



Sanlam Corporate: Investments

Sanlam Umbrella Fund Protection Strategies

Investment Report

**Quarter 4 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-term investment losses.

The strategy will most likely result in lower returns than the 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 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.

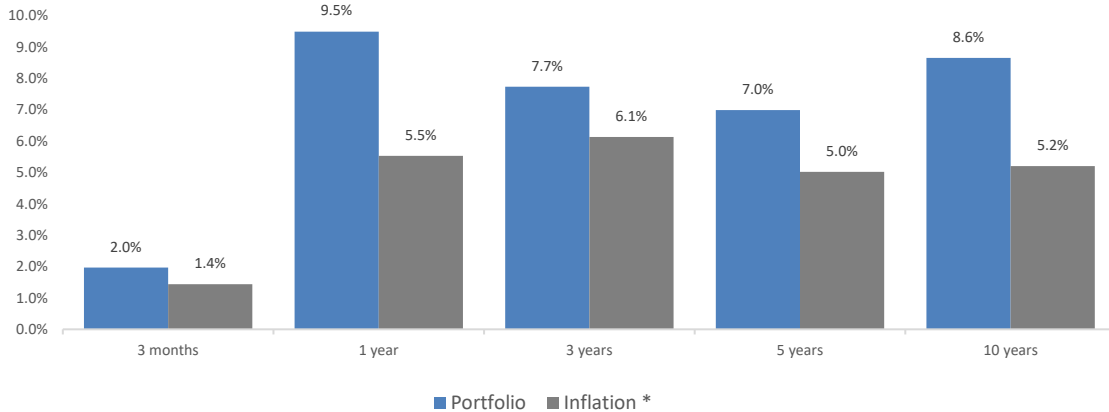
The strategy will most likely result in lower returns than the four Lifestage strategies over the long term as a consequence of the implicit cost of the underlying guarantees and lower effective equity exposure. Nonetheless, the trustees recognise that such a strategy is suitable for many members – particularly 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

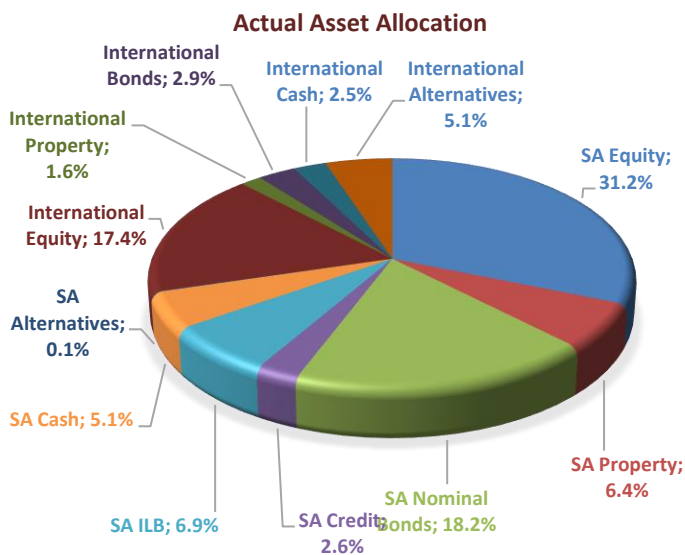
Gross Bonuses as at 31 December 2023



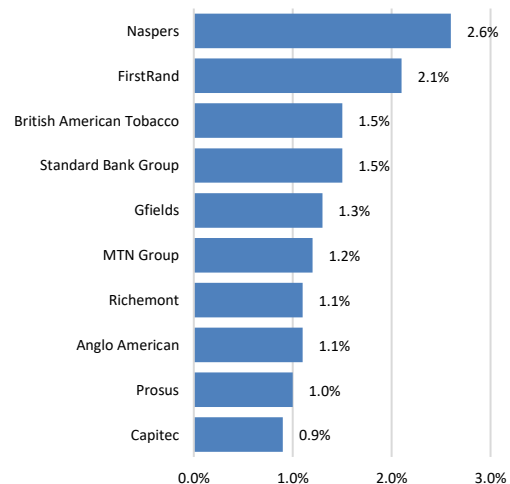
The Sanlam Monthly Bonus Fund returned 2.0% for the quarter and 9.5% for the one year ended 31 December 2023.

The portfolio consistently outperformed inflation over all periods. The returns over the last decade have exceeded inflation by over 3.0% p.a. For this portfolio, Sanlam can never remove or reduce any of the monthly bonuses once declared.

\*Inflation is lagged by one month



Top 10 Equity as % Fund

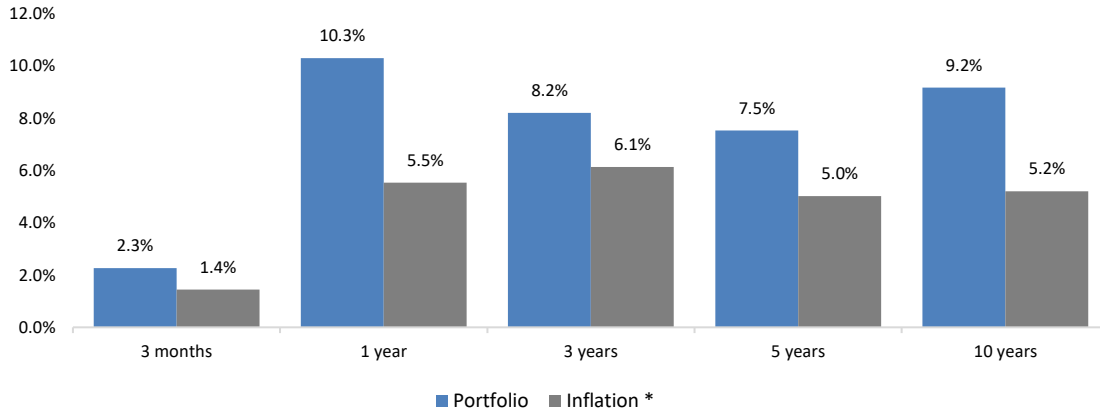


Examining the portfolio composition as of December 2023, there were overweight positions in SA ILBs, International Cash, SA Equity, SA Nominal Bonds, International Bonds, and International Alternatives. Conversely, the portfolio maintained underweight positions in all other asset classes, including International Equity, SA Alternatives, SA Cash, SA Credit, International Property, and SA Property.

# Sanlam Stable Strategy

## Sanlam Stable Bonus Portfolio

Gross Bonuses as at 31 December 2023

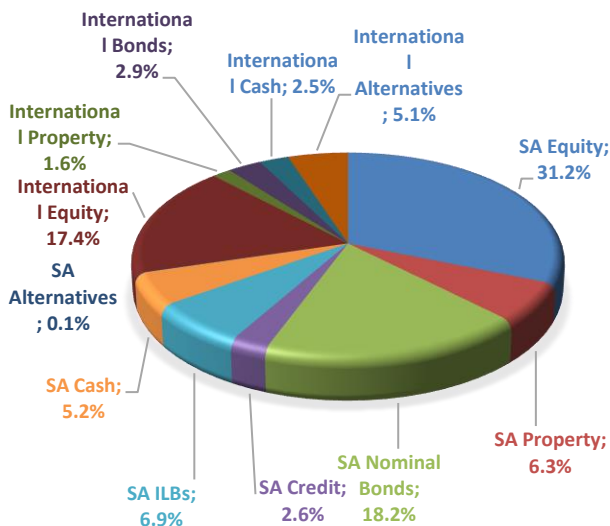


The Sanlam Stable Bonus Portfolio returned 2.3% for the quarter ended 31 December 2023 and a return of 10.3% for the year. Over the long term, the portfolio posted strong inflation beating returns.

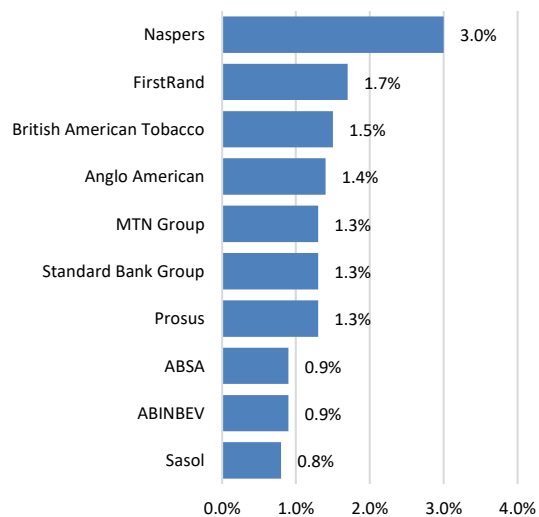
The Sanlam Stable Strategy provides monthly bonuses, roughly half of which is vesting and half non-vesting. In an extreme market downturn Sanlam may remove some of the accumulated non-vested bonuses, although we have not done so since launching the underlying portfolio in 1986. This strategy provided real returns of 4.0% p.a. over the last 10 years, with very stable and predictable returns over the period.

\*Inflation is lagged by one month

Actual Asset Allocation



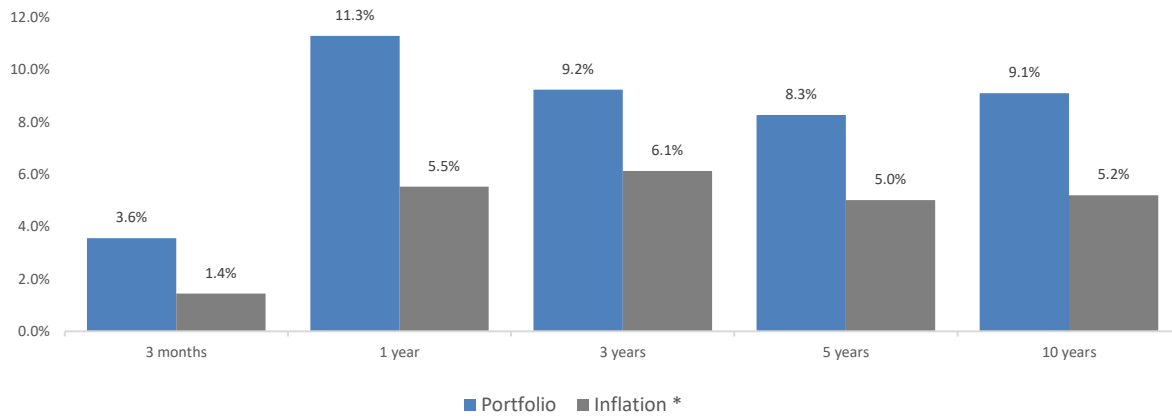
Top 10 Equity as % Fund



Looking at the current composition of the portfolio, the overweight positions are SA ILBs, International Cash, SA Equity, SA Nominal Bonds, International Bonds, and International Alternatives. The underweight positions in the portfolio are International Equity, SA Alternatives, SA Credit, SA Cash, International Property and SA Property. SA Property, SA Inflation-Linked Bonds, Foreign Equity and Foreign Property.

# Volatility Protection Strategy

## Gross Bonuses

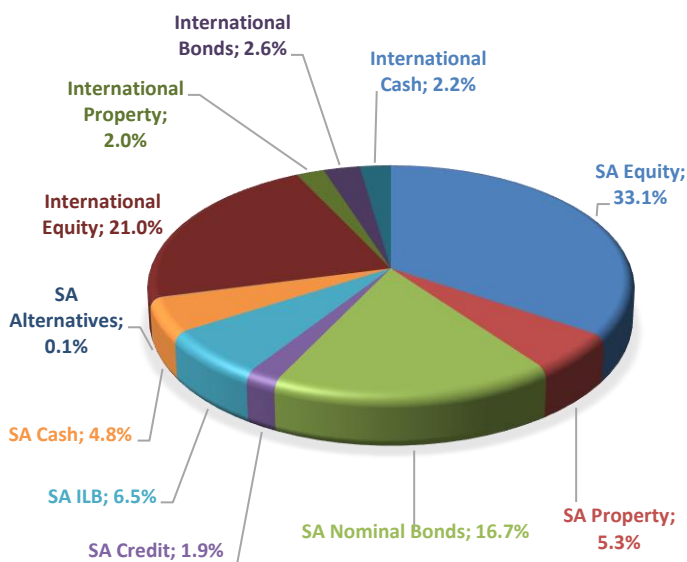


The Volatility Protection Strategy returned 3.6% for the quarter and 11.3% for one year ended 31 December 2023.

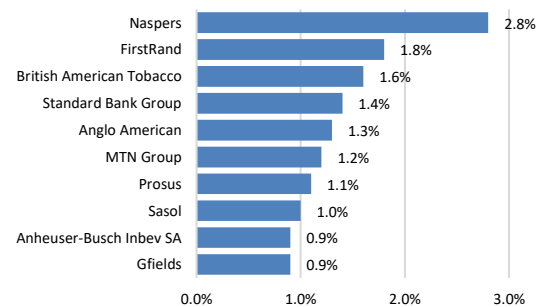
The Volatility Protection Strategy has given a similar return to the Sanlam Secure Strategy over the last 10 years, but with a bit more volatility. This is due to the strategy since 2017 having a 25% exposure to the Satrix Enhanced Balanced Tracker fund, which is an aggressive passive portfolio. This 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 than a normal balanced fund.

\*Inflation is lagged by one month

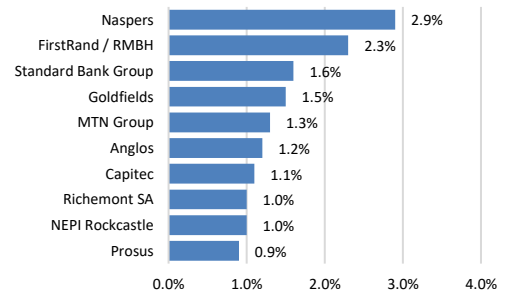
## Actual Asset Allocation



## Top 10 Equity as % Fund – Monthly Bonus



## Top 10 Equity as % Fund – Satrix Enhanced



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

31 December 2023	3 Months	6 months	1 year	3 years	5 years	10 years
<b>Sanlam Secure Strategy</b>						
<b>Sanlam Monthly Bonus Fund</b>	3.6%	4.8%	11.3%	9.2%	8.3%	9.1%
<b>CPI*</b>	1.4%	2.8%	5.5%	6.1%	5.0%	5.2%
<b>Sanlam Stable Strategy</b>						
<b>Sanlam Stable Bonus Portfolio</b>	2.0%	4.5%	9.5%	7.7%	7.0%	8.6%
<b>CPI*</b>	1.4%	2.8%	5.5%	6.1%	5.0%	5.2%
<b>Volatility Protection Strategy</b>						
<b>Volatility Protection Strategy</b>	2.3%	5.0%	10.3%	8.2%	7.5%	9.2%
<b>CPI*</b>	1.4%	2.8%	5.5%	6.1%	5.0%	5.2%

\*CPI figures are lagged by one month

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

- ▶ FOMC leaves rates unchanged, signals a pivot in 2024.
- ▶ US Fed's dot-plot points to three rate cuts in 2024 but fed fund futures price in more aggressive cuts.
- ▶ Red Sea commercial shipping attacks risk renewed supply-side cost pressures.
- ▶ Israel/Hamas conflict risks higher oil prices despite non-OPEC+ production.
- ▶ China's clampdown on gaming triggers sharp sell-off in Tencent

### Local

- ▶ SA's Q3 GDP contracts by 0.2% quarter-on-quarter and 0.7% year-on-year
- ▶ Load shedding remained a bind on growth despite positive contribution by the energy sector.
- ▶ Local listed property was the best performing broad asset class for quarter 3 2023.

## Global economics

### Global Equities

After a sharp decline in the third quarter, global equities rebounded in the fourth quarter, propelled by a dovish stance from the US Federal Reserve signaling the end of the rate hiking cycle. The positive sentiment was reinforced by a drop in the University of Michigan's one-year inflation forecast from 4.3% to 3.1%. Despite the Fed's dot-plot indicating a cumulative 75 basis points of rate cuts in 2024, the market's pricing is more aggressive, anticipating 150 basis points of rate cuts with the first cut expected in May. Potential deferral of rate cuts until later in the year, coupled with a tight labor market and persistent wage inflation, could pose challenges for equities. Additional risks include supply-side pressures from Houthi attacks rerouting shipping and the EU's withdrawal of energy subsidies, impacting inflation.

Investor optimism about the interest rate outlook, fueled by generally beating inflation estimates, led to lower nominal and inflation-linked bond yields.

The bull curve steepening reflects the market's consensus view of a soft-landing scenario for the US economy, supported by the World Bank's forecast of global growth slowing to 2.4% in the current year. The MSCI ACWI gained 7.8% for the quarter, while emerging market equities underperformed due to negative returns from Chinese stocks, influenced by ongoing deflation, oversupply, and regulatory restrictions on online gaming. The unpredictability of the Chinese regulator raises concerns about China's investability. Despite a rebound in equity markets, stretched valuations, geopolitical risks, and uncertainty about rate cuts suggest a near-term underweight position for equities, followed by a medium-term neutral weighting.

### Global Bonds

Global bonds experienced a rally following the US Federal Reserve's shift in interest rates, leading to a decrease in both nominal and inflation-linked bond curves. The Bloomberg Capital Global Aggregate Bond Index yielded 8.1% in dollars and 4.9% in rands, with yields dropping from 4.2% to 3.5% in the quarter. Similar returns were observed in emerging market bonds as spreads narrowed from 316 basis points to 297 basis points.

Inflation-linked bonds also rallied, with the Bloomberg Capital Global Government Inflation-Linked Bond Index yielding 8.1% in dollars as real yields decreased from 1.7% to 1.2%. Despite the expectation of continued disinflation, there are potential upside risks later in the year due to low base effects. December's US inflation data, released in January, indicated higher-than-expected core and headline inflation.

However, certain risks exist, including the possibility of a broader Israeli/Hamas conflict impacting oil prices, which could affect the positive outlook for rates. Higher-for-longer interest rates pose a risk to economic growth, and rising supply chain cost pressures are evident due to Houthi attacks on commercial shipping in the Red Sea. Insurers' reluctance to cover US and UK ships in the Red Sea has prompted rerouting via SA, contributing to increased freight rates.

Despite these challenges, the rate hiking cycle seems to be over, with the neutral rate of interest significantly lower than current policy rates in the US and EU. Given US inflation at 3.1%, assuming a 0.5% real neutral rate implies an implied long-term fed funds rate of around 3.6%. In the EU, with a real neutral rate closer to 0%, the implied policy rate is around 2.9%, much lower than the current refinancing rate of 4.5%.

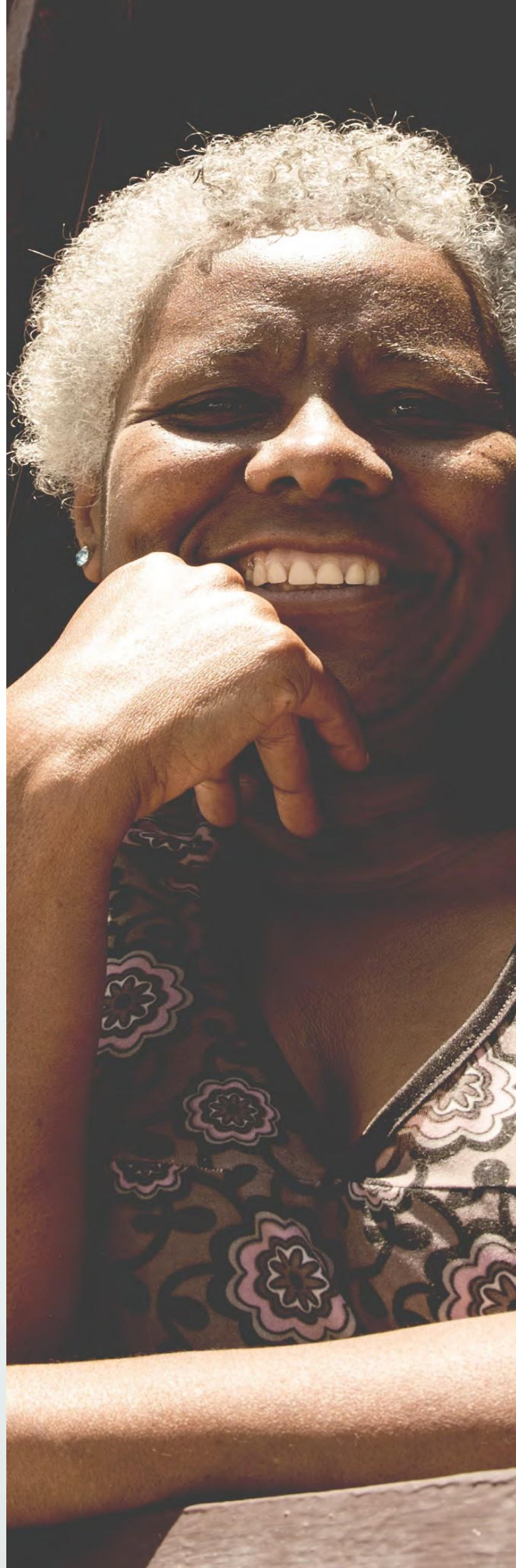
## Global Listed Property

Global listed property experienced a surge in the quarter, driven by lower bond yields and a dovish shift from the US Federal Reserve. The FTSE EPRA Nareit Developed Markets Property Index showed strong returns, with a quarterly yield 12.0% in rands. The annual gains reached 17.0% in rands. The sector's rerating was evident, with the price-to-book ratio rising from 1.15X to 1.32X, still below the historical mean of 1.46X. Despite the recent rally, real estate investment trusts (REITs) offer value, trading at an 11% discount to net asset value with an attractive dividend yield of about 4.3%. Lower funding costs are expected to aid in refinancing loans and deleveraging, with the sector recommended for overweight positioning in the second half of the year as the rate-cutting cycle begins.

## Local economics

### Local Equities

Despite the third quarter's disappointing GDP contraction of -0.2% quarter-on-quarter, the fourth quarter saw a positive market trend. The FTSE/JSE All Share Index gained 6.9% in rands, outperforming the emerging markets composite index which returned 0.8% for the same period. The rally was driven by SA Inc. sectors, particularly mid and small-cap stocks, reflecting the market's anticipation of rate cuts in 2024. Financials led gains, followed by consumer discretionary, healthcare, and defensive consumer staples.





Industrial and technology sectors also showed positive momentum, while basic materials, specifically industrial metals and mining, faced challenges due to Chinese growth concerns. Precious metals, however, surged.

The GDP contraction in Q3 was attributed to declines in household consumption and gross fixed capital formation, with machinery, transport equipment, and construction contributing to the latter. Production declines in mining, manufacturing, and a significant contraction in agricultural output also influenced economic performance. Electricity supply and demand issues persist, despite the positive contribution from the electricity sector following five consecutive quarters of declines.

The 2023 Integrated Energy Plan revealed a continued electricity deficit until 2030, with reduced emphasis on renewable energy. Factors include delayed decommissioning of coal-fired power stations, lower demand forecasts, and a shift from the previous plan's allocations. Expectations for modest economic growth in 2024 are reflected in upwardly revised consensus earnings estimates. Looking ahead, a forecast of mid-teen returns from equities in 2024, supported by a historically cheap market and expected re-rating as interest rates decrease, aligns with returns anticipated from domestic bonds.

## Local Bonds

In the fourth quarter, South African bonds performed well, gaining 8.1% in rands despite higher-than-expected domestic inflation. The All-Bond Index saw its yield decrease from 12.1% to 11.23%. Positive fiscal year revenue receipts exceeded expectations, but higher expenditure raised concerns about the fiscal deficit.

Risks for the rand in 2024 include a drawdown from the Gold and Foreign Exchange Contingency Reserve Account, upcoming elections in May, and uncertainty about the SA Reserve Bank Governor's reappointment. The drawdown may increase exchange rate volatility, while election outcomes, especially an ANC-EFF coalition, could negatively impact the market, leading to a sell-off in equities, bonds, and the rand. The potential weaker rand could result in imported inflation, limiting rate-cut possibilities.

## Local Listed Property

Due to lower bond yields and a surge in global listed property stocks, the domestic sector put in a sterling performance to end the quarter up 16.4% in rands and 19.9% in dollars. It was the best performer of the broad asset classes. The sector rerated relative to the 10-year bond, with the property-to-bond yield ratio declining from 0.74X to 0.59X, well above the 0.85X mean. This suggests that property stocks are expensive relative to bonds. With reported escalations on new leases continuing to trend lower, an oversupply of property in many subsectors and high vacancy rates, distribution growth is expected to be subdued over the coming year. Higher finance costs and liquidity constraints have also necessitated capital retention, again pointing to lower distributions over the coming year. Dividends per share were down almost 17% over the quarter, justifying concerns about distribution growth. Although the sector does show value, trading at a 49% discount to net asset value, return expectations lag those of the other broad asset classes, especially after the recent rally. As a result, an underweight position is retained in South African listed property. The biggest gainers in the quarter included Lighthouse Capital (36.1%), Nepi Rockcastle (21.4%) and Hammerson PLC (18.3%), while the laggards included Fortress (7.3%), Hyprop (8.8%) and Mas Real Estate (10.9%).



## Summary

The investment outlook for 2024 is expected to present greater challenges compared to 2023, marked by escalating geopolitical risks, escalating trade wars, and a global economic slowdown. This slowdown is attributed to the lagged effect of aggressive rate hikes, diminished Chinese growth, and a notable deceleration in global trade. Although the World Bank has maintained its global growth estimate for the current year at 2.4%, it has revised the estimate for 2025 downward to 2.7%. The drivers of last year's growth, including buoyant consumption expenditure due to Covid-era stimulus measures, the US CHIPS Act, the US Inflation Reduction Act, and the EU's Green Deal Industrial Plan, are anticipated to lose momentum. This is because the additional expenditure is now incorporated into the baseline. With the US reinforcing export restrictions on high-tech chips and chip manufacturing equipment to China and the EU initiating trade investigations into Chinese EV subsidies, Chinese economic growth is expected to decelerate from 5.2% in 2023 to 4.5% this year.

The EU's Carbon Border Adjustment Mechanism (CBAM), a tax on emissions of carbon-intensive imports into the EU, is another restrictive measure, initially targeting cement, iron, aluminium, fertilizers, electricity, hydrogen, and steel. Although effective in 2026, exporters to the EU are now obligated to provide emissions data to customs authorities or face fines from January this year. The UK aims to introduce its own carbon tax in 2027, and other countries like the US and Japan may also implement similar taxes. The CBAM is expected to be a significant obstacle for China, with officials labeling it as "green protectionism." However, these protectionist measures against China stem from the overproduction of manufactured goods, leading to deflation, with China's surplus now equivalent to about 2% of global GDP.

# Market performance summary (in ZAR) to 31 December 2023

		3 months	6 months	1 year	3 years	5 years	10 years
Local	Equities (All Share Index)	6.9%	3.2%	9.3%	13.5%	11.9%	8.8%
	Equities (Capped SWIX)	8.2%	4.1%	7.9%	12.7%	9.0%	7.1%
	Property	16.4%	15.2%	10.1%	14.9%	0.2%	2.9%
	Nominal Bonds	8.1%	7.7%	9.7%	7.4%	8.2%	8.0%
	Inflation Linked Bonds	6.2%	7.0%	7.0%	8.9%	6.5%	5.6%
	Cash	2.1%	4.2%	8.1%	5.7%	5.9%	6.4%
International	Equities (MSCI ACWI)	7.8%	3.8%	31.3%	13.8%	17.2%	14.1%
	Equities (MSCI EM)	0.8%	-2.4%	13.8%	0.9%	8.0%	8.6%
	Bonds	4.9%	0.9%	13.6%	1.7%	4.6%	6.1%
	Property	12.0%	5.1%	17.0%	8.8%	7.7%	10.1%
	Rand vs US Dollar	-2.9%	-3.2%	7.5%	7.6%	4.9%	5.7%
Equity Sector	Financials	12.3%	14.3%	20.0%	18.5%	6.1%	7.5%
	Resources	3.0%	-1.5%	-11.8%	8.2%	14.6%	6.8%
	Industrials	5.9%	-0.7%	16.6%	12.4%	11.6%	8.2%
Size	Small Cap	8.6%	9.7%	11.2%	23.9%	12.7%	8.4%
	Medium Cap	10.0%	11.0%	9.7%	12.8%	7.3%	6.8%
	Large Cap	6.6%	1.6%	9.0%	13.4%	12.5%	8.9%

# call us<sup>®</sup>



Marie du Plessis  
Sanlam Corporate Investments  
+27 (21) 950 7548  
[Marie.duPlessis@sanlam.co.za](mailto:Marie.duPlessis@sanlam.co.za)

Matimu Ngobeni  
Sanlam Corporate Investments  
+21 (21) 950 2085  
[Matimu.Ngobeni@sanlam.co.za](mailto:Matimu.Ngobeni@sanlam.co.za)

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2 Strand Road, Bellville, Cape Town | PO Box 1, Sanlamhof 7532, South Africa

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Licensed Financial Services Provider.

T +27 (0)21 947 9111  
F +27 (0)21 947 8066

[www.sanlam.co.za](http://www.sanlam.co.za)

