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FOREWORD

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Life in South Africa cannot be described as dull. We should never be at a loss for dinner-party conversation and round-the-braai small talk following the May elections and formation of the GNU. Our feature article in the issue of *Foreword* focuses on just that topic. Nancy Hossack shares her assessment of the election outcome and what this means for South African investors in *Instability Will Be Our GNU Reality*. Dhersan Chetty addresses a pre-election backfire in *NHI Bill Signed — What's Next For Private Healthcare?*

We have news on several important milestones for Foord as well. In my article *Green Light For The Foord International Fund,* I discuss the enhanced sustainable investment programme for our flagship global fund. Brendan Africa outlines Foord's transformation status in *Empowerment Credentials Credited*. And Julie Macleod-Henderson shares insights and observations from our first professional investor tour to Asia in *Beyond The Great Firewall Of China — An Investment Immersion*.

We round off with *Markets in a Nutshell* — a neat summary of market movements over the past quarter.

Enjoy this read.

Paul Cluer
Managing Director

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INSTABILITY WILL BE OUR GNU REALITY

As the dust settles on South Africa's national elections, we can all heave a sigh of relief. With the formation of a clunky Government of National Unity (GNU) that excludes the two most radical parties, South Africa has again walked back from the abyss. Markets nervously cheered the result. Portfolio manager NANCY HOSSACK discusses the election outcome and what South African investors might expect from the GNU government in the years ahead.

When Jacob Zuma infamously appointed 'Weekend Special' Des Van Rooyen as Finance Minister for a spectacular 48-hour term in 2015, a radio commentator — possibly Bobby Godsell — memorably noted that 'South Africa has a history of repeatedly walking up to the precipice, peering over it, and then deciding "not today"'. This has been the reality under which South Africans have lived since the formation of the Union. Arguably, life was even more volatile before then.

This observation describes well the current state of the nation following South Africa's 29 May 2024 national and provincial elections. In my opinion, the election result was not good news. Faced with ten years of declining living standards, voters abandoned the ANC in large numbers. A decade ago, the ANC received ten million votes. In this election, the party only managed to scrape together six million votes.

What the poll numbers don't show is that the vast majority of South Africans chose not to vote. In a damning indictment of the democratic process, 60% of eligible voters did not vote. This cohort includes eligible voters who did not register and registered voters who did not vote. This highlights the distaste that has developed for politicians in general and a growing feeling of helplessness in the country.

Where voters did shift their votes, they shifted them to Jacob Zuma's MK Party. The MK Party advocates a radical-left ideology that includes state ownership of all land and the dismantling of South Africa's constitution. Its leadership is thoroughly associated with corruption. In the face of the hopelessness created by many of these individuals, South Africans are turning to more radical policies proposed by the same people.

This is not good news. A silver lining has been the formation of a GNU, comprising the ANC, DA, IFP and other smaller parties. Freed of its most radical elements, the ANC has chosen to turn back to the political centre — in essence, stepping back from the precipice.

While this is welcome relief, we also remain cautious. We have agonised over the different trajectories that this election could determine for the country. Knowing the possible set of coalition partners, we think there is a high probability that no coalition — in the GNU or at provincial and metro level — may last even five years. Instability will be our new reality.

The last few weeks provide ample examples. I would point to the last-minute negotiations between the ANC and the DA, which were incomplete even as the day dawned to elect the president. In fact, there was still 'no deal' as the Chief Justice was swearing in members of parliament. And then came the haggling over cabinet and provincial posts, which continues to threaten the stability of the GNU.

The trouble is that the ANC is a tricky coalition partner. While it is less divided than it was in 2018 when Ramaphosa was elected as party president, it is still highly factionalised, with many competing interests. These competing interests will now be fighting over diminishing spoils, which will increase internal pressure. Many party members are implicated in corruption and now risk prosecution if portfolios are handed over to other parties.

This is well illustrated in President Ramaphosa's cabinet. It is obvious that despite the Statement of Intent signed between the DA and the ANC, he awarded a disproportionate number of ministries to his own party and other smaller parties, at the expense of the DA. It suggests that the ANC has not quite come to terms with the sharing of power.

Markets nervously cheered the results. While the rand, SA bonds and SA Inc. shares — notably financials — rallied, none of these assets are trading at optimistic levels relative to history: rather, the valuations suggest only relief that a very negative outcome has not come to pass. We saw a similar market event in 2018, after Ramaphosa's earlier ANC elective conference win — by the thinnest of margins — which the market dubbed 'Ramaphoria'. It did not last long.

The political — and therefore policy — uncertainty I have described produces what the investments industry calls 'risk premia'. The risk premium (see *'Did You Know?'*) describes the extra return investors in SA assets require to compensate them for potential for negative outcomes. The adverse risk premium on SA assets is likely to remain a headwind unless the country achieves consistent economic growth. And everything will depend on growth, which has been elusive for the past decade.

The big question is whether this coalition can deliver the structural growth that South Africans — and investors in South African assets — need. We think that in the near term there should be improved growth from a very low base. We know that discretionary and fixed-asset spending has been extremely low leading up to the election. For example, the value of building plans passed (adjusted for inflation) has stagnated at 2004 levels. We should see some normality in these and other metrics, which will be positive.

However, longer term structural growth is going to be harder to achieve. It requires that we deal decisively with infrastructure failures and invest more money in fixed capital formation. To do so, we need competent ministers and directors general in portfolios like Public Works, Transport, Electricity, Trade and Industry, Water and Sanitation, and Finance. We also need increased competence from the Presidency to influence the renewal of state-owned enterprises. In this regard, Ramaphosa's cabinet announcements were a mixed bag: competent appointments were made in the Electricity, Finance and Public Works portfolios, but appointments in the four other key portfolios were underwhelming.

If South Africa fails to achieve meaningful growth, it will suffer from an increasingly accelerating debt trap. With this risk growing, Foord has maintained a low weighting to South African nominal bonds in its South African multi-asset portfolios, which include the Foord Conservative, Balanced and Flexible Funds. However, we have been increasingly adding to our inflation-linked bond investments, which we think offer considerable value and capital protection.

Foord's investment style is to err on the side of protecting investor capital instead of speculatively chasing rainbows. Accordingly, in the lead up to the election we were overweight offshore assets to protect investors from a very negative — and underappreciated — coalition outcome. However, as the ANC's negotiations with the DA progressed positively, we increased our exposure to SA Inc. assets, including nominal bonds and bank shares. This was fortunate as these assets rallied when the GNU became likely. Nevertheless, our portfolio returns will lag those of more aggressively positioned peers.

We broadly segment SA equities into SA Inc. shares, resources and offshore companies. At the time of writing, SA Inc. investments have rallied 9%, while resources and offshore shares are down mid-single digits on rand strength. Any changes we now make to portfolios will be circumspect. We continue to think that there may be some legs to the relief rally, but longer term growth is not guaranteed. Fortunately, SA asset prices — despite the recent rally — remain inexpensive. We continue to favour investment opportunities where companies can grow earnings despite the macro environment, as well as those that have considerable upside optionality.

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NHI BILL SIGNED – WHAT'S NEXT FOR PRIVATE HEALTHCARE?

President Ramaphosa hurriedly signed the controversial National Health Insurance (NHI) bill into law days before the end of his term. Foord's healthcare analyst DHERSAN CHETTY unpacks the implications of the NHI, given the widespread worries about its implementation and the feared death knell of the private healthcare industry.

There was much uncertainty and fear surrounding the signing of the National Health Insurance (NHI) bill into law just days before the end of President Ramaphosa's previous mandate. The timing could have been driven by emerging clarity that the ANC would lose its parliamentary majority — and some hope that the NHI might boost the ANC's electoral chances.

In this regard, it backfired spectacularly. While the NHI is aspirational in its objectives of providing free healthcare to all South Africans, it has created much worry for the voting members of the country's private medical aid industry — of all races — in terms of potentially higher taxes, execution and risk of corruption.

The NHI's proposal to create free healthcare for all citizens — including GP visits and hospital care — is admirable. In its current form, however, the NHI introduces tremendous and unresolved constitutional, commercial, implementation and political challenges.

The most worrying provision for existing medical aid members — covered by section 33 of the Act — is that private medical schemes will be banned from providing cover for any procedure covered by the NHI. This is the most legally contentious issue and the one that is likely to face the most constitutional challenges. The implication is that — in time — private medical aids will shrink to providing only the most fringe medical services not covered by the NHI.

Commercially, the NHI fund seems highly ambitious and unaffordable, given the country's poor financials and high tax rates. Assuming that all other challenges are resolved, to provide full primary and hospital coverage to the nation is estimated to cost north of R200 billion annually. For context, this accounts for 36% of national payroll tax or 62% of corporate tax. The ANC has yet to propose a funding model for the NHI, saying only that it will be developed over time. The magnitude of the funding requirements suggests that the likelihood of NHI getting to the point of replacing medical schemes anytime soon is extremely low.

From an implementation perspective, it would take at least five to seven years just to set up the structures of the single NHI fund, excluding time taken to resolve court challenges and political adjudication. Once the fund is established, it would focus primarily on primary healthcare, and then start contracting for hospital care with accredited providers. However, as there are very few public hospitals that meet the quality criteria to contract with the NHI fund, it would therefore have to contract predominately with private hospitals. The expectation is that this second phase of NHI implementation could also take five to seven years. The process would be one of negotiation — private hospitals will not be forced to contract with the NHI, they will only do so if they enjoy spare capacity.

Politically, the NHI fund faces headwinds from the GNU coalition government — it was not supported by the ANC's DA and IFP coalition partners (both voted against the bill in parliament). Nevertheless, it remains a multi-decade vision for the ANC, which might return to majority power in time. It is therefore likely to remain unrescinded, but with difficult and slow implementation in the near term.

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The NHI has obvious implications for the private healthcare industry in South Africa. For investors, these relate principally to private hospital groups on the one hand and medical aid providers on the other. In the long term, the risk is that government might implement a payroll tax on a sliding scale to fund free cover for only some medical procedures. Medical aid members will suffer this tax plus the cost of their medical aid premiums.

While this scenario is negative and frustrating to the consumer, it does not have a material impact on the hospital stocks that we own, such as Netcare and Life Healthcare, because consumers are likely to keep their medical scheme cover rather than move to the public sector. In contrast, medical schemes — such as those provided by Discovery — are the most exposed to NHI. We have no exposure to medical aid scheme providers or administrators in the Foord unit trust funds.

For hospital groups then, we see no impact in the short to medium term. In the long term, they could actually benefit from contracting with the NHI to fill up spare capacity, since the proceeds of a payroll tax will most likely be used to fund primary healthcare and to upgrade public hospitals rather than provide full hospital cover.

Hospital stocks have performed well in the recent market rally — rising 23% since the May elections — given their high 'SA Inc.' exposure and the lower probability of the NHI being implemented in a coalition government. Nevertheless, we believe that the sector could still provide significant upside from current share price levels, given the prospect for defensive earnings growth, high free cash flow generation and strong balance sheets.

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GREEN LIGHT FOR THE FOORD INTERNATIONAL FUND

Sustainable income streams have always been fundamental to Foord's long-term investment philosophy. Portfolio managers bring an acute awareness of environmental, social and governance (ESG) factors to the stock selection process when buying stocks for the long term. Foord global funds director PAUL CLUER writes that Foord has now formalised an enhanced sustainable investment programme for the Foord International Fund.

Foord's flagship global multi-asset fund is the Foord International Fund. Launched in March 1997, the fund aims to achieve meaningful inflation-beating US dollar returns over the long term from a conservative but actively managed portfolio of mostly developed — but also emerging — market investments that reflect Foord's prevailing best investment view for cautious investors.

The Foord International Fund is domiciled in Luxembourg, the world's largest cross-border fund distribution market. Luxembourg has established itself as a global hub for investment funds, attracting fund promoters and managers from around the world due to its progressive regulatory environment, political stability and leading financial infrastructure.

Luxembourg's regulatory arsenal includes EU-wide standards on the marketing of products that promote sustainable investment characteristics or that explicitly have sustainable investment objectives. These regulations are known as the Sustainable Finance Disclosure Regulation, or SFDR. SFDR provides for three categories of funds that engage in some form of sustainable investment practice, referred to as Article 6, 8 and 9 funds — bizarrely skipping a categorisation in Article 7 of the SFDR regulation.

Foord has always integrated sustainable investment practices into its investment process, but otherwise made no specific commitments. It has until now been categorised as an Article 6 fund. Article 8 funds, sometimes referred to as 'light green' funds, promote environmental or social characteristics but do not have sustainable investment as their main purpose. The 'dark green' funds are categorised in Article 9 and have sustainable investment as their main objective.

Given Foord's long-term 'buy-and-hold' investment philosophy, sustainable investing has been in our DNA. The fund managers have always applied a forward-looking investment approach that seeks to preserve investor capital and safely compound long-term, inflation-beating US dollar returns. As part of its rigorous bottom-up, fundamental research into companies, the fund managers have also considered ESG factors that could materially impact the valuation or financial performance of its investments.

Uplifting the fund's classification from Article 6 to Article 8 did not require a change of process or philosophy. Rather, we needed only to tweak our process by formally applying exclusion criteria to investments that do not meet qualifying ESG peer-group scores or norms-based requirements. The uplift reflects Foord's commitment to integrating ESG factors into its investment process, as well as promoting environmental and social characteristics for the benefit of its investors and society at large.

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In this regard, the fund now excludes the lowest scoring 25% of issuers within the peer group, based on the methodology provided by Bloomberg ESG Score. In addition, Foord also applies screening and exclusion against international norms violations, such as the UN Global Compact, which covers human rights, labour standards, environmental harm, corruption and unethical practices, controversial weapons and international sanctions.

It was no surprise that that the fund's current portfolio holdings easily met these enhanced requirements. This will be of comfort to long-term investors in the fund. Moving forward, we will now monitor the ESG risk scores of the fund's investments and engage with company management on ESG issues to encourage positive change — activities we were already doing informally. Claiming Article 8 compliance for the fund does bring with it added reporting requirements, which we will attend to in due course in the requisite forums.

We chose to pilot the Article 8 uplift for Foord International Fund only, given its less complex portfolio of share investments. Foord's other Luxembourg-domiciled funds — Foord Global Equity Fund (Luxembourg) and Foord Asia ex-Japan Fund — will for now remain Article 6 products. However, we expect to uplift them once we have successfully completed the sustainable investment reporting cycles for Foord International Fund. Again, we would expect that almost all the investments would meet the enhanced ESG requirements we would set for the funds under Article 8.

BEYOND THE GREAT FIREWALL OF CHINA – AN INVESTMENT IMMERSION

Asia is the backyard of Foord's global investment team, which is based in the booming city-state of Singapore. In May, the Foord Singapore investment team hosted 22 South African investment professionals on an 11-day, in-depth investment immersion of Singapore, Macau, Hong Kong, Shenzhen and Beijing. JULIE MACLEOD-HENDERSON recounts the concept behind the tour and key observations from this maiden voyage.

The tour started in Singapore, home of Foord's global asset management team. From there, we travelled to four quite different Chinese cities: Macau, Hong Kong, Shenzhen and Beijing. The purpose was to facilitate an understanding of these markets and provide direct insight into the investment opportunities they hold.

As a practical learning journey, the tour included site visits, company presentations, networking sessions and discussions with key industry figures across the investment spectrum. From AI to electric vehicles, retail to gambling, SOEs to property, delegates accessed unforgettable spaces and experiences that offered a rare on-the-ground perspective of what is driving this region and why we regard it as highly investible.

David Bacher, Chief Investment Officer at Corion Capital and delegate on the Understanding Asia Tour, explained, 'China is a very important investment decision to get right, to establish what we believe is the correct investment rationale for our clients.' Bacher noted that the ability to leverage Foord's contacts and local-market knowledge was a game changer.

His conclusion? 'The extent of what we saw and experienced was beyond expectation.' These were some of his observations:

China's car market — the world's largest — stood out for its high-quality, competitively priced vehicles from numerous domestic manufacturers. For example, a car comparable to a quality European manufactured vehicle offered luxury and advanced technology at a much lower cost. China's focus on clean-energy vehicles and rapid market growth has therefore drawn global attention.

China's Great Firewall had a significant impact: while some aspects were surprisingly positive, pervasive censorship was evident. Access to foreign apps like Google and WhatsApp was restricted, redirecting users to Chinese equivalents, under strict surveillance. The widespread use of surveillance cameras, as seen near Tiananmen Square, underscored the omnipresent state monitoring.

Pollution was unexpectedly low, especially in tier-one cities. Contrary to initial expectations of smog, the air quality was clear — thanks to efforts to relocate manufacturing plants outside of large cities. Over the past six years, pollution levels have significantly decreased in major cities.

China's strict regulations quickly dispelled the perception of counterfeit goods flooding the market. It seemed clear to me that China deserves the label as the world's largest luxury brand market, contributing 35 to 45% of global luxury revenues. There was an abundance of high-end stores, such as Gucci and Louis Vuitton.

State-owned enterprises (SOEs) play a significant role in China's economy, impacting poverty reduction and policy implementation. Despite concerns about transparency, well-managed SOEs — something we are not used to in South Africa — can provide substantial societal benefits.

China's work culture, witnessed at companies like JD.com, emphasised efficiency and dedication, reflecting a strong societal emphasis on work ethic and productivity. This cultural norm values personal investment in professional output.

Other notable observations were the domestic focus in the face of US trade wars, the focus on renewable energy and ESG practices, and the explosion of patent registrations. So, is China investible? Bacher points out that China is very attractive from a valuation perspective. ‘Coupled with a high work ethic and a country at the forefront of technology and innovation, it substantiates our thesis that we need to be overweight China. Don’t write off China,’ he concludes. ‘The country is a machine, maybe an automated machine, but it is a machine.’

I can only echo David’s comments. I was also struck by the sheer scale of innovation evident in each city we visited. The dynamic interplay between tradition and modernity, especially in places like Beijing and Shenzhen, was palpable. Witnessing firsthand the strategic efforts in technology and clean energy highlighted the region's forward-thinking approach.

One of the standout experiences was taking an autonomous taxi ride with Pony-AI, which showcased the cutting-edge advancements in AI and transportation technology. Equally impressive was the hospitality and openness of the industry leaders we engaged with, who provided invaluable insights into the intricacies of their operations.

This experience has reinforced my belief in the immense potential and importance of the Asian markets, especially China, as a cornerstone of global investment strategies. The cultural immersion and professional interactions have provided us with a nuanced understanding that will undoubtedly shape my understanding of these markets going forward.

EMPOWERMENT CREDENTIALS CREDITED

South African financial services firms are obliged to report empowerment progress under the Financial Sector Charter Code. The financial services regulators — the Financial Sector Conduct Authority and the Prudential Authority — take empowerment factors into consideration when awarding and maintaining financial services sector licenses. Progress in this area is therefore not only the right thing to do but is also a regulatory requirement. Director BRENDAN AFRICA explains Foord's path to achieving an empowerment milestone

Foord's independent verification agency has now rated Foord Asset Management as a Level 1 Broad-based Black Economic Empowerment (B-BBEE) contributor — the highest level possible under the current financial sector codes. This outcome reflects the firm's commitment to building a diverse and inclusive South African business that embraces the principles of employment equity and redress.

Foord has achieved this outcome by embedding the principles of transformation within its overall business strategy and by implementing various purpose-specific initiatives. These include meaningful ownership diversification to include an empowerment trust and senior staff, achieving a balanced staff composition in terms of race and gender, proactively developing and promoting staff into leadership positions, and facilitating broad skills development programmes within the firm and externally.

Foord has also implemented structured procurement programs to prioritise emerging black and women suppliers. The firm has developed an industry-first series of illustrated children's books on savings and investing that also serves as the foundation for its investment in proactive consumer education, another requirement under the code. While we are pleased with the Level 1 rating, we take more pride in the small, but important, socio-economic difference we are contributing to the country and the next generation of investors.

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DID YOU KNOW? RISK PREMIUM

Risk premium refers to the additional return investors expect as compensation for taking on additional risk. In financial markets, every investment carries a degree of risk, whether it's market risk, credit risk, liquidity risk, or others. Investors require compensation for bearing these risks beyond the risk-free rate of return (traditionally, the yield on US government bonds).

The concept is grounded in the idea that higher risk investments must offer higher returns to attract investors. For instance, shares are generally riskier than bonds, given the greater uncertainties regarding the timing and amount of future cash flows. As an asset class, they typically provide higher returns over the long term. Similarly, within fixed income, poorer quality bonds — those with higher credit risk — must offer higher yields to compensate for the increased likelihood of default.

Understanding risk premia is crucial for investors when assessing the attractiveness of different investments. It helps in making informed decisions about asset allocation and balancing risk and return in a portfolio. Moreover, it underscores the fundamental principle that higher returns are generally associated with higher risks in financial markets.

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MARKETS IN A NUTSHELL

	WORLD	SOUTH AFRICA
Equities	The index of global share markets rallied narrowly, pulled up by a handful of mega-cap US tech stocks as the AI theme continued — European shares traded lower, while emerging markets also gained as Chinese shares recovered from recent lows	JSE-listed shares rallied over 8% in an eventful quarter, which included resources shares recovering from recent selloffs — but the standout performers were SA Inc. shares that include banks and construction companies, which surged as the most market-friendly elections outcome eventuated
Bonds	Developed market bond yields rose and bond markets fell as it became evident that the US central bank would not be cutting interest rates quickly — given the strength of the US economy and inflation sticky above target levels	The All Bond Index gained over 7% as investors reduced the risk premium on South African bonds, as a government that excluded the most radical parties became assured — with longer dated bonds advancing most
Currencies	US dollar strength persists against the majors, given the US economy's sustained resilience, high interest rates and AI dominance — meanwhile the Japanese yen weakened to 38-year lows against the US dollar as the country persists with ultra-low interest rates	The rand was volatile intra-quarter, but advanced aggressively on hopes that a more centrist government would move quickly on market-friendly policies — the unit broke through R18/$, but has subsequently retraced some of the gains
Commodities	Commodities mostly retraced after a bullish run this year, with copper down meaningfully and gold flat despite continued dollar strength — but crude oil prices rose on summer demand and OPEC supply cuts	
Economy	US economic growth slowed demonstrably, but the economy is still expanding at enviable levels compared to other developed markets, although European growth prospects are finally starting to improve — Chinese growth remains stable at around 5%, but the economy still faces headwinds from a protracted property crisis and adverse investor sentiment	South Africa's GDP has not grown in 10 years, but business confidence is improving after 100 days of no loadshedding and hopes of political renewal since the creation of a Government of National Unity — government finances are improving, but SA's debt levels remain extremely elevated
Monetary and fiscal policy	The US central bank again kept rate cuts on hold, with the 'dot plot' forecasts of future moves turning more hawkish, leaving the US as an outlier — the European Central Bank moved to cut interest rates ahead of the US for the first time ever, with interest rate cuts also being executed in other developed economies	The South African Reserve Bank also left rates unchanged, citing upside risks to inflation from administered prices (fuel and electricity) and inflation expectations — despite core inflation moderating towards the middle of SARB's 3 – 6% target range

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