



"With us the **safest**  
distance between  
**two** points is also  
the **smoothest**"

# Smoothed Bonus Report

Second Quarter 2023

**momentum**  
corporate





# Reviewing the last quarter

Dear valued investors

Geopolitics has exerted significant influence on the global economic landscape in recent years, thus impacting a wide range of stakeholders. Notable developments include the ongoing conflict between Russia and Ukraine, the persistent tensions between the United States and China, and the current efforts of the European Union to mitigate its dependence on China by reducing risks. In July 2022, a bilateral agreement was reached between the United Nations, Turkey, and Russia, facilitating the exportation of grain from Ukraine through the Black Sea region. One year later, Russia has subsequently withdrawn from the agreement, posing a renewed risk of a worldwide food crisis and an escalation in food prices.

In global markets, investment returns increased notably in the second quarter compared to the first quarter. The MSCI All Country World Index, with a return of 13.1%, demonstrated that this upward trend was evident across various sectors. In both the first and second quarters of the year, developed market equities have surpassed emerging market (EM) equities. The MSCI World Index (Developed Markets) experienced an investment return of 13.8% during the quarter, primarily due to the strong performance in United States stock markets. In contrast, the MSCI Emerging Markets Index lagged with an investment return of 8% during the quarter.

After experiencing relatively underwhelming performance in the South African equity market over the past five-year period, the year ended 30 June 2023 witnessed a notable increase in returns. The FTSE JSE All-Share index (ALSI) provided a return of 19.58% for the year. Despite facing challenges in the first quarter of 2023 with a return of 0.66%, the investment performance in the second quarter improved with a return of 1.35%. When examining shares held within the local equity market, the FTSE JSE Capped Shareholder Weighted Index (Capped SWIX) returned 1.16% over the quarter. Furthermore, it achieved a notable performance in June 2023 with a return of 3.84%. The primary factors influencing the returns during the previous quarter were the financial sector, which experienced a positive return of 5.27%, the industrial sector, which saw a return of 3.40%, and the resources sector, with a return of -6.09%.

The South African rand continued to weaken relative to the United States dollar (USD). During the first quarter of 2023, there was a depreciation of 4.67% relative to the USD. Subsequently, in the second quarter, it weakened further with 6.48%. In May 2023, the South African Reserve Bank (SARB) raised the primary lending rate by 0.50 percentage points to reach a level of 8.25%.



This action was taken in response to escalating inflationary pressures. In June 2023, the rate of headline inflation experienced a greater decline than anticipated, primarily due to reduced food expenses, resulting in a figure of 5.4%. As a result, the inflation rate is now within the desired range of 3% to 6% set by the SARB. The prevalence of rolling blackouts persists as Eskom continues to grapple with generation capacity issues, thereby exerting a detrimental impact on economic growth.

Herman van Papendorp and Sanisha Packirisamy, members of the macro research team at Momentum Investments, provide additional analysis and insights on the market and economic landscape in their publication located on page 6.

## Momentum Corporate expanded the smoothed bonus offering

The South African equity market underperformed over the last six months relative to global equity markets. We are looking to enhance our offshore exposure in several of our portfolios, but we are not in a rush due to perceived rand weakness and underpriced local shares. Most of our smoothed bonus portfolios are fully funded, which means that if the third-quarter returns are as strong as expected, bonus rates will remain healthy.

The presence of volatility is a common characteristic in markets, but there has been a notable rise in volatility in recent years, with expectations for this trend to persist. This is where our smoothed bonus portfolios shine, as they produce a consistent bonus rate pattern with significantly fewer fluctuations than investors would otherwise see. The option of capital guarantees in the Momentum Corporate smoothed bonus range enhances the level of reassurance for investors.

We recently launched the Universal Fifty Smooth Return Fund (UFSRF). The UFSRF is a smoothed bonus portfolio targeting a return of CPI +4.5% after fees, where the focus is more on the smoothing of returns than the investment guarantees. This provides the investor with a cost-effective smoother investment journey and complements our smoothed bonus offering.

We are excited about the opportunity to navigate through these challenging market conditions and steer your members towards achieving financial success.

Warm regards

## Steed Duncan-Smith

Client Relationship Manager  
Momentum Corporate





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A focus on preservation  
of retirement savings

# A perspective on investment choices in the two-pot retirement system



## Introduction

The proposed two-pot retirement system aims to improve the preservation of retirement savings, taking into consideration the financial challenges faced by members of retirement funds. Unlike the current practice where members have full access to their retirement savings when changing jobs or experiencing job loss, this system allows for limited access to money while they are still working for their employer. By implementing this system, a larger portion of members of retirement funds are expected to build the necessary savings for their retirement.

**Ryan Olivier**

Product Specialist  
Structured Solutions

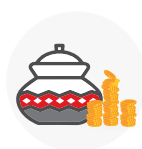
### Under the two-pot system, retirement savings will consist of these three components:



**Savings component:** will consist of one-third of retirement contributions from 1 March 2024, as well as an amount transferred from the vested component on 1 March 2024. Members will be allowed to withdraw money from the savings component on 1 March 2024 and thereafter once in a tax year.



**Retirement component:** The remaining two-thirds of the retirement contributions from 1 March 2024 will be allocated to this component and cannot be accessed before the age of 55. The retirement savings in this component must be used to buy an annuity unless the accumulated amount falls below the prescribed threshold.



**Vested component:** will consist of a member's retirement savings on 29 February 2024 except for the amount transferred to the savings component, and will continue to operate under the current retirement framework. No further contributions will be made to this component after the implementation of the two-pot retirement system.





For more detailed information on the upcoming two-pot system, please refer to our Q1 2023 Quarterly Report, which includes an article on page 4.

While the two-pot retirement system is designed to improve the preservation of retirement savings by restricting members' access to it when changing jobs, they must understand the consequences of withdrawing money from the savings component before retirement.

## The impact of pre-retirement withdrawals

Retirement fund members must balance their long-term goals against their short-term needs and tolerance for market volatility. In this section, we will look at an example showing the impact of withdrawing money from the savings component and how this will affect a member's standard of living during retirement.

The net replacement ratio, which calculates the income in the year following retirement divided by the salary in the year before retirement, is the industry standard for measuring the standard of living in retirement. A ratio of 75% is typically considered sufficient to maintain a similar standard of living during retirement.

Consider Jared, who starts saving for retirement at 25, earning a monthly salary of R20 000. He plans to retire at 65. Assuming his salary grows by 6,5% annually, assuming an inflation rate of 5%, his income increases by 1.5% in real terms each year. Jared contributes 15% of his gross salary towards his retirement savings. For his retirement savings, Jared chooses to invest in a growth portfolio with a real return of 4% per annum after fees. When he retires, Jared plans to buy an inflation-linked annuity.

After 10 years of contributing to his pension fund, the two-pot system is introduced. Jared now needs to decide how he will invest the money in his savings component. He can either continue investing in the growth portfolio or choose a more stable money market portfolio, which serves as a safety net for unexpected financial needs. The money market portfolio generates a real return of 1% per annum after fees.

## Consider the following scenarios:

- **Scenario 1:** Jared decides to continue to invest the money in his savings component in the same growth portfolio as before and refrains from withdrawing from his savings component before retirement. By maintaining this strategy, he stays invested in a growth portfolio until he retires. At retirement, Jared can buy an inflation-linked annuity, resulting in a replacement ratio of 80%.
- **Scenario 2:** Jared decides to invest the money in his savings component in a money market portfolio, serving as a safeguard for unexpected financial needs. Fortunately, Jared doesn't have a situation that results in him having to withdraw money from his savings component. On retirement, Jared can buy an inflation-linked annuity, resulting in a replacement ratio of 73%.
- **Scenario 3:** Jared decides to invest the money in his savings component in a money market portfolio and starts withdrawing money from his savings component as soon as they become available. On retirement, Jared can buy an inflation-linked annuity, resulting in a replacement ratio of 62%.

By investing the money in his savings component in a money market portfolio, Jared can buy an inflation-linked annuity that will result in a replacement ratio of 73% at retirement. This ratio is 7% lower than if he had invested his money into a growth portfolio, highlighting the long-term impact of having less exposure to growth assets. If Jared decides to withdraw money from his savings component before retirement, the situation worsens, resulting in a replacement ratio that is 18% lower compared to what he could have achieved by staying invested for the long term and benefiting from exposure to growth assets.

These scenarios demonstrate how Jared's retirement outcomes can significantly vary based on his investment portfolio choices throughout his career.

## In closing

The introduction of the two-pot retirement system presents a significant reform to improve the preservation of retirement savings. But, retirement fund members must understand the implications of the decisions they make about their savings component.

We want to highlight the importance of members making well-informed investment decisions and the consequences of adopting a short-term perspective and prematurely withdrawing money from their savings component. By considering these factors, members can make more informed choices and strive for financial security in their retirement planning.



# Momentum Investments market commentary for the quarter ended June 2023

by Sanisha Packirisamy and  
Herman van Papendorp

## Highlights

### Markets

The main global themes driving the outlook for financial markets in the next year

- In our view, the potential for a United States (US) recession and the evolution of the US policy rate cycle will be the main global themes driving the outlook for financial markets in the next year and are paramount for portfolio positioning.
- We think the outcome of the recession theme will determine whether there is substantial downside risk for global equities from here. The US equity market seems to currently not expect a recession.
- We don't only think it makes sense to favour an allocation to US bonds as a portfolio hedge against recession risk, but also because US bonds look attractive from both a rate cycle perspective and a relative valuation angle.
- Our preference to take a more defensive stance in our portfolios, makes us cautious about exposure to the global property asset class in the interim.

### Factors driving South African equities and bonds

- South African (SA) equities still trade at huge valuation discounts to the rest of the world and its history. Although the SA equity market will likely also suffer during any global equity drawdowns in risk-off periods, it could perform relatively better in subsequent risk-on recoveries due to its positive valuation underpin.
- SA real bond yields are attractive against their history, as well as relative to those in global markets, with part of the high real yield differential due to a fiscal and country risk premium. We expect falling inflation in the coming year to become less supportive of inflation-linked bonds (ILBs). The prospective SA real cash yield has been rising from a low level in line with policy rate increases and now expected falling inflation and is currently cheap versus history.
- Although SA listed property companies are experiencing improving operational performance (in terms of vacancy rates, net operating income and property values), financial conditions have deteriorated (e.g. loan-to-value, interest cover and the cost of debt).
- There is always a strategic rationale for gold as a portfolio risk diversifier, as it is expected to hold its value through turbulent times and has limited correlation with other asset classes. Historically, the rand gold price has been a strong relative asset class performer for a SA investor.



## Economics

- With central banks stating their hesitancy to lower interest rates until clear signs of inflation decline and a sustainable improvement in underlying inflation are evident, a tighter monetary policy stance could worsen growth challenges in the global economy and heighten the risks of a more severe downturn.
- While financial strains have historically followed periods of rapid interest rate hikes, the recent turmoil in the smaller, regional banking sector in the US does not necessarily indicate a precursor to systemic stress. In our view, it instead reflects isolated challenges arising from tighter financial conditions.
- Prospects for more robust Chinese growth have once again weakened. Factors such as declining global export activity, subdued consumer sentiment, an uneven housing market recovery and elevated youth unemployment suggest that China's growth outperformance compared to the government's official target of 5% may be more limited than initially thought.
- The global circumstances present a significant challenge for SA's economic growth, especially when combined with local obstacles such as subdued business and consumer confidence, severe constraints in network industries and ongoing political uncertainty.
- The primary risk to SA's growth is the prevailing power predicament, which is expected to keep growth flat this year. However, an improvement in energy supply is anticipated to boost growth to 1% in 2024 and 1.6% in 2025.
- The feasibility of reducing the budget deficit to 3.9% during the fiscal year 2023/24, as anticipated by Treasury, is cast into doubt due to mounting social obligations, an overrun in civil servant wages and burdensome debt-servicing obligations.
- Despite expectations for headline inflation to dip below 6% in the latter half of this year, we expect another 25-basis point interest rate hike at the July rate-setting meeting, to a peak of 8.5%. Looser fiscal policy adds to the burden of SA's monetary policy authorities and as such, interest rates could be kept tighter for longer.

## First half equity market rally defies interest rate increases and risk of recession

The potential for a US debt default captured headlines in the first two months of the quarter. A bipartisan agreement was reached just a few days into June 2023. The agreement did not impose a major tightening in fiscal policy, which financial markets deemed positive for growth. The outcome removed a significant amount of uncertainty from markets, resulting in Wall Street's fear gauge (the CBOE Volatility Index or VIX) falling to its lowest level since pre-pandemic levels. The VIX ended the quarter at 13.5 points, significantly off the highs of 33.6 experienced in October last year.

With major central banks still tightening monetary policy leading to higher levels of macroeconomic and policy uncertainty, the Merrill Lynch Option Volatility Estimate (MOVE), which captures a yield curve-weighted index of the normalised implied volatility on one-month Treasury options, remained historically high (ending the quarter at 111 points), after hitting a peak of 198 in March 2023. Despite this retreat, the MOVE index is still 11 points up since the end of last year.

According to News24, there have been 90 interest rate hikes so far this year, relative to only 17 cuts. Interest rates have been hiked by a cumulative 500 basis points in the US and 400 basis points in the Eurozone since the start of 2022, while interest rates have climbed nearly 500 basis points in the United Kingdom since the start of the interest rate hiking cycle in December 2021.

After falling from an earlier peak of US\$30 470 in mid-April to US\$24 928 in mid-June, the Bitcoin price recovered to its highest level in a year. CNBC attributes the jump in price to BlackRock's application for the first-ever spot bitcoin exchange-traded fund in the US.

Weak high-frequency data highlighting a faltering economic recovery in China led global commodity prices lower. The Bloomberg Commodity Price Index (the four largest weights in this index include gold at 15%, WTI Crude oil at 8%, natural gas at 8% and Brent Crude oil at 7%) sank 3.4% in the second quarter and tracked 7.7% weaker on a year-to-date basis.



Large year-to-date price declines were observed in energy-related commodities, including natural gas and crude oil. The international price of Brent crude oil is nearly 13% lower since the end of 2022, with natural gas prices between 40% and 50% lower over the same period. Within metals, prices of iron ore and gold were higher year to date, while the prices of nickel, steel and aluminium dropped the most. The dollar price of gold tracked 2.8% weaker during the second quarter in line with a pause in interest rates by the US Federal Reserve (Fed) but was still up 4.9% on a year-to-date basis.

Meanwhile, the dollar price of platinum and palladium dropped by 16.4% and 30.2% (respectively) year to date and 9.7% and 14.5% (respectively) during the second quarter. Within agricultural commodities, the biggest gainers were cattle and sugar in the second quarter, while the biggest price declines were evident for wheat and corn, driving expectations for a further decline in global inflation.

It was a quarter of two halves for global equities. The MSCI All Country World Index tracked broadly sideways until June, rising in the last weeks of the quarter. Global equities ended the quarter a firm 5.1% in the black (12.8% year to date) and were mainly driven by the performance in developed markets (DM). Big gains were seen in technology-driven stocks in particular.

The MSCI DM Index advanced 5.6% in the second quarter, supported by robust gains in the Japanese equity market. Within the DM composite, US equities increased by 7.4% over the quarter and 15.5% year to date, primarily on the back of strong year-to-date gains in information technology, telecommunications, and consumer discretionary stocks, while energy, utilities, healthcare, and financial stocks dipped since the start of the year.

The Eurostoxx 50 Index lagged the performance in US and Japanese markets but still managed to end the quarter 4.2% higher (8.4% higher for the first half of the year) despite bank failures and the European Central Bank (ECB) continuing to tighten monetary policy.

During May, the Japanese Nikkei 225 Index hit a 33-year high following foreign equity inflows after a three-year hiatus. The New York Times attributes this stellar performance to a return in inflation, a rise in consumer spending, a return of foreign tourists and a change in boardroom attitudes for Japanese corporates. The

Nikkei 225 Index jumped 18.5% in the second quarter and 28.7% in the first half of the year.

The performance in emerging market (EM) stocks was more muted. The MSCI EM Index edged up 0.6% in the second quarter, with divergent performance across the contributing indices. Equity markets in Latin America shot up 13.7% in the second quarter, while Asian stocks shed 1.1% considering deteriorating economic data out of China. With officials failing to unveil major stimulus measures outside of small interest rate cuts, the performance of equities has remained muted. Meanwhile, equity markets in Europe, Middle East, and Africa (EMEA) inched up 2.5% in the quarter.

Government bond yields rose further into the second quarter of the year. The yield on the US 10-year government bond picked up 36 basis points to 3.8% over this period, while the German 10-year government bond yield climbed 12 basis points to end June at 2.4%. While the Fed's dot plot - a chart that records each Fed official's projection for the central bank's key short-term interest rate - suggests two more interest rate hikes in the US, markets are pricing in one more increase of 25 basis points in July, with a 30% chance of another before November. Markets have also reduced the number of interest rate cuts they are expecting next year. Meanwhile, in the Eurozone, markets are pricing in two more hikes by the ECB.

As the yields on shorter maturities have risen, yield curve inversion has deepened, signalling the risk of a recession as previous interest rate tightening starts to bite.

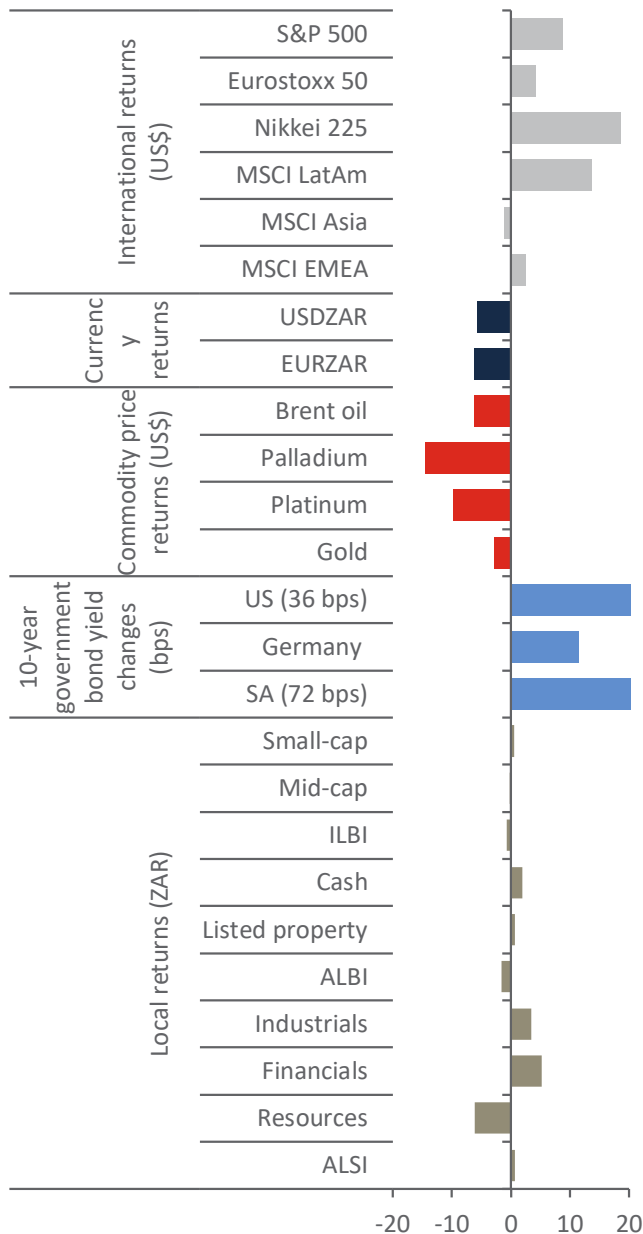
Mimicking lower risk aversion in equity markets, the JP Morgan EM Bond Index (EMBI) spread dipped nine points and ended the quarter at 364 points. Chile and Peru experienced the largest quarterly narrowing in credit default swap (CDS) spreads of 31 points and 29 points, respectively, in the second quarter of the year, while spreads widened the most for Thailand (6 points).

The local equity market lagged its global counterparts and shifted 0.7% higher in the quarter and ended the first half of the year 4.3% firmer. Gains in financial and industrial shares in the quarter were wiped out by losses in resource shares. The FTSE/JSE Resources Index sank 6.1% in the second quarter in line with weaker commodity prices. In contrast, the FTSE/JSE Financials Index gained 5.3% and the FTSE/JSE Industrials Index eked out an increase of 3.4% in the quarter.



The FTSE/JSE Mid-cap index ended the quarter 0.2% lower while small-cap equities experienced mild gains of 0.5%.

**Chart 1: Quarterly asset class returns (%)**



In SA's fixed income markets, the 10-year government bond yield sold off 73 basis points in the quarter, after touching an intra-quarter high of 12.1%. The JSE Assa All Bond Index declined 1.5% for the quarter, with the JSE Assa Government ILB Index dropping by 0.7% in the corresponding period. The FTSE/JSE SA Listed Property Index crept 0.7% higher in the second quarter of the year.

It was a mixed bag for EM currencies during the second quarter. Prior to the Turkish elections, the central bank intervened in the currency markets. However, with limited intervention since, the Turkish lira sold off 15.6% against the US dollar in the quarter. The Russian rouble plunged 9.2% over the same period driven weaker by domestic political concerns late in the quarter. The Argentine peso and Colombian peso had the best performance in the quarter from a basket of major EM currencies, strengthening by 17.6% and 14.7%, respectively.

The rand weakened by 3.6% against the US dollar in the second quarter of the year, strengthening towards the end of the quarter as loadshedding lessened on a higher energy availability factor and reduced demand on Eskom supply. Year to date, the rand was the third weakest performing currency against the US dollar after the Russian rouble (8.6%) and Turkish lira (12%).

During the second quarter, the rand weakened by 6.2% against the euro and 8.3% against the British pound.

In line with a retracement in the SA 10-year government bond yield and the currency, SA's ten-year CDS spread narrowed by seven points in the quarter to 360 but remained five points higher since the end of 2022.

Source: Iress, Momentum Investments

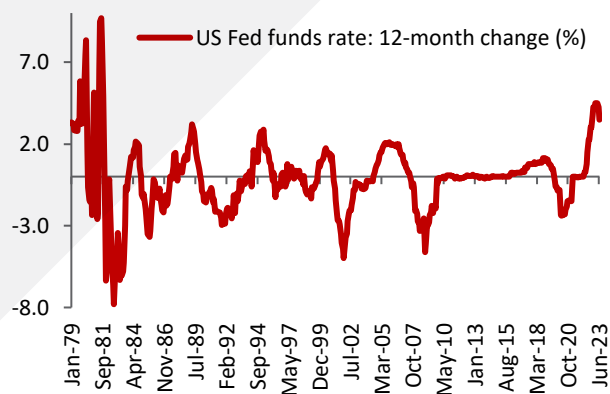
Chart truncated for US and SA 10-year bond yields

# Possibility for US recession and the US policy rate cycle paramount for portfolio positioning

In our view, the outcome of the US recession theme will determine whether there is substantial downside risk for global equities from here. Although the debate about the probability for a US recession has been ongoing since the latter part of last year, the jury is still out on whether we'll see a US recession in the coming quarters, or whether a recession can be avoided altogether. Although we think the balance of evidence currently points to a better-than-even chance that we will see a US recession either later this year or in the early part of next year, there is still a significant possibility that a recession might not happen. We think four main indicators currently point to a meaningful probability for a US recession.

The first is the monetary transmission lag. Since the US central bank started its hiking cycle in March last year, policy rates have increased more over the last 12 months than at any time since 1981 (see chart 2). If policy works with a 12-18-month lag as it typically does, the full effect of all this tightening on the US economy is still very much to come, even if rates are now approaching their peaks. And since the starting point for interest rates was close to zero, one can argue that the rate hikes in the latter part of the hiking cycle could be disproportionately more detrimental for consumers and businesses than increases earlier in the cycle. The risk is that the mounting cumulative impact of the sequential rate increases later in the rising rate cycle could retrospectively turn out to have been the proverbial straw that broke the US economy's back.

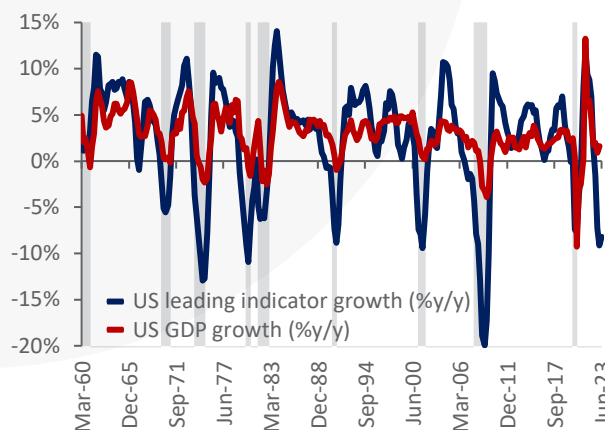
**Chart 2: Sharpest 12-month rise in US policy rates since 1981**



Source: Iress, Momentum Investments

The US leading economic indicator (LEI) provides the second warning sign for possible US recession. Momentum in this composite indicator, which includes 10 variables across the US manufacturing sector, labour market, housing sector, the equity, credit, and rate markets, as well as consumer sentiment, has gone significantly negative (see chart 3). Never before, across 60 years of history, has the LEI momentum been this negative without a recession following.

**Chart 3: Never before has US LEI momentum been this negative without recession following**

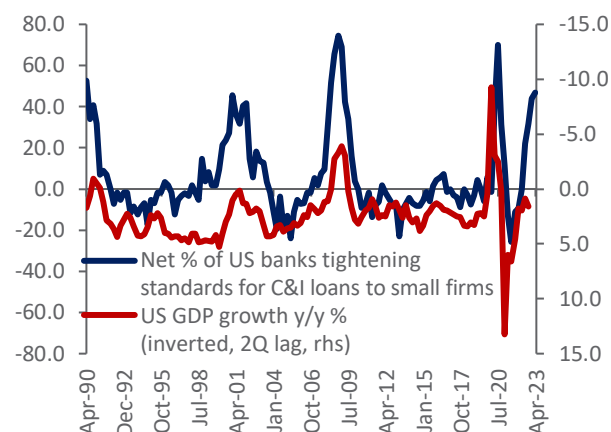


Source: Iress, Momentum Investments

A third potential signal for an oncoming US recession is the significant tightening in lending standards undertaken by US banks since late 2022 (see chart 4).

Banks' lending criteria were loose in the aftermath of the pandemic of 2020, but as banks became worried towards the back end of 2022 that consumers and businesses were coming under strain from higher interest rates, they started tightening lending conditions. Limiting the availability of finance for the US corporate sector, increases the risk of a sharp slowdown in US economic activity, or even recession, in the quarters ahead, as lending criteria have typically led US GDP growth by around two quarters.

**Chart 4: Tighter US bank lending criteria increases the risk for recession**



Source: Federal Reserve Bank of St. Louis, Iress, Momentum Investments

Fourthly, a three-month/10-year US yield curve inversion has been an infallible recession indicator historically, never giving a false signal (see table 1). Whenever this part of the yield curve inverted in the past, we have always seen a US recession following somewhere between five months and 16 months after inversion. This time, the yield curve inverted in October last year. If history is any guide, one should thus expect a US recession anytime between March 2023 and February 2024. On average, the recession started 10 months after curve inversion, which would imply the US recession to start in August of this year.

**Table 1: Yield curve inversion was historically an infallible US recession indicator**

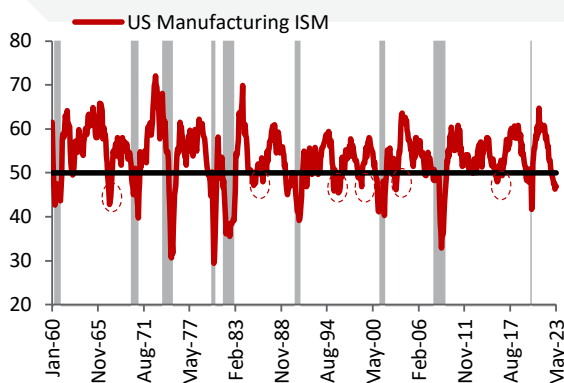
US 3-month/ 10-year yield curve inversion date	US recession start date	Lead (months)
Dec-68	Dec-69	11
Jun-73	Nov-73	5
Nov-78	Jan-80	14
Oct-80	Jul-81	8
Jun-89	Jul-90	13
Jun-00	Mar-01	7
Aug-06	Dec-07	16
Jul-19	Feb-20	7
<b>Average</b>		<b>10</b>
<b>Median</b>		<b>10</b>

Source: Credit Suisse

One indicator that has often given false signals about the US recession in the past has been the US manufacturing Purchasing Managers' Index (ISM). As a diffusion index, whenever this falls below the 50 level, it is indicative of a looming contraction in US manufacturing activity. As this indicator has been below the 50 level since November last year, it is often referenced as pointing to a forthcoming US recession (see chart 5). However, since this indicator is only reflective of the shrinking US manufacturing sector that now constitutes just slightly more than 10% of the economy, it is unsurprising that it has given so many false recession signals in the past and as such is not a trustworthy recession indicator.

**Chart 5: US PMI an unreliable recession indicator**

Note: Shaded areas depict official US recessions



Source: Iress, Momentum Investments

It is possible that this time could be different and the seeming infallible recession indicators such as the US LEI and the inverted yield curve could be wrong for the first time, but one would be betting heavily against history if you make such an assumption. As responsible custodians of our clients' money, we think it is more prudent to assume that there is a significant probability that there could be a US recession and that this should be reflected in portfolio positioning. History has shown that whenever there was a US recession, it was also associated with significant drawdowns in the US equity market. Indeed, as table 2 indicates, the US equity market has never bottomed before a recession started, but always only after it began. If we thus do get a recession this time, it seems likely that the US equity market hasn't reached its bottom yet.

**Table 2: US equities always only bottom after the start of a recession**

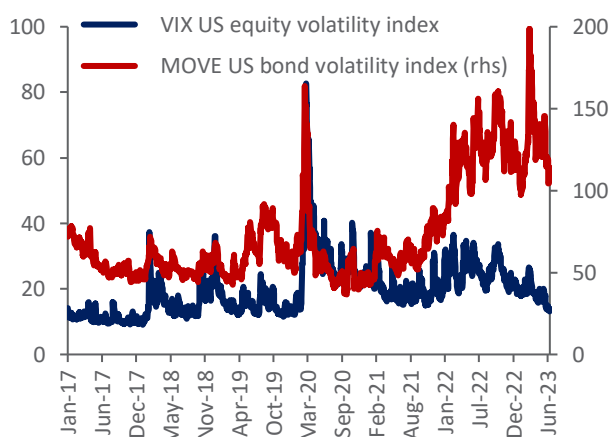
US recession start date	US equity market through date	Difference (months)
Apr-60	Oct-60	6
Dec-69	May-70	5
Nov-73	Oct-74	10
Jan-80	Aug-82	31
Jul-90	Oct-90	2
Mar-01	Oct-02	19
Dec-07	Mar-09	14
Feb-20	Mar-20	1
<b>Average</b>		<b>11</b>
<b>Median</b>		<b>8</b>

Source: Credit Suisse

For future asset class performance, it also matters whether markets are already discounting a recession or not. In our view, two factors seem to indicate that the US equity market is currently not expecting a recession.

Firstly, from analysing, the so-called fear gauges for the US equity and bond markets (see chart 6), it is surprising that the VIX is currently indicative of the lowest equity volatility since pre-COVID at a time that there are huge uncertainties about US growth, inflation, and policy rates. Contrast that with the current MOVE Index that has settled at an elevated level versus the pre-COVID era. It thus seems that the US equity market is much more complacent than the bond market about the economic outlook.

**Chart 6: US equity market seems complacent about risks**



Source: Bloomberg, Momentum Investments

Secondly, expectations for US corporate profits also don't seem to be reflecting a recession scenario. Table 3 shows that in the previous seven recessions, the average and median peak-to-trough declines in earnings were 24% and 18%, respectively.

The consensus expectation is for a 5% peak-to-through earnings decline this time, well short of the historical recession experience and pointing to likely sharp profit downgrades should a recession materialise.

**Table 3: US profit expectation not reflecting a recession scenario**

US recession	US EPS peak	US EPS trough	%Δ EPS
1974	9.4	7.7	-18%
1983	15.3	12.5	-18%
1986	16.9	14.4	-15%
1990	26	15	-42%
2001	56	41	-27%
2008	94	62	-34%
2020	167	140	-16%
<b>Average</b>			<b>-24%</b>
<b>Median</b>			<b>-18%</b>

Source: Bank of America

In our view, one thus has to be somewhat circumspect about equity markets and portfolio positioning when the balance of probabilities is pointing to a meaningful chance of a US recession at a time that the equity market doesn't seem to attach a high probability to this. We therefore need to protect portfolios against the potential downside risk for the US and global equity markets in case of a US recession, as global equities could still go down significantly from current levels in such a scenario. In our view, it thus makes sense to favour exposure to US bonds, gold and alternative assets like infrastructure as portfolio hedges against potential downside global equity risk.

Of course, if a recession is avoided, the downside momentum in the US economy would be contained and the equity market could chug along, even if returns could be unexciting at times. In the absence of recession, portfolios would not have to be positioned as defensively to limit downside risks and exposure to growth assets would feature more prominently in overall asset allocation.

We don't only think it makes sense to favour an allocation to US bonds as a portfolio hedge against recession risk, but also because US bonds look attractive from both a rate cycle perspective and a relative valuation angle.

It currently looks likely that we will soon see the peak in US policy rates as inflation declines to levels the US central bank would be more comfortable with. How did US equities perform around past rate peaks? Table 4 shows that over the past half a century or so, it depended on whether inflation was high or low at the time of the rate peak. US equity returns were only high after past rate peaks when inflation was low. Whenever inflation was high, like now, the subsequent US equity performance after the rate peak was poor. This makes sense because when inflation is high, one doesn't see a pivot to rate cuts very soon after the peak in interest rates. Therefore, if inflation remains at high levels for the next six to 12 months, we won't see the Fed cutting rates and equities could perform poorly. However, if inflation drifts down closer to the Fed's implicit target, then we might see the first cut early next year, with positive ramifications for equities leading up to this. Again, this calls for circumspection about US equity market returns around the rate peak this time in a high inflation environment.

**Table 4: US stock market returns post past rate peaks**

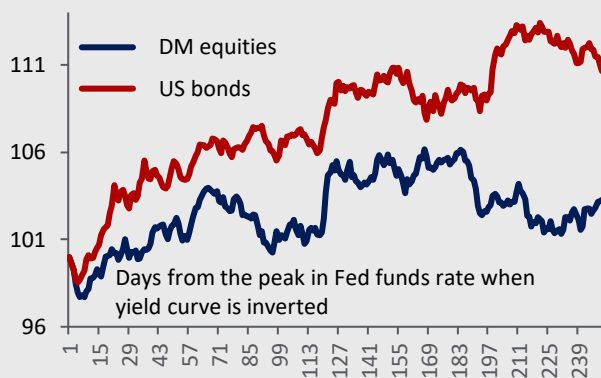
US equity returns post peak front-end interest rates				
Peak rate year	Elevated inflation?	3-month return	6-month return	12-month return
1969	Yes	-4.6%	-18.4%	-7.0%
1973	Yes	-8.0%	-7.7%	-30.8%
1981	Yes	-7.4%	-4.7%	-15.6%
1989	No	7.8%	18.4%	15.3%
2000	No	6.8%	-7.4%	-11.6%
2006	No	7.9%	12.7%	14.0%
2018	No	0.9%	-0.3%	13.8%
<b>Average: Inflation elevated</b>		<b>-6.7%</b>	<b>-10.3%</b>	<b>-17.8%</b>
<b>Average: Inflation not elevated</b>		<b>5.9%</b>	<b>5.9%</b>	<b>7.9%</b>

Source: Morgan Stanley



Chart 7 shows that US bonds historically strongly outperformed DM equities in the year following the peak in US policy rates during cycles when the yield curve was inverted, as is now the case. The maximum outperformance was as much as 11.5% in the subsequent year. This implies that one would normally want to favour bonds over equities in the year after US rates peak when the yield curve is inverted.

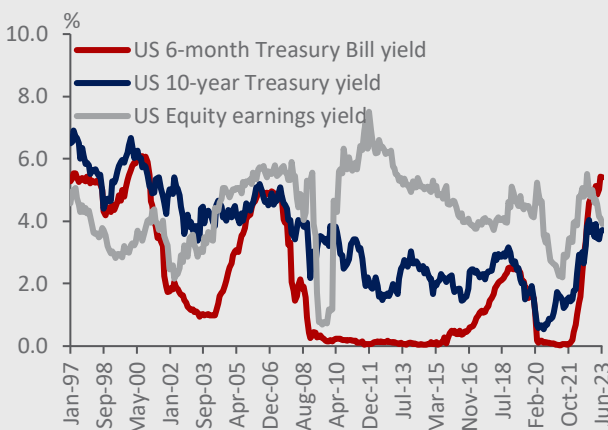
**Chart 7: Bonds outperform equities post the last Fed hike if the yield curve is inverted**



Source: Morgan Stanley

Furthermore, sharp global policy rate rises in 2022-23 have caused the largest increase in US cash and bond yields in 40 years. As a result, US fixed-income assets have again become viable income-providing alternatives to equities (see chart 8). The last time this was the case was in 2007 before the onset of the global financial crisis (GFC). This means that investors can nowadays again get investment income from fixed income assets as it's normally supposed to be, whereas for more than a decade after the GFC, cash and bond yields were so close to zero that investors' only income alternative was to explore the equity asset class for better income from dividends.

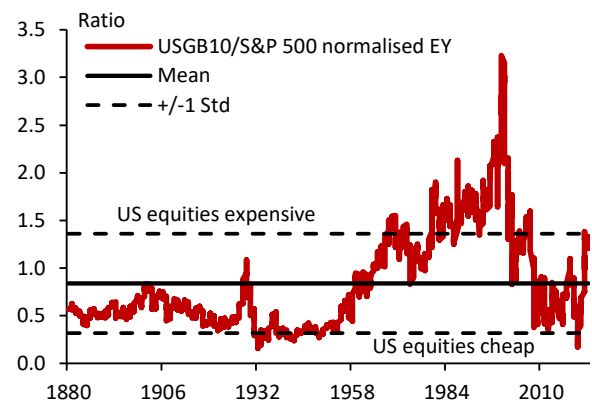
**Chart 8: US cash and bonds now provide attractive relative income**



Source: Iress, Momentum Investments

Finally, after the sharp rise in bond yields and the strong equity performance in recent years, US bonds are now attractively valued relative to US equities (see chart 9). Comparing the current US bond yield to the through-the-cycle equity earnings yield, equities are now almost one standard deviation expensive relative to bonds against history. This was not the case for a long time since the GFC, when equities were consistently cheap versus bonds.

**Chart 9: US bonds now cheap versus equities**



Source: Iress, Momentum Investments

US real estate investment trust (REIT) occupancy rates remain high outside the Office sector and US balance sheets have strengthened since the GFC with lower leverage and a longer maturity profile. However, elevated Office sector leverage could exacerbate near-term operating challenges and lead to dividend cuts and asset sales.

Although REIT sensitivity to interest rates has declined since the GFC with more fixed-rate debt at lower interest rates, there is a risk for more distressed sales due to higher debt levels associated with the rapid rise in interest rates and banks tightening lending standards.

Global property currently looks expensive versus some fixed income asset classes like US Treasuries and global investment grade bonds, fair value against US Treasury inflation-protected securities (TIPS), but cheap against equities.

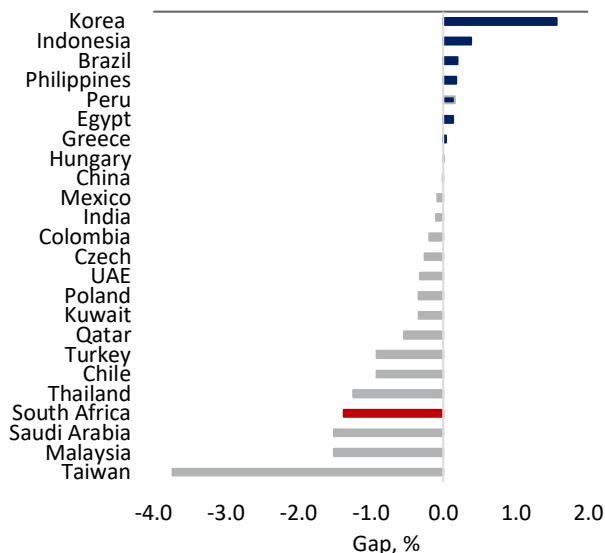
In aggregate, our preference to take a more defensive stance in our portfolios against the backdrop of lingering US recession risks and uncertainties about the path for global inflation and policy rates, makes us cautious about exposure to the global property asset class in the interim.

For SA investors, we prefer SA asset classes over global assets in the next year. Firstly, our expectation for some rand appreciation as global risk appetite improves later this year in anticipation of future policy rate declines, would erode the local currency returns from global assets. Furthermore, SA assets are supported by more attractive valuations than global assets and discount significant amounts of bad news.

# Valuation is the main support for future SA equity market returns

SA equities continue to be attractively valued relative to global equities, as well as against its history. This should provide some support in case of potential global equity drawdowns, but more so during subsequent risk-on recoveries when global risk appetite increases. SA equity valuations remain cheap against EM (and even more so against DM), with SA a superior dividend payer within EM and at a large forward P/E discount to EM (see chart 10). Only in the period between the 1998 EM crisis and the 2000 dot-com collapse did SA equities trade at a larger forward P/E discount versus EM than the current more than one standard deviation discount.

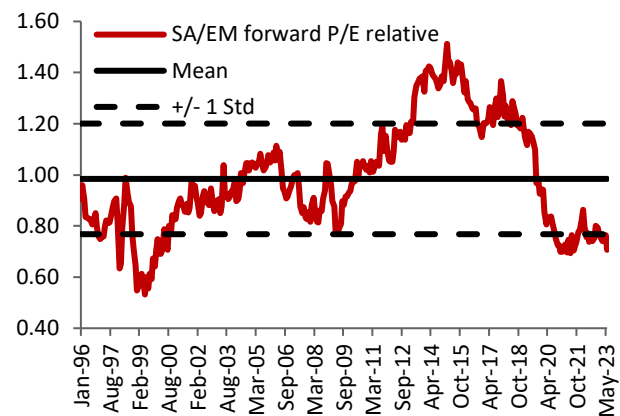
**Chart 10: SA forward P/E relative to EM**



Source: SBG Securities

Furthermore, SA is the fourth most underowned market within global EM (GEM) equity funds (see chart 11), and as such, should have meaningful rerating potential from current cheap valuations when global risk appetite improves.

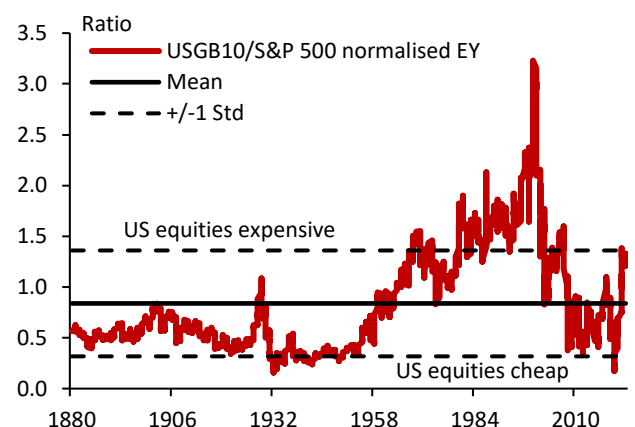
**Chart 11: GEM funds' % allocations to EM countries versus benchmark**



Source: SBG Securities

Even assuming a conservative 9% earnings growth in the next year, the SA equity market is now one and a half standard deviations cheap on a forward P/E basis against the average since 1999 (see chart 12). In our view, a lot of bad news is currently priced into SA equities, enhancing the future return potential from current levels. The SA economy will likely remain trapped in a low-growth quagmire until the country's electricity and logistical deficiencies are rectified and structural policy reforms are successfully implemented to drive the country's growth potential to a higher plain. However, the fortunate reality for investors in the SA equity market is that the local economy is only a secondary driver for the overall local stock market. We have relayed before that analysis done by RMB Morgan Stanley shows that only around 30% of the aggregated operating performance of the companies in the JSE Top 40 index currently originates from SA.

**Chart 12: ALSI forward P/E**



Source: Iress, Momentum Investments

## SA bonds remain attractive in real terms and against global bonds

Although DM government bond yields have risen meaningfully and inflation rates have come down from peak levels, DM real yields remain in significantly negative territory due to still-elevated inflation readings. Although there are rampant inflation outliers like Türkiye within EM, in general, inflation rates in the emerging world have lagged those in DM. As such, EM real bond yields based on current inflation rates remain positive in most EM countries, with SA's real yields among the highest (see table 5).

**Table 5: Real ex-post 10-year government bond yields**

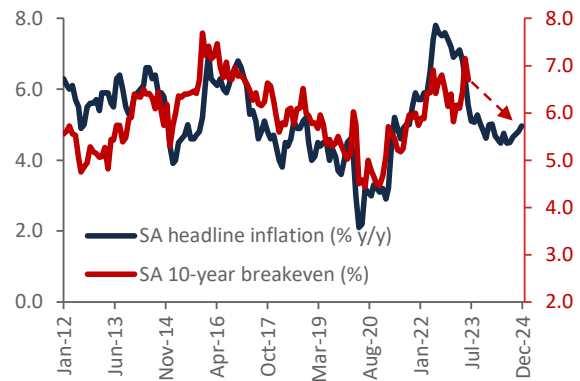
DM	
US	-0.3%
Japan	-2.9%
Europe	-3.7%
UK	-4.4%
EM	
Russia	8.5%
Brazil	7.1%
South Africa	5.2%
Mexico	2.8%
Türkiye	-23.8%

Source: Iress, Momentum Investments

Not only are SA real bond yields currently attractive versus DM and EM yields, but SA's real yield premiums against DM are also high against historical averages. Furthermore, SA's prospective real yield is around one and a half standard deviations higher than its historical average. In our view, SA's high real bond yields already discount high fiscal and country risk premiums.

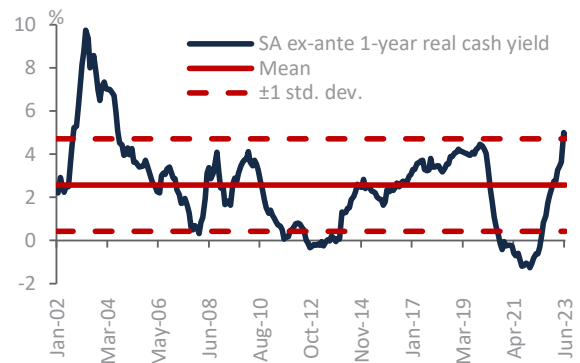
In the ILB space, lower-than-average monthly inflation accruals are expected from the second half of 2023 into the first quarter of 2024. Together with expected break-even tightening as inflation falls in the coming year (see chart 13), this should provide less fundamental support for ILBs going forward. The prospective SA real cash yield has been rising from a low level in line with policy rate increases and now expected falling inflation and is currently more than one standard deviation above its historical average (see chart 14).

**Chart 13: Breakeven tightening expected in line with falling inflation in the coming year**



Source: IRESS, Momentum Investments

**Chart 14: Prospective SA real cash yield**



Source: Iress, Momentum Investments

Relative to SA equities and cash, SA nominal bonds have consistently been the cheapest asset class since 2013 (see chart 15). Aggressive COVID-related SA Reserve Bank (SARB) interest rate cuts have made cash the most expensive asset class since 2020, but cash is now close to equity valuations after recent sharp rate rises.

**Chart 15: SA asset class valuations**



Source: Iress, Momentum Investments

## Better operational performance amid worse financial conditions for SA property companies

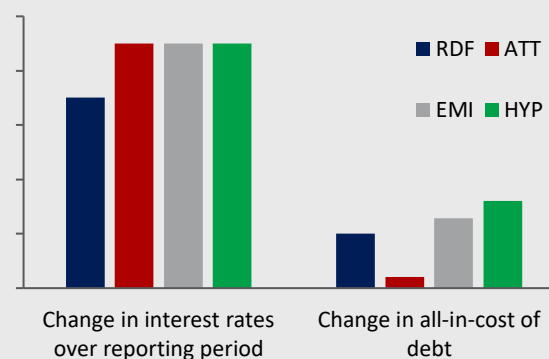
Although SA listed property companies are experiencing improving operational performance (in terms of vacancy rates, net operating income and property values), financial conditions have deteriorated (e.g. loan-to value, interest cover and the cost of debt). At least the increase in the cost of debt is somewhat mitigated by in-place interest rate hedges (see chart 16).

In the Retail subsector, the demand for Retail space continues to be firm, with vacancies falling and rental growth now positive. Escalations look like they are stabilising but remain lower than in other sectors. Better trading conditions are supporting a turnaround in negative reversions.

Improved demand for offices is driven by return-to-office corporate policies and loadshedding, but fundamentals remain weak, with escalations still trending lower and reversions still significantly negative. In the Industrial sector, escalations are holding up and reversions are improving, albeit still negative.

From a portfolio construction perspective, the potential for meaningful listed property return upside from attractive valuation levels must be weighed against the remaining negative fundamental factors.

**Chart 16: Increase in listed property companies' cost of debt mitigated by in-place interest rate hedges**



Source: Company reports, Momentum Investments

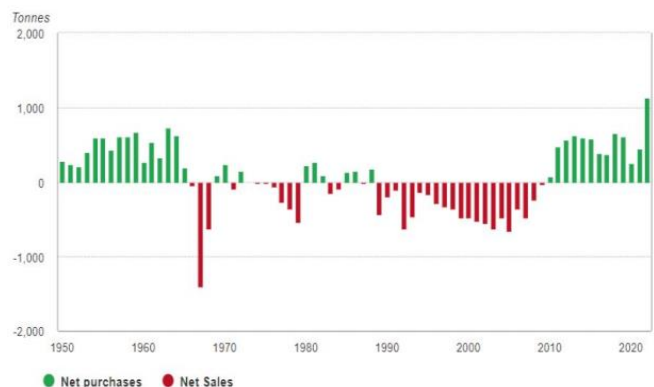
## Strategic rationale for gold as a portfolio diversifier and perceived safe-haven asset

US real rates have been the dominant driver for the US dollar gold price for a couple of decades, as the fundamental driver for gold is the opportunity cost of holding a non-interest-bearing asset. However, this relationship has broken down since the Russia/Ukraine war – we estimate that non-TIPS factors are adding more than \$1,000/oz to the current gold price.

This is likely due to the highest-ever gold buying from global central banks in 2022 (see chart 17), probably for geopolitical and diversification reasons. So far in 2023, the strong central bank buying trend has continued. Central banks have an affinity for gold reserves as it is deemed a safe haven in risk-off periods and does not rely on any issuer or government, unlike currencies and bonds. Gold also enables central banks to diversify their reserves away from assets like US Treasuries and the dollar, particularly for countries wary of future confiscation of their international US dollar reserves should the US decide to impose Russia-like sanctions on them. Banks including those of Türkiye, China, Egypt, and Qatar said they bought gold last year. But around two-thirds of the gold bought by central banks last year was not reported publicly, according to the World Gold Council.

With geopolitical strife likely to remain high in coming years as deglobalisation continues and a multipolar world order establishes itself (between the West and China), gold is likely to maintain its strategic attractiveness in investment portfolios as a hedge against political volatility and uncertainty.

**Chart 17: Central bank gold buying highest ever in 2022**

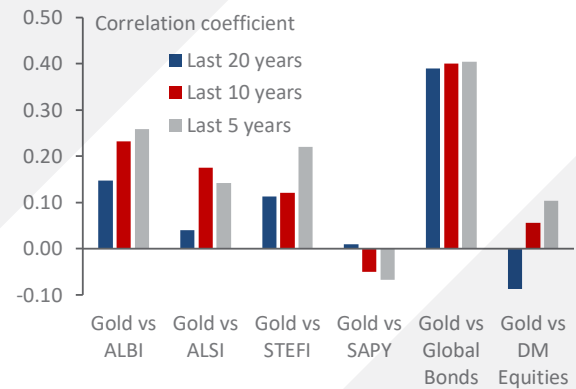


Source: Refinitiv, World Gold Council



This will likely maintain the strategic rationale for gold as a portfolio risk diversifier, because it is expected to hold its value through turbulent times and has limited correlation with other asset classes (see chart 18). For a SA investor, the rand gold price has been a strong relative asset class performer historically, as perennial rand weakness has provided huge support over many years.

**Chart 18: Gold has limited correlation with other asset classes**



Source: Iress, Bloomberg, Momentum Investments

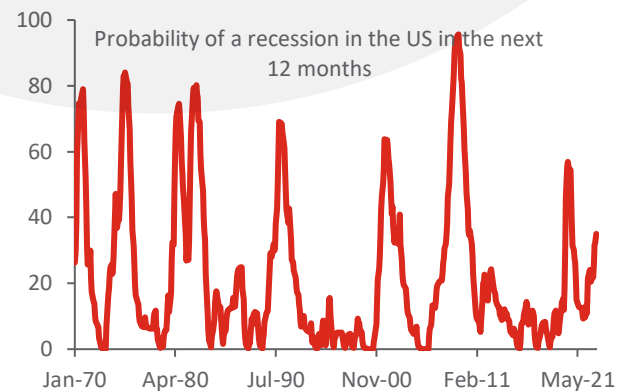
## Disruption in a rising rate environment

The future holds inherent uncertainty, and currently, the global economy faces an unusually high number of unknown factors. As famously stated by former US Secretary of Defense, Donald Rumsfeld, there are 'known unknowns' - things we know we don't know. In this age of ongoing crises, there is a lengthy list of these known unknowns.

The first known unknown revolves around how the world will manage the sudden transition from extremely accommodative monetary policy to a more aggressive tightening stance. Following the GFC and the subsequent pandemic, the world's major central banks, such as the US Fed and the ECB, injected liquidity into the markets through bond purchasing programmes. However, recently, central banks have had to grapple with the highest inflation rates in decades, which led to a swift rise in short-term interest rates. With central banks stating their hesitancy to lower interest rates until clear signs of inflation decline and a sustainable improvement in underlying inflation are evident, a tighter monetary policy stance could worsen growth challenges in the global economy and heighten the risks of a more severe downturn (see chart 19).

While indicators like consumer and labour market metrics remain relatively strong due to pandemic savings and stronger balance sheets, there are emerging concerns in areas such as global export volumes, sentiment surveys and leading indicators, all pointing to tougher growth conditions ahead. These challenging growth conditions follow the most significant pace of monetary policy tightening in nearly forty years.

**Chart 19: Rising risks of a US recession**



Source: MRB Partners, data up to May 2023

In this context, global governments are not in a position to proactively ease their policies as they did during the pandemic due to elevated levels of debt. As such, this leads to the second known unknown, which is the potential impact of excessive global debt levels on the global economy. The Bank for International Settlements (BIS) warns that mounting debt poses yet another challenge for central bankers as they attempt to rein in rising inflation. The world's debt has now reached a staggering 250% of GDP, which is 20% higher than in 2008. However, the risk to global economic growth goes beyond on-balance sheet debt.

The BIS has highlighted the risk of hidden off-balance sheet debt in the global economy, particularly in pension funds and other non-bank financial institutions, with more than US\$80 trillion worth of debt in foreign exchange swaps. Policymakers may overlook this potential funding squeeze, as it represents a blind spot.

This brings us to the third known unknown, which centres around concerns regarding the stability of financial markets. While financial strains have historically followed periods of rapid interest rate hikes, the recent turmoil in the smaller, regional banking sector in the US (with spillover effects in Europe) does not necessarily indicate a precursor to systemic stress. Instead, in our view, it reflects isolated challenges arising from tighter financial conditions. Nonetheless, banks have tightened lending standards, and consumers have become more cautious about borrowing, which will likely result in reduced growth in borrowing activity and consequently slower economic growth globally.

Although the global economy initially showed surprising growth earlier this year due to factors like an atypically mild European winter reducing energy demand and a quicker reopening of the Chinese economy, prospects for more robust Chinese growth have once again weakened. Factors such as declining global export activity, subdued consumer sentiment due to prolonged COVID-19 policies affecting mobility, stress in the property sector and elevated youth unemployment, along with an uneven housing market recovery, suggest that China's growth outperformance compared to the government's official target of 5% may be more limited than initially thought. Nevertheless, there have been growth-supportive monetary policy measures, including interest rate cuts and an additional

reduction in reserve requirements. Additionally, on the fiscal front, growth will be bolstered by tax deductions and spending from the proceeds of special local bonds issued.

That said, the era of high single-digit growth in China appears to be largely over due to a shrinking population, slowing productivity growth, and the country's significant debt burden, primarily driven by credit provided to state-owned entities. China aims to shift toward a more domestically focused economy that prioritises consumption spending and services over exports, manufacturing, and fixed investment. As a result, growth is expected to decelerate compared to previous decades. This raises the fourth known unknown, which is the impact of slower growth in China on commodity prices and net commodity-exporting nations. Traditional net-exporting economies of base metals may not benefit as much from China's revised growth model. However, economies supplying raw materials for consumer-led rather than industrial-led activities could still find support for their exports from the Asian giant.

Despite China's shift towards inward-looking policies, its authorities' Sino-centrist worldview indicates a desire to regain centrality in the international system and exert dominance over global governance institutions. However, China's efforts in global governance have deepened divisions with other countries, particularly democracies committed to existing norms and institutions. Ultimately, this divide could impede collaborative efforts by states to address major international challenges and undermine multilateral cooperation. Consequently, the future of the global order and global influence becomes the fifth known unknown, especially in a world increasingly characterised by geoeconomic fragmentation.

## Power predicament poses the primary risk to local growth

The global circumstances present a significant challenge for SA's economic growth, especially when combined with local obstacles such as subdued business and consumer confidence, severe constraints in network industries and ongoing political uncertainty.

In our assessment, the primary risk to SA's growth is the prevailing power predicament, which is expected to keep growth flat this year. However, an improvement in energy supply is anticipated to boost growth to 1% in 2024 and 1.6% in 2025.

According to energy utility Eskom, the recent increase in the energy availability factor to 56% has been attributed to factors such as warmer weather, increased diesel deliveries, improved generation capacity and reduced electricity demand due to private sector investments in alternative energy sources. Nonetheless, the risk of higher levels of load shedding remains significant in the short term due to offline generating units and delays in connecting renewable energy projects.

Nevertheless, a substantial improvement in energy supply is anticipated starting next year. Government expects that temporary repairs to three damaged units of the Kusile power plant due to a flue gas duct failure (around 2 100MW) will be completed by December this year, Koeberg's Unit 2 (around 920MW) will be back online by April next year and repairs to fix the damage by an explosion in Medupi's Unit 4 (800MW) will be finished by July next year. Additionally, Kusile's Unit 5 (around 720MW) is scheduled to come online by April 2024.

In addition, Meridian Economics further anticipates that 150MW, related to the risk mitigation independent power producers, will be connected from November this year, while c.784MW from Bid Window 5 should be operational by August next year, with an additional 1759MW of additional renewable capacity available by early 2025.

While inadequate energy supply and logistical bottlenecks have hindered growth prospects in SA, businesses continue to perceive high levels of political uncertainty as a major obstacle to investing in the country. The upcoming national elections in April/May next year are expected to be highly contentious, and the electoral outcome remains uncertain. The ruling party, the African National Congress (ANC), has experienced a decline in popularity due to economic failures and corruption. In our base case scenario, we anticipate the ANC forming a coalition government with smaller minority parties in Gauteng and KwaZulu-Natal, with a possibility of a coalition government at a national level.

In a worst-case scenario, we envision the ANC's support dropping significantly below 45%, which would necessitate an alliance with a larger coalition partner like the Economic Freedom Fighters. In this low-road scenario, policies may take a more leftist direction, negatively impacting investment prospects for SA.

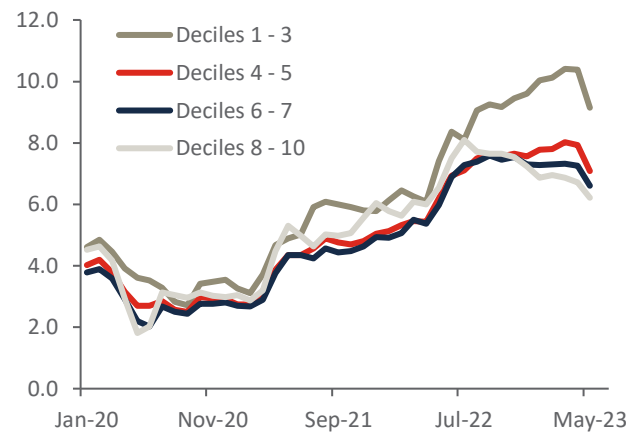
Weaker economic growth, rising costs associated with alternative energy sources, disruptions to business operations and declining commodity prices are expected to exert downward pressure on government revenue growth. Furthermore, expenditure pressures and social demands pose challenges to fiscal discipline. The feasibility of reducing the budget deficit to 3.9% during the fiscal year 2023/24, as anticipated by Treasury, is cast into doubt due to mounting social obligations, an overrun in civil servant wages and burdensome debt-servicing obligations. Projected fiscal slippage, along with increased external financing needs stemming from global challenges and issues in local network industries affecting exports, further strain monetary policy and raise the risk of higher financing costs.



**Sanisha Packirisamy**

**Economist**  
Momentum Investments

**Chart 20: A steep 3% gap in inflation faced between the lowest 30% and highest 30% of spenders in SA**



Source: Statistics SA, Momentum Investments

Therefore, despite expectations for headline inflation to decrease in the latter half of this year, driven by disinflation in food and fuel prices, we anticipate the SARB to continue tightening monetary policy. The SARB has expressed concern about cost-of-living pressures affecting the most vulnerable segments of society, as the lowest 30% of spenders in SA have experienced inflation close to 10% in the past six months according to Statistics SA, almost 3% higher than the top 30% of spenders. Additionally, businesses' inflation expectations (surveyed by the Bureau for Economic Research) have shifted unfavourably from the midpoint of the SARB's inflation target range of 3% to 6%. This development is worrisome to the SARB as businesses are considered influential in setting prices in the economy.

We expect another 25-basis point interest rate hike at the July rate-setting meeting, bringing the SA repo rate to a peak of 8.5%. Looser fiscal policy adds to the burden of SA's monetary policy authorities and as such, interest rates could be kept tighter for longer. This suggests that the first interest rate cut may be delayed to the middle of next year or beyond.



**Herman van Papendorp**

**Head: Macro Research and Asset Allocation**  
Momentum Investments

# Partially Vesting Smoothed Bonus Range

## Universal Multi-Manager Smooth Growth Fund



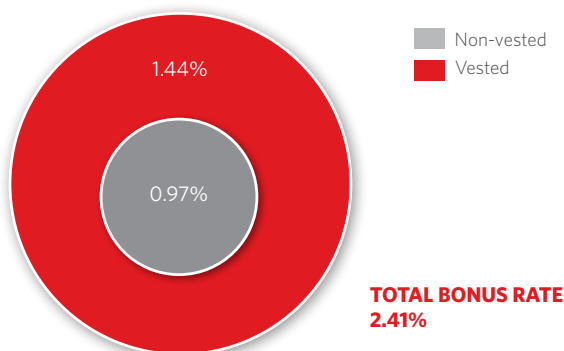
### Fund Snap Shot

INCEPTION DATE	FUNDING LEVEL RANGE	FUND SIZE	ANNUALISED 3-YEAR VOLATILITY OF BONUS RATES	ANNUALISED 3-YEAR UNDERLYING ASSET RETURN
Jun 2020	100% - 105%	R562.9m	0.94%	11.96%

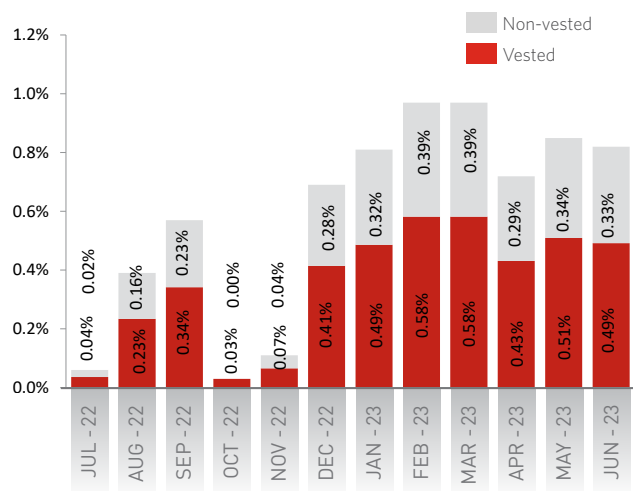
<sup>1</sup>Based on back-tested bonus rates and returns

### Performance

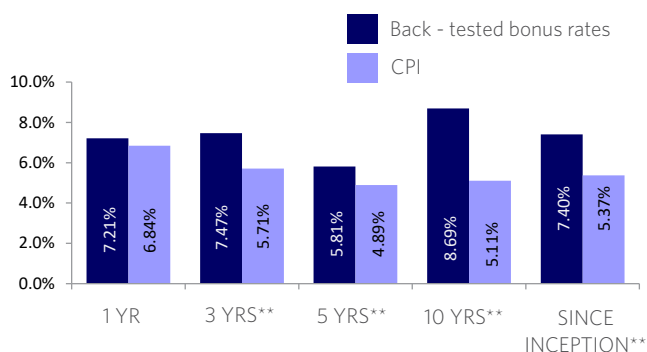
The total bonus rate\* for the past quarter on the **Universal Multi-Manager Smooth Growth Fund** is shown below.



The chart below shows the monthly bonus rates\* for the past 12 months



The chart below shows the long term bonus\* performance of the **Universal Multi-Manager Smooth Growth Fund** against CPI



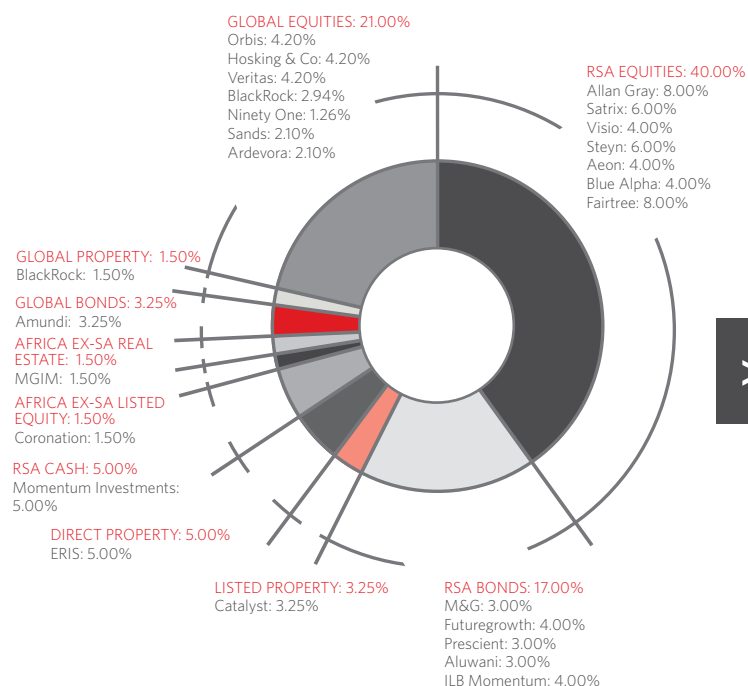
CPI figures are lagged by two months

\* Bonus rates are net of underlying asset charges but are gross of the policy fee

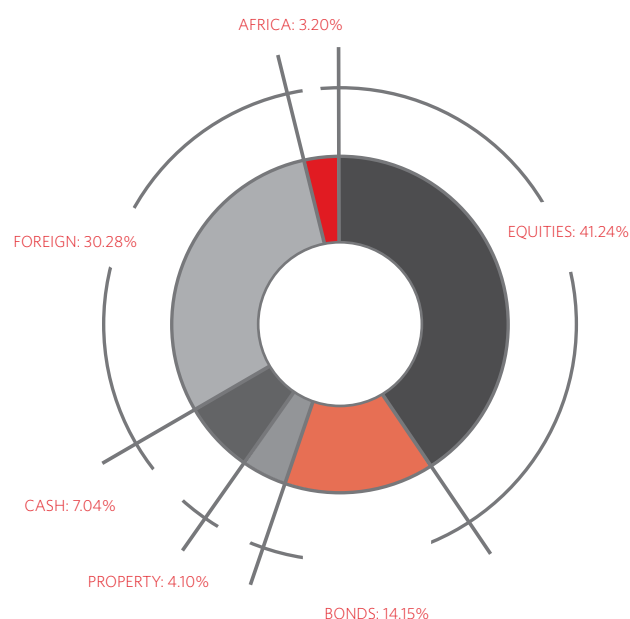
\*\* Annualised

### Asset Allocation

The Africa ex-SA Real Estate allocation is expected to increase gradually over the next 5 years to a total of 2.50%, in line with drawdown notices from Momentum Global Investment Management (MGIM). The strategic asset allocation of the portfolio is shown below.



The effective asset allocation of the portfolio is shown alongside.





# Partially Vesting Smoothed Bonus Range

## Universal Smooth Growth Fund



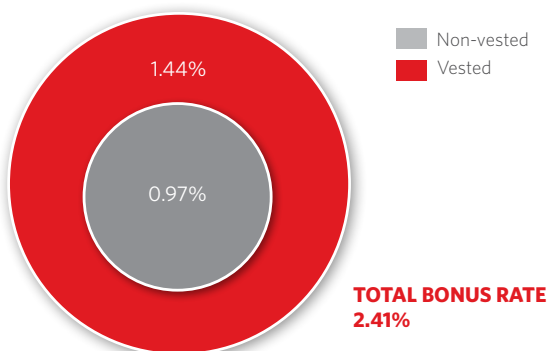
### Fund Snap Shot

INCEPTION DATE	FUNDING LEVEL RANGE	FUND SIZE	ANNUALISED 3-YEAR VOLATILITY OF BONUS RATES	ANNUALISED 3-YEAR UNDERLYING ASSET RETURN
Jun 2020	100% - 105%	R386.3m	0.96% <sup>1</sup>	11.23% <sup>1</sup>

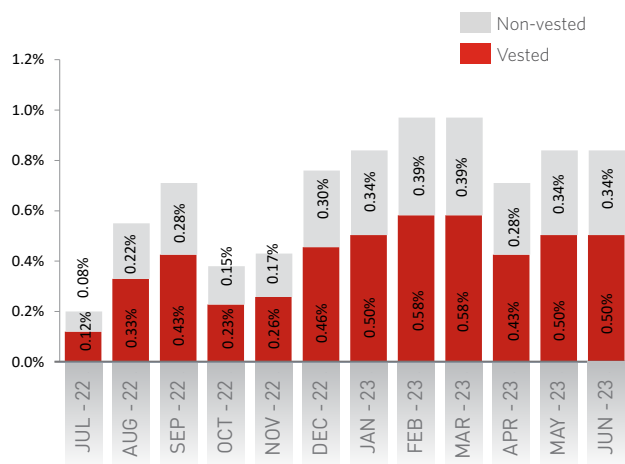
<sup>1</sup>Based on back-tested bonus rates and returns

### Performance

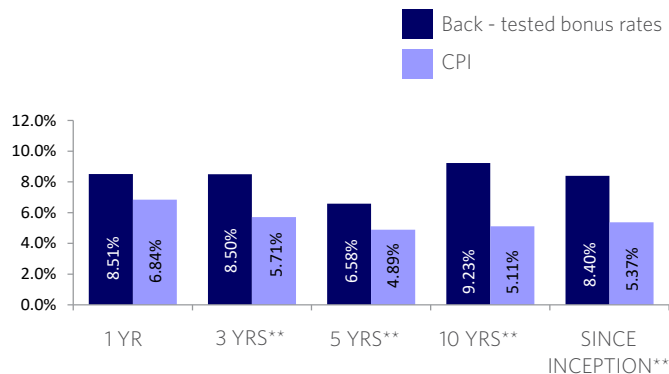
The total bonus rate\* for the past quarter on the **Universal Smooth Growth Fund** is shown below.



The chart below shows the monthly bonus rates\* for the past 12 months



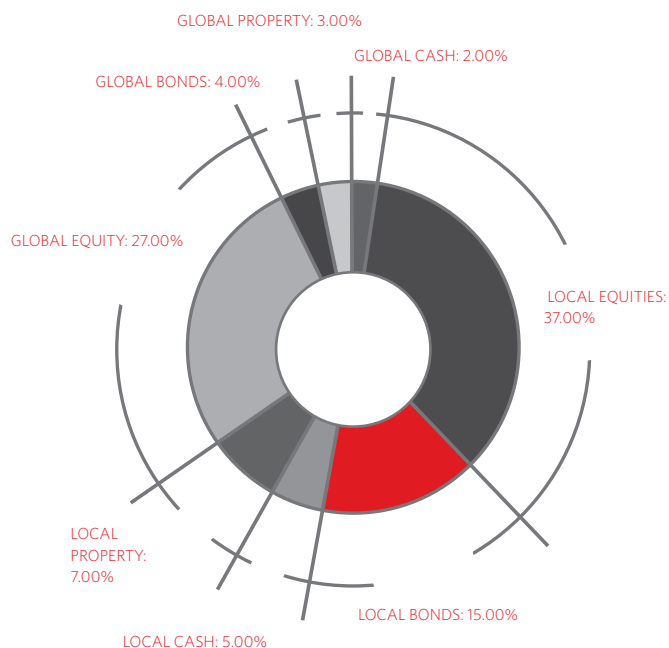
The chart below shows the long term bonus\* performance of the **Universal Smooth Growth Fund** against CPI



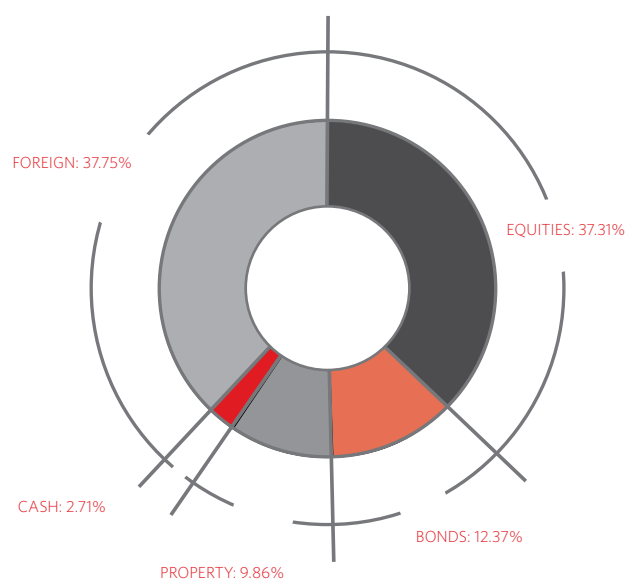
CPI figures are lagged by two months

### Asset Allocation

The strategic asset allocation of the portfolio is shown alongside.



The effective asset allocation of the portfolio is shown alongside.



\* Bonus rates are net of underlying asset charges but are gross of the investment management fee

\*\* Annualised

# Partially Vesting Smoothed Bonus Range

## Multi-Manager Smooth Growth Fund Global

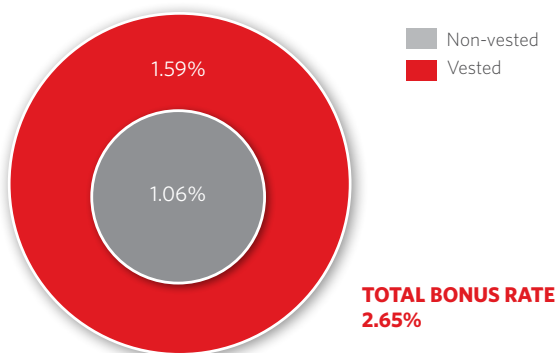


### Fund Snap Shot

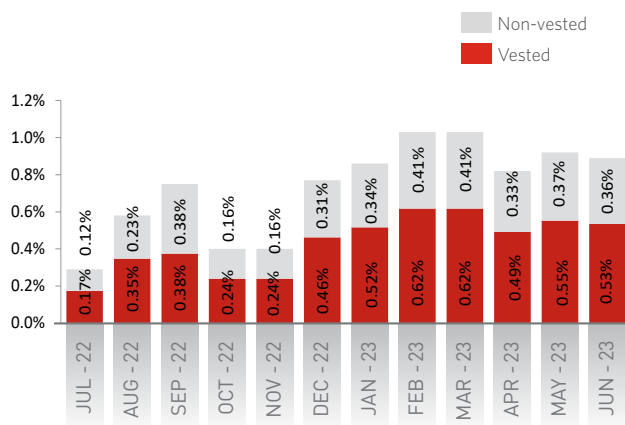
INCEPTION DATE	FUNDING LEVEL RANGE	FUND SIZE	ANNUALISED 3-YEAR VOLATILITY OF BONUS RATES	ANNUALISED 3-YEAR UNDERLYING ASSET RETURN
Jan 2004	100% - 105%	R6.4bn	1.12%	10.62%

### Performance

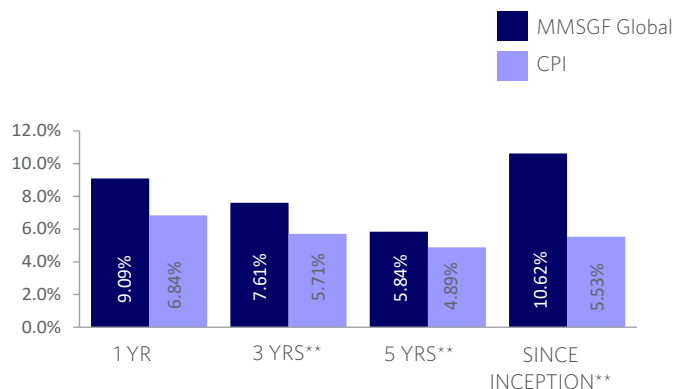
The total bonus rate\* for the past quarter on the **Multi-Manager Smooth Growth Fund Global** is shown below.



The chart below shows the monthly bonus rates\* for the past 12 months



The chart below shows the long term bonus\* performance of the **Multi-Manager Smooth Growth Fund Global** against CPI



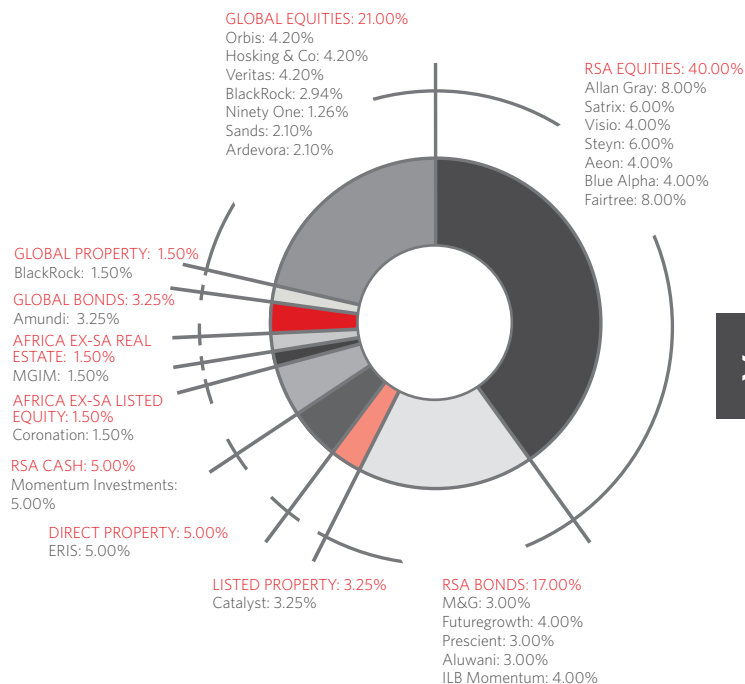
CPI figures are lagged by two months

\* Bonus rates are net of underlying asset charges but are gross of the policy fee

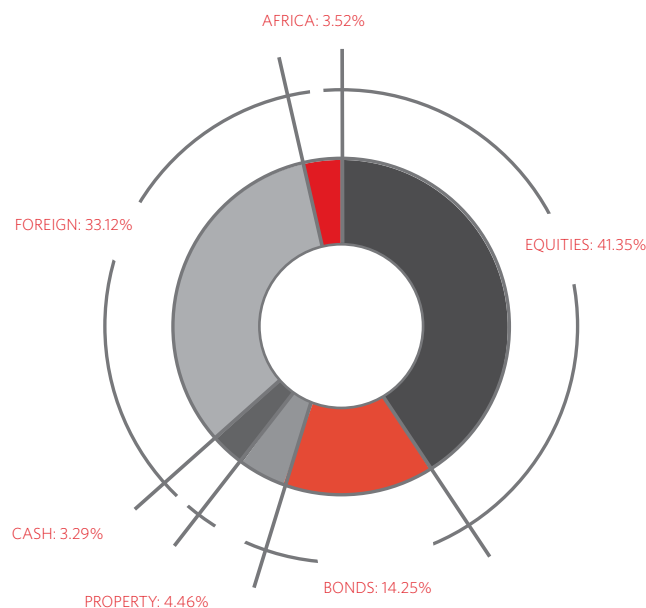
\*\* Annualised

### Asset Allocation

The Africa ex-SA Real Estate allocation is expected to increase gradually over the next 5 years to a total of 2.50%, in line with drawdown notices from Momentum Global Investment Management (MGIM). The strategic asset allocation of the portfolio is shown below.



The effective asset allocation of the portfolio is shown alongside.



# Partially Vesting Smoothed Bonus Range

## Smooth Growth Fund Global

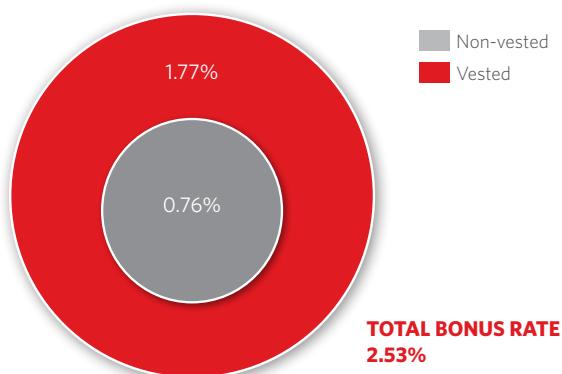


### Fund Snap Shot

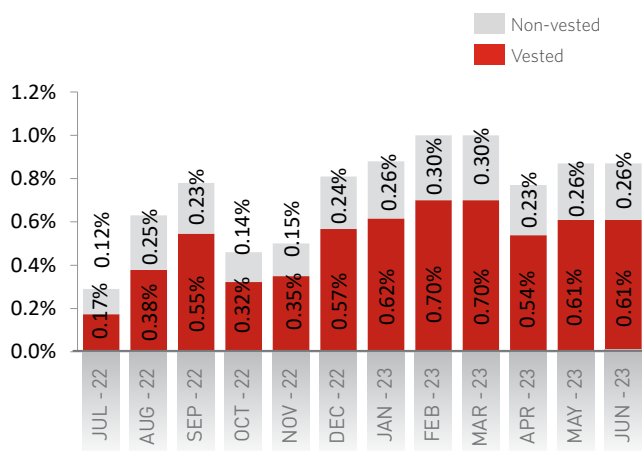
INCEPTION DATE	FUNDING LEVEL RANGE	FUND SIZE	ANNUALISED 3-YEAR VOLATILITY OF BONUS RATES	ANNUALISED 3-YEAR UNDERLYING ASSET RETURN
Jan 1989	100% - 105%	R1.7bn	1.19%	12.68%

### Performance

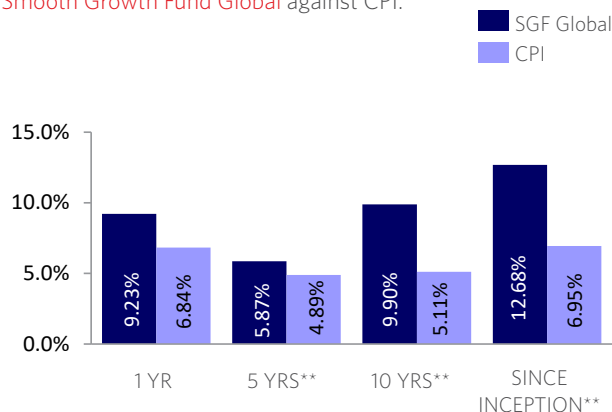
The total bonus rate\* for the past quarter on the Smooth Growth Fund Global is shown below.



The chart below shows the monthly bonus rates\* for the past 12 months.



The chart below shows the long term bonus\* performance of the Smooth Growth Fund Global against CPI.

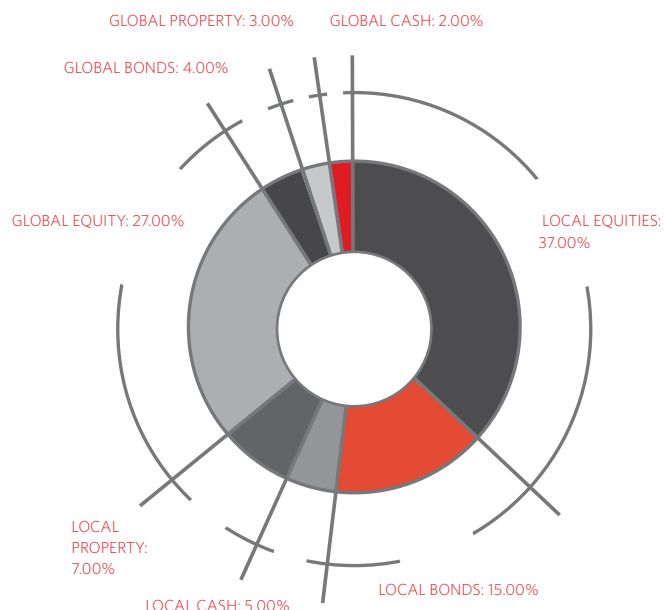


\* Bonus Rates are net of underlying asset charges but are gross of the Investment Management Fee

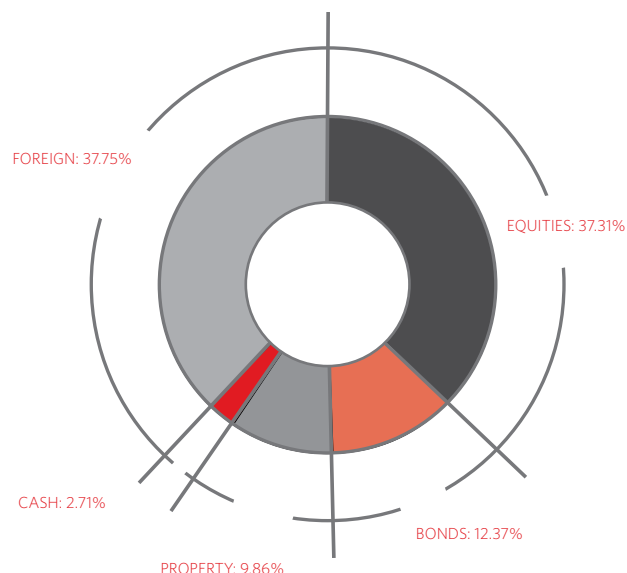
\*\* Annualised

### Asset Allocation

The strategic asset allocation of the portfolio is shown alongside.



The effective asset allocation of the portfolio is shown alongside.



# Partially Vesting Smoothed Bonus Range Multi-Manager Smooth Growth Fund Global Bonus Series 2020<sub>(previously MMSGF Local)</sub>

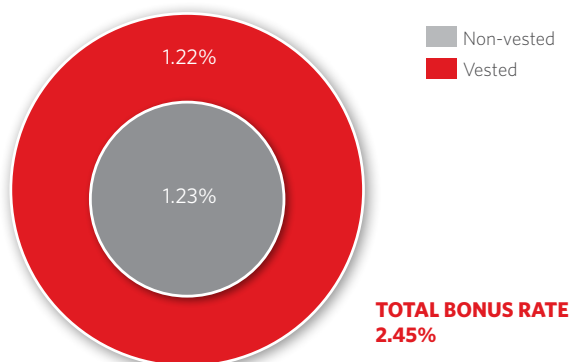


## Fund Snap Shot

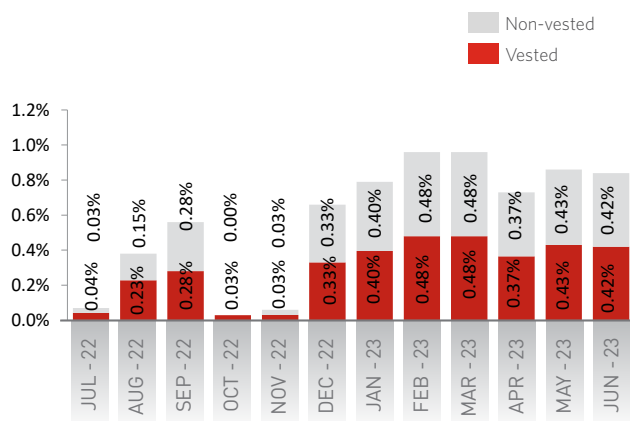
INCEPTION DATE	FUNDING LEVEL RANGE	FUND SIZE	ANNUALISED 3-YEAR VOLATILITY OF BONUS RATES	ANNUALISED 3-YEAR UNDERLYING ASSET RETURN
Jan 2004	100% - 105%	R138m	1.16%	12.86%

## Performance

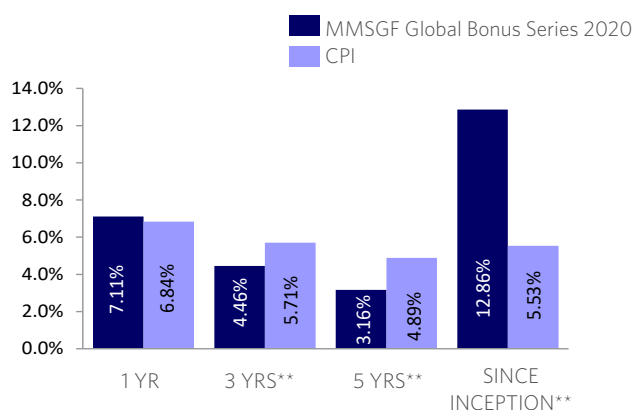
The total bonus rate\* for the past quarter on the **MMSGF Global Bonus Series 2020** is shown below.



The chart below shows the monthly bonus rates\* for the past 12 months.



The chart below shows the long term bonus rates\* performance of the **MMSGF Global Bonus Series 2020** against CPI



CPI figures are lagged by two months

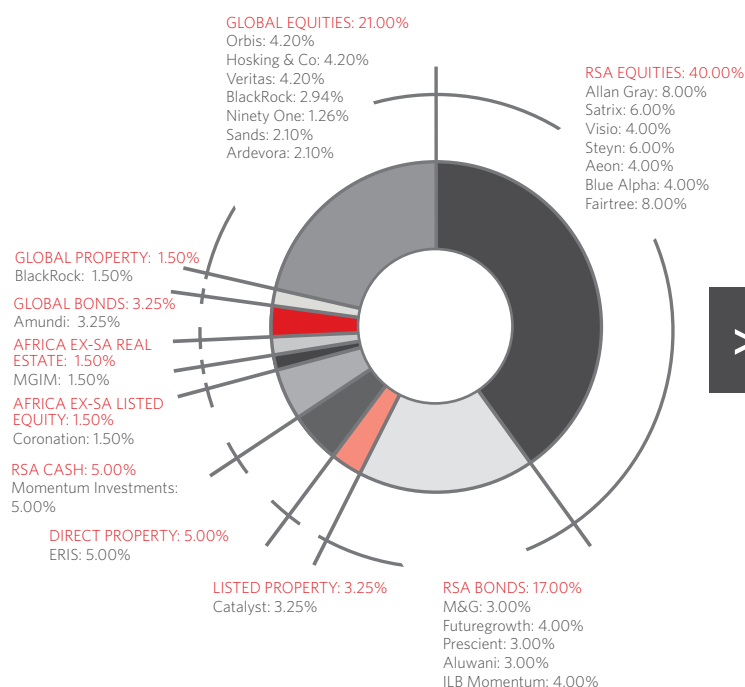
\* Bonus rates are net of underlying asset charges but are gross of the policy fee

\*\* Annualised

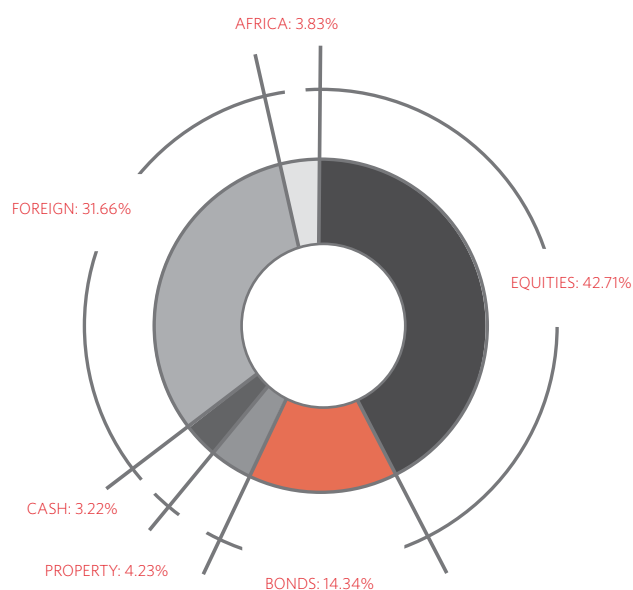
## Asset Allocation

The strategic asset allocation of the portfolio is shown alongside.

The Africa ex-SA Real Estate allocation is expected to increase gradually over the next 5 years to a total of 2.5% in line with drawdown notices from Momentum Global Investment Management (MGIM).



The effective asset allocation of the portfolio is shown alongside.





# Partially Vesting Smoothed Bonus Range

## Smooth-Edge Fund



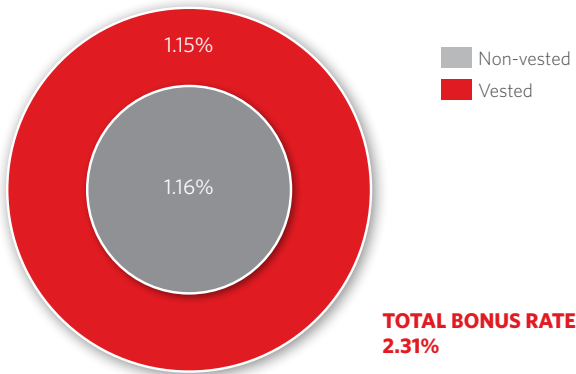
### Fund Snap Shot

INCEPTION DATE	FUNDING LEVEL RANGE	FUND SIZE	ANNUALISED 3-YEAR VOLATILITY OF BONUS RATES	ANNUALISED 3-YEAR UNDERLYING ASSET RETURN
Feb 2019	100% - 1105%	R1.4bn	1.13% <sup>1</sup>	10.91% <sup>1</sup>

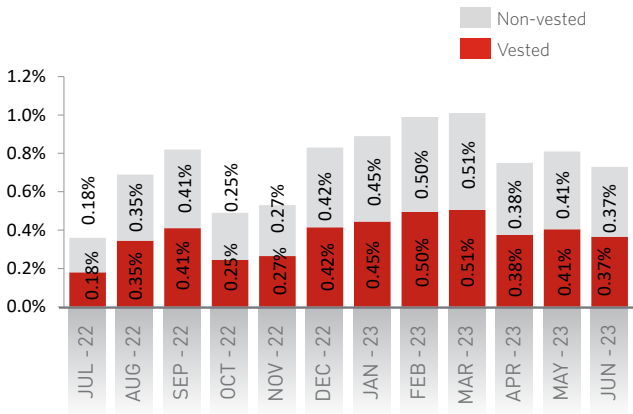
<sup>1</sup>Based on back-tested bonus rates and returns

### Performance

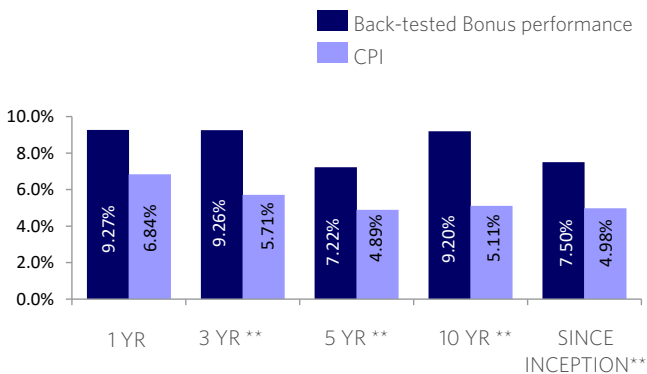
The total bonus rate for the past quarter on the Momentum Smooth-Edge Fund is shown below.



The chart below shows the actual monthly bonus rates\* for the past 12 months.



The chart below shows the long term back-tested bonus rates\* performance of the Smooth-Edge Fund against CPI

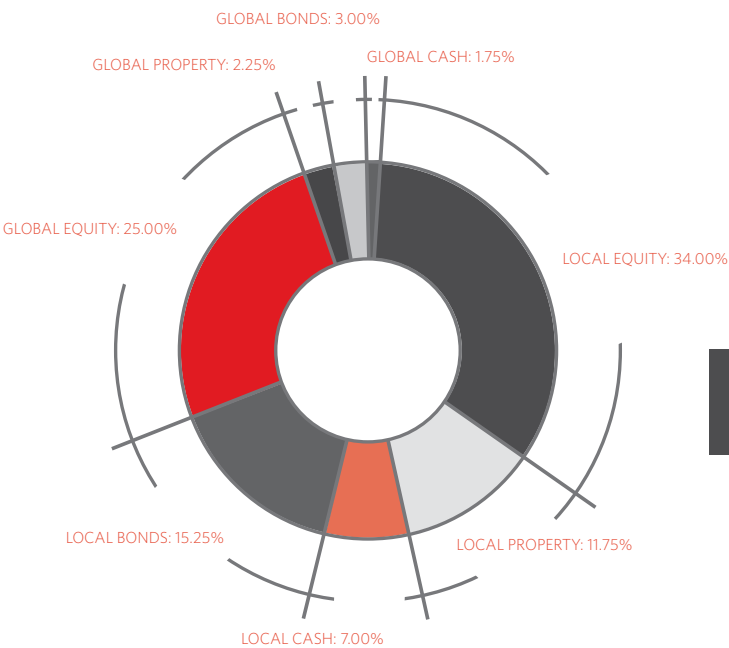


CPI figures are lagged by two months

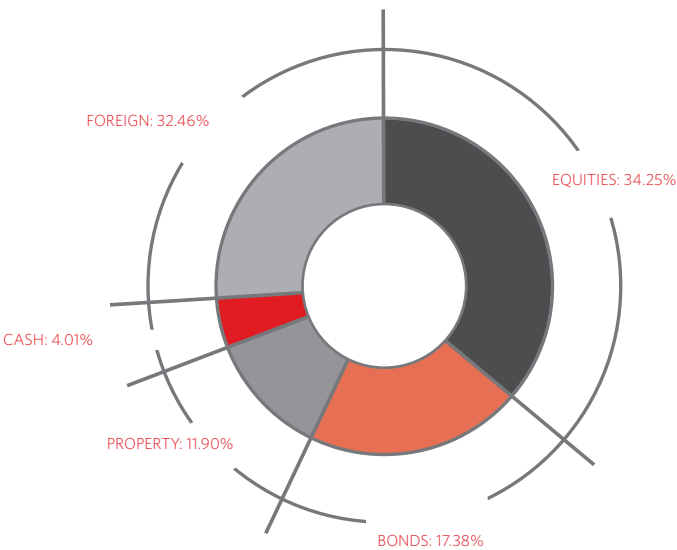
\* The bonus rates and back-tested bonus rates are gross of the investment management fee  
\*\* Annualised

### Asset Allocation

The strategic asset allocation is shown alongside.



The effective asset allocation of the portfolio is shown alongside.



# Fully Vesting Smoothed Bonus Range

## Universal Smart Guarantee+3 Fund

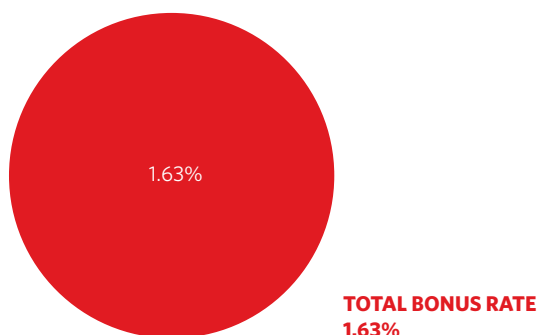


### Fund Snap Shot

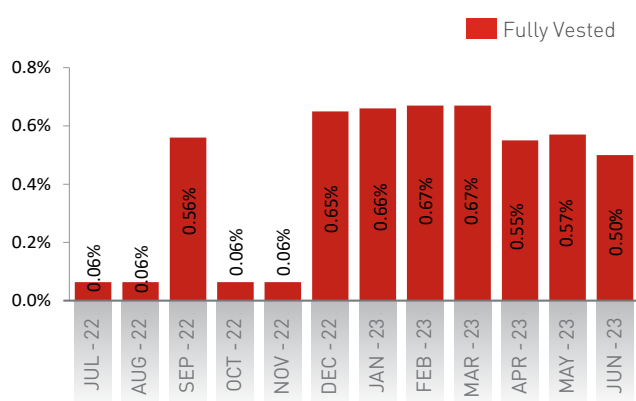
INCEPTION DATE	FUNDING LEVEL RANGE	FUND SIZE	ANNUALISED 3-YEAR VOLATILITY OF BONUS RATES	ANNUALISED 3-YEAR UNDERLYING ASSET RETURN OF BONUS GENERATING PORTFOLIO
Oct 2013	95% - 100%	R537.9m	1.22%	11.36%

### Performance

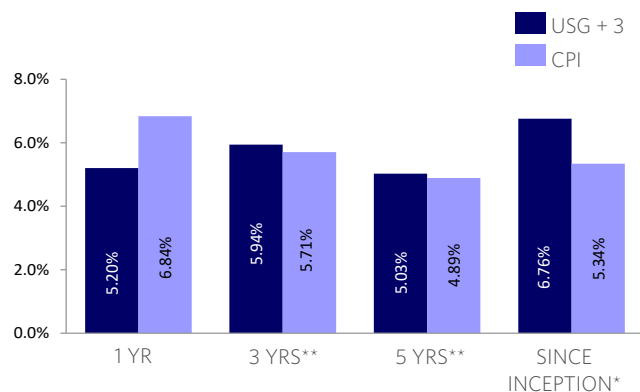
The total bonus rate\* for the past quarter on the **Universal Smart Guarantee +3 Fund** is shown below.



The chart below shows the actual monthly bonus rates\* for the past 12 months.



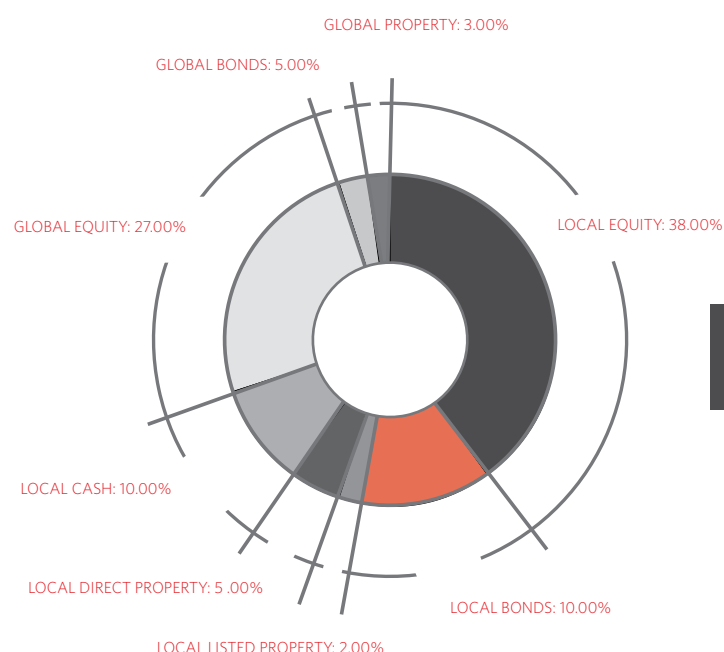
The chart below shows the long term bonus\* performance of the **Universal Smart Guarantee +3 Fund** against CPI.



CPI figures are lagged by two months

### Asset Allocation

The strategic asset allocation of the bonus generating portfolio (Momentum Dynamic Hedging Reference Portfolio) is shown alongside.



For bonus declarations, 90% of the underlying asset returns of the bonus generating portfolio are smoothed over a three-year period as per the smoothing formula.

The liability driven investment strategy employed includes a dynamic protection overlay to secure the guarantee. As a result, the value of the underlying asset portfolio is sensitive to changes in asset values (and interest rates) and the effective asset allocation will reflect both the bonus generating portfolio and the dynamic protection overlay.

### USG +3: Bonus rates to be declared

Given that the monthly bonuses are based on the weighted average of the previous 36 months' returns of the bonus generating portfolio, it is possible to calculate the future bonuses that will be declared under various future investment return assumptions. Assuming zero returns over the following 34 months (there is a 2 month lag), around **10.87%** of bonuses will still be declared.

\* Bonus rates are net of underlying asset charges but are gross of the investment management fee  
 \*\* Annualised

# Fully Vesting Smoothed Bonus Range

## Multi-Manager Secure Growth Fund

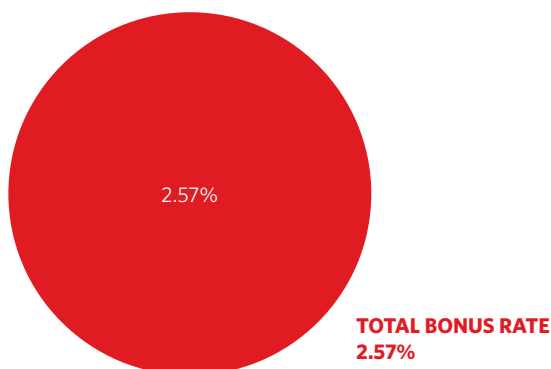


### Fund Snap Shot

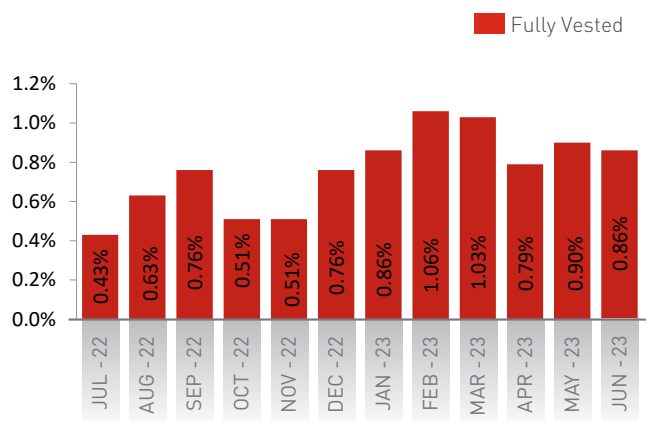
INCEPTION DATE	FUNDING LEVEL RANGE	FUND SIZE	ANNUALISED 3-YEAR VOLATILITY OF BONUS RATES	ANNUALISED 3-YEAR UNDERLYING ASSET RETURN
Nov 2007	105% - 110%	R74.2m	1.05%	10.37%

### Performance

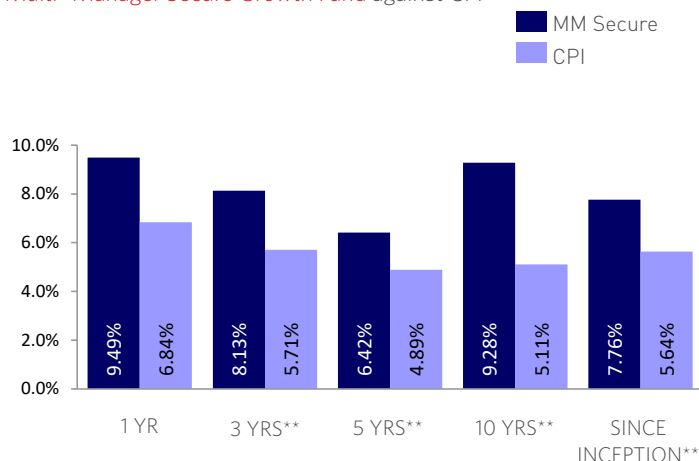
The total bonus rate\* for the past quarter on the Multi-Manager Secure Growth Fund is shown below.



The chart below shows the monthly bonus rates\* for the past 12 months.



The chart below shows the long term bonus\* performance of the Multi-Manager Secure Growth Fund against CPI



CPI figures are lagged by two months

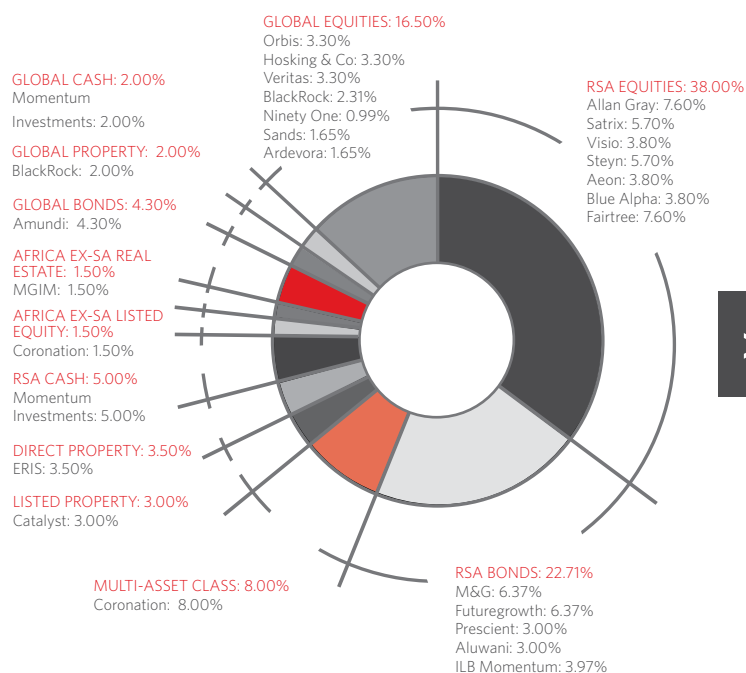
\* Bonus rates are net of underlying asset charges but are gross of the policy fee

\*\* Annualised

### Asset Allocation

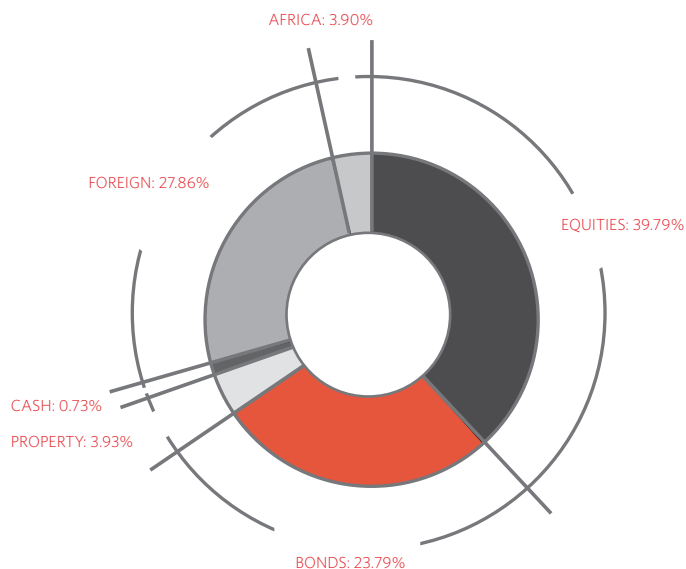
On 1 December 2020, changes were made to the strategic asset allocations.

The Africa ex-SA Real Estate allocation is expected to increase gradually over the next 5 years to a total of 2.50%, in line with drawdown notices from Momentum Global Investment Management (MGIM). The strategic asset allocation of the portfolio is shown alongside.



\*No asset manager has been appointed.

The effective asset allocation of the portfolio is shown alongside.





# Smoothed Bonus Portfolios

## Key Features

		Fund Return Objective	Manager	Mandate Type	Guarantee on Policy Benefits <sup>1</sup>	Market Value Adjustment on Voluntary Exits <sup>2</sup>	Capital Charge	Policy Fee or Investment Management Fee*	Inception Date
Partially Vesting	Multi-Manager Smooth Growth Fund Global	CPI + 4% pa, net of the policy fee and underlying asset charges over the long term	Multi-Manager	Moderate Balanced	100% of net capital invested and vested bonus declared (net of the Policy fee)	Yes	0.90% pa	0.35% of the first R50m, 0.25% of the excess above R50m <sup>3</sup>	January 2004
	Universal Multi-Manager Smooth Growth Fund								June 2020
	Multi-Manager Smooth Growth Fund Global Bonus Series 2020								January 2004
	Smooth Growth Fund Global	CPI + 4% pa, net of the investment management fee and underlying asset charges over the long term	Momentum Investments	Moderate Balanced	100% of net capital invested and vested bonus declared (net of the investment management fee)	Yes	0.90% pa	0.45% of the first R10m, 0.35% of the next R40m, 0.25% of the excess above R50m <sup>3</sup> *	January 1989
	Universal Smooth Growth Fund								June 2020
	Smooth-Edge Fund	CPI + 4% pa, net of the investment management fee and underlying asset charges over the long term	Momentum Investments	Moderate Balanced	100% of net capital invested and vested bonus declared (net of the Investment management fee)	Yes	0.60% pa	0.25% pa <sup>3</sup> *	February 2019
Fully Vesting	Multi-Manager Secure Growth Fund	CPI + 2% pa, net of the policy fee and underlying asset charges over the long term	Multi-Manager	Moderate Conservative Balanced	100% of net capital invested and total bonus declared (net of the Policy fee)	Yes	1.40% pa	0.35% of the first R50m, 0.25% of the excess above R50m <sup>3</sup>	November 2007
	Universal Smart Guarantee+3 Fund	CPI + 3% pa, net of the investment management fee and underlying asset charges over the long term	Insurer Liability Driven Investment	Insurer Liability Driven Investment	100% of net capital invested and total bonus declared (net of the Investment management fee)	Yes	0.50% pa	0.75% pa <sup>3</sup> *	October 2013

\*Policy fee includes the cost of investment administration.

\*Investment management fee includes policy fee and certain fees related to the management of the assets (not included in underlying asset charges).

1. Policy benefits include but are not limited to death, disability, resignation or retirement. The full list policy benefits is outlined as well as other terms and conditions specified in the client policy contracts.
2. Market value adjustments may be applied on member switches out, terminations and other non-policy benefits if a client is underfunded.
3. Underlying asset charges include capital charge and net priced asset fees and performance fees (where applicable).



## Contact details

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Website: [www.momentum.co.za](http://www.momentum.co.za)

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