Sanlam

Sanlam Corporate: Investments

Protection Strategies

Investment Report

Quarter 2 2023

Insurance | Financial Planning | Retirement | Investments | Wealth

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Overview

In order to cater for divergent client preferences, the trustees of the **Sanlam Umbrella Fund** have approved the three **protection strategies** that can be chosen as a default investment strategy at participating employer level depending on the required investment objectives and product option. These strategies provide different levels of guarantees and smoothing of investment returns for our clients.

The protection strategies consist of 3 options which members can invest in. (1) Sanlam Secure Strategy which invests 100% in the *Sanlam Monthly Bonus Fund*, (2) Sanlam Stable Strategy which invest 100% in *Sanlam Stable Bonus Portfolio*, and the (3) Volatility Protection Strategy which invest 75% in *Sanlam Monthly Bonus Fund* and 25% in *Satrix Enhanced Balanced tracker Fund*

Protection Strategies Portfolios

Sanlam Secure Strategy

The trustees have approved an alternative default investment strategy suitable for members who wish to achieve inflation-beating real returns over the medium to long term, but who are particularly concerned against significant short-terms investment losses.

The strategy will most likely result in lower returns than the Lifestage Strategies over the long term as a consequence or the implicit cost the underlying guarantees and lower effective equity exposure. Nonetheless, the trustees recognise that such a strategy is suitable for many members – particularly those members who are not financially sophisticated and who might not appreciate that a high equity exposure inevitably implies some risk of capital loss over the short-term.

The strategy could be considered by investors preferring a cautious approach to money management; investors who require capital security and investors who regard financial security as highly important. The strategy currently invests all contributions in the Sanlam Monthly Bonus Fund which declares fully vesting bonuses with full guarantees.

Sanlam Stable Strategy

The trustees have approved an alternative default investment strategy, suitable for members who wish to have exposure to the financial markets, while protecting themselves against adverse movements in the markets.

This is achieved by smoothing the returns over time, and guaranteeing (for resignation, retirement, death, retrenchment and disability events) the net contributions invested together with the vested bonuses.

Non-vested bonuses are also declared on top of that. These can be removed in very extreme circumstances though this has never yet occurred since the portfolio's commencement in 1986.

The strategy could be considered by investors preferring a cautious, arm's-length approach to money management; investors wishing to avoid any chance of losing money; investors who require capital security and investors who regard financial security as highly important. The strategy currently invests all contributions in the Sanlam Stable Bonus Portfolio.

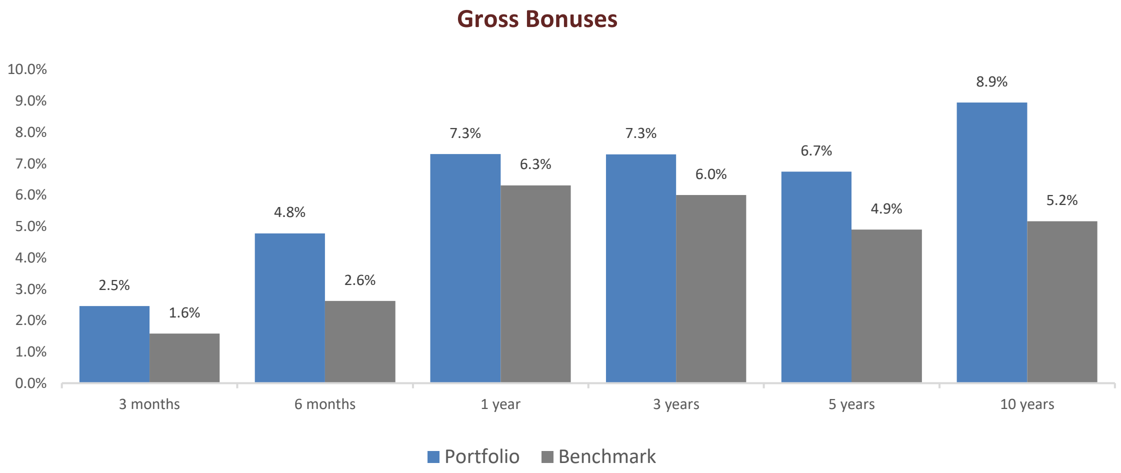
Volatility Protection Strategy

The default investment strategy is suitable for members who wish to achieve inflation-beating real returns over the medium to long term, but who are particularly concerned about protecting against significant short-term investment losses.

The strategy will most likely result in lower returns than the four Lifestage strategies over the long term as a consequence of the implicit cost of the underlying guarantees and lower effective equity exposure. Nonetheless, the trustees recognise that such a strategy is suitable for many members – particularly those members who are not financially sophisticated and who might not appreciate that a high equity exposure inevitably implies some risk of capital loss over the short-term.

The trustees review the investment strategy of the Volatility Protection Strategy continually and will make periodic changes to the underlying investments in line with the objectives of the strategy. The Volatility Protection Strategy aims to invest 75% in the Sanlam Monthly Bonus Fund and 25% in the Satrix Enhanced Balanced Tracker Fund.

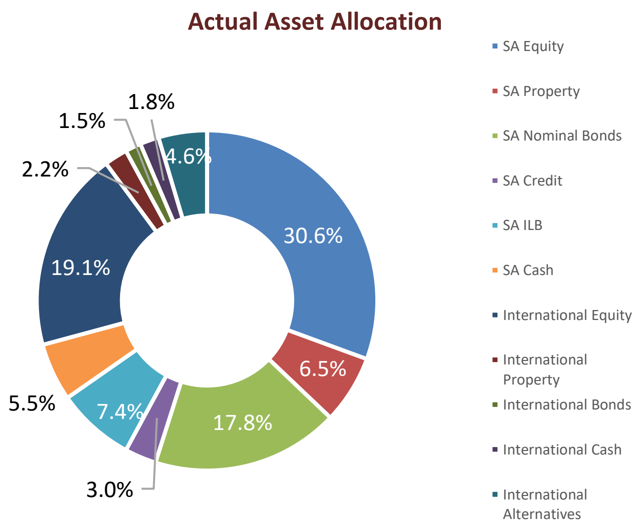
Sanlam Secure Strategy
Sanlam Monthly Bonus Fund

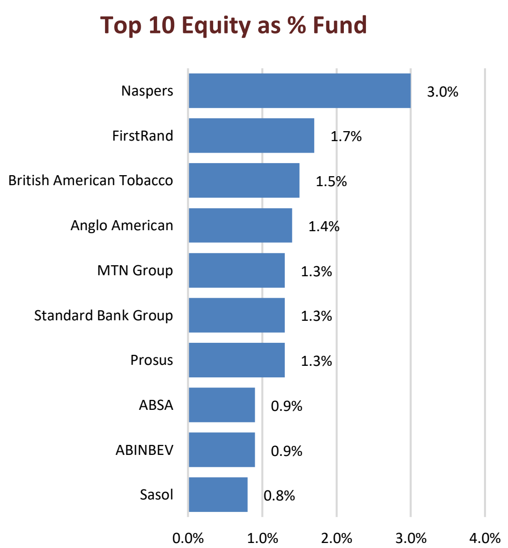


The Sanlam Monthly Bonus Fund returned 2.5% for the quarter and 7.3% for the one year ended 30 June 2023.

The portfolio consistently outperformed inflation over all periods,. The returns over the last 10 years have exceeded inflation by 3.8% p.a. Under this product, Sanlam can never remove or reduce any of the monthly bonuses once declared.

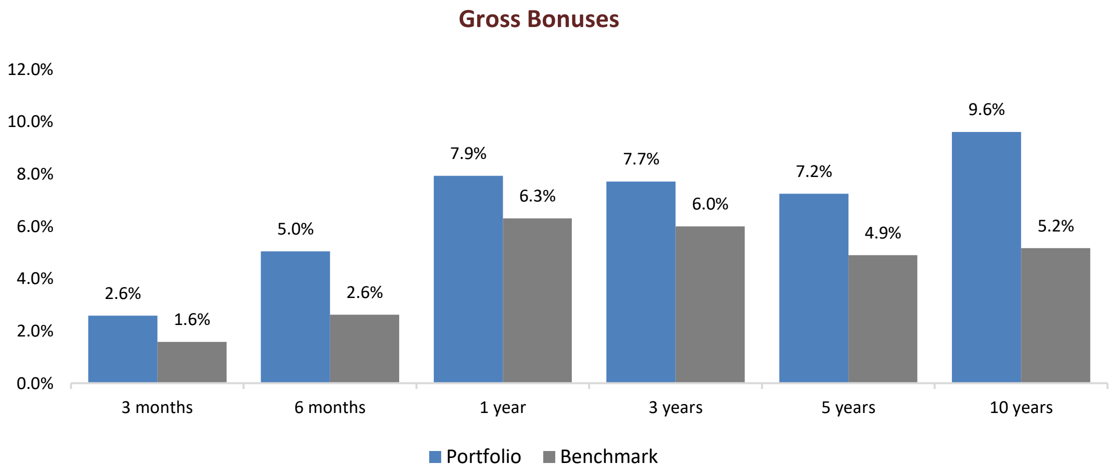
*Inflation is lagged by one month





Looking at the current composition of the portfolio, the overweight positions are SA ILBs, International Cash, SA Equity. The portfolio had a neutral position in SA Property. The underweight positions in the portfolio are SA Cash, SA Nominal Bonds, SA Credit, International Bonds, International Alternatives, International Equity and International Property.

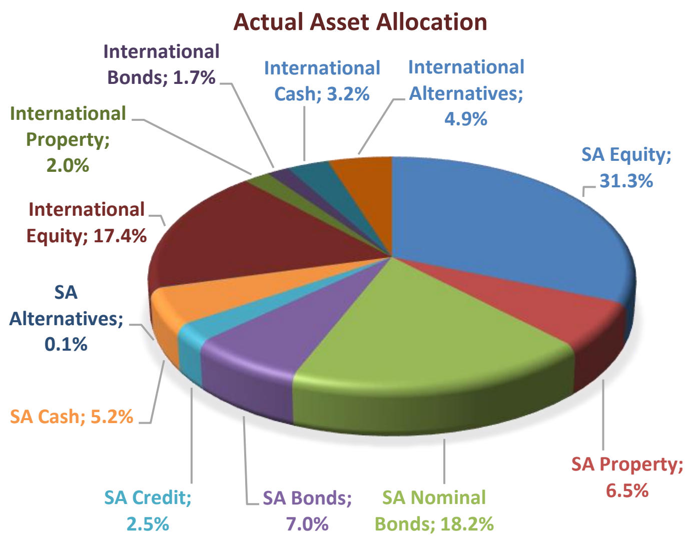
Sanlam Stable Strategy
Sanlam Stable Bonus Portfolio

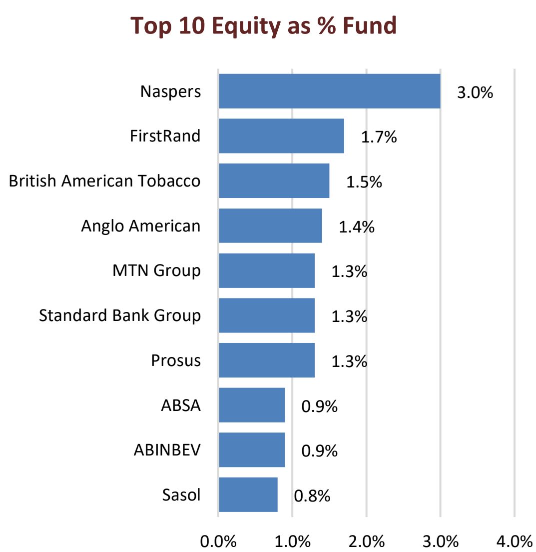


The Sanlam Stable Bonus Portfolio returned 2.6% for the quarter ended 30 June 2023 and a return of 7.9% for the year. Ended 30 June 2023. Over the long term, the portfolio also posted strong inflation beating returns.

Sanlam Stable Strategy provides monthly bonuses, roughly half of which is vesting and half non-vesting. In an extreme market downturn Sanlam may remove some of the accumulated non-vested bonuses, although we have not done so since launching the underlying portfolio in 1986. This strategy provided a real return of 4.7% p.a. over the last 10 years, with very stable and predictable returns over the period.

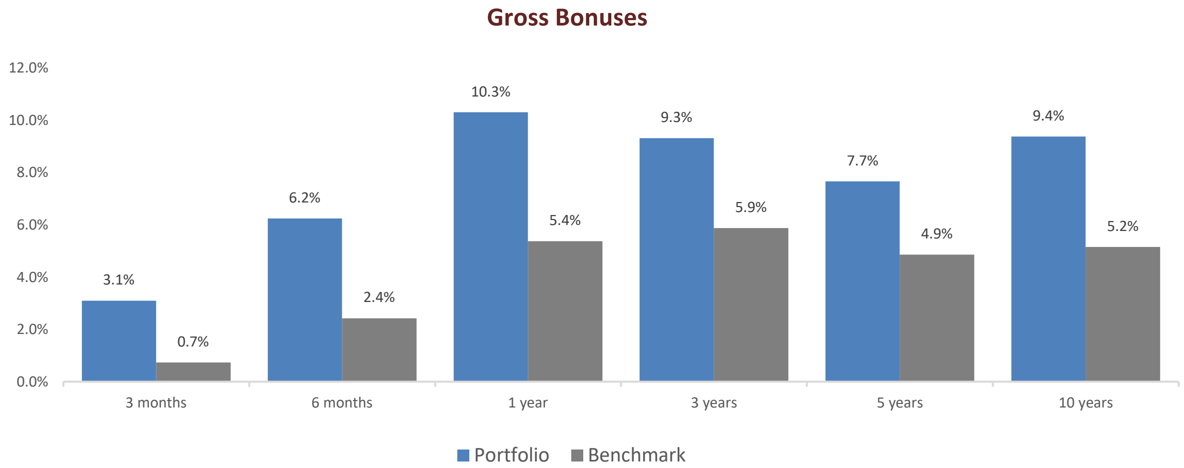
*Inflation is lagged by one month





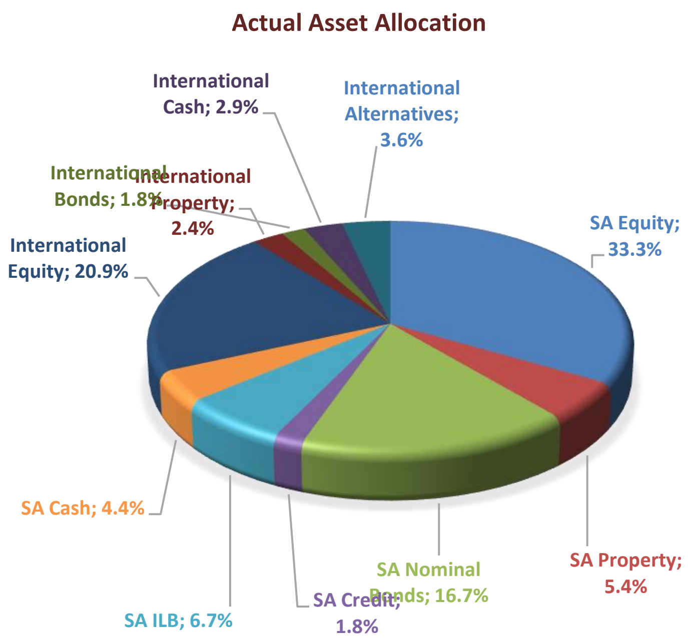
Looking at the current composition of the portfolio, the overweight positions are SA Alternatives, International Equity, SA ILBs and International Cash. The portfolio is neutral in SA Nominal Bonds and underweight in all the other asset classes.

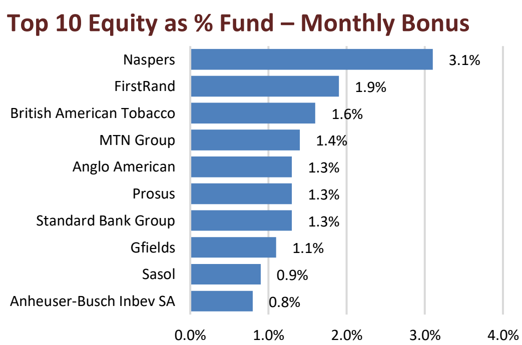
Volatility Protection Strategy

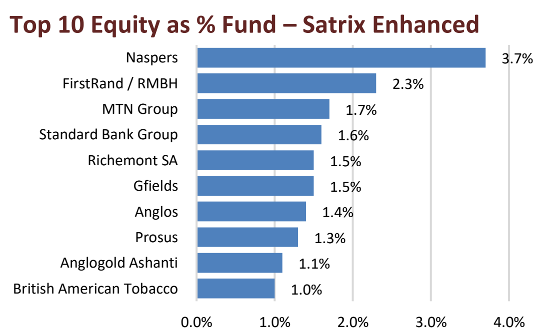


The Volatility Protection Strategy returned 3.1% for the quarter and 10.3% for the one year ended 30 June 2023.

The Volatility Protection Strategy has given a similar return to the Sanlam Secure Strategy over the last 10 years, but with a bit more volatility. This is due to the strategy since 2017 having a 25% exposure to the Satrix Enhanced Balanced Tracker fund, which is an aggressive passive portfolio. This passive component can add extra returns when markets are strong but, can lead to the strategy having occasional negative returns. It is important to note that the Volatility Protection Strategy does not provide a capital guarantee but provides returns which are far less volatile that a normal balanced fund.







The trustees review the investment strategy of the Volatility Protection Strategy continually and will make periodic changes to the underlying investments in line with the objectives of the strategy. The Volatility Protection Strategy aims to invest 75% in the Sanlam Monthly Bonus Fund and 25% in the Satrix Enhanced Balanced Tracker Fund.

Performance summary

30 June 2023	3 Months	6 months	1 year	3 years	5 years	10 years
Sanlam Secure Strategy						
Sanlam Monthly Bonus Fund	2.5%	4.8%	7.3%	7.3%	6.7%	8.9%
CPI*	1.6%	2.6%	6.3%	6.0%	4.9%	5.2%
Sanlam Stable Strategy						
Sanlam Stable Bonus Portfolio	2.6%	5.0%	7.9%	7.7%	7.2%	9.6%
CPI*	1.6%	2.6%	6.3%	6.0%	4.9%	5.2%
Volatility Protection Strategy						
Volatility Protection Strategy	3.1%	6.2%	10.3%	9.3%	7.7%	9.4%
Benchmark	1.6%	2.6%	6.3%	6.0%	4.9%	5.2%

**CPI figures are calculated to end of May 2023*
Benchmark used for Volatility Protection Strategy is 75% of Inflation and 25% of the Composite Benchmark for Satrix Enhanced Balanced Tracker Fund.

Macroeconomic commentary

Highlights

Global

- US Q1 GDP revised higher to 2% on robust consumption expenditure
- Eurozone enters technical recession following downward revision to Q1 GDP
- China's State Council announces financial support for property developers, tax exemptions on electric EVs and tax breaks for high-end manufacturers
- US Democrats and Republicans reach agreement on two-year debt limit suspension
- US Fed pauses on rate hikes; ECB raises rate 25 basis points and the BOE 50 basis points
- China imposes export restrictions on semiconductor manufacturing metals

Local

- SA avoids technical recession, expanding 0.4% q/q in Q1
- SA bonds rebound as threat of secondary sanctions subsides
- SARB leading economic indicator declines further, signaling slower growth
- ABSA and S&P Global PMIs still in contractionary territory

Global economics

Global Equities

Global equities rallied strongly in the second quarter of the year, supported by positive economic factors such as upward revisions to US Q1 GDP growth, a surge in consumer confidence, and robust services sector performance. For the quarter ended 30 June 2023, the MSCI All Country World Index gained 13.1% in rand terms, outperforming the emerging markets as measured by the MSCI Emerging Markets Equities which returned 9.3% in rand terms. The South African equities underperformed both developed and emerging markets due to a 6.1=5% depreciation in the rand/US dollar exchange rate. The FTSE/JSE All Share Index gained a modest 0.7% in rands, with resources being the major drag on performance (-6.1%). Precious metals counters experienced significant declines, while consumer discretionary and financial stocks showed positive momentum. However, the sector derated over the quarter, and the price-to-book ratio declined. The positive market mood was driven by the suspension of the US debt ceiling, better-than-expected retail - sales, and the US Fed's decision to pause raising interest rates. Inflation measures were favorable. Additionally, China's stimulus measures aimed at countering deflation provided support. Despite the upbeat data, global growth momentum slowed raising concerns about a potential recession. Forward earnings estimates declined, and valuations became stretched, warranting caution for risk assets. The impact of export controls on semiconductor equipment between major economies and rising interest rates poses risks to equity markets.

Global Bonds

In the second quarter, concerns about a potential US debt default and hawkish actions by central banks, including the US Federal Reserve, the European Central Bank (ECB), and the Bank of England (BOE), led to higher bond yields. The Bloomberg Global Aggregate Bond Index saw its yield increase to 3.84% from 3.54%. Global bonds returned 4.8% in rands. However, corporate bonds outperformed sovereign bonds, and high-yield credit performed well. .

Global Listed Property

In the second quarter, the global listed property sector faced challenges due to the rise in global bond yields. The FTSE EPRA/NAREIT Developed Dividend+ returned a modest 0.5% in US dollars and 6.3% in rands. Concerns about rising office vacancies and retailer bankruptcies weighed on the sector throughout the quarter. Despite attractive valuations, the sector derated, and the price-to-book ratio declined to 1.21X from 1.22X, still below the historical mean of 1.46X. Another risk is the potential for stranded assets resulting from the transition to a green economy, as 'greenifying' old buildings could be costly and impact net asset value.

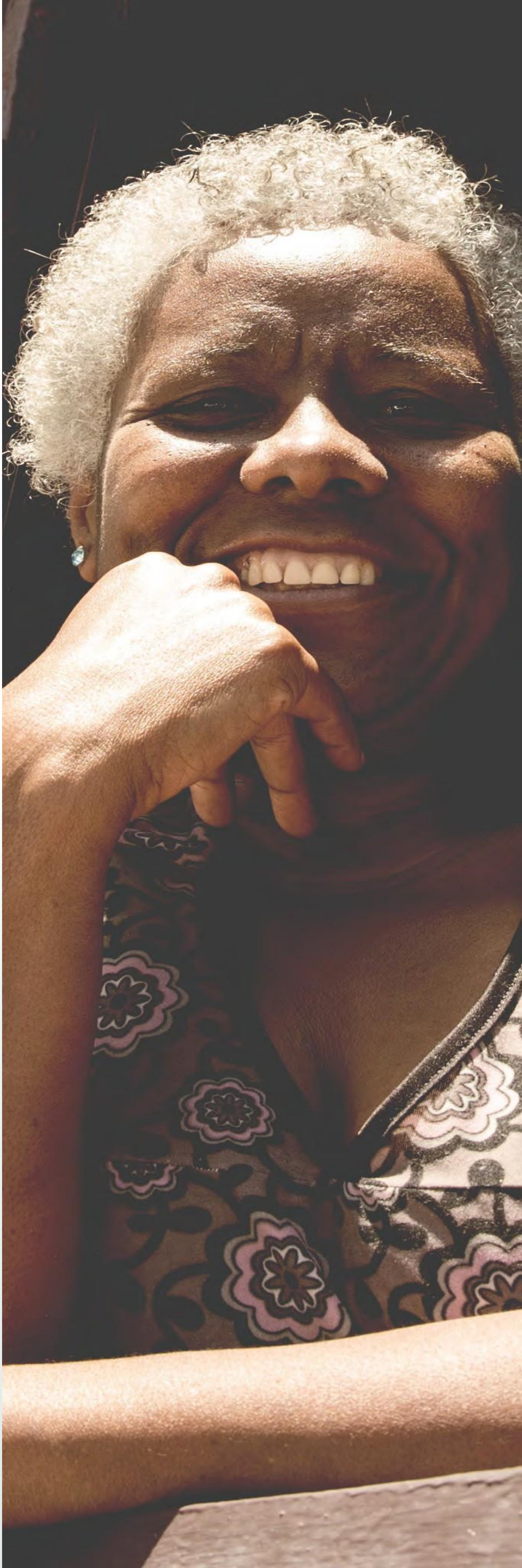
Local economics

Local Equities

In the second quarter, South African equities underperformed both developed and emerging markets due to a 6.1% depreciation in the rand/US dollar exchange rate. The FTSE/JSE All Share Index gained a modest 0.7% in rands but declined by -5.5% in US dollars, with resources sector being the major drag on performance. Precious metals counters experienced significant declines, while consumer discretionary and financial stocks showed positive momentum. However, the sector derated over the quarter, and the price-to-book ratio declined. The forward price-to-earnings ratio for the ALSI and the MSCI SA Index increased, but the earnings growth outlook is expected to soften, especially for large cap rand hedge counters. The valuation gap between trailing earnings and market price may narrow due to rand appreciation, reducing investor interest in domestic equities. The SA Inc complex is highly dependent on domestic economic growth, which is expected to remain flat or soften over the coming year.

Local Bonds

In the second quarter, South African bonds were the worst-performing asset class, affected by escalating political tensions between SA and the US over its non-aligned stance with Russia. A thawing in the standoff in June, following a proposed change in venue for the upcoming BRICs summit to China, saw bond yields decline, partially reversing May's losses. However, political risks resurfaced in July, leading to a repricing of risks and higher bond yields. Despite a disinflationary trend, risks to the inflation outlook remain, including a weaker rand and inflationary effects from load shedding. The budget deficit is tracking higher than expected, impacting the fiscal outlook.



Local Listed Property

The domestic listed property asset class faced challenges in the second quarter, as the increase in bond yields functioned as a headwind. Returns were subdued at 0.7% in rands and -5.5% in US dollars . Despite a slight decline in dividends per share, the property sector became more expensive compared to the 10-year bond, with the property-to-bond yield ratio declining below the long-term mean. Several factors, such as potential increases in commercial rates and taxes, the risk of stranded assets in central business districts, higher stages of load shedding, and possible further rate hikes, are expected to constrain rental escalations and resets in the sector over the coming year. Due to return expectations lagging other asset classes, an underweight position is retained in listed property. Some of the biggest gainers in the sector included Sirius Real Estate, Fortress B, and Fortress A, while the losers included Equites Equity Fund, Emira, and Growthpoint.

Summary

Over the second quarter, economic surprises extended growth momentum and supported the risk-on trade, pushing out the anticipated recession further in time. Global equities outperformed defensive assets, driven by positive economic indicators and better-than-expected GDP growth in the US and China. Emerging market returns lagged due to the trade war's impact on the Hang Seng Index. South African assets underperformed due to the sharp depreciation of the rand, influenced by the diplomatic standoff with the US over its stance on Russia. Developed market central bankers are nearing the peak of their interest rate cycles, with inflation expected to decline, leading to optimism in markets. A soft landing for the global economy is anticipated, with the US recession now likely only in 2024, as higher interest rates eventually reduce consumption expenditure.

Market performance summary (in ZAR) to 30 June 2023

		3 months	6 months	1 year	3 years	5 years	10 years
Local	Equities (All Share Index)	0.7%	5.9%	19.6%	16.1%	9.6%	10.3%
	Equities (Capped SWIX)	1.2%	3.6%	13.5%	15.7%	6.9%	8.5%
	Property	0.7%	-4.4%	10.0%	11.3%	-3.5%	1.5%
	Nominal Bonds	-1.5%	1.8%	8.2%	7.6%	7.4%	7.4%
	Inflation Linked Bonds	-0.8%	0.0%	1.1%	8.7%	5.3%	5.3%
	Cash	1.9%	3.7%	6.8%	5.0%	5.8%	6.3%
International	Equities (MSCI ACWI)	13.1%	26.5%	34.4%	14.1%	15.3%	16.0%
	Equities (MSCI EM)	9.3%	18.5%	19.5%	5.9%	8.0%	10.4%
	Bonds	4.8%	12.6%	13.8%	-2.3%	5.5%	6.9%
	Property	6.3%	11.4%	8.7%	6.1%	6.4%	10.0%
	Rand vs US Dollar	6.5%	11.0%	15.3%	2.8%	6.6%	6.6%
Equity Sector	Financials	5.3%	5.0%	13.6%	19.7%	3.5%	7.5%
	Resources	-6.1%	-10.5%	3.0%	13.9%	15.0%	9.2%
	Industrials	3.4%	17.5%	34.2%	14.5%	8.5%	10.2%
Size	Small Cap	0.5%	1.3%	10.8%	29.8%	8.5%	9.0%
	Medium Cap	-0.2%	-1.2%	7.5%	14.2%	5.3%	6.8%
	Large Cap	0.9%	7.2%	22.2%	16.3%	10.3%	10.8%

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