AYLETT EQUITY PRESCIENT FUND
Q1 2024 COMMENTARY

Aylett [&Co] Fund Managers

FUND MANAGER COMMENTARY

MARKET REVIEW

For the quarter ended March 2024, the JSE ALSI declined 2.2%, the ALBI was down 1.83% and cash returned a positive 2%. The South African equity market materially underperformed the ACWI Global Index, which climbed 12.2% in ZAR for the quarter. Over the same period, the rand weakened, starting the period at R18.36/$ and finishing at R18.88/$.

FUND PERFORMANCE

The fund was down 1.5% for the quarter, outperforming its benchmark by 0.7%. Positive contribution to the performance was driven by the offshore holdings in the fund, namely Rubis, Bath & Body Works, Berkshire Hathaway, British American Tobacco, and Spirit Aerosystems. The detractors were Remgro, Sabre, BHP, AECI, and Standard Bank.

OUTLOOK

In our last quarterly commentary, we said that we felt the market was underestimating the normalised level of long-term inflation in the developed world. Our view is increasingly becoming consensus, with the number and total quantum of interest rate cuts expected now greatly reduced from three months ago, with a minority now even calling for rate hikes. Trying to predict interest rates is a fool's errand and not what we do, but we continue to believe the world, particularly the developed world, will have to get used to higher long-run normal interest rates. This has profound implications for those owning highly valued, long-duration assets.

The outperformance of the US equity markets has been driven by just a few large listed technology companies. Market expectations are high, fuelled by the promise of artificial intelligence. We have no dog in this particular hunt but would be wary of disappointment from both the technology itself and the companies' share prices, which seem to us to be priced for perfection. Higher interest rates will not help.

This quarter saw a marked divergence in performance between the South African exposed and offshore exposed constituents of the portfolio. As a result, the discount to fair value on the offshore portfolio has closed while the discount locally has widened. It is no surprise, therefore, that we sold more than we bought offshore with the reverse true locally. South Africa continues to screen very cheaply, almost as cheap as it has ever been. We could easily fill the portfolio with attractively priced South African shares but are mindful of the risk inherent in deploying capital locally (see past quarterlies for our thinking on this topic).

At the end of the quarter, 30% of the fund comprised of "SA Inc." vs. 28% at the start. We know the South African businesses we own in the fund well; they are run by competent management and have been bought at low prices. This 30% of the fund in South Africa presents an attractive balance between valuation and risk. We note the steady drumbeat of hydrocarbon discovery news off our coast and that of our neighbours. Many of the global energy majors are devoting a material amount of their exploration budgets to our waters, and it seems increasingly likely that they have found one of (if not the) world's next major resources off the Namibian coastline. Although it's early days, this may become a much-needed tailwind for the region.

The South African general election will be held during the upcoming quarter, and we expect the run-up to the 29th of May 2024 to be very noisy. South African equities are generally priced for very negative outcomes, but even an "okay" election result may be warmly received by the capital markets.

At quarter end, the fund was just over 96% invested, which is on the high side versus history and indicative of the current value we see in the market. The fund's combined discount to fair value is unchanged from three months ago, continuing to offer a lot of latent value. We remain optimistic about the long-term expected returns from the fund.

As always, we thank you for the trust you place in us.

Justin Ritchie

31 March 2024

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