ALLANGRAY

Allan Gray Life-Orbis Global Balanced (RRF) Feeder Portfolio

Inception date: 1 August 2015

31 August 2019

Portfolio objective and benchmark

The Portfolio aims to balance capital appreciation, income generation and risk of loss in a diversified global multi asset class portfolio. The benchmark is a composite consisting of 60% of the MSCI World Index (net dividends reinvested) and 40% of the JPM Global Government Bond Index.

Product profile

- This is a feeder portfolio, investing in the Orbis SICAV Global Balanced Fund which is actively managed by Orbis.

Investment specifics

- This Portfolio is available as a linked policy issued by Allan Gray Life Limited available only to retirement funds.
- Minimum investment: R20m.
- The Base Refundable Reserve Fee is levied in the underlying Orbis SICAV Global Balanced Fund.

Fund manager quarterly commentary as at 30 June 2019

The performance of the Orbis SICAV Global Balanced Fund over the last year has been poor. These results have also dragged down the Portfolio's longer-term performance numbers, which are now far below the standards we set for ourselves.

We appreciate how uncomfortable these periods are. It is challenging to hear the market shouting that you are wrong, even when the fundamental evidence says you are right. But maintaining our discipline in the face of this discomfort is at the core of our job, and we believe it is the very reason we can add value over the long term.

As we would always expect, the recent performance was driven chiefly by our security selection, not by our stances towards different asset classes. This is by design. We aim to deliver maximum exposure to our security selection skill, while maintaining a risk profile consistent with the Portfolio's mandate. In 2018, we had our fair share of losers, had few big winners, and suffered as dislocations between prices and fundamentals widened for many of our favourite (and least favourite) securities.

The underperformance in 2019 has been a different story. In our view, the trends that have hurt returns are clearly cases of market prices moving ever further away from fundamentals. This leaves us more enthusiastic about the relative return potential of the Portfolio. This divergence is clear in fixed income, where a record near-$13 trillion of bonds globally now trade at negative yields. It's also clear in the substantial outperformance of financial assets (like stocks and bonds) over hard assets (like commodities). It makes sense that central bank money printing would push up stock and bond prices, but not compared to commodities. Central banks can't print gold and oil.

The most significant trends year to date have occurred within equities. Some might remember what came to be called the TMT (Tech, Media, Telecom) bubble of the late 1990s. The narrowness of the current market is beginning to bear some striking similarities to this period. In 1999, the very largest stocks were driving the market higher to the exclusion of all else. The same is happening now, both globally and in the US.

The headline indices are dominated by the largest shares, and they're doing fine. The top 50 shares in the US set new record highs last January, again in October, and again this April. But if we look instead at an equal-weighted index of global stocks, we see that the average stock remains mired 18 months into a bear market that started on 26 January 2018. Well, so what? Maybe these trends are justified by fundamentals. But they aren't. Once again, non-fundamental drivers appear to have taken the steering wheel.

In the current environment, it's clear that, as ever, investors don't take the same degree of comfort from all quality companies. Good businesses with hard-to-see risks trade at great company prices, and good businesses with easy-to-see risks trade at bad company prices.

For example, consider our discussion of Coca-Cola last quarter. To recap: the company's revenues and earnings have failed to grow, it is paying out every cent it earns to support the dividend, and it is piling on ever more debt. Those are big fundamental risks, but they aren't obvious, and they will never be on the front page of a newspaper. Google, on the other hand, has an obvious, front-page-friendly risk: tech regulation.

Today, in the collective wisdom of investors, 0% growth Coke merits a valuation of 32 times earnings, while Google, which has grown revenues and earnings by over 15% per annum, merits a valuation of 24 times (ex-cash) earnings. To us, that looks unreasonable. And yet Coke has been, by far, the more comfortable company to own over the last three months. But it doesn't for one second make us think we should sell Google and buy Coke.

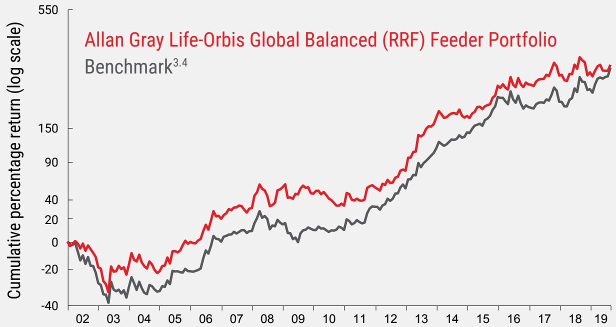
At a high level, that is one of the dominant patterns in the Portfolio today. We own what we think are some very high quality businesses that the market has excessively punished for having obvious risks – and we don't own what we think are the stretched businesses trading at silly prices. Shares of underappreciated but fundamentally strong businesses currently represent over a third of the Orbis SICAV Global Balanced Fund. That leaves us increasingly enthusiastic about what we own and new opportunities the market is coughing up. We believe that the divergence among securities is extreme and at irrational levels. Unfortunately, irrationality doesn't correct on any set schedule, and we humbly appreciate your patience while we wait this out.

Portfolio information on 31 August 2019

Assets under management	R612m

Performance net of fees[1]

Cumulative performance since inception



% Returns[1,2]	Portfolio		Benchmark[3,4]	
	ZAR	US$	ZAR	US$
Since inception	8.4	6.8	8.2	6.6
Latest 10 years	10.2	3.1	13.9	6.5
Latest 5 years	8.3	0.8	12.1	4.4
Latest 3 years	3.6	2.6	7.7	6.6
Latest 2 years	4.7	-3.1	14.1	5.6
Latest 1 year	-5.9	-9.2	7.8	4.1
Latest 3 months	4.7	0.7	9.1	4.9

Asset allocation on 31 August 2019

This portfolio invests solely into the Orbis SICAV Global Balanced Fund

	Total	North America	Europe	Japan	Asia ex-Japan	Other
Net equity	58.8	11.4	22.4	6.6	14.3	4.1
Hedged equity	18.8	11.8	3.9	0.0	1.9	1.1
Fixed interest	16.4	15.9	0.2	0.0	0.2	0.1
Commodity-linked	5.6	0.0	0.0	0.0	0.0	5.6
Net current assets	0.5	0.0	0.0	0.0	0.0	0.5
Total	**100.0**	**39.1**	**26.5**	**6.6**	**16.4**	**11.4**
Currency exposure						
Fund	100.0	43.2	34.0	10.9	6.6	5.3
Index	100.0	57.5	26.2	13.1	1.0	2.2

1. The returns prior to 1 August 2015 are those of the Allan Gray Life Foreign Portfolio since its inception on 23 January 2002. This Portfolio invested in a mix of Orbis funds. The Investor Class Fee was levied in the underlying Orbis funds.
2. Investment returns are annualised (unless stated otherwise), except for periods less than one year. Performance as calculated by Allan Gray as at 31 August 2019.
3. 60% of the MSCI World Index (net dividends reinvested) and 40% of the JPM Global Government Bond Index.
4. The benchmark prior to 1 August 2015 is that of the Allan Gray Life Foreign Portfolio which is 60% of the MSCI All Country World Index and 40% of the JPM Global Government Bond Index.

Note: There may be slight discrepancies in the totals due to rounding.

Disclaimer

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