected to ease going into 2022 and central banks are still accommodative. This is generally supportive of risky assets.

QUARTERLY MACROECONOMIC DATA

GDP figures released in the third quarter were for Q2 2021, where many developed markets were bouncing back from winter spikes in COVID and so showed solid growth. Inflation increased during the third quarter overall whilst unemployment generally fell as restrictions were lifted and economies continued recovering.

	Previous Quarter Growth (annualised)			Inflation		Core Inflation	Unemployment		Comment
Region	Latest Reading	Change	Detail	Latest Reading	Change	Latest Reading	Latest Reading	Change	
UK	23.9%	↑	Above expectations	3.2%	↑	3.1%	4.6%	↓	Inflation highest since March 2012 and Core Inflation highest since November 2011
US	6.7%	↑	Slightly above expectations	5.3%	↑	4.0%	5.2%	↓	Unemployment lowest since March 2020
Eurozone	9.1%	↑	Slightly above expectations	3.0%	↑	1.6%	7.5%	↓	Inflation highest in 10 years
Japan	1.9%	↑	Above expectations	-0.4%	↑	0.0%	2.8%	↓	
China	5.3%	↑	Slightly above expectations	0.8%	↓	1.2%	5.1%	↑	
Brazil	-0.4%	↓	Slightly worse than expectations	9.7%	↑	6.1%	13.7%	↓	Inflation highest since February 2016
India	8.7%*	↓	* Q1 2021 figure - latest datapoint	5.3%	↓		8.3%	↓	
Russia	0%*	↑	* Q1 2021 figure - latest datapoint	6.7%	↑	7.1%	4.4%	↓	Inflation highest since August 2016
South Africa	4.9%	↑	Above expectations	4.9%	↓	3.1%	34.4%	↑	Highest unemployment figure since quarterly data began (2008)

Note: Change is from value as at previous quarter (revised if necessary). Core inflation omits volatile items such as energy and food.
Note 2: Some of the quarterly growth figures are annualised data points, others we have annualised ourselves using the latest quarterly data
Source: tradingeconomics.com

MONETARY POLICY (RATES & EXTRAORDINARY MEASURES)

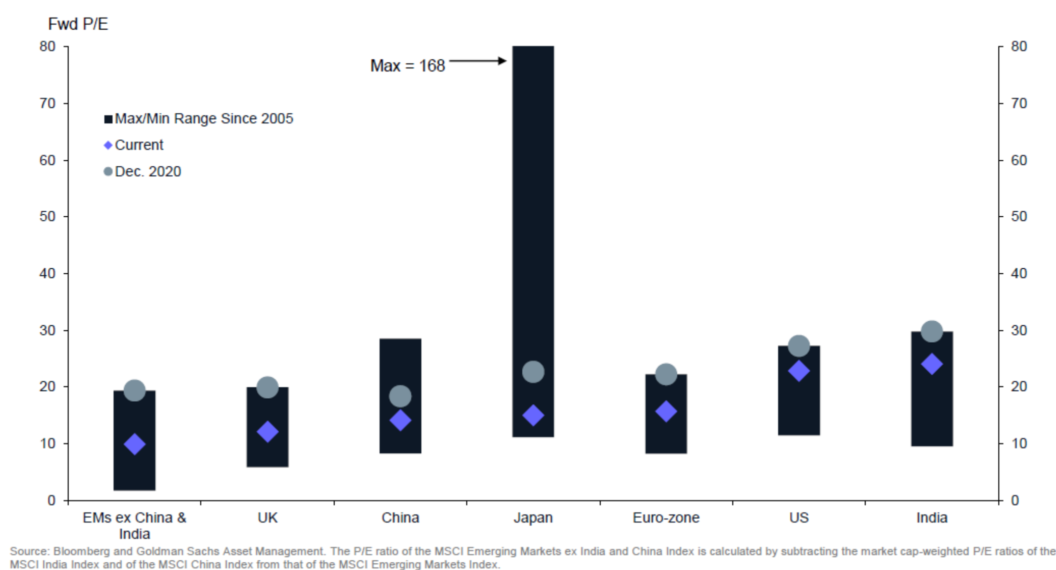
There was little change in developed market central bank action over the quarter as rates were kept low and central bankers maintained quantitative easing, although there was certainly more hawkish messaging around future rate rises and tapering of bond purchases. A number of emerging markets raised rates to control surging inflation in their local markets.

	Monetary Rate			Detail
Central Bank	End Q2 2021	End Q3 2021		
US Federal Reserve	0%-0.25%	0%-0.25%	→	Indicated that a reduction in the pace of asset purchases "may soon be warranted". And a faster pace of interest rate rises is expected in the next couple of years
Bank of England	0.10%	0.10%	→	Expect to cease reinvesting income from QE purchases once the interest rate reaches 0.5% and will consider actively reducing QE once the rate reaches 1%
European Central Bank	0%	0%	→	Announced a moderation in the pace of asset purchases under the Pandemic Emergency Purchase Programme
Bank of Japan	-0.10%	-0.10%	→	Confirmed details on lending programme - 1 year interest free loans for financial institutions providing financing to help Japan address climate change issues
China	3.85%	3.85%	→	
Brazil	4.25%	6.25%	↑	100 basis points rise in both August & September 2021
India	4.00%	4.00%	→	
Russia	5.50%	6.75%	↑	100 basis points rise in July 2021 & 25 basis points rise in September 2021
South Africa	3.50%	3.50%	→	

Source: global-rates.com

LOOKING AHEAD

Despite the inflation risks, we are still cautiously optimistic around our portfolios. From a global investor's perspective, it's difficult to make a very attractive case for cash and bonds under a high inflation scenario. Ignoring for now more alternative assets, this boils down to acknowledging that mainstream portfolios have three main asset classes to choose from: cash, bonds and equities. With cash and bonds looking unattractive, equities are seen as the only remaining asset class for protecting and growing wealth going forward. This should continue to support investor demand for the asset class, provided global growth does not decline too severely. Equity valuations have also reined in from the end of 2020 leaving a constructive backdrop despite the risks.



Source: Goldman Sachs Asset Management

This is not to say that cash and bonds should not form a part of portfolios. In fact, there are very good reasons why these asset classes should remain in most well-diversified, appropriately risked portfolios.

As is always the case, there are risks that may or may not materialise and portfolios need to be able to weather either scenario. Our portfolios continue to hold many diversified return sources and we believe that this is the best way to navigate what is likely to be a risky and unpredictable environment.

BUILDING BLOCK COMMENTARY

BUILDING BLOCK PERFORMANCE TABLE

	3 Months			1 Year			3 Year			5 Year		
	Fund	Index	Rel.	Fund	Index	Rel.	Fund	Index	Rel.	Fund	Index	Rel.
Global Sovereign Bonds	-0.88%	-0.88%	0.00%	0.35%	-0.91%	1.26%	4.66%	4.24%	0.42%	2.83%	1.99%	0.84%
Global Corporate Bonds	-0.47%	-0.76%	0.29%	2.24%	1.72%	0.52%	5.04%	6.00%	-0.95%	--	--	--
Global High Yield Bonds	0.53%	-0.37%	0.90%	15.20%	9.49%	5.71%	5.62%	5.75%	-0.13%	--	--	--
Emerging Market Bonds (LC)	-2.61%	-3.10%	0.49%	4.00%	2.63%	1.36%	4.57%	3.66%	0.90%	2.38%	2.06%	0.32%
Global Listed Infrastructure	-1.18%	-0.25%	-0.93%	20.48%	15.87%	4.61%	14.23%	7.70%	6.53%	--	--	--
Global Property	0.89%	-0.34%	1.23%	26.16%	31.76%	-5.59%	8.90%	7.77%	1.13%	6.73%	5.53%	1.20%
Global Equity	-0.38%	-1.05%	0.68%	30.82%	27.44%	3.39%	--	--	--	--	--	--

All returns for periods greater than 1 year are annualised

Global Sovereign Bonds: Bloomberg Barclays Global Aggregate, Global Corporate Bonds: Bloomberg Barclays Global Corporates, Global High Yield Bonds: Bloomberg Barclays Global High Yield, Emerging Market Bonds (LC): JPM GBI EM Global Diversified Composite, Global Listed Infrastructure: FTSE Global Core Infrastructure 50/50, Global Property: Global Property (Dev. Rental), Global Equity: MSCI ACWI, Global Equity (EM Funds): MSCI ACWI, Global Equity (Styles): MSCI ACWI, Global Bonds: Bloomberg Barclays Global Aggregate.

Note: All returns provided are in US dollars

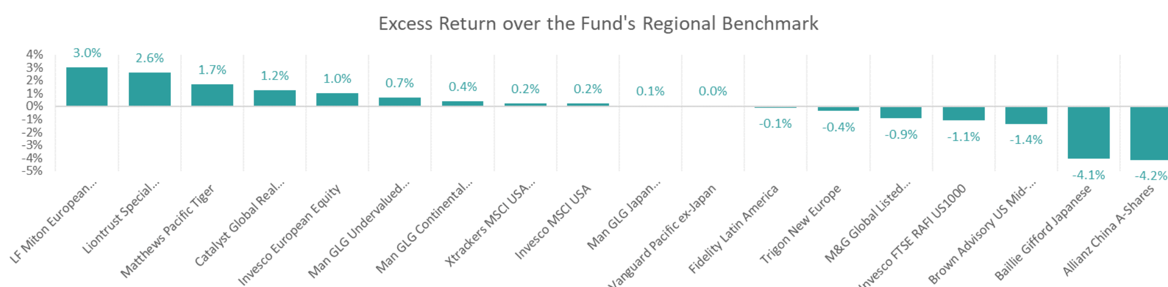
GLOBAL EQUITY COMMENTARY

Overview

The PortfolioMetrix Global Equity fund outperformed by 3.4% over the past 12 months (27.4% vs 30.8% for the fund) relative to its MSCI ACWI benchmark,

- Over the quarter the fund outperformed by 0.7%, as the index returned -1.1% and the fund generated -0.4%

The performance of the underlying funds (versus their respective regional indices) for the quarter is shown below (in USD). Strong outperformance in developed Europe drove alpha as all fund selections in the region outperformed. Main alpha drivers were Miton European and Liontrust Special Situations. Matthews Asia continued to perform well in the emerging Asia region despite difficult conditions given China's dominance of the market. Biggest underperformers were the Allianz China A Onshore fund and Baillie Gifford Japanese. These two positions are around 7% of overall exposure and so the effect on the overall fund was limited.



Detail

- Developed markets (DM) outperformed emerging markets (EM) as regulatory uncertainty out of China and a stronger U.S. dollar dampened risk taking and appetite for EM equity.
- Japanese equity was the best performing DM region over the quarter with political change and vaccine progress boosting prospects for its economy.

- In the EM space emerging Europe performed strongly but the dominant Asian region dragged down the overall asset class.
- Latin American equities were very volatile and again showed their high beta nature and sensitivity to China due to the regions outsized reliance on commodities
- Value underperformed growth for the quarter as growth expectations started to fade and market participants favored those stocks that can grow earnings in a weak environment.
- Momentum was the best performing factor for the quarter with small caps and quality the worst performing.
- Although China was generally under pressure, there was an extreme dislocation in the onshore and offshore market with the offshore market (typically dominated by offshore investors) underperforming by 14%.
- The above speaks to offshore investors dissatisfaction of regulatory uncertainty and the effects of this on growth in the short to medium term.
- Active fund implementation drove outperformance over the quarter and the year for the fund
- There were no fund changes over the quarter

GLOBAL BONDS COMMENTARY

Overview

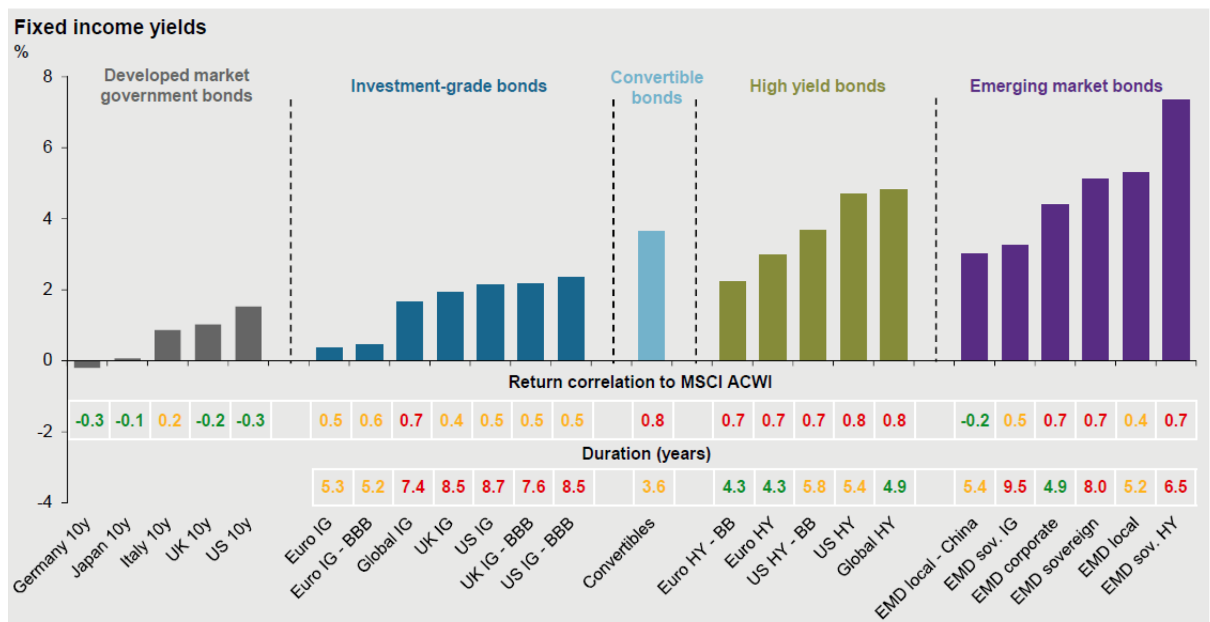
Underlying funds over the quarter produced the following relative returns (vs Bloomberg Barclays Global Aggregate):

- PIMCO GIS Global Bond: outperformed by 0.01%
- Allianz Global Credit: outperformed by 0.41%
- Amundi Pioneer Global High Yield: outperformed by 1.42%
- PIMCO GIS Asia High Yield: underperformed by 4.18%
- PIMCO GIS Emerging Local Bond: underperformed by 1.73%
- PIMCO GIS Emerging Markets Bond (EUR): underperformed by 2.13%
- PIMCO GIS Emerging Markets Bond (USD): outperformed by 0.32%

Detail

- The past quarter served as a mirror of the previous; fixed income sold off, fears of higher global inflation outpacing growth, and a withdrawal of the addictive central bank stimulus (or at the very least a reduction thereof). Returns of the high-level sectors:
    - Global Treasuries -1.11%
    - Global Corporates -0.76%
    - Global High Yield -0.37%
    - Emerging Markets -3.10%
- The inflation equation is threatening markets on an “expected” basis, however the various indicators point to a more sustained impact as global PMIs rise. According to JP Morgan Developed markets PMI rose to 58.3, Emerging Markets PMI rose to 49.6.
- The inflation equation is down to the rates action taken by central banks around the globe, particularly since consumption has been the largest driver behind the elevated levels of inflation over the last quarter. The first major central bank to move is likely to be the US Federal Reserve who will look to taper their $120bn per month bond purchase programme. Thereafter raising rates to reduce the negative policy.

- The road to "normalization" has already shown to be a bumpy one as investors come to grasps with the lower levels of stimulus, the state of the global economy, and of course the relative valuation between fixed income sectors, and risk assets. Despite this the reward for taking on fixed income risk has been diluted dramatically over the past 20 years, using spreads as indicators of this (and comparing to their 5-year average), followed by a chart of absolute yields of different fixed income sectors:
  - IG Corporate 0.88% (1.19%)
  - High Yield 3.82% (4.42%)
  - Emerging Markets 3.24% (3.56%)



Source: JPM Morgan Guide to the Markets 2021Q3

GLOBAL PROPERTY COMMENTARY

Overview

The Catalyst Global Real Estate fund underperformed by 5.6% over the past 12 months (31.8% vs 26.2% for the fund) relative to its Global Property (Dev. Rental) benchmark,

- Over the quarter the fund outperformed by 1.2%, as the index returned -0.3% and the fund generated 0.9%

Detail

- Global listed property has delivered approximately 22.9% in USD in the first eight months of 2021 the best year-to-date returns on record for the sector.
- The Biden administration unsuccessfully tried to extend the moratorium on evictions beyond 31 July 2021 with an estimated 2.5-3.5 million households behind on rent amounting to $12- 17bn due to landlords.
- It's not just last year's trend pieces that have fallen out of favour – so have the once-loved malls who sell them. Online shopping has led to a somewhat redundant customer offering, and malls no longer serve the purpose in society they once did. Foot traffic, retail sales and tenant demand continue to fall, and shopping malls are experiencing higher natural levels of vacancy, lower market rents, cash flows and valuations.

- Most of the real estate sectors that are set to boom have technology driven societal change at their core. Logistics warehousing, manufactured housing, detached housing, medical office buildings, private hospitals, self-storage facilities, data centres, and biotech laboratories are among the sectors set-up for strong future growth.
- Falling home ownership rates with societal change, are leading to a greater propensity to rent rather than own, with rental housing being a major beneficiary.
- At the end of the quarter, Catalyst had material overweights in the Industrial and Residential sectors, with meaningful underweights to the Retail and Office sectors relative to the benchmark.

GLOBAL LISTED INFRASTRUCTURE COMMENTARY

Overview

The M&G Global Listed Infrastructure fund outperformed by 4.6% over the past 12 months (15.9% vs 20.5% for the fund) relative to its FTSE Global Core Infrastructure 50/50 benchmark,

- Over the quarter the fund underperformed by 0.9%, as the index returned -0.2% and the fund generated -1.2%

Detail

- Dividends from the fund's holdings have been on a positive footing all year, with most companies either reinstating or increasing their payouts. Transurban, however, bucked the trend as the Australian toll road company cut its dividend for the fiscal year ended 30 June 2021. The final dividend was 34% higher than last year's payment but not enough to recoup the halving of the interim dividend.
- The fund added one new name to its holdings over the quarter, initiating exposure to Xinyi Energy, a pure solar power company which provides exposure to the structural growth in Chinese renewables with the additional benefit of an attractive yield.
- The fund increased its exposure to Home REIT after supporting the company in an equity raise. The issue was oversubscribed, and the company now has the financial fire power to accelerate its long-term strategy. Home REIT has a key role to play in addressing a critical social need, namely the provision of accommodation for the homeless in the UK.
- Keyera provided the biggest drag on performance over the quarter, as lower product prices weighed on sentiment in the energy sector. The share-price weakness remains at odds with the company's solid fundamentals. The midstream business, which owns and operates pipelines, storage terminals and processing facilities, reported solid second quarter results and continues to offer compelling long-term prospects, driven by its exposure to some of the most prolific basins in North America. The stock remains attractively valued, in the fund's view, with a dividend yield of more than 6%.
- Sydney Airport received an unsolicited takeover approach from a consortium of pension funds and private equity, which offered a 42% premium to buy the owner and operator of the unique asset outright. The shares jumped 35% but remained below their pre-COVID peak. The board rejected the proposal after reaching a unanimous conclusion that the bid undervalues the company.
    - This is the third instance this year when a fund's holding has attracted interest from private buyers. Naturgy Energy, a world leader in liquefied natural gas (LNG), was the first to come under scrutiny in January, where an offer to pay a 20% premium for a 23% stake in the Spanish company was received. CCR, the Brazilian toll road company, was next as IG4 Capital Investimentos offered to buy a 14.8% stake at a premium in May. These examples of private capital buying listed companies which own and operate critical infrastructure assets are symbolic events, that highlight the latent value in listed infrastructure.

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