AllanGray

Inception date: 1 April 2015

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

31 December 2021

Portfolio objective and benchmark

The objective of the Portfolio is to outperform the MSCI World Index at no greater-than-average risk of loss in its sector. The benchmark is the MSCI World Index, with net dividends reinvested.

Product profile

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

Investment specifics

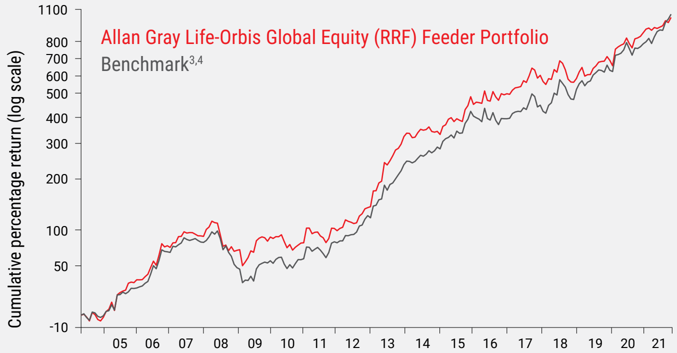
- This Portfolio is available as a linked policy issued by Allan Gray Life Limited available only to retirement funds.
- Minimum investment: R20m.
- The Base Refundable Reserve Fee is levied in the underlying Orbis Institutional Global Equity Fund.

Portfolio information on 31 December 2021

Assets under management	R595m

Performance net of fees[1]

Cumulative performance since inception



% Returns[1,2]	Portfolio		Benchmark[3,4]	
	ZAR	US$	ZAR	US$
Since inception	14.8	9.3	14.9	9.5
Latest 10 years	19.0	11.2	20.5	12.6
Latest 5 years	13.4	10.1	18.6	15.0
Latest 3 years	19.2	15.2	25.9	21.7
Latest 2 years	19.5	12.1	26.6	18.8
Latest 1 year	18.2	8.9	32.2	21.8
Latest 3 months	7.0	1.1	14.0	7.8

Asset allocation on 31 December 2021

	Total	North America	Europe and UK	Japan	Asia ex-Japan	Other
Net equities	98.7	40.7	26.3	10.5	14.0	7.1
Net current assets	1.3	0.0	0.0	0.0	0.0	1.3
Total (%)	**100.0**	**40.7**	**26.3**	**10.5**	**14.0**	**8.4**
Currency exposure of the Orbis Institutional Global Equity Fund						
Fund	100.0	44.6	27.9	10.6	9.8	7.1
Index	100.0	72.3	18.2	6.2	1.1	2.2

1. The returns prior to 1 April 2015 are those of the Allan Gray Life-Orbis Global Equity Portfolio since its inception on 18 May 2004. The Investor Class Fee was levied in the underlying Orbis Global Equity Fund.
2. Investment returns are annualised (unless stated otherwise), except for periods less than one year. Performance as calculated by Allan Gray as at 31 December 2021.
3. MSCI World Index, with net dividends reinvested.
4. The benchmark prior to 1 April 2015 is that of the Allan Gray Life-Orbis Global Equity Portfolio which is the FTSE World Index, including income.
5. Underlying holdings of Orbis funds are included on a look-through basis.
6. Includes holding in Prosus N.V., if applicable.

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

Top 10 share holdings on 31 December 2021 (updated quarterly)[5]

Company	% of Portfolio
British American Tobacco	6.0
GXO Logistics	3.6
XPO Logistics	3.4
UnitedHealth Group	3.2
Naspers[6]	3.1
Anthem	3.1
Global Payments	2.8
ING Groep	2.8
FLEETCOR Technologies	2.7
Howmet Aerospace	2.6
Total (%)	**33.4**

Fund manager quarterly commentary as at 31 December 2021

As 2021 draws to a close, we are as frustrated about the performance of the Portfolio as we are confident about the opportunities in it.

The market environment has been shaped by investor psychology around COVID-19. At times, it's felt like the market is valuing companies for the next 10 years based on the COVID-19 outlook for the next 10 weeks. From November 2020 through May 2021, vaccine optimism was a tailwind for our relative performance, but since then, variant pessimism has been a headwind.

While we naturally cannot control the environment, what we can control is which companies we choose to own in the Portfolio.

Some stocks that we haven't owned in the Portfolio, or haven't owned as large positions, such as Apple, Microsoft, and Google, performed fantastically well in 2021, especially from May through November. In fact, just five stocks accounted for almost all of the return of the FTSE World Index over that period.

But many of the highest-flying stocks in 2021 do not have anything like the entrenched dominance or firehose-like cash generation of the tech giants. Some 70 shares in the US trade for more than 10 times revenues, or 10 times money coming in the door before any expenses. With such sky-high valuations, in our view many of today's glamour darlings are likely to leave investors nursing losses. We remain happy to avoid the froth. Closer to home, some stocks we have owned have performed poorly, with a nearly eight percentage point drag on the Portfolio's returns from the 10 largest detractors.

We still hold nine of those 10. We think the value of our companies is little changed, but the market has reassessed them far more negatively. As a result, we think the discount to intrinsic value is wider – in some cases much wider – than it was six months ago. The same is true for many other holdings. That has been a frustrating experience to date, but it leaves us more enthusiastic about the Portfolio today.

The best way to understand that enthusiasm is to look at the Portfolio as we do – from the bottom up, company by company. The following positions, which together represent over a quarter of the Portfolio, exemplify the value we see.

Growth cyclicals

Investors have grown accustomed to thinking of growth as synonymous with tech – virtual businesses that can deliver growth regardless of the economic cycle. Yet companies with exposure to the economic cycle can offer attractive growth potential, too. We believe we've found five such opportunities in the US: XPO and GXO Logistics, which we discussed in March, as well as Howmet Aerospace and two specialised payments companies.

Howmet Aerospace makes precision aerospace parts. That is a good business – specifications are demanding, reliability is paramount, and customers insist on proven suppliers. The parts Howmet makes are so specialised that in some cases it is the only company on earth capable of producing them. The company has faced headwinds as COVID-19 took an axe to commercial air travel, but cut costs substantially and raised prices, managing to keep margins relatively flat and free cash flow positive despite a substantial hit to revenues. In a more normal demand environment, we believe Howmet can eventually earn US$3 a share – roughly triple its 2019 earnings – making its current US$32 share price a bargain for long-term investors prepared to wait out the recovery in air travel.

Fleetcor and Global Payments are payments businesses focused on small business niches. The two shares were roundly thrashed over the past few months following disappointing spending data from Visa and weak trading among many small businesses. In our view, the sell-off is a clear overreaction to short-term concerns, and over the long term, both businesses offer outstanding growth potential. By focusing on their customer niches, we believe both Fleetcor and Global Payments can grow earnings by roughly 20% per annum over the long term, a far faster rate than the average stock, yet today both trade at just 15 times our estimate of forward earnings, a substantial discount to the wider market.

The boring middle

We've never found the distinction between "growth" and "value" to be all that useful. Yet investors often rush to bucket stocks into one or the other camp, focusing on expensive, fast-growing upstarts or cheap, slow-growing dinosaurs. That neglects plenty of stocks in the "boring" middle – letting us find several compelling ideas there. In addition to US health management organisation UnitedHealth Group, which we discussed last quarter, this group also includes Comcast and Dollar General.

Comcast is the leading cable and broadband provider in the US, and it also owns NBC Universal, and Sky in the UK. We got an exceptional opportunity to buy Comcast in 2020, when investors punished the stock as COVID-19 hurt the film, theme park, and sports broadcasting businesses. A year on, we believe the stock is still underappreciated due to worries about COVID-19 and cord cutting (when a customer drops TV in favour of streaming services). COVID-19 challenges will recede in time, and cord cutting is actually beneficial for Comcast's margins – as customers tend to purchase more bandwidth when switching to streaming services. Our proprietary data analysis suggests that Comcast should be able to out-compete slower service from competitors. We believe Comcast can grow earnings at a double-digit rate over our investment horizon, yet it trades at a steep discount to the wider market.

Dollar General is the original dollar store and still the leader, with over 17 000 stores in the US. Over the long term, the company has steadily grown earnings by 16% per annum while generating above-average returns on capital. By focusing on smaller stores, building those stores more cheaply, staffing them more efficiently, and filling them with only essential goods, Dollar General generates much higher returns than its peers on each store it opens. While Amazon offers cheap goods too, delivery is slower and more costly in rural areas, often making Dollar General a more convenient choice for rural customers. And because it focuses on lower-cost goods, Dollar General's sales are often counter-cyclical, benefiting as consumers become more price-conscious in recessions. Yet today, we do not have to pay up for these attractive fundamental strengths – we see Dollar General as a much-better-than-average business trading at an average price.

Chinese internet

We remain enthusiastic holders of NetEase and Naspers (whose key asset is a stake in Chinese internet goliath Tencent) despite the turbulence of 2021. As we wrote last quarter, we believe both shares trade at larger discounts to intrinsic value following their recent share price weakness, though the position sizes are tempered by our sober assessment of the potential regulatory risks.

The whole Portfolio

The stocks above show a pattern that is common to the wider Portfolio: getting much better quality than we are paying for. In aggregate, the companies in the Portfolio have grown revenues more quickly than the average business over the long term, while generating similar returns on equity. Yet today our shares trade at a 35% discount to the average stock. Getting similar or better quality at a 35% discount strikes us as exceptionally good value – value that leaves us both excited and confident about the opportunities ahead.

Adapted from a commentary contributed by Rob Perrone, Orbis Investment Advisory Limited, London

Tel 0860 000 654 or +27 (0)21 415 2301 **Fax** 0860 000 655 or +27 (0)21 415 2492 **Email** institutional@allangray.co.za **www.allangray.co.za**

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MSCI Index

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FTSE Russell Index

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