

Namibian Enhanced Income Fund: Protecting capital through active management

1 August 2024



M&G Investments

Since inception ten years ago, the M&G Namibian Enhanced Income Fund continued to distinguish itself by demonstrating robust performance and reduced volatility through active management and downside protection. This achievement underscores the fund's strategic positioning to navigate dynamic market conditions.

Steady performance

The fund's active management strategy remains pivotal, continuously assessing market conditions to enhance returns while safeguarding capital. This approach reflects M&G's commitment to delivering consistent performance relative to benchmarks, ensuring clients benefit from sustained value over time.

The fund maintained its approach of focusing on a diversified portfolio of lower-risk fixed income instruments which resulted in pleasing performance during the recent period of election-induced volatility. For the latest one-year period, the fund delivered a return of 9.2% surpassing its cash benchmark, Namibia's IJG Money Market Index, which returned 8.5%. Over the three-year period, the fund achieved an impressive return of 7.2%, outperforming the benchmark's 6.7% (all figures A class annualised, after fees to 30 June 2024).

Asset allocation and positioning

The fund benefits from a flexible investment mandate, allowing it to allocate across a broad spectrum of assets including listed property, equities, and offshore investments. Over the past year, the fund's managers adopted a cautious stance, particularly mindful of the risk posed by the South African election, which could potentially increase asset price volatility. They also exercised caution with respect to the SA property market, maintaining a modest position in the asset class. Exposure to offshore credit was tilted towards the investment grade universe, opting to avoid high yield due to inadequate spreads relative to the associated risk that investors would assume.

The Fund has a significant stake in the [M&G Enhanced Income Fund](#), with the remainder allocated to Namibian assets such as inflation-linked bonds, bank floating rate notes, and the [award-winning M&G Namibian Money Market Fund](#).

Tactically alert

In managing this fund, we remain focused on managing drawdowns, are mindful of cyclical trends, and alert to tactical opportunities in the market in order to deliver positive outcomes to our clients.

During April, we seized the opportunity presented by the steepness of the Inflation Linked Bond (ILB) yield curve by executing a pairs trade. We extended the duration of our real government bond exposure, moving from the short-term end towards the middle of the curve, resulting in a significant increase in yield while maintaining a neutral duration stance. Despite the apparent attractiveness of implied real yields from nominal bonds compared to inflation-linked bonds, we retain some allocation to inflation-linkers. This decision is driven by the relatively high absolute level of real yields they offer and their role as a hedge in the portfolio against potential inflation persisting above the SARB's 4.5% target.

Following the election and the May MPC meeting, we opted to increase our exposure to interest rate risk along the nominal rate curve, maintaining this higher duration position for the remainder of the second quarter. This strategy supported performance amidst declining yields. However, our preference remains for the shorter end of the yield curve.

Throughout the quarter, we maintained modest positions in defensively favoured, high-yielding South African listed property stocks recommended by our property team. Additionally, we augmented our foreign bond exposure by adding short-term US Treasury bonds to our existing portfolio of US investment grade floating rate securities. Both positions offered attractive yields in hard currency terms. We initially held these foreign exposures without currency hedging leading up to the election, but subsequently hedged them back into rand during a period of heightened volatility and currency depreciation immediately following the South African national elections.

Our management of duration risk was tactical over the second quarter, proving advantageous amidst the ensuing market volatility.

Namibian bonds, represented by the IJG All Bond Index, returned 9.9% in Q2 2024 (in N\$), contributing positively to the fund's performance. Similarly, South African bonds delivered a return of 7.5% for the second quarter. This saw the yield on the 10-year SA government bond fall from 12% at the beginning of the quarter to end around 11.25%. For the year to date, Namibian bonds delivered 4.8% return, South African bonds represented by the All Bond Index also performed well, returning 5.6%, outpacing global bonds which returned -3.5% (both in rands).

Looking ahead, forecasts suggest a downward trend in inflation for both Namibia and South Africa, with expectations of declining local interest rates in the medium-term, mirroring global trends. This anticipated environment could positively impact the performance of South African bonds, equities, and listed property, potentially leading to revaluations from their current undervalued levels. However, it may pose challenges for cash-related instruments, making income-focused solutions like the M&G Namibian Enhanced Income Fund an attractive option for investors, which is also well-positioned to take advantage of a decreasing interest rate environment.

In conclusion, the [M&G Namibian Enhanced Income Fund](#) stands as a testament to our investment approach and process in delivering robust returns amidst market complexities. With a forward-looking approach and the flexibility to capitalize on evolving market dynamics, the fund is well-positioned to continue outperforming benchmarks and meeting investor expectations. As economic landscapes evolve, investors can rely on the fund's disciplined management and diversified portfolio to navigate uncertainties and seize opportunities across various asset classes.

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