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

Inception date: 1 April 2015

31 August 2019

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 manager quarterly commentary as at 30 June 2019

Contrarian investing is a strange profession. When things are going well, you can look like a magician — earning extraordinary returns while others flounder. At other times, you can follow precisely the same process and look hopelessly out of touch. We have spent an embarrassingly large amount of time in the latter camp of late.

In truth there is very little alchemy to our approach, in either the positive or negative direction. The fluctuations in relative performance mask what is ultimately a rather solitary endeavour: studying financial statements and waiting patiently to purchase shares of good businesses at a discount. The challenge at times like this, as expressed so eloquently by Rudyard Kipling in his most famous poem, is to "meet with triumph and disaster, and treat those two impostors just the same".

Markets tend to do the opposite. Share prices, driven by fickle human emotions of greed and fear, are far more volatile than the fortunes of the real companies they represent. Exploiting these emotional extremes is what enables the contrarian investor – with a focus on intrinsic value and a willingness to be different – to earn superior long-term returns.

Unfortunately, we don't get all our investment decisions right. We recognise that we have tested your patience and lost the authority simply to say "trust us". But if you can allow us a bit of enthusiasm, we believe the value inherent in the Portfolio increasingly tells an exciting story.

Our definition of a bargain lies in the 'sweet spot' between price and quality – an above-average company trading at discount price. In the market environment of the last few years – characterised by insatiable appetite for perceived "safety" – we have found such opportunities to be rare. Instead, the above-average companies have been expensive, while many of the discounted ones have been cheap for good reason.

Encouragingly, the stocks held in the Portfolio today are significantly cheaper than the World Index and they are fundamentally better businesses. Honda Motor is an example. At current prices, Honda's valuation is trading below levels last seen during the global financial crisis. But what about self-driving cars, the trade war, ride-sharing and electric cars? While the risks facing Honda are pertinent, our assessment is that they may ultimately prove to be overblown over our investment horizon. Instead of seeking to predict the future with certainty, our approach is to assess the full range of possible outcomes, and to compare that with the expectations embedded in Honda's current share price.

The results are illuminating. At only 0.7 times tangible book value, Honda's shares are trading at less than half their long-term historical average rating, and are embedding a significant destruction of value that we believe is wholly inconsistent with the company's four-decade history of consistent profitability. It is true to say that the transition to electrified vehicles will be a challenge for all car makers, but it's sobering to recall that – even some 15 years after Elon Musk founded Tesla – electric cars still only made up two out of every 100 cars sold globally last year. As for all the hype around ride-sharing, it's easy to forget that the most common form of shared vehicles have been around for decades (we used to just call them "taxis").

At $45 billion, Honda's current market price seems to ignore its most attractive asset. Honda is the world's largest motorcycle manufacturer with a dominant (75%+) share in emerging markets such as Thailand, Vietnam, Indonesia and Brazil. Giving due credit for this gem of a business, one almost gets Honda's car manufacturing business (with its $100 billion of revenues) for free. Such are the opportunities that become available when investors focus relentlessly on predictability.

Looking more broadly at the current Portfolio, we see similar mispricings for many other high-quality businesses. For example, there are three China-related shares – NetEase, Autohome, and Naspers (Tencent) that stand out as highly profitable, cash-rich entrepreneurial businesses with above-average growth prospects. Together these comprise 18% of the Portfolio and more than half of the Portfolio's emerging markets exposure. Clients have often asked how we get comfortable with this positioning, particularly amid a raging trade war and protests in the streets of Hong Kong. Our answer is that being "comfortable" isn't our goal – delivering superior risk-adjusted returns is – and the two things don't always go together.

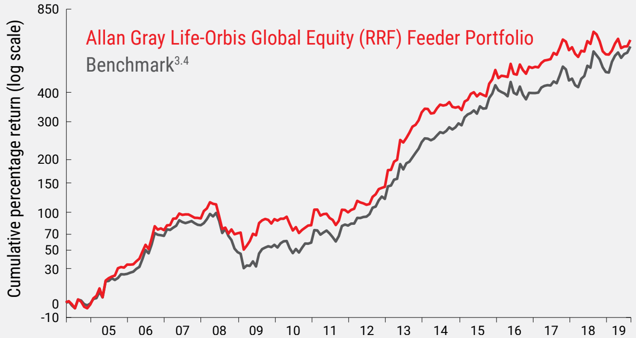
That's not to say all of our stock selections will turn out to be great investments. But it is fair to say that the individuals managing your capital – and our own – are feeling significantly more excited about the Portfolio today than we have been for some time. We remain humbled by your persistence and determined to earn your trust and confidence.

Portfolio information on 31 August 2019

Assets under management	R940m

Performance net of fees[1]

Cumulative performance since inception



% Returns[1,2]	Portfolio		Benchmark[3,4]	
	ZAR	US$	ZAR	US$
Since inception	14.1	8.3	13.7	7.9
Latest 10 years	14.8	7.4	16.7	9.2
Latest 5 years	10.5	2.9	13.8	6.0
Latest 3 years	6.5	5.4	10.7	9.6
Latest 2 years	5.9	-2.0	15.1	6.5
Latest 1 year	-6.1	-9.4	3.9	0.3
Latest 3 months	6.4	2.3	9.1	4.9

Asset allocation on 31 August 2019

	Total	North America	Europe	Japan	Asia ex-Japan	Other
Net equity	96.4	33.0	17.6	13.8	21.6	10.3
Net current assets	3.6	0.0	0.0	0.0	0.0	3.6
Total (%)	**100.0**	**33.0**	**17.6**	**13.8**	**21.6**	**13.9**
Currency exposure of the Orbis Institutional Global Equity Fund						
Fund	100.0	45.9	24.8	8.1	10.4	10.8
Index	100.0	66.8	20.8	8.1	1.6	2.6

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 August 2019.
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.

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

Disclaimer

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