FOREWORD

DID YOU KNOW? RESERVE CURRENCY

A reserve currency occupies a privileged position within the global financial landscape. It denotes a currency that numerous countries and central banks maintain in substantial quantities as a component of their foreign exchange reserves. Essentially, it serves as a form of financial safeguard. In international trade relations, reserve currencies are frequently utilised owing to their extensive recognition and credibility.

The rationale behind the existence of reserve currencies lies in their capacity to facilitate international trade and financial transactions, functioning as a universal monetary language that transcends borders. By holding a reserve currency, a nation can readily engage in the acquisition of goods, settle debts, and stabilise its own currency as and when necessary.

The most renowned among reserve currencies is the United States dollar, which enjoys a prominent status in the global financial realm due to the robustness of the United States economy and the stability of its government. Former French President Valery Giscad d'Estaing referred to the US dollar as America's 'exorbitant privilege'. Other reserve currencies encompass the euro, the Japanese yen, and the British pound. Their limited number is attributable to the imperative requirement of trustworthiness and widespread acceptability on a global scale.

In essence, reserve currencies play an instrumental role in ensuring the seamless functioning of the worldwide financial system. They are akin to the admired individuals in the realm of currencies, cherished for their reliability and coveted by all to include in their financial portfolios.

IN THIS ISSUE

- *Foord Flex Income Fund Turns One*
- *Will The Dollar Remain the Global Reserve Currency?*
- *Thematic Investing*
- *Foord Asia-ex Japan Fund Explained*
- *Gender Diversity in Asset Management*

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THE FOORD FLEX INCOME FUND TURNS ONE

FARZANA BAYAT
Portfolio Manager

Foord's fixed interest product suite has now reached its one-year anniversary. The funds have gained good traction with retail and institutional investors alike. Portfolio manager FARZANA BAYAT takes a closer look at the Foord Flex Income Fund — the flagship of the fixed interest product range.

The Foord Flex Income Fund is suitable for investors looking to earn a high and stable income and who can tolerate small amounts of volatility. The fund aims to:

- Protect investor capital by avoiding negative returns over periods as short as three months
- Generate high levels of stable and consistent income and
- Beat inflation by up to 3% per year over time.

To achieve these objectives, the portfolio has at its disposal a broad universe of income-producing investments. The fund can invest judiciously offshore, but we typically hedge out the currency risk for investors.

We aim to hold an optimal blend of investments based on how cheap they are, the yield pickup as well as the additional risk they add to the portfolio. Where an attractively priced investment introduces material risks to the fund, we ration how much we buy to limit drawdowns should the market move against us. We structure the portfolio to at least deliver cash returns in worst-case outcomes. In our good-case scenarios, we expect the fund to produce returns of 2 – 3% more than cash deposits.

Over the year, the fund has returned 8.6% after fees and expenses when official inflation averaged 5.3%. The fund also outperformed its benchmark, which returned 8.0% for the year. The benchmark is 110% of the Alexander Forbes Short-term Fixed-interest Call Deposit Index (Stefi Call). The Stefi Call is a recognised benchmark of returns in the South African money market.

Foord is a safety-first investment manager — we don't gamble with investors' money. The Foord Flex Income Fund is accordingly conservatively positioned against a myriad of rising risks in the fixed interest universe. Nevertheless, the fund is still delivering an attractive yield of over 10% with a very low level of credit and interest rate risk. We are comfortable that the fund will achieve its investment objectives and will do so with very little risk of drawdown. After a year of building resilience in the portfolio, the fund is split 90:10 in favour of South African investments, with very little currency risk.

Given the elevated fiscal, political and credit risks in South Africa, there are two areas of the market we are actively avoiding. The first is SA government fixed-rate bonds, also called 'nominal' bonds. These offer a high fixed rate of interest but disappoint if interest rates rise or inflation runs higher than we expect. We will aim to buy nominal bonds tactically during bond market selloffs. The other area of the market we are cautious on is the South African corporate credit market. Given higher yields, investors are pouring money into cash and income funds, which in turn are driving up the prices of credit instruments to worrying levels. Unlike many competitor funds, we are steering clear of credit instruments until the market normalises.

WILL THE DOLLAR REMAIN THE GLOBAL RESERVE CURRENCY?

RASHAAD TAYOB
Portfolio Manager

De-dollarisation has become a trending geopolitical topic after the perceived weaponisation of the greenback as a tool to sanction Russia for its invasion of Ukraine. Portfolio manager RASHAAD TAYOB suggests that the threat of de-dollarisation is an underappreciated risk, given the speed at which geopolitical shifts are materialising.

The US dollar has been the de facto global reserve currency since the middle of the last century. Before then, the United Kingdom's pound sterling dominated global reserves from the early 19th century. However, sterling fell from favour after the UK nearly bankrupted itself during the first and second world wars. Today the US dollar accounts for almost 60% of global central bank foreign-currency reserves, while pound sterling is less than 5%.

Other currencies have also occupied dominant status in history, including those from Portugal, Spain, the Netherlands and France from the Renaissance onwards. The lesson here is that dominant reserve currencies do change from time to time — and do so swiftly. But hope for swift de-dollarisation may be premature thinking.

Aside from its global central bank reserve status, the US dollar accounts for about 90% of the foreign exchange — or FX — market. Neither the euro nor the Chinese renminbi has been able to make significant inroads over the last three decades. For all intents and purposes, the FX market is the dollar market. Despite China being the largest trading partner for much of the world, global trade is still conducted primarily in US dollars.

The recent freezing of Russian central bank US dollar reserves was a watershed moment and a wake-up call to countries not aligned with the US. This weaponisation of the dollar, combined with recent high inflation and reckless US fiscal spending, has provided renewed impetus to the push for de-dollarisation. The US has benefited from the dollar being the global reserve currency for the last 70 years. Recent events created concerns that it may be abusing its 'exorbitant privilege' (see Did You Know?).

The BRICS group of countries — Brazil, Russia, India, China and South Africa — has proved to be the ideal platform through which China and Russia could drive the de-dollarisation agenda. The recent addition of six new member countries — including oil heavyweights Saudi Arabia, UAE and Iran — was a big win for the BRICS (there are reports that other nations are lining up to join). The 11-member grouping now represents a major bloc of energy producers, 45% of global GDP and 50% of the world's population.

In my view, it is too early to announce the end of the petrodollar system, given that the currencies of the UAE and Saudi Arabia are still pegged to the US dollar — they are effectively dollarised. It nevertheless suggests a desire to pivot from the existing system and be less dependent on the US and its currency. For example, the currencies of the UAE and Saudi Arabia also suffered effective devaluations from US dollar printing and reckless spending during the COVID-19 pandemic. Their own large holdings of US Treasuries and other assets are at risk if they suffer Russia's plight by ever incurring US sanctions.

The economic impact of de-dollarisation would be felt in the US in terms of the value of the dollar and potentially in US interest rates. As the issuer of the global reserve currency, the US has never had to worry about its persistent trade deficits as it pays for its imports in the currency it controls and prints — the 'exorbitant privilege' of owning the global reserve currency.

> *"The US has benefited from the dollar being the global reserve currency for the last 70 years. Recent events created concerns that it may be abusing its 'exorbitant privilege.'"*

US trade deficits have been consistently recycled into US bond and equity markets: countries like China, which are net sellers to the US, place those dollars back into the US financial system in the form of central bank reserves, or by investing in US Treasuries. Since 2008, the US has run with ultra-low interest rates as well as massive amounts of money printing — without affecting the dollar's value. However, should the US be forced to run a more balanced trade position, the dollar would need to weaken. Its ability to inflate its way out of its sovereign debt problems may also diminish if global reserve holdings of US dollars are reduced.

What are the alternatives? And what of the proposal of a BRICS currency? As the idea of a BRICS currency gets fleshed out, it seems increasingly clear that the potential exists for the currency to work, but only if it is backed by gold. Russia and China have accumulated large gold reserves since 2010 and have accelerated their purchases in recent years. Gold was effectively the global reserve currency from the time the Bank of England adopted the gold standard in 1821 until the US terminated convertibility of the US dollar to gold in 1971 (Britain left the gold standard in 1931). No countries still use the gold standard today and its role in the financial system has been greatly diminished.

We have been positive on gold bullion and hold it in our portfolios as it has proven to be a reliable store of value and a hedge against geopolitical and systemic risks. We viewed the remonetisation of gold as a small-probability event, but one with a potentially massive effect on the gold price. Should gold be allowed back into the financial and banking system through the BRICS currency, it would provide an alternative to fiat currencies (government-issued currencies not backed by commodities such as gold). There is a strong probability that it would take a meaningful share of global savings, reserves and trade.

Having gold as an alternative available currency would also limit the ability of other countries to run zero — or negative — interest rates and devalue their currencies through money printing, because global savers would instead quickly convert savings to gold-backed currencies. There are many hurdles to the remonetisation and rebanking of gold, but it is one that has moved from a small probability to one that is foreseeable — and even to one that is being planned for. It further cements our view that gold has an important part to play in multi-asset portfolios.

THE FOORD ASIA EX-JAPAN FUND EXPLAINED

Asia offers a diverse matrix of fast-growing, emerging-market investment opportunities — although not without risk. In 2021, Foord Singapore launched the Foord Asia ex-Japan Fund to offer investors bespoke access to this dynamic market. Portfolio manager JC XUE delves into the fund's genesis, strategy and performance.

Given Foord's location in Singapore, Asia is a natural hunting ground for long-term investment opportunities by an investment team that counts in its number five Asian investment professionals, including four Mandarin speakers. Their comprehensive knowledge of this vast market and its companies served as motivation for the fund's genesis.

It is noteworthy that the fund's Asian investment universe excludes Japanese securities. Before China's ascendance, Japan was the second-largest economy in the world. Historically, there was a proliferation of Japanese-specific funds and the idea of 'Asia excluding Japan' was born. Given Japan's slow growth rates, its exclusion from a universe of fast-growing countries still makes sense.

In managing the fund, portfolio managers Ishreth Hassen and JC Xue apply the same philosophy of finding value and managing risk that Foord applies to all its investment strategies. Our focus is investing into quality businesses run by capable management teams with demonstrable track records of capital allocation.

In the two years since the fund's inception, Asian share markets have faced headwinds on worries over China's economic policies, geopolitical positioning and slowing growth. The fund's benchmark — the MSCI All Country Asia ex-Japan Index — has fallen by nearly 23% in this time. The Foord Asia ex-Japan Fund has nevertheless outperformed the benchmark by over 7%.

A pivotal aspect underpinning our success in limiting the drawdowns is the meticulous, granular approach to stock selection. The team's profound understanding of the leading businesses, enriched by in-depth prior research and experience in building the Foord Global Equity Fund portfolio, offered a distinct advantage from the get-go.

Two thirds of the fund is invested in China, compared to its one-third weight in the benchmark. The investment thesis is predicated on rock-bottom valuations compared to Asian peers rather than overarching macroeconomic considerations. Many of the Chinese names in the fund are currently priced for low growth into perpetuity — in contrast, we forecast their recovery and continued structural growth. This is a market dislocation that we are exploiting in the fund.

> *"In the two years since inception, the fund has outperformed the benchmark by over 7%."*

Despite the prevailing macroeconomic headwinds in China and the bear-market sentiment, we remain constructive on the investments we own at these very attractive valuations. We know that bear markets will end and the returns for patient, long-term investors will be material. We don't expect to always run an overweight position to China in this fund — our geographic allocations will invariably be steered by evolving valuation dynamics.

The Foord Asia ex-Japan Fund is approved for distribution in South Africa. Investors interested in the product should understand that it comprises a mix of companies and industries that are quite diverse from those available locally, but whose emerging-market macro fortunes are correlated to South Africa's. So, while we expect that returns from these valuations could be outsized, South African investors should accordingly proceed with caution.

THEMATIC INVESTING

NAVIGATING THE INVESTMENT LANDSCAPE

In the dynamic world of investing, identifying and capitalising on emerging themes can be key to long-term investment success. While change often creates near-term noise, LINDA EEDES writes that it also creates opportunities for patient, forward-thinking investors.

Thematic investing is about recognising secular trends and marrying them with individual investment opportunities. This means understanding how broad market forces will affect future earnings of companies in the investment universe. Over the long term, share prices always respond to rising earnings.

Foord's 'top-down' investment approach allows us to carefully assess risks and opportunities on the investment horizon. We establish thematic parameters that identify sectors or regions offering the potential for superior returns. This is complemented by our 'bottom-up' stock selection process, which populates portfolios with securities that we believe will achieve the best long-term returns for an acceptable level of risk.

The first step in thematic investing is identifying the themes themselves. These can range from sweeping, broad-based trends to more specific, micro-level ideas. But how do we pinpoint them? Foord uses a blend of keen observation and rigorous research. We keep a watchful eye on anything that might significantly affect economic growth, company earnings or global operations. This involves monitoring trends that could reshape entire sectors.

We have written before about global and local themes that have captured our attention. A good South African example was the correct premise that massive government spending on social grants under the Jacob Zuma administration would drive record consumption expenditure to the benefit of the SA retail sector. A current theme is South Africa's growing debt burden and rising risk of a debt crisis. We wrote about this in last quarter's Foreword.

Other global examples include the internet of things, global food security, the rise of the Asian middle class and an ageing first-world demographic driving rising expenditure across the whole health care spectrum. Last quarter, we wrote about our high conviction call on the global energy transition. In this newsletter, JC Xue references the digitalisation theme.

One of the questions that often arises is what the time horizon should be for thematic investments. At Foord, we adopt a pragmatic and flexible perspective. While some themes indeed play out over the long haul, others may offer shorter term opportunities. There is no rigid adherence to timelines. Instead, we prioritise the value and potential of each theme.

While time horizons may differ, timing can be a crucial element in thematic investing. We look for the right entry points — considering many factors such as current company valuations and potential catalysts. Technical analysis also guides our timing decisions. We assess whether a theme has experienced excessive price inflation or if it remains undervalued. However, we recognise that at times the strength of a theme justifies entry at a higher price, given the long-term potential it holds.

Finally, it's essential to acknowledge that not all themes play out as expected. Unforeseen events — such as regulatory changes, market shocks, technological advancements, or economic shifts — can disrupt even the most promising themes. Company-specific issues and changing consumer preferences may also pose challenges, while geopolitical dynamics and market sentiment can also introduce uncertainty into the investment landscape.

MARKETS IN A NUTSHELL

WORLD

SOUTH AFRICA

EQUITIES

Global equities were lower as hawkish major central banks signalled that interest rates would be higher for longer — global emerging markets fell in line while European stocks fell most on translation to the stronger US dollar

The FTSE/JSE Capped All Share Index tracked global bourses lower — led lower by industrial giants Richemont and Naspers/Prosus, as well as by resources shares on generally lower commodity prices

BONDS

Developed market bond yields continued to rise (the US 10-year yield hit its highest level since 2007) with bond markets selling off — as investors anticipate higher rates with the risk of near-term recession moderating

The All Bond Index was little changed for the quarter as the yield curve steepened — bonds with shorter maturities outperformed longer dated bonds

CURRENCIES

US dollar strength persisted with the greenback now advancing in eight of the past 11 quarters — the euro and pound were sharply lower on slower growth while the yen continued its slump

The rand was volatile but ended the quarter little changed against a generally stronger US dollar — the unit remains vulnerable, given SA's lacklustre growth and weakening terms of trade

COMMODITIES

Industrial commodity prices were again lower on expectations for slower growth out of China, while gold and silver were down on the opportunity cost of higher rates for longer — crude oil surged towards $100 a barrel as OPEC+ extended production cuts into next year

ECONOMY

The US and European economies resiliently defied gravity, albeit with challenges in the Eurozone as the German economy contracted — Chinese GDP growth rebounded from a low base, but the World Bank forecasts growth to slow to 4.4% in 2024 amid a continuing property crisis

Second-quarter GDP growth surprised to the upside but was still understandably anaemic — SA's debt and deficit metrics will continue to deteriorate with the SA Reserve Bank forecasting annual growth of just 1.1% by 2025

MONETARY AND FISCAL POLICY

There was hawkish rhetoric but no rate changes by the leading central banks — meanwhile the US lost another triple-A credit rating and again narrowly temporarily escaped a government shut down

The SARB held rates unchanged despite strong advocacy amongst its ranks for a rate hike — the governor urged more fiscal restraint as the SA Revenue Service warned of lower receipts

FEZEKA PROGRAMME FOR GENDER DIVERSITY IN ASSET MANAGEMENT

BRENDAN AFRICA
Financial Director

The Fezeka Graduate Programme is a graduate readiness programme for black women looking to enter the asset management industry. Foord has partnered with a select group of investment firms to deliver this exciting initiative. Director BRENDAN AFRICA takes a closer look at the programme.

The Fezeka programme aims to provide structured development opportunities to high-achieving, black women graduates wanting to build careers in investment management. The programme combines theoretical knowledge, professional development and practical work experience within established investment management firms committed to growing the talent pool.

Incepted in 2022, the programme is hosted and administered by the ASISA Academy — the educational arm of the Association for Savings and Investment South Africa (ASISA). The Academy is also responsible for the theoretical knowledge component through delivery of the Financial Markets Practitioner qualification.

Structured as an intensive 15-month internship, the programme goes beyond theoretical knowledge and classroom learning. It is designed to produce industry-ready professionals who can hit the ground running. Continuous assessment, coaching and mentoring are fundamental tenets of the programme to ensure a high standard of professional development and skills transfer.

Participants rotate between three different investment firms over the term of the internship. This ensures a breadth of exposure, delivering comprehensive on-the-job training in various aspects of the investment management function. Participants receive exposure to investment research and security evaluation, market trading, risk assessment, regulatory compliance, portfolio administration and client reporting. They also gain insight into cutting-edge technology and industry best practices.

With its proud track record of gender inclusivity and support for educational development, Foord jumped at the chance to participate in this groundbreaking initiative. In July, we welcomed Mikano Mashiti into our team. Mikano is a Chemical Engineering graduate participating in the inaugural Fezeka programme.

The Fezeka Programme is a visionary initiative with a clear purpose to empower women graduates to excel in the financial services industry. The programme bridges the skills gap, fosters diversity, builds industry-ready professionals, creates a diversified talent pipeline, and promotes ethical business practices. It is a testament to the industry's commitment to investing in the future and nurturing the next generation of women leaders in finance.

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