Ninety One

Emerging Companies Fund

Market context

The consensus coming into 2025 was for a continuation of US exceptionalism under a new Republican administration. Instead, investors were served with unpredictable trade policy, leading to heightened volatility, weaker US growth expectations, and a shift in leadership abroad.

In the US, equity markets struggled, weighed down by renewed trade tensions, inflation concerns and the unwinding of big tech dominance. The S&P 500 posted its worst quarterly return in three years, while investor sentiment shifted toward more traditional sectors.

In contrast, European equities delivered strong returns, buoyed by a structural shift in fiscal policy towards higher defence spending and relative economic resilience. UK equities followed suit, supported by large-cap banks and defence firms.

South African equities delivered a standout performance, with the All Share Index gaining 9.0%, outpacing the MSCI World (-1.8%) and MSCI Emerging Markets (+2.9%) in US dollar terms. The rally was underpinned by a significantly stronger resources sector, fuelled by a surge in precious metal prices. Gold was the standout performer, as investors sought safe-haven assets amid growing geopolitical uncertainty and the implementation of global trade tariffs.

To read more, please click here or visit the Insights section of www.ninetyone.com.

Performance

For the quarter, the portfolio outperformed its benchmark and its peer group.

Overweight positions in Master Drilling, AECI and Metrofile all contributed positively to relative performance. Master Drilling reported its 2024 result as at quarter-end. It was a good performance, with earnings up materially, strong cash generation and a healthy pipeline of work. The share price responded positively and helped the portfolio's performance. The most pleasing aspect is that Master Drilling is still only trading on a PE of 4x and has a good chance of growth into 2025, even with the current macro backdrop. Metrofile also reported its results, but that was not what helped the share price. The group has received "approaches" with regard to acquiring the business. This resulted in an instant increase in the share price and helped to provide a floor, even as global markets declined.

The portfolio is underweight many of the larger South African retailers (Mr Price, TFG, Truworths, and Pepkor), which helped relative performance as prices fell on the back of tariff news out of the US and tensions within South Africa's Government of National Unity. Valuations for these stocks have become more attractive, but we still prefer smaller retailers and industrial companies.

Some of the largest detractors from relative performance over the quarter were key holdings, namely WBHO, Raubex and Hudaco. These shares all performed well in 2024, and the market decided to take profits and reallocate the capital. We are not concerned by this correction since these counters still trade at PEs of less than 8x and have solid business models and prospects. Illiquid shares tend to trade in this fashion. We are confident that if the companies deliver on their expectations, their stock prices will continue to perform over time.

Not holding Impala, Sibanye Stillwater, and enough of Harmony Gold detracted from relative performance. Precious metal prices bounced in the first quarter, causing the share prices of these companies to increase quickly. The impact was, however, mitigated to a degree due to the portfolio holding some Harmony Gold (for most of the quarter) and Northam Platinum.

Portfolio activity

The past quarter saw the portfolio take profits on its holdings in Harmony Gold, Life Healthcare and Pick n Pay. These counters had performed well and we decided to reallocate the capital to other opportunities.

The most significant buying over the last quarter related to Impala Platinum, Exxaro, Northam and Sun International. We decided to close our underweight position in the PGM sector. The commodity basket seems to have found a bottom and the fundamentals (and price action) suggest that the markets are "tight" and that small movements in demand or supply could push the prices significantly higher. In addition, we felt the rand's strength was at risk and therefore decided to increase the portfolio's exposure to a weakening currency. We increased our exposure to Sun International during the quarter. The current multiples (PE of about 8x and dividend yield close to 10%) seem disconnected from the group's fundamentals. The large land-based casinos are solid and highly cash-generative, while the online gambling portion of the business is growing quickly and requires very little capital to do so.

The portfolio's cash position is now relatively low and should result in minimal drag should the current rally continue.

Outlook

We continue to focus on bottom-up mid- and small-cap ideas. These will be based on fundamental research that highlights mispricing by the market. Over the short term, the portfolio's relative performance may be impacted by sentiment and macroeconomic changes. However, in the long run, the portfolio's positioning should support performance even if the environment only partially aligns with our expectations.

The portfolio is still exposed to SA Inc. stocks, with a large exposure to the industrials sector. It currently has a good balance of rand-hedge stocks, interest rate-sensitive businesses, precious metals producers and strong local industrial stocks. We believe the portfolio's average valuation metrics are attractive, with what looks like a very low through-the-cycle price-to-earnings ratio (PE) of about eight (even the 12-month forward PE is now close to 8x and the forward dividend yield is over 6%.

Disclaimer

Further information

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