

# SA equities: where from here?



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*South African equities have rebounded strongly since the May 2024 elections, driven by reforms, improved business confidence, and a stronger rand, with SA-sensitive sectors leading the gains. Despite the recent rally, we believe valuations remain attractive, and the investment case compelling.*

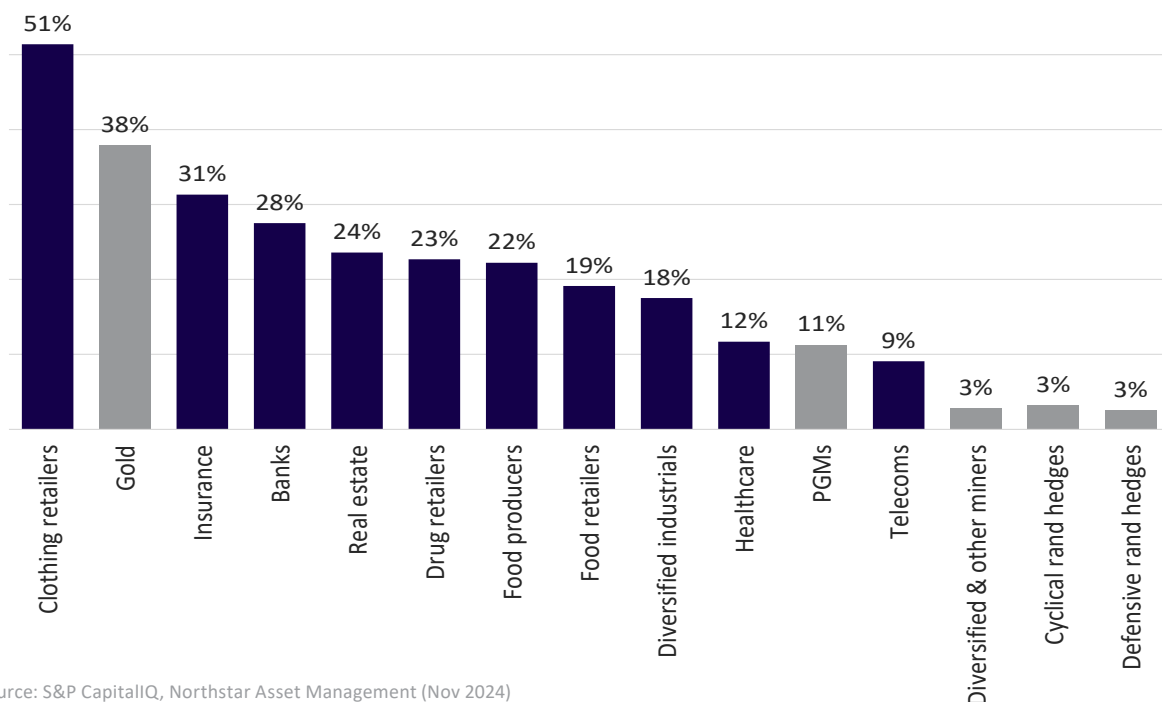
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## Background

Over the past two years, we have emphasised the "South African equity opportunity" despite a challenging macroeconomic environment and various structural bottlenecks in key areas such as rail, ports, and electricity. Eighteen months ago, while most South African-focused investors acknowledged the market's undervaluation, they were primarily concerned with the effects of load-shedding and speculating on how long it would take to resolve. Over the past year, however, several positive catalysts have emerged. The outcome of South Africa's national elections in May and the subsequent formation of a Government of National Unity (GNU) proved to be pivotal, igniting a rally in SA-sensitive assets and sparking a recovery in the rand.

Since the beginning of April 2024, the local equity market (JSE Capped Swix) has surged by 18%, with South African-sensitive sectors significantly outperforming the broader index. As highlighted in the chart below, 9 out of the top 10 best-performing sectors (highlighted in blue) are driven by SA-related factors. These sectors, previously underperformers due to weak growth, have shown marked improvement, coinciding with a stronger rand, which has appreciated approximately 11% against the US dollar during this period. Remarkably, in US dollar terms, SA equities rank as the third-best-performing emerging market year-to-date, trailing only Taiwan and Peru.

**Chart 3: SA equities – median sector performance – 01 April to 31 Oct 2024**



Source: S&P CapitalIQ, Northstar Asset Management (Nov 2024)

**What's changed since the elections? Medium-term growth expectations**

From an economic perspective, since May 2024, South Africa has experienced a strong recovery in leading indicators and a significant improvement in business confidence. This recovery is largely attributed to enhanced electricity capacity and the successful transition to a coalition government. Notably, opposition parties have embraced Operation Vulindlela, a joint initiative between the National Treasury and the Presidency aimed at modernising and transforming network industries such as electricity, water, transport, and digital communications.

According to Nedbank (November 2024), successful reforms in electricity, rail, and port freight, combined with improved policy certainty, could elevate South Africa's potential GDP growth to 3.9% by 2027, up from the current 0.9%. While potential and actual growth differ, consensus GDP growth estimates for 2025 and 2026 have also risen to 1.4% and 1.8%, respectively, as economists anticipate improvements in gross fixed capital formation and household consumption to drive growth.

Additionally, credit rating agencies have responded positively. S&P, for example, revised its credit rating outlook for South Africa to "positive" from "neutral" in November 2024, citing the government's commitment to private-sector-friendly infrastructure reforms.

**SA stocks: What's priced in?**

Although the SA equity rally over the past few months has reduced some of the potential upside, we believe valuations remain attractive and the investment case compelling. While the deep discounts previously embedded in local stocks have moderated to more normalised levels, current prices still do not fully reflect the potential for a cyclical upswing driven by lower interest rates and inflation.

Based on our local equity buy-list, we see double-digit return opportunities across most SA-sensitive sectors, particularly among banks, insurers, retailers, and in the diversified industrial space. Despite an uncertain global macroeconomic backdrop, including slowing Chinese growth and uncertainty surrounding new US foreign policies under Trump, we also see positive medium term prospective returns for local miners and global cyclical stocks at current levels.

**How are we positioned and outlook**

Northstar's local equity portfolios have benefited from the strong rebound in South Africa-sensitive assets over the past six months. While some volatility is expected as we approach year-end, we remain optimistic about the medium-term outlook for South African cyclicals and select rand-hedge opportunities.

Our approach to portfolio construction is based on a fundamental bottom-up methodology, focusing on detailed risk assessments and stock valuation work. We apply this approach rigorously when allocating capital. Our portfolio's best risk-adjusted opportunities are currently concentrated in the diversified industrial and financial sectors, as well as select opportunities among diversified miners, cyclical rand hedges, and Naspers/Prosus. We are underweight in local defensives and maintain a gold equity position as insurance.

# NORTHSTAR

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