



AUTUS

*wealth care specialists*

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QUARTERLY  
ECONOMIC  
COMMENTARY

Q4 | 2017

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# AUTUS BCI EQUITY FUND

## Quarterly Commentary - Autus BCI Equity Fund

During the quarter a more conservative approach was maintained as the equity exposure of the fund remained under 85%. Some changes include buying Investec, Sanlam, Mr Price, Clicks, Dischem, Glencore, MTN and Vodacom and selling Life Healthcare the few remaining Steinhoff shares. The offshore exposure was increased to more than 18%, which is in line with most equity funds in this space. The core holdings still focus on the big index counters being Naspers, Billiton, Mondi, Richemont, British American Tobacco, Anglo American and Standard Bank. We remain positive on the SA equity market and valuations may offer good entry points to up our equity holdings in the following quarter.

Sustained global economic growth and apparent optimism in broad equity markets characterised the final quarter of 2017. Central banks seemed to share the positive outlook on the health of their respective economies, with conversations increasingly drifting towards the return of inflation and more restrictive monetary policy. Jerome Powell was announced to replace Janet Yellen as the new chair of the Federal Reserve and will take office in February 2018. The Federal Funds Rate was increased in December to the 1.25% to 1.5% range, while the bank's balance sheet normalisation is expected to continue as planned. In November, the Bank of England hiked its policy rate for the first time in slightly over 10 years as inflation creeps up to the 3% mark. Akin to its developed market peers, the European Central Bank unveiled its plan to change course on monetary policy by announcing that it will begin halving the value of its monthly asset purchases.

United States President Donald Trump signed the Tax Cuts and Jobs Act into law in December. In addition to lowering tax rates on households, the bill includes a remarkable cut in corporate taxes from 35% to 21%. It is expected that the tax cuts will boost corporate profits and spur economic growth. The extent of the benefits of these cuts on corporate profits and economic growth remains to be seen, but there are already signs of sector rotation in the US stock market. Specifically, the shares of lower-tax paying companies – especially in the technology sector – has lost some ground to shares in the higher-tax paying industrial and financial sectors.

The long-awaited elective conference of the ANC took place towards the end the quarter. The outcome was a clear victory for Cyril Ramaphosa and his supporters. The immediate fate of incumbent president Jacob Zuma is the likely to remain the subject of speculation in the financial markets. In November, Standard & Poor's downgraded South Africa's local currency debt to non-investment grade. On the other hand, Moody's has decided to retain its investment grade rating and will review its decision after the February budget speech.

The year ended off with a shock that will resonate with corporate South Africa for decades to come. Details remain scant at the time of writing, but the stunning resignation of Marcus Jooste on 6 December 2017 as CEO of Steinhoff International gave sudden credibility to accusations of accounting irregularities and serious corporate governance issues at the retail behemoth. The share price lost nearly 90% of its value in the days following the announcement. PwC has been appointed to conduct an independent investigation into the Steinhoff's accounting practices as the company and its subsidiaries struggle for survival in a liquidity-constrained environment. The saga is expected to continue to play out into 2018 as new details come to light.

Managing any portfolio in South Africa is becoming more challenging mainly due to two conditions, namely political uncertainties and corporate governance (refer to the Steinhoff saga). Trust in both these variables is at a low, but a recent chain of events (Ramaphosa leadership, the Hawks' actions on crime and hopefully a rethink on corporate governance in companies) can enhance trust in the financial markets.

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