NEDGROUP INVESTMENTS

UNIT TRUSTS | INTERNATIONAL | RETIREMENT FUNDS

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# NEDGROUP INVESTMENTS CORE INCOME

Quarter Two, 2021

Taquanta Asset Management

| Performance to 30 June 2021 | Fund Performance[1] | SteFI | *Hit Rate vs SteFI** |
|---|---|---|---|
| 1 month | 0.36% | 0.31% | *97%* |
| 3 months | 1.03% | 0.92% | *100%* |
| 12 months | 4.20% | 4.01% | *100%* |

**percentage of rolling periods since 01/01/2015 the fund has outperformed its benchmark.*

**Market Commentary**

At the G7 leaders' summit in June 2021, the World Bank stated that the global economy is expected to only recover to pre-pandemic levels by 2022 and emphasized that countries need to do more in terms of donating vaccines and investment into the production of vaccines.

Globally, inflation increased in May. US CPI increased to 5% y/y in May from 4.2% y/y in April and UK inflation rose to 2.1% y/y in May from 1.5% y/y in April. In the Eurozone, inflation increased to 2% y/y in May from 1.6% y/y previously. All the above-mentioned increases were mainly due to higher fuel prices.

On the domestic front South Africa's CPI inflation spiked to 5.2% y/y in May from 4.4% y/y in April. Product price inflation (PPI) also spiked in May rising to 7.4% y/y from 6.7% y/y in April, in line with market expectation. Private sector credit extension (PSCE) declined in May to -0.4% y/y from -1.8% y/y in April, this was mainly driven by a corporate credit that contracted to -5% y/y in May from -6.7% y/y in April.

President Cyril Ramaphosa addressed the nation with great concern and implemented a level 4 lockdown towards the end of June 2021. Restrictions were put in place to try and mitigate the risk of increase in COVID-19 cases and deaths within the country. South Africa's overdue vaccine roll-out could halt the country's economic recovery despite the government imposing stricter restrictions to curb further spread of Covid-19 infections.

It was an active second quarter of the year with issuance of just over R40.2 billion in the SA corporate bond and commercial paper market. Issuance volume continues to be dominated by the banks and corporate issuance remains subdued compared to pre-covid levels. Despite the volume of debt issued in the second quarter of the year, issuance spreads have remained flat given the excess liquidity in the market. Auctions have continued to be relatively well bid in Q2 2021 and the expectation is for demand to remain strong in the primary market on the back of excess market liquidity. The Land Bank default and subsequent Liability Solution journey continues to make investors weary of SOEs.

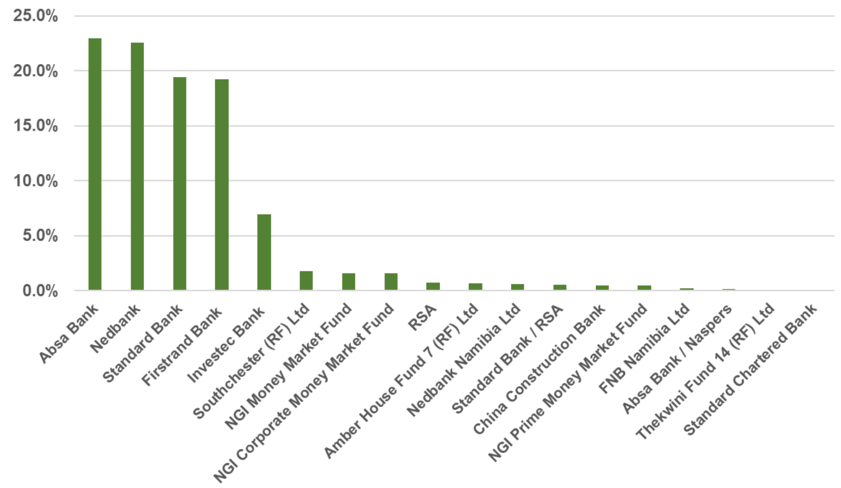
**Current positioning and outlook**

The fund's investment philosophy of conservative credit selection continues to support returns. The high-quality credit profile reduces the risk of default which is crucial to the protection of capital. The fund has a bias towards issuers whose business model has stable annuity-type revenue streams. Compared to the benchmark, the fund has exposure to corporates, securitisations, and SA Government issued debt which is currently paying a credit premium over and above the bank exposure.

[1] Net return for the Nedgroup Investments Core Income Fund, A class. Source: Morningstar (monthly data series).

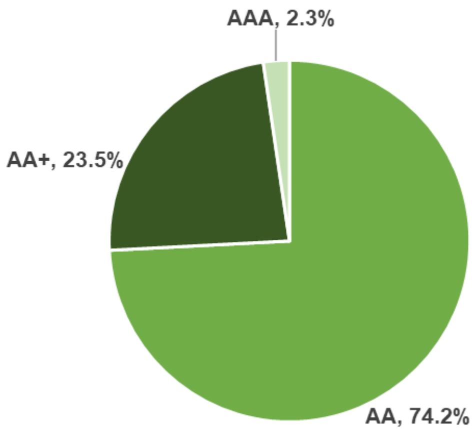
### 1. Portfolio Credit Exposure

The primary objective of the Fund is to outperform a cash benchmark, with low volatility. To achieve this, the fund sets out by investing in only high-quality credit counters with a low probability of default. The Fund's counterparty exposure at June quarter-end is shown in the chart:



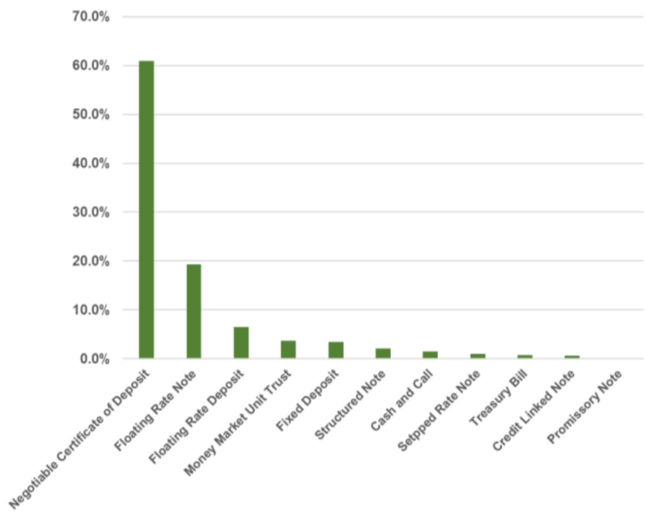

The portfolio was well invested across all local and foreign banks as well as having exposure to AAA rated entities. The fund is within its mandate limits, with investments in high quality investment grade issuers.

The pie chart represents the issuer credit rating breakdown as at 30 June 2021:




### Instrument Holdings

Another key feature of the portfolio is to hold fixed income securities that will have limited exposure to interest rate risk. As a result, the predominant securities in the fund are bank negotiable certificates of deposit, floating rate notes and floating rate deposits linked to 3-month Jibar. All of these instruments reprice on a regular basis, meaning that if interest rates rise or fall, the fund will track this movement.




## Maturity Profile and Duration

One of the key features of the fund that differentiates it from a money market fund or cash deposit account, is that it can hold fixed income securities that have longer maturity dates than the typical 12-month restriction in money market fund. As described above, these notes are floating rate, meaning that the coupon paid on the bond is reset at the end of specified period, generally 3-months. At the maturity date of the bonds, the issuer must go into the market and refinance the debt. With shorter dated bonds, there is better line of sight to whether the issuer will be able to refinance this, while with a longer maturity bond, there is risk that the financial profile (or even the credit profile) of the issuer can change and the issuer may not be able to refinance its debt obligations. For thisuncertainty, investors received higher returns, and to reduce and minimise risk, the Core Income fund issues to high quality credit issuers with a minimum credit rating of above AA (zaf) as demonstrated above. As a result of buying these longer-term bonds, through a conservative and considered investment approach, the fund is able to achieve higher returns than a typical money market fund.

As at 30th June 2021, the weighted average term to final maturity of the fund was 2.7 years and the fund had a duration of 38 days. The maturity profile (term to final maturity) of the assets in the fund at June quarter-end is shown in the table:

| Tenor | Fund Holdings (%) |
|---|---|
| 0-1 YEAR | 24.3% |
| 1-2 YEARS | 13.1% |
| 2-3 YEARS | 21.2% |
| 3-4 YEARS | 14.3% |
| 4-5 YEARS | 19.7% |
| 5-6 YEARS | 5.6% |
| 6-7 YEARS | 1.8% |
| | **100.0%** |

## Market Expectations

Looking ahead, the market expectation is for short-term interest rates to recover from current levels. Key drivers to this interest rate outlook are underpinned by a recovery in the global inflation cycle as well as a narrowing output gap. Slow progress in reducing the debt burden of beleaguered SA State-owned Enterprises (SOEs), the third COVID-19 wave, and increasing global inflation pressures are also expected to exert moderate pressure on yields.

The fund is positioned defensively given inflation concerns and the current uncertain and fragile economic climate. The fund's low duration creates a defensive position which mitigates the impact from rising rates as bond coupon payments will rise with short term interest rate hikes. Taking on longer dated instruments, which are floating rate, allows us to extract higher yield (i.e. term spread vs cash).

## Summary and Conclusion

We remain cognisant of the low spread environment and the current disconnect between pricing and credit fundamentals due to excess market liquidity. With the country being at level 4 lockdown and South Africa at the third COVID-19 wave we remain cautious as the woes around SA's vaccination rollout continues. We have positioned the fund defensively in response to the uncertainties that exist on an economic and policy front. While we look for opportunities, we remain prudent around credit, and we continue to manage the liquidity and maturity risk as efficiently as possible.

# Disclaimer

**WHO WE ARE**
Nedgroup Collective Investments (RF) Proprietary Limited is an authorised Collective Investment Scheme and the representative of Nedgroup Investments Funds PLC in terms of the Collective Investment Schemes Control Act. It is a member of the Association of Savings & Investment South Africa (ASISA)..

OUR TRUSTEE
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**HOW ARE OUR FUNDS PRICED**
Funds are valued daily at 15:00. Instructions must reach us before 14:00 (12:00 for Nedgroup Money Market Fund) to ensure same day value. Prices are published daily on our website and in selected major newspapers.

**FEES**
A schedule of fees and charges is available on request from Nedgroup Investments. One can also obtain additional information on Nedgroup Investments products on our website.

**DISCLAIMER**

Unit trusts are generally medium to long-term investments. The value of your investment may go down as well as up. Past performance is not necessarily a guide to future performance. Nedgroup Investments does not guarantee the performance of your investment and even if forecasts about the expected future performance are included you will carry the investment and market risk, which includes the possibility of losing capital. Our funds are traded at ruling prices and can engage in borrowing and scrip lending.

Some funds may hold foreign securities including foreign CIS funds. As a result, the fund may face material risks, which could include foreign exchange risks, market conditions and macro-economic and political conditions.

A fund of funds may only invest in other funds, and a feeder fund may only invest in another single fund, both will have funds that levy their own charges, which could result in a higher fee structure.

The Nedgroup Investments Money Market Fund offering aims to maintain a constant price of 100 cents per unit. A money market fund is not a bank deposit. The total return to the investor is made up of interest received and any gain or loss made on any particular instrument held. In most cases the return will merely have the effect of increasing or decreasing the daily yield, but in an extreme case it can have the effect of a capital loss. Excessive withdrawals from the fund may place the fund under liquidity pressures and that in such circumstances a process of ring-fencing of withdrawal instructions and managed pay-outs over time may be followed. The yield is calculated using an annualised seven day rolling average as at the relevant dates provided for in the fund fact sheet. Nedgroup Investments has the right to close its funds to new investors in order to manage it more efficiently.

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