Bateleur Flexible Prescient Fund

2024 final report back

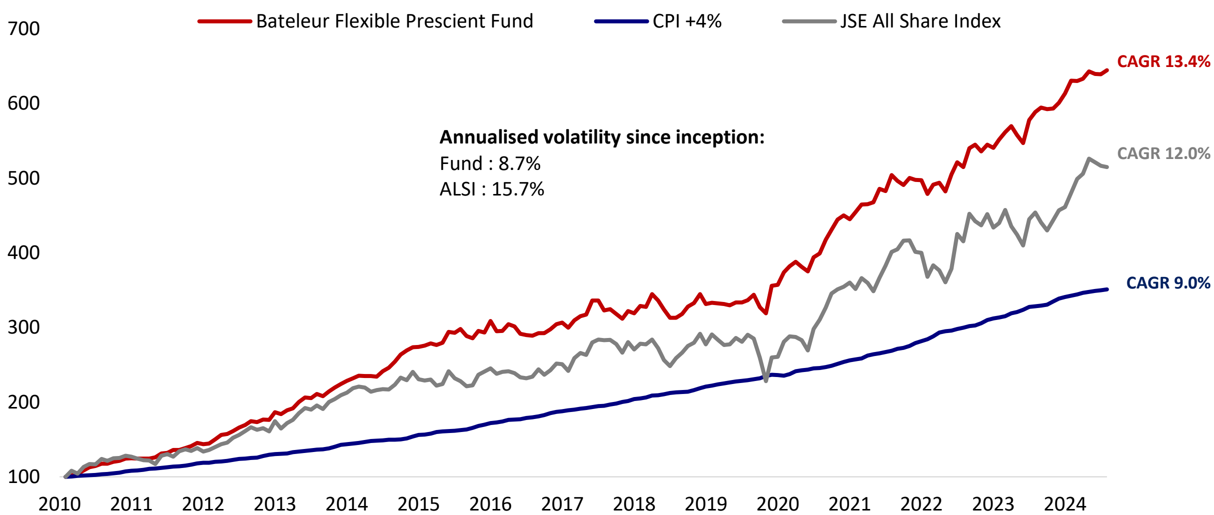
bateleur capital

Bateleur Flexible Prescient Fund ("The fund") – 2024 final report back to unitholders

The fund appreciated 9.2% net of fees in calendar 2024[i]. As comparatives, the JSE All Share Index (ALSI) rose 13.4%, a basket of SA government bonds (ALBI) gained 17.2%, while cash (STeFI) returned 8.2%.

Since inception in July 2010, the fund has compounded at 13.4% per annum net of fees (Chart 1). This compares to 12.0% for the ALSI before fees and 9.0% for the fund's benchmark (CPI + 4%). Returns were generated at lower volatility than the market (annualised 8.7% for the fund vs. 15.7% for the ALSI).

Chart 1: Bateleur Flexible Prescient Fund illustrative performance since inception – 1 July 2010 (indexed)



Source: Bateleur, as at 31 December 2024

Attribution by strategy and the top contributors and detractors for 2024 are displayed in Table 1. JSE listed equities added 5.0% to returns, foreign listed equities 3.1%, and government bonds 1.9%. The top contributors were largely technology focused (Naspers, Amazon, TSMC and Alphabet) while detractors were commodity linked (African Rainbow Minerals, Glencore and Aker BP) or European listed (Heineken and Novo Nordisk).

Table 1: Calendar 2024 - Fund attribution by strategy and top contributors and detractors

Strategy	Return (%)	Top contributors	%	Top detractors	%
JSE listed equities	5.0%	Naspers/Prosus	1.8%	African Rainbow Minerals	-0.7%
Foreign listed equities	3.1%	Amazon	1.7%	Glencore	-0.7%
Government bonds	1.9%	TSMC	1.3%	Heineken	-0.7%
Cash & money market	0.6%	Italtile	0.9%	Novo Nordisk	-0.6%
Costs (and other)	-1.4%	Alphabet	0.7%	Merck	-0.4%
Total	9.2%	Philip Morris	0.7%	Aker BP	-0.4%

Source: Bateleur, as at 31 December 2024

Although returns were ahead of the CPI + 4% benchmark, 2024 was an average year for the fund, especially considering the more robust returns delivered by the broader SA equity and government bond markets, and the outsized returns registered by US equities.

While the top-down asset allocation decisions were sound - including the healthy allocation to equities, and the upweighting of SA government bonds in the portfolio - the stock picking environment proved more challenging, both domestically and globally.

In SA, a significant portion of 2024 equity market returns came from a re-rating (P/E multiple expansion) as opposed to earnings growth. This was driven by a lower risk premium being applied to SA listed assets following the pro-business election outcome and formation of the Government of National Unity (GNU).

The re-rating was especially apparent in lower quality, more cyclical companies – based on improving macro-economic prospects that have yet to play out.

Ultimately these companies will need to deliver higher earnings growth to justify the re-rating. This, in turn, is dependent on a continuation of structural reform implementation, additional interest rate cuts, and a further uptick in business and consumer confidence.

The fund's JSE listed holdings tend to have a quality bias and are concentrated on companies that have delivered profitable and growing cash flows over a lengthy period - even during a stagnant economy. These include Bidcorp, Bidvest, Shoprite, FirstRand and Standard Bank.

Notwithstanding strong operational results, the above-mentioned companies either de-rated or did not materially re-rate during calendar 2024 (Chart 2). In contrast, higher beta shares that are more leveraged to an expected upswing in the SA economy such as the apparel retailers, construction companies and 'cheaper banks', re-rated sharply (Chart 3).

Chart 2: Change in 2024 P/E (x) – select quality

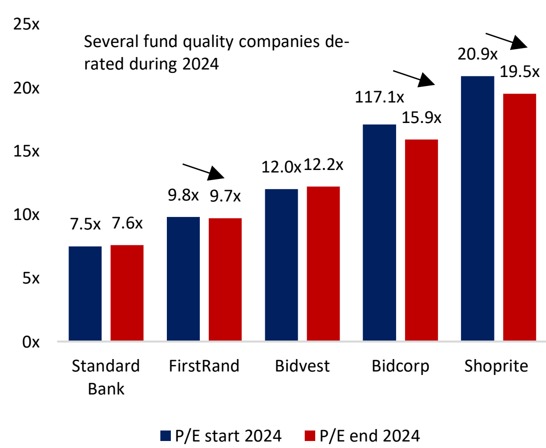
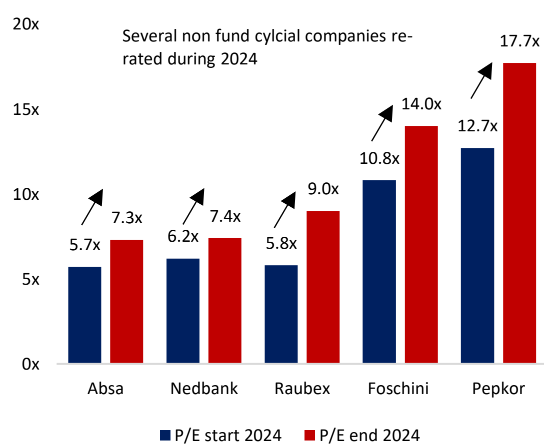


Chart 3: Change in 2024 P/E (x) – select cyclical



Source: Bateleur, Bloomberg

The fund increased its weighting to these higher quality domestic counters in the second half of 2024 at a large discount to estimated fair value.

Globally, the fund's technology holdings (Amazon, Alphabet, Microsoft and TSMC) contributed soundly to absolute returns. However, the fund was underweight technology shares compared to the major indices (S&P 500 and MSCI World Index) which impacted relative returns.

The continued outperformance of large cap technology shares in 2024 was partially supported by strong industry fundamentals and sound earnings growth, but also by a sizable re-rating. Valuations are becoming stretched - particularly in the case of Nvidia and Tesla.

US listed companies currently comprise almost three quarters of the overall country exposure in the MSCI World Index (Chart 4), well above the US's contribution to global GDP of 26.5%*.

The US weighting, in turn, is dominated by seven tech companies that now account for one third of the S&P 500 weighting, driving index concentration to levels last seen in the 1960's (Table 2).

Chart 4: MSCI World Index Country Weighting

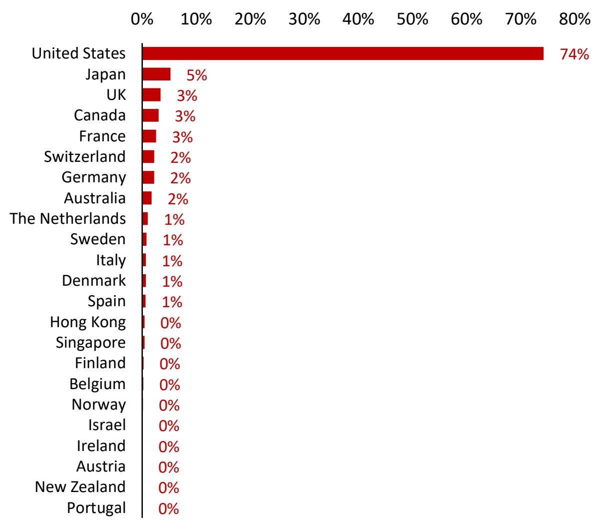


Table 2: US large cap tech return (USD) and weighting

	% Weight in S&P 500	Price Return 2024
Nvidia	6.6%	+171.2%
Meta	2.6%	+65.4%
Tesla	2.3%	+62.5%
Amazon	4.1%	+44.4%
Alphabet	4.0%	+35.5%
Apple	7.6%	+30.1%
Microsoft	6.3%	+12.1%
US large cap tech	**33.5%**	**+47.9%**
S&P500	**100.0%**	**+23.3%**
S&P500 excl. US large cap tech	**66.5%**	**+12.5%**

Source: FactSet, Bateleur Capital, UBS

2025 outlook:

The US economy (Chart 5) and US corporate earnings growth (Chart 6) have outperformed the rest of the developed market world since Covid – consistently surprising to the upside.

Chart 5: US cumulative GDP growth vs G7

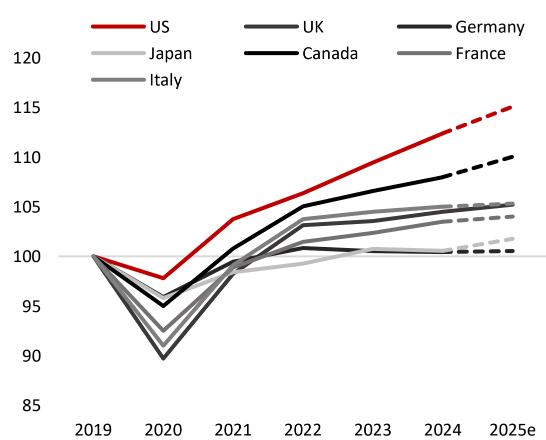
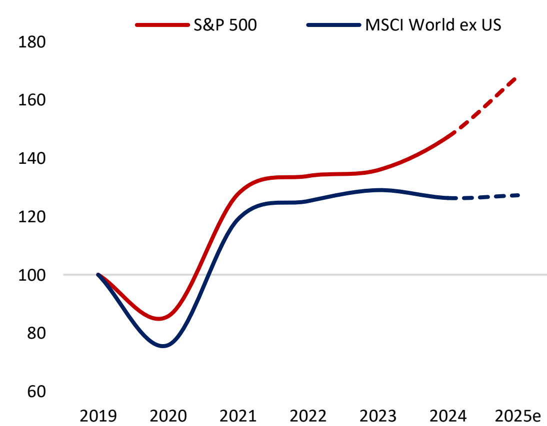


Chart 6: US EPS growth vs ROW



Source: Bateleur Capital; Bloomberg *per IMF 2024 world economic output report.

The robust growth has been assisted by sizable fiscal support. Beyond the USD 5.0 trillion deployed during Covid, an additional USD 2.2 trillion has been provided for strategic investments, dwarfing the more conservative policies adopted by Europe and other developed markets.

At the same time, the US is extending its already healthy lead in the global technology and AI race, benefitting from a continuous cycle of investment, innovation and improved productivity. Since 2014, U.S. private investments into AI total USD 430 billion, with a global market share of 70% (Chart 7).

Capital expenditure (largely AI and cloud based) from the seven major listed U.S. technology companies rose to USD 240 billion in 2024, and is projected to grow to USD 282 billion this year, reinforcing the US's first-mover advantage (Chart 8).

Chart 7: Private capital invested into AI (USD bn)

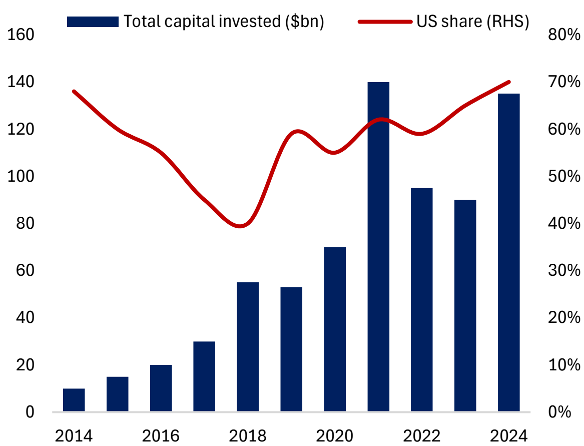
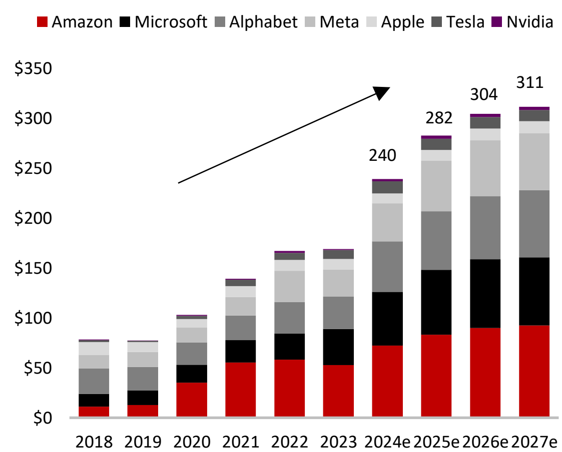


Chart 8: Major listed US tech capex (USD bn)



Source: Bateleur Capital; Bloomberg, JP Morgan

2025 US GDP estimates have been revised upward from +1.6% in January 2024 to +2.1% currently (Chart 9). Expectations have improved following the US election in November 2024, given the anticipation of a broadly pro-growth policy to be adopted by President Trump.

Legendary investor Stanley Druckenmiller in a recent January 2025 interview[1] commented *"I've been doing this for 49 years, and we're probably going from the most anti-business administration to the opposite. We do a lot of talking to CEOs and companies on the ground, and I'd say CEOs are somewhere between relieved and giddy."*

In contrast, European real GDP estimates for 2025 have fallen from +1.4% in January to +1.1% today. The absolute level of economic growth in Europe remains subdued, requiring a more co-ordinated and stimulative policy response in the region.

From a corporate earnings perspective (Chart 10), consensus expectations are for the US to deliver another strong year of EPS growth in 2025 (S&P500 +14.6%) well ahead of a recovering Europe (Stoxx Europe 600 +7.9%).

[1] CNBC interview 20 January 2025

To put these growth rates into context, EPS compounded at +7.4%, and +3.8% per annum (in USD) for the S&P500 and Stoxx Europe 600 respectively in the 10 years to 2024[2].

Chart 9: 2025 Real GDP Growth Estimate (%)

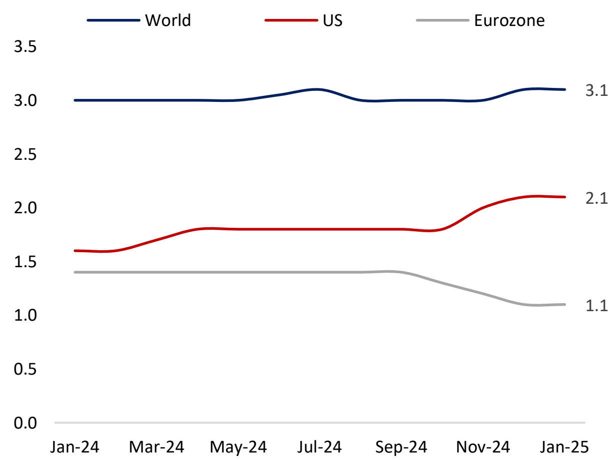
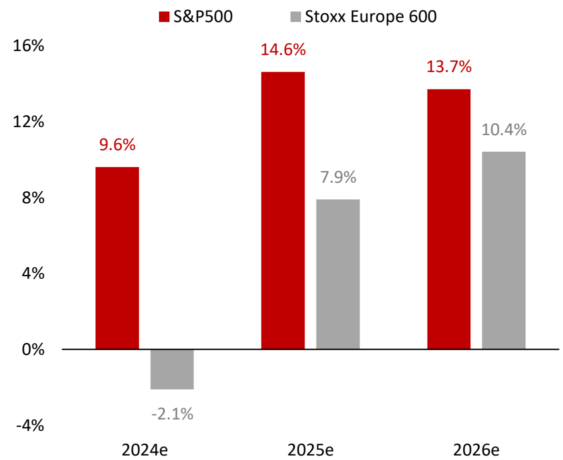


Chart 10: Annual EPS Growth Estimates (USD)



Source: Bloomberg, Bateleur Capital

Unsurprisingly, US equities have outperformed global equities based on superior earnings growth (Chart 11). Valuations are currently elevated relative to both history and major global indices, reflecting investor optimism for continued economic expansion and earnings outperformance (Chart 12). Should US corporate earnings growth disappoint, there is little margin of safety at current ratings.

Chart 11: S&P 500 vs MSCI AC ex-US

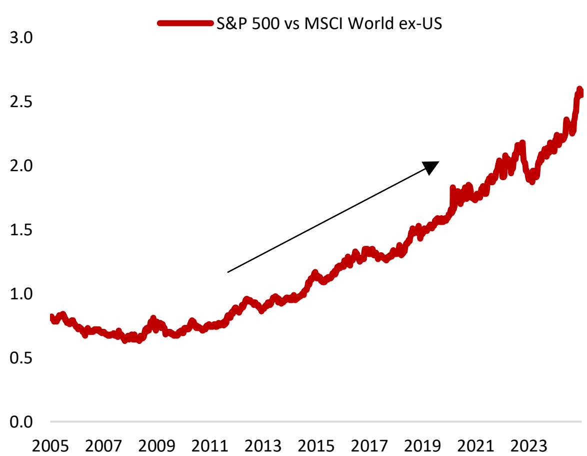
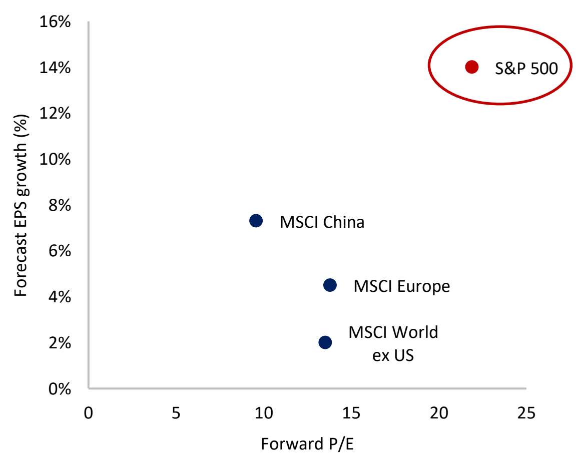


Chart 12: EPS growth vs Forward P/E



Source: Bloomberg, Bateleur Capital

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[2] Source: FactSet, January 2025, Bateleur Capital

China:

China's economy faces ongoing challenges. While exports remain strong, particularly in high-value sectors like electric vehicles and renewable energy (Chart 13), declining property prices and record low consumer confidence have hindered growth (Chart 14).

Chart 13: China automotive exports

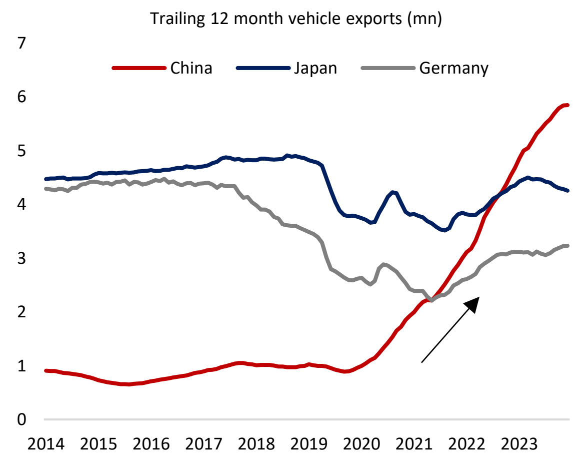
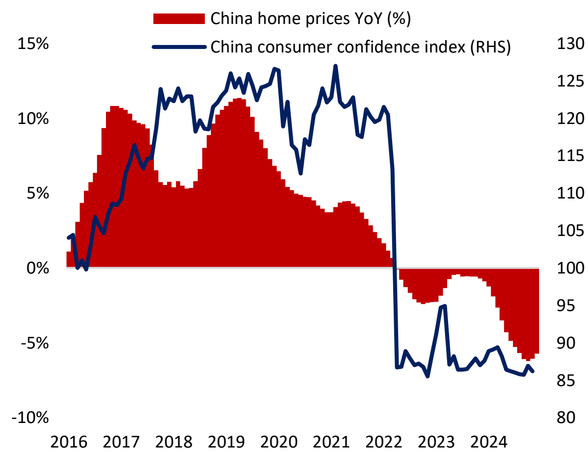


Chart 14: Consumer sentiment & property prices



Source: Bloomberg, Bateleur Capital

The divergence between healthy external demand (exports) and subdued domestic demand (consumption) has increased pressure on the government to introduce additional stimulus measures, especially as the export sector faces the prospect of increased tariffs from the Trump administration.

During the final quarter of 2024, policymakers began shifting their approach by introducing stimulus measures worth approximately 10% of GDP (Table 3). While substantial, these measures are somewhat smaller than those implemented during the Global Financial Crisis (GFC).

Current economic indicators suggest that more intervention may be necessary: bond yields are near record lows, CPI data shows deflationary pressures and consumer spending remains weak. These factors all point to the need for additional monetary easing.

Table 3: China stimulus today vs. GFC

	Percent of GDP (%)	
Stimulus Measure	**GFC**	**Present**
Investment programs	11.5%	
Tax cuts	0.4%	
SOE bailouts	1.4%	
Accomodative monetary policy	13.9%	0.8%
Stock market support		0.7%
Local Government investment projects		0.2%
Local Government debt swap plan		7.9%
Total	**27.2%**	**9.6%**

Source: Blackstone, Bateleur Capital

At their December 2024 meeting, the Politburo loosened the policy approach of China's central bank and called for 'extraordinary' measures to support economic activity.

Should this monetary easing materialise, it could provide a meaningful tailwind for global markets and offset the expected pressure from anticipated US tariffs. It would be especially beneficial for Chinese and Hong Kong listed companies that are consumer facing (including Tencent), which are currently trading at low valuations with conservative growth forecasts.

<u>South Africa:</u>

SA commences the year with a better GDP growth outlook than the last two years, but still below the required rate to meaningfully reduce unemployment.

Consensus expectations are for the SA economy to grow by 1.9% and 2.0% in 2025 and 2026 respectively (Chart 15), driven by an increase in consumer spending, lower interest rates, improving business confidence, and an increase in fixed investment spend (Chart 16).

Chart 15: Accelerating SA GDP growth

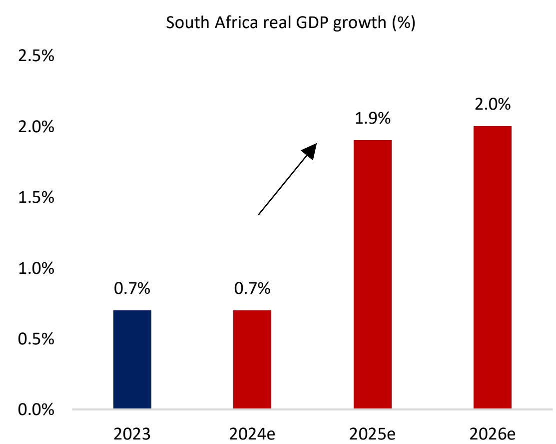
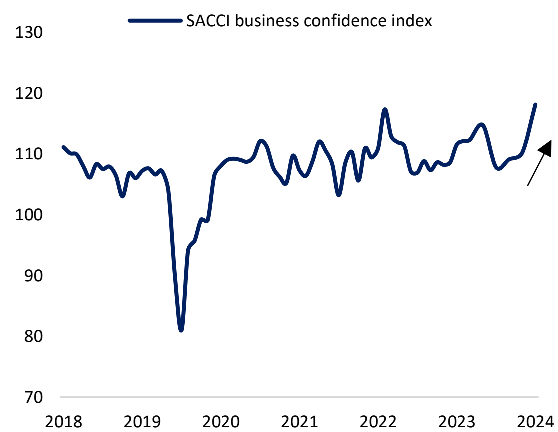


Chart 16: Improving SA business confidence



Source: Bateleur Capital; Bloomberg

A combination of attractively priced domestic assets (equities and government bonds) and the likelihood of accelerating GDP growth is a positive set-up for South African risk assets in the short-term. Nevertheless, it is too soon to envisage a scenario where the economy grows, at a sustainably high rate, beyond the next couple of years.

More recently, there has been an acceleration in both automotive sales (Chart 17) and apparel sales (Chart 18) in the final quarter of 2024, asisited by two-pot pension withdrawals. Feedback from our fourth quarter 2024 interaction with more than twenty listed SA company mangement teams reflects a more confident business outlook but no material uptick yet in trading activity.

Chart 17: SA passenger auto sales improving

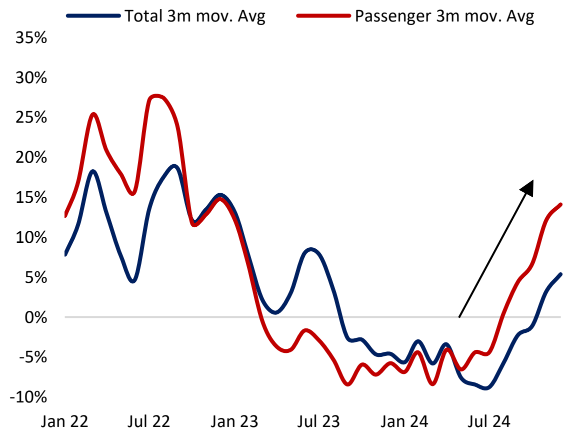
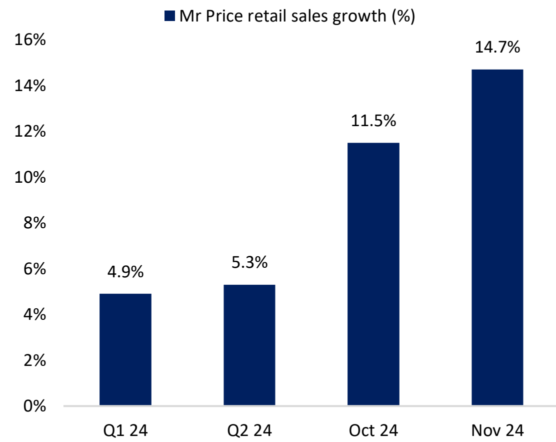


Chart 18: Mr Price sales growth accelerating



Source: Bateleur Capital; Bloomberg, Company reports

One of the major impediments to near term growth in SA is that the SA Reserve Bank continues to hold real interest rates at the highest level in 20 years, reflecting an overly hawkish inflation focus (Chart 19).

Two declines of 0.25% each since September 2024 are inadequate to assist the country's quest for higher economic growth and employment. Consensus currently forecasts only 0.5% of rate cuts in 2025 to complete the current rate cutting cycle (Chart 20).

With inflation at very low levels currently (3.0% in December 2024), there remains ample room to reduce interest rates well in excess of current expectations. This would significantly bolster consumption expenditure, bank advances and GDP growth.

Unfortunately, despite lagging global interest rate cuts to date, the SA interest rate cycle is unlikely to decouple meaningfully from developed market peers in the short-term.

Chart 19: SA real rates are elevated

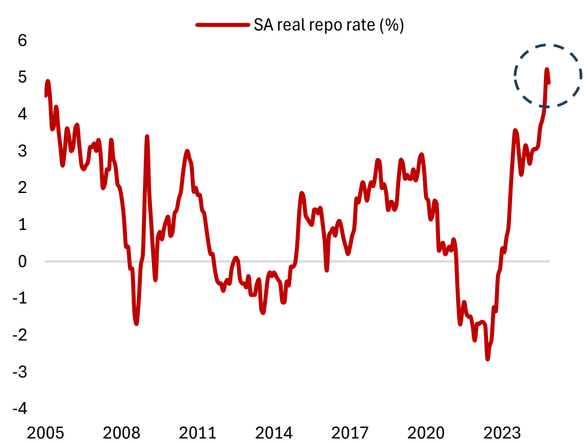
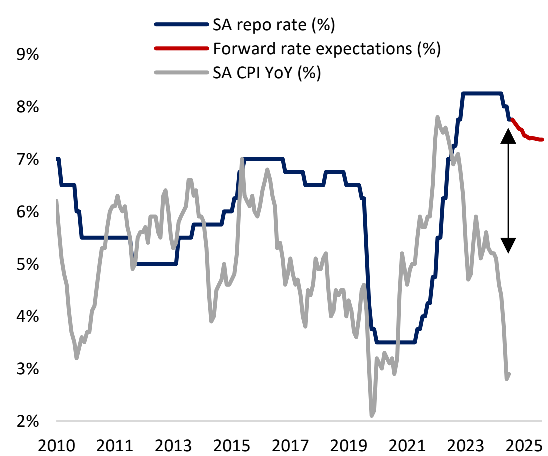


Chart 20: SA repo rate expectations



Source: Bateleur Capital; Bloomberg

Current fund positioning:

Current fund positioning as well as implemented asset allocation changes between the third quarter and end of calendar 2024 are shown in Table 4 overleaf.

The fund's weighting in JSE listed equities showed little change over the quarter, ending the year at 48% of fund NAV. SA domestic equities remain attractively valued and under owned despite the 2024 re-rating.

A new investment in Premier was initiated in the final quarter. Premier is a well-run food business with a focus on milling and baking. The company has been growing at the expense of the incumbent players, especially in bread, where it currently has a market share in excess of 25%.

Although the foreign equity portfolio weighting of 27% was in line with the third quarter – various changes were made to the composition.

The investment in ASML was sold following a weak new order update, while the Novo Nordisk holding was reduced on increasing competition and a disappointing trial outcome from potential blockbuster drug CagriSema. Profits were also partially realised in Philip Morris and Total, while the Comcast holding was fully realised.

New investments were initiated in diversified industrial business Honeywell - where a spin-off of its aerospace business is expected, online travel business Expedia, and global consulting group Accenture.

Foreign equities comprise an appropriate mix of growth and defensive companies – with no single investment accounting for more than 4% of fund value. While exposure is centred on US companies given the strong earnings outlook, we are mindful of elevated valuations, and remain underweight technology relative to the S&P 500 Index.

Domestic government bond exposure totalled 15% of fund value at year-end, marginally down from 16% at the end of June. The fund's bond holdings have an average maturity of 9 years.

SA government bonds remain attractive relative to cash – offering a high real yield into a declining rate environment. Following strong capital gains in 2024, we expect the majority of bond returns in 2025 to come from income yield.

Cash levels are healthy at 10%, earning a reasonable yield domestically, and are available to be swiftly deployed when opportunities arise.

The fund has no exposure to global bonds given the unattractive risk/reward trade-off, especially considering the potential for inflation to surprise to the upside in the US.

Table 4: Fund allocation changes between Q3 and year-end 2024

	Q3 2024 allocation (%)	Q4 2024 allocation (%)
JSE listed equities	48%	48%
Foreign listed equities	27%	27%
Total Equities	**75%**	**75%**
Domestic government bonds	16%	15%
Foreign government bonds	0%	0%
Domestic cash	4%	7%
Foreign cash	5%	3%
Total Cash & Fixed Income	**25%**	**25%**

We remain confident in delivering on the fund's investment objectives.

Sincerely,

Kevin Williams
23 January 2025

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[i] A1 Class Performance:
Since Inception (July 2010) Fund 13.4% | Benchmark 9.0%
1 Year: Fund 9.2% |Benchmark 6.9%
10 Year : Fund 9.8% | Benchmark 8.9%
Highest rolling 1 year return 39.0%, Lowest rolling 1 year return -7.2%.

The forecasts are based on reasonable assumptions, are not guaranteed to occur and are provided for illustrative purposes only.
Collective Investment Schemes in Securities (CIS) should be considered as medium to long-term investments. The value may go up as well as down and past performance is not necessarily a guide to future performance. CISs are traded at the ruling price and can engage in scrip lending and borrowing. A schedule of fees, charges and maximum commissions is available on request from the Manager. A CIS may be closed to new investors in order for it to be managed more efficiently in accordance with its mandate. Performance has been calculated using net NAV to NAV numbers with income reinvested. The performance (A1Class) for each period shown reflects the return for investors who have been fully invested for that period. Individual investor performance may differ as a result of initial fees, the actual investment date, the date of reinvestments and dividend withholding tax. Full performance calculations are available from the manager on request. There is no guarantee in respect of capital or returns in a portfolio. Annualised performance shows longer term performance rescaled to a 1-year period. Annualised performance is the average return per year over the period. Actual annual figures are available to the investor on request. Highest and lowest is returns for any 1 year over the period since inception have been shown. NAV is the net asset value represents the assets of a Fund less its liabilities.
Prescient Management Company (RF) (Pty) Ltd is registered and approved under the Collective Investment Schemes Control Act (No.45 of 2002). For any additional information such as fund prices, fees, brochures, minimum disclosure documents and application forms please go to www.bateleurcapital.com.
Prescient is a member of the Association for Savings and Investments SA. Bateleur Capital Pty Ltd, an AFSP; is the investment manager of the Funds.
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