



ASSET ALLOCATION

'We have never owned more local equity'

ClucasGray believes investors shouldn't underestimate the South African opportunity set.

by **PATRICK CAIRNS**

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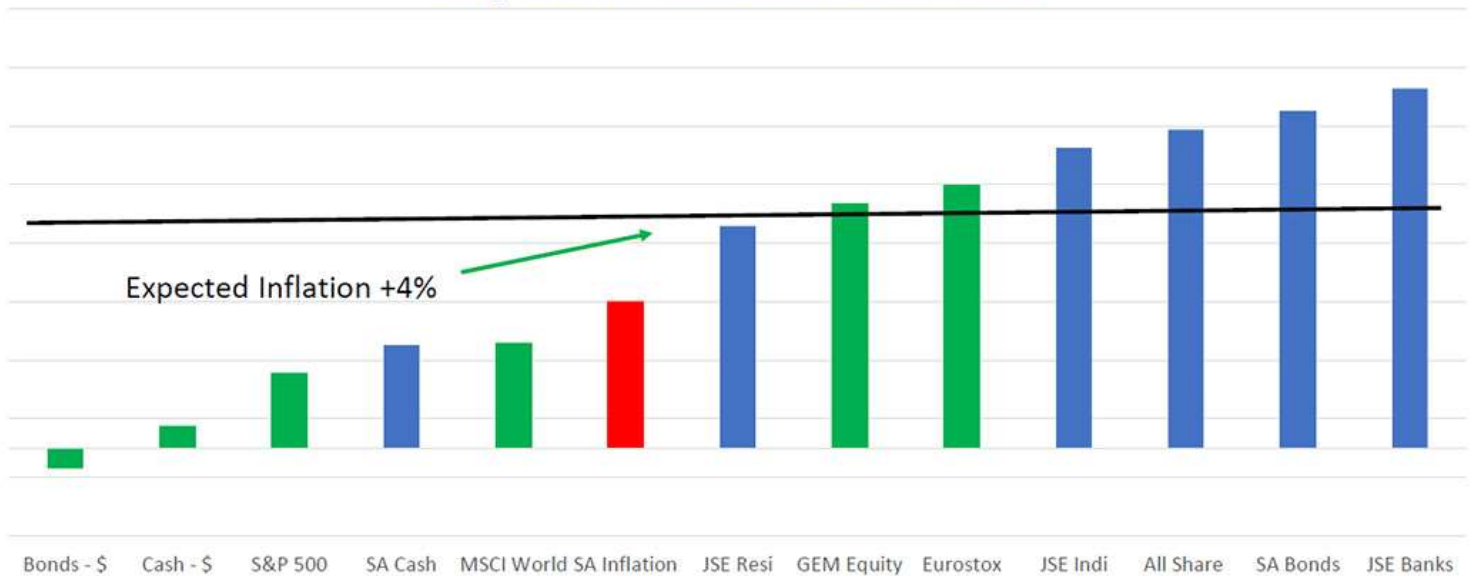


ClucasGray Asset Management's [Andrew Vintcent](#) remains bullish on local assets.

Speaking at the Meet the Managers event hosted by The Collaborative Exchange, Vintcent (pictured) said that, particularly in relative terms, South African equities and bonds offer a highly attractive risk-return opportunity.

'Although global markets have been pretty weak over the last while, it's quite clear that, outside of a few regions, the large majority of global equity markets look relatively fully-priced,' Vintcent said. 'The only way you can justify holding them in a multi-asset balanced fund, we think, is for the rand to depreciate quite materially from here.'

Expected Annualised Return



Source: ClucasGray Asset Management (click to enlarge)

Bond markets in the developed world are possibly even less attractive, with 10-year US Treasuries currently yielding 1.8% and 10-year German bunds 0.6%.

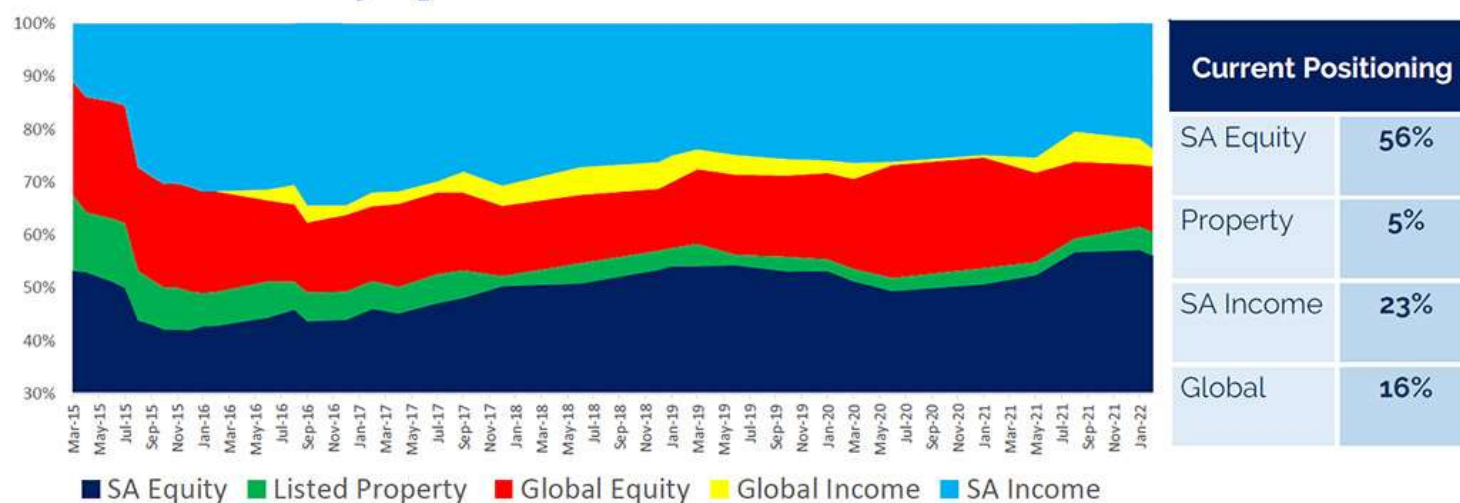
'If you are trying to generate a real rand return of inflation plus 4%, which has to be close to 10% in nominal terms, it's very difficult to make an investment case in some of these global assets at the moment.'

Conversely, ClucasGray is seeing highly attractive opportunities in local markets. Despite the strong recovery over the past 18 months, Vincent said that he still very much favours South African equities.

'We have never owned more local equity in the [ClucasGray Equilibrium Prescient fund](#). And global equity, we have never owned less.

'We have to invest where the opportunities are. And we are finding very limited opportunities in some of the global regions compared to what we believe is being presented to investors domestically.'

ClucasGray Equilibrium Fund Asset Allocation



Source: ClucasGray Asset Management (click to enlarge)

An indication of this is the amount of corporate action that has been seen on the local bourse.

‘Unless you start to see a rerating of a number of these companies in South Africa, we would expect that to continue,’ Vintcent said.

The attractiveness of local stocks is based on an improving earnings backdrop, the significant support of low valuations, and a weak, but stabilising currency.

‘The rand, in real terms, remains as weak as it was against the dollar in the 2015/2016 emerging markets crisis,’ Vintcent said. ‘It looks pretty stable over the last five to seven years, but if you throw any perspective at it, you get the sense that it remains a very weak currency.’

‘The opportunity set globally requires us to have a weak currency to justify owning large weightings in global assets. That eventuality may not play out because the rand remains structurally a weak currency.’

‘Real gems’

This is borne out by looking at purchasing power parity, based on the differential between the South African inflation rate and inflation in the US.

‘That has flatlined as our inflation has been moderating and US inflation has been rising. So, we would be cautious about expecting significant further weakness in the local currency.’

At the same time, the relative cost of capital in South Africa remains elevated, with the differential between local 10-year bond yields and 10-year US treasury yields ‘stuck at levels that are unusual relative to history’.

This not only creates an attractive investment opportunity in local bonds, but adds to the valuation argument for local equities.

'That elevated cost of capital is currently hampering the equity market rerating. We think that as that cost of capital subsides, we would expect to see a commensurate rerating of the equity market.

'There are some real gems that are undervalued in this country.'