

QC

Quarterly Commentary
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COMMENTS FROM THE CHIEF OPERATING OFFICER

Rob Formby



... avoiding risk entirely
may present you with
an unforeseen outcome
of missing opportunities ...

I recently attended a presentation by trend analyst Dion Chang. He spoke passionately about the way the world is transforming as industries digitise and competition from unexpected sources comes knocking on the door of entrenched household names. Add to this the changing needs and demands of Generation Z (born between 1995 and 2010), who seem more focused on sharing everything from vehicles to workspaces, as opposed to selfies and a minute-by-minute account of their day like their millennial counterparts.

If, like me, you have Gen Z kids, you may be grappling with how best you can equip and educate these digital natives to face a future that is set to be the embodiment of the science fiction movies we grew up thinking were far-fetched. A daunting task.

Of course, while we often fight it, change is positive and should be expected. Technology has increased the rate of change, but if you look back through the generations, you'll no doubt find many worried parents pondering their children's redundancy in the workforce due to one invention or another.

Investing where the future is unknowable

Our parents and their parents' parents and the parents who came before them had to prepare their offspring for a changing world. What exactly the changes would mean, and their knock-on impact, has always been unclear. They had to encourage and guide and make decisions with imperfect information. Likewise, this is the case with investing, where information is not perfect and outcomes are uncertain.

Andrew Lapping touches on this theme in his article. He notes that the future is unknowable, and that for this reason, we have to build portfolios that can weather a host of different storms. This is something we think about all the time, and the golden thread that laces through all this quarter's investment articles.

In his lens into the portfolio holdings, Leonard Krüger discusses the investment case behind five of our top equity holdings. Although many of these shares have underperformed of late, Leonard is optimistic: Each of these shares trades at a cheap valuation today and materially below our assessment of its true long-term intrinsic value.

Our offshore partner, Orbis, is similarly excited about their holdings. Brett Moshal and Michael Heap defend the case for their choices in their article. Although Orbis is going through a period of painful underperformance, they maintain that what makes it bearable is that the shares they like and own have become cheaper, offering buying opportunities.

In a world where the future is unknowable, sound economic policy strives to create a greater degree of consistency. In his article, Sandy McGregor offers some comments on the Economic Policy Paper that was recently published by the minister of finance.

It's not always easy being contrarian

While periods of underperformance are an expected and necessary part of contrarian investing, they are not pleasant for our clients and can be extremely stressful. We recognise that at this point in the cycle, where both us and Orbis are underperforming, staying the course can be very difficult. We thank you for your trust and commitment to your long-term goals.

We often speak about contrarian investing, but it's not always clear exactly what it means. Radhesen Naidoo provides an explanation in the Investing Tutorial. In essence, being contrarian means you have to be comfortable swimming against the tide, owning the unpopular companies which are underperforming, and not owning the popular ones when they are doing well. To get the benefit of the approach, you have to remain committed during some very uncomfortable moments.

Uncomfortable moments, typically felt during uncertain times, may make you feel like you are taking on too much risk. As an individual, it is important that you have a clear understanding of your own risk appetite as this will influence your investment decisions. But it is also important to be aware that avoiding risk entirely may present you with an unforeseen outcome of missing opportunities, and therefore not achieving your investment goals. Nadia van der Merwe weighs up the risks and opportunities presented by the current environment and delves into how we define risk at Allan Gray.

Conversations to have with your loved ones

Talking to family members about death and making plans for this eventuality are not things any of us feel easily comfortable with. However, it is infinitely easier to have an open conversation outside of the stress of these tragic situations, and to deal with many of the requirements upfront, than leaving it to a family who is grieving. The process

behind death claims is different for various investment products, and particularly complex for retirement funds. Sonja Smit candidly touches on some of the important aspects you should consider.

... no matter what the journey
lands up looking like,
saving gives you options.

Of course, it's important to speak to your loved ones about your investments, but it's also important to encourage them to start thinking about their own investments from early on. While, as Dion Chang notes, life may not be the linear birth-school-work-retirement-death journey textbooks suggest, no matter what the journey lands up looking like, saving gives you options.

Thank you for your continued support.



Rob Formby

WHAT CAN BE DONE TO IMPROVE SOUTH AFRICA'S PROSPECTS?

Sandy McGregor



Hopefully the new plan will stimulate the action required to set us back on a growth path.

When the National Treasury first published its Economic Policy Paper, there was widespread puzzlement as to why yet another such report was needed. It repeated much of what was already contained in former plans. It has now become apparent that its purpose was to set the agenda for discussions on economic policy within the ANC and to serve as a framework for the economic policy of President Cyril Ramaphosa's government. While not fully accepted, it seems to have successfully served this purpose. Sandy McGregor offers some perspective.

Over the past year, there has been growing concern that the country has become trapped in economic stagnation because the Ramaphosa administration has failed to act decisively to address the many problems which we face. Hopefully the new plan will stimulate the action required to set us back on a growth path.

The paper rightly emphasises that policy should be focused. Successful economic policy requires that priority be given to interventions which offer the greatest impact at the least cost. The current situation is dire. However, there are simple things

that can be done that can have a meaningful impact in a relatively short period of time. Rapid action to promote these opportunities is the best way to get the economy going again. Among these are the following:

1. Export earnings and foreign investment

Economic growth in South Africa is leveraged off its export earnings. Accordingly, priority must be given to supporting initiatives which boost exports or generate service receipts. However, this alone will not be enough. Given South Africa's shortage of domestic savings, stimulating economic growth requires foreign investment. The president's programme to attract foreign investment recognises this reality. This will succeed only if policy is rationally formulated so that investors have confidence in the long-term sustainability of South Africa as an investment destination.

2. The shortage of skills

The most important cause of South Africa's present economic woes is a shortage of technical and managerial skills. This is most clearly seen in government, but is a problem throughout

the economy. The increasing income disparity between the skilled and unskilled referred to in the paper is a direct consequence of this shortage. Notable business failures in the public sector, such as Eskom, and the scandalous state of public hospitals, can be directly attributed to appalling mismanagement. The failures of the state educational system are well known and understood.

It will take a long time to fix this and to build up the required skills base. In the interim, if South Africa is to get its economy going again, it must be open to importing skills where required.

3. Decisive changes at Home Affairs

In the modern global economy, skills are mobile. Multinational companies require the freedom to transfer key personnel from country to country. They will not willingly locate their operations in countries which deny them this right. South African business also needs to tap into such skills.

It must be understood that in a society with a skills shortage, inward migration of persons who can fill this gap does not create unemployment. On the contrary, as a rule, every skilled person entering the country contributes to economic growth, which creates work opportunities in the domestic economy. This is cautiously admitted in the Treasury paper, which argues for the admission of persons with acceptable tertiary degrees. Policy changes need to be much bolder. At the very least they should be expanded to include persons who are willing to establish a business and those whom existing businesses are willing to sponsor.

Retired persons from other countries who have an acceptable pension income should also be made welcome. It is better that they spend their pensions here rather than elsewhere. Unless the byzantine complexities of the present system for gaining permission for permanent residence are radically simplified, we shall be unable to attract the skills we so desperately need.

4. The tourism opportunity

It is encouraging that President Ramaphosa has publicly stated that in recent years, visa regulations have damaged our tourism industry and that steps are being taken to remedy this. Tourism probably represents South Africa's greatest short-term economic opportunity. When one compares the contribution of tourism to the South African economy with that of countries such as Spain or Italy, we are clearly attracting far fewer visitors than we should.

An important reason for this is unnecessary impediments to entry imposed by Home Affairs. If these are removed, tourism could boom.

Apart from instituting a welcoming visa regime, little else is required of government. Some international promotion is desirable, and the proposal that there be some mechanism to reduce red tape has merit. The rest can be left to the private sector. Tourism is the simplest way to create jobs for relatively unskilled persons. It can have a big impact on the economy, especially as it generates foreign exchange earnings. The economy is leveraged to export and service receipts. Growth in tourism will have a strong multiplier effect on the economy.

5. Documentation of property ownership

There is widespread occupation of land and houses by persons who are legally entitled to a property but do not have title deeds to confirm their ownership. A serious effort by the state to remedy this is required not merely on grounds of simple justice, but also because registered ownership would provide collateral which entrepreneurs could use to raise capital, thereby boosting the small business sector.

Tourism probably represents South Africa's greatest short-term economic opportunity.

6. The opportunity in agriculture

In the past decade, agriculture has been one of South Africa's success stories. Its farmers have taken advantage of growing demand in Africa, and China becoming a major food importer. This has been achieved despite serious climatic challenges.

This success is the outcome of the consolidation of the industry into a small number of well-managed operations, which are large enough to take advantage of the economies of scale required for profitable farming. It is often said that 800 farmers produce 80% of South Africa's food production. While this is a soft statistic, it provides an accurate representation of reality. Only well-managed, efficient farming businesses can meet the demand of domestic

retailers and the international food trade for low prices. These farmers provide large numbers of sustainable jobs for unskilled workers.

Agricultural policy should be focused on taking advantage of this success. Policies aimed at promoting subsistence farming may have considerable social value, but are unlikely to be sustainable without continuing financial support from the state.

7. Eskom

Everyone now recognises that fixing Eskom is an urgent priority. Underlying its financial collapse has been a flawed business model. It ignored the simple law of economics that increasing prices reduces demand. Massive price increases have decimated demand as consumers have reorganised their affairs to reduce consumption. Certain energy-intensive industries have been driven into closure.

The electricity price shock has been a significant contributor to South Africa's current economic malaise. Tariff increases have wiped out a significant proportion of Eskom's potential sales, leaving them 10% lower than they were eight years ago. This, in turn, has diminished the cash flow available to service Eskom's financial obligations. Further tariff hikes will exacerbate matters. The debate on tariffs should not be about how much they should be increased to make Eskom financially viable; rather, it should be about how Eskom should be structured to keep prices low enough to promote growth.

The most important task in fixing Eskom is to install an efficient and credible management team.

The paper correctly sees the opportunity presented by renewables. However, a baseload of coal will be required for many years. The economically best outcome requires optimal use of existing capital stock. The idea of selling existing coal-fired stations looks good in theory, but it may prove difficult in practice. Coal is increasingly being demonised. Large pension funds in developed economies are unwilling to invest in coal. Banks are being pressured

by lobby groups to cease lending to the carbon economy. Funding of any purchase of coal stations is likely to be very expensive.

The most important task in fixing Eskom is to install an efficient and credible management team. While a lot of attention has been given to how Eskom is to be funded, nothing can be done until the management issues are resolved. A sustainable funding package requires a management team in which credit providers have confidence.

More resources need to be allocated to maintaining law and order and to training the police on how to maintain civic peace.

8. The urban rail system

The commuter rail system in South Africa's major cities is in a state of serious decay due to a combination of mismanagement and neglect. This diverts traffic onto the roads, aggravating an already serious congestion problem. High priority should be given to fixing the management of the urban rail system as this can deliver at relatively low cost a significant improvement in the quality of life of commuters and will have a positive economic impact on major cities.

9. Labour laws

While the political impediments to creating a more business-friendly labour dispensation are well known, it needs to be clearly recognised that the present dispensation is a principal cause of the high level of unemployment. It constitutes a formidable obstacle to starting a new business and has the unintended consequence that investment is biased towards technologies that require a minimal workforce. Curtailing the activities of labour brokers has eliminated what was one of the easiest ways for a new entrant to the labour market to find a job.

Promoting apprenticeships is probably the most effective intervention which can ameliorate the adverse consequences of labour legislation. A combination of further subsidies and incentives to promote apprenticeship schemes is required.

10. Law and order

Perhaps the most serious immediate threat to the South African economy is increasing lawlessness. The operation of many businesses is being disrupted by extortionate demands from communities and opportunists who are conducting what can be described as protection rackets. Given increasing poverty and the lack of legitimate work opportunities, these developments are understandable. However, social disorder is imposing a serious additional burden on business, which will have

a cost in the form of reduced economic growth, which, in turn, will further exacerbate poverty.

If the police are unable to protect those conducting legitimate businesses, many of these businesses will close. The president's ambitious programme to attract foreign investment is being put at risk. More resources need to be allocated to maintaining law and order and to training the police on how to maintain civic peace.

Sandy joined Allan Gray as an investment analyst and economist in October 1991. Previously, he was employed by Gold Fields of South Africa Limited in a variety of management positions for 22 years, where much of his experience was focused on investment-related activities. His current responsibilities include the management of fixed interest portfolios. Sandy was a director of Allan Gray Limited from 1997 to 2006.

HOW TO CONSTRUCT A PORTFOLIO FOR A RANGE OF OUTCOMES

Andrew Lapping



... just because a particular asset class or share is not performing well today, doesn't mean it should be abandoned or excluded in the future.

The future is extremely uncertain. This isn't because of any particular global situation; it is always the case. This is why it is important that we build portfolios for a range of possible outcomes, rather than for a single forecast or expectation. Andrew Lapping explains using the Allan Gray Stable Fund to illustrate his arguments.

Fixed interest has been the best-performing asset class in South Africa over the past three years. The All Bond Index (ALBI) returned an annualised 8.9% and money market assets returned 7.4%, compared to the FTSE/JSE All Share Index (ALSI) return of 5.1% and inflation of 4.7% over the period. Furthermore, money market returns have been very stable, whereas the stock market bounced around in a 20% price range.

It is clear why the Allan Gray Bond and Money Market funds are experiencing record inflows – investors can get excellent real returns with little volatility. Unfortunately, to have benefited from these returns, investors had to identify fixed interest as the best asset class three years ago, not today. For fixed interest to outperform equity over the

next three years, a similar set of circumstances will have to recur, which is very possible, but also just one of many paths the future may follow.

Using cash as a base

When we construct asset allocation portfolios at Allan Gray, we start with a blank sheet, which is 100% cash. We then add selected investments that we think, based on our normal valuations, will outperform cash with a margin of safety. For example, if we think cash will return 7% for the next four years, we only invest in equities where our expected total return is at least 5% above this rate.

The same process applies when allocating funds offshore. Our offshore partner, Orbis, invests in a portfolio of shares that their portfolio managers believe will generate real returns. We then allocate to Orbis funds while considering our estimate of the rand's fair value. Given the vagaries of the rand, the offshore allocation can add price volatility to the Stable and Balanced funds. However, this additional volatility is often less than you might expect as the movements in share prices and the rand often offset one another.

An offshore allocation can be extremely valuable to cover for uncertain future outcomes. South Africa is a relatively small emerging market with both a current and fiscal account deficit. Historically, foreign investors have been happy to fund these deficits through both equity and bond investments. If foreign investors lose faith in the government's ability to control the fiscal deficit and decide to withdraw their support, a situation could arise where South African fixed interest investments rapidly lose purchasing power.

This is just one potential future path, but it is something we must consider when constructing a portfolio and choosing between an international investment and a South African investment, which may otherwise have very similar expected total returns.

Weighing up the long-term opportunities from different assets

Every asset we pick for our portfolios is carefully weighed up and considered. And just because a particular asset class or share is not performing well today, doesn't mean it should be abandoned or excluded in the future. The Allan Gray Stable Fund provides a useful example.

Over the past three years, the portion of the Stable Fund invested offshore with Orbis has returned a disappointing 3.4% per year, a clear detractor when compared to inflation and a 50/50 cash/equity benchmark, which returned 9.6%. So, the root cause of this underperformance was not that offshore assets have done poorly, but rather that Orbis has had a particularly severe period of underperformance.

Orbis is a contrarian value manager (see the Investing Tutorial on page 23) and, similar to all managers that outperform over the long term, they go through periods of underperformance. Orbis invested in shares that they thought were undervalued; these shares have subsequently fallen further. Importantly, in most cases, the Orbis valuation is unchanged, so the potential gain when prices reach fair value is now greater. This bodes well for future returns.

Like Orbis, the domestic equities we own in the Stable Fund have underperformed the broader market, returning only 3.4% over the past three years and falling 8.4% over the past year. We selected these investments because we thought the shares in question were trading at a discount to fair value and, as you can imagine, the discount to fair value is greater now than 12 months ago in many, but not all, instances. (For more insight into our stock selection, please see Leonard Krüger's article on page 11.)

Diversifying through Africa ex-SA assets

The different assets held in our asset allocation funds give the funds the opportunity to earn returns from different sources, in different scenarios. It may seem strange to some investors that 5% of the Stable Fund is invested in bonds in other African countries (Africa ex-SA). People often think of other African countries as inherently more risky than South Africa – and granted, many are. However, there is no reason why a diversified portfolio of African debt, bought at the right price, should have a greater risk of loss than rand-denominated South African debt. This is particularly true when you consider that 37% of the Stable Fund is invested in South African cash and bonds. Can you imagine what a global investor would say if their asset manager told them 37% of their portfolio was invested in rand-denominated fixed interest? Rand assets may not be a bad investment, but this would definitely present a very concentrated risk. In fact, we think rand fixed interest has a good risk reward profile, hence the 37% exposure in the Stable Fund.

Applying our shared investment philosophy and process has led both Allan Gray and Orbis to outperform over long periods of time ...

Interestingly, the Africa ex-SA bonds have been the Stable Fund's best-performing asset class over the past three years, returning an annual 18.4%. Given the strong returns, and therefore smaller discount to fair value, we have begun to reduce our exposure to the asset class. To our mind, including assets like Africa ex-SA bonds both diversifies the Fund's risk profile and augments returns. The same applies to Africa ex-SA equities, a much smaller position at 1.5% of the Fund.

The Stable Fund's current mix of assets, as shown in **Table 1** on page 10, is different from 10 years ago, when the Fund was basically 25% SA equity, 55% SA cash, and 20% Orbis Optimal. In hindsight, these asset allocation changes were the right decision as bonds outperformed cash, Global Balanced outperformed Optimal, and the African

assets have added value. As discussed above, the main factor detracting from returns over the past three years has been equity selection. We think this is a cyclical factor that should move back in our favour over time.

Applying our shared investment philosophy and process has led both Allan Gray and Orbis to outperform over long periods of time, and we have no reason to believe this period

is any different. One thing that has not changed over the Stable Fund's history is the goal of generating real returns for our clients, while minimising the risk of loss. We will use all the tools available to us to achieve this goal.

Table 1: Stable Fund performance attribution (three years to end September 2019)

Allan Gray Stable Fund	% of Fund	3-year return*	Benchmark return**	Contribution
SA equity and property	28	3.4	5.1	0.9
SA interest bearing	39	9.3	8.0	3.2
Commodities	2	8.8	-	0.2
Africa bond and equity	6	16.0	6.5	1.1
Orbis funds	25	3.4	9.6	0.7
Total	100	-	8.1	6.1

*The three-year return may not reconcile with the asset class contribution as the exposure changed over time and, in the case of African assets, we added and reduced exposure timeously.

**Asset class benchmarks: SA equity and property = FTSE/JSE All Share Index, SA interest bearing = 50% STeFI 3-month and 50% JSE All Bond Index, Africa bond and equity = J.P. Morgan GBI EM Global Diversified Index, Orbis = 50% USD cash and 50% FTSE World Index. Fund benchmark is deposit rate + 2%.

Andrew joined Allan Gray in February 2001 as a fixed interest trader and moved to the Investment team as an equity analyst in February 2003. He was appointed as fixed interest portfolio manager in June 2006, began managing a portion of client equity and balanced portfolios in February 2008 and was appointed as chief investment officer in March 2016. He also manages African equities. Andrew holds a Bachelor of Science degree in Engineering and a Bachelor of Commerce degree in Accounting, both from the University of Cape Town, and is a CFA® charterholder.

REFLECTING ON OUR TOP EQUITY HOLDINGS

Leonard Krüger



We constantly reassess and test our investment case for each holding against market and company-specific developments and prices.

The performance of the Allan Gray Equity, Balanced and Stable funds has been disappointing over the past couple of years. Low single-digit returns from equities listed on the Johannesburg Stock Exchange (JSE) have contributed to these low returns. In addition, the equities specifically selected for our portfolios have experienced challenging performance relative to the market over the past year. Leonard Krüger appraises our decisions.

A review of the recent performance of shares on the JSE reveals a large discrepancy between individual names. Whereas three of the largest counters, namely Naspers and the large diversified miners BHP and Anglo American, have delivered good returns to investors, most other shares, apart from the precious metal miners that rallied off an extremely depressed base after many years of negative returns, have struggled. Allan Gray portfolios were and continue to be underweight this subset of names compared to average. In other words, our portfolios had fewer of the relative winners and more of the relative losers.

Yet, we have not made large wholesale changes to these “relative losers”. In fact, in some instances, we have bought more of these shares recently. This may feel counterintuitive, but should not be unexpected for clients familiar with our long-term investment philosophy and approach. We constantly reassess and test our investment case for each holding against market and company-specific developments and prices. A brief recap of and update on some of the largest detractors from our recent performance will hopefully illustrate this approach. In this piece, we focus purely on the equity holdings. To learn more about how we approach portfolio construction overall, please see Andrew Lapping’s piece on page 8.

Sasol

Late delivery and cost overruns of Sasol’s massive Lake Charles Chemicals Project in the United States have been extremely disappointing. Compounding this disappointment is the material uncertainty created by the delayed release of financial results to allow the board of directors time to complete an independent review of the underlying reasons for the overruns. At the time of writing, we await the findings of this review.

What is already clear is that future returns from the Lake Charles project will be lower than initially expected. This has reduced our assessment of the intrinsic value of Sasol. The market has, however, taken a much dimmer view of Sasol's future prospects than we believe will prevail over the long term.

Construction of Lake Charles is largely complete and certain units have achieved beneficial operation. Sasol's plants in South Africa and the rest of the world operate in line with expectations and profitably. Material geopolitical risks of disruption across energy markets abound, creating upside risk. Yet Sasol trades on less than six times our assessment of normal earnings, adequately reflecting the now widely known debt, project and management risks resulting from Lake Charles.

British American Tobacco (BAT)

Conversely, BAT's capital investment (acquiring Reynolds's minorities in 2017) in the United States has progressed largely as planned from the company's point of view. The market's faith in the sustainability of the financially attractive business model of large tobacco firms has been shaken by disruptive new alternative tobacco entrants/technology and regulatory interventionist plans. Our market research and conversations point to limited evidence of this occurring in the near term. In fact, BAT recently reiterated its medium-term guidance of continued earnings, cash flows and dividend growth. Furthermore, BAT is making substantial investments in its portfolio of next-generation products with promising initial signs in many categories and markets. Shares in BAT offer investors over a 7% dividend yield today, in hard currency, and that dividend is likely to grow every year for the foreseeable future.

Remgro

Remgro is the quintessential South African investment holding company. With diverse underlying investments in banking, insurance, healthcare, telecommunications and food businesses, among others, an investment in Remgro can be thought of as a portfolio within our portfolios. Facing an environment of low growth and low business and consumer confidence in South Africa's economic prospects, owning some of South Africa's strongest businesses and best management teams at below-average prices provides some safety in uncertain times.

In addition to its defensive diversification benefits, financial risk is also low since Remgro is in a net cash position.

The cherry on top for us, however, is that an investor can buy the above positive attributes at the largest discount (roughly 25%) to the net asset value (NAV) seen in Remgro for over 10 years.

Glencore

In contrast to peers BHP and Anglo American, this diversified miner and commodity trader has no exposure to the iron ore market, which is currently experiencing high prices. Extraordinary profits in iron ore following large supply disruptions from Brazil are not sustainable, in our opinion. Experience from investing in commodity companies has taught us that falling profitability is rarely an ingredient for strong share price performance, irrespective of perceived low multiples.

Valuations today
offer a margin of safety
larger than we have found
in many years ...

Glencore's commodity price basket has as a result been weaker than that of peers, and its share price performance has followed suit. But Glencore's production has also disappointed – a matter being addressed by the company and which we believe is solvable without requiring meaningful capital expenditure.

Apart from the difference in its iron ore exposure, other positive attributes that differentiate Glencore from peers are its commodity trading business and the close alignment of interests between shareholders and its management team. Commodity trading is a higher return, less volatile business than mining. Glencore's management owns around 20% of the business and is driven more by share price performance than annual salaries and bonuses. Active share buybacks at the current share price demonstrate this and add value to remaining shareholders, in our view. Glencore currently trades at less than six times our assessment of normal free cash flow.

Investec

The well-known UK and South African banking and asset management franchise has served its clients and employees well over many years. Since the financial crisis

of 2009, this has not been equally true for shareholders. Dealing with large legacy issues and a more onerous and capital-intensive regulatory environment in the banking world, Investec's returns have disappointed, particularly returns from its UK banking unit. Brexit and record low interest rates have certainly not made matters easier.

This has overshadowed Investec's success in growing and broadening its asset and wealth management divisions. These are substantial and valuable businesses. New management, together with the board, has resolved to split the asset management business from the rest of the Investec group in 2020. Regulatory approvals are in place and a shareholder vote will be held shortly. While no panacea to unlock the inherent value of the group's assets, it demonstrates the increased shareholder focus of Investec to also serve shareholders better going

forward. At 7.5 times normal earnings, the valuation is attractive against this shareholder-friendly backdrop.

Looking forward

While the reasons for the recent underperformance and the investment rationale for holding each investment discussed above may differ, all of these investments have one thing in common: Each one trades at a cheap valuation today and materially below our assessment of its true long-term intrinsic value.

Investing is never entirely risk-free, even at low valuations and after a period of underperformance. There are known risks to monitor, and the possibility of unforeseen negative surprises always exists. Valuations today offer a margin of safety larger than we have found in many years and we are optimistic about the outlook for higher returns.

Table 1: Top equity holdings in Allan Gray Equity, Balanced and Stable funds

Equity Fund		Balanced Fund		Stable Fund	
Company	% of portfolio	Company	% of portfolio	Company	% of portfolio
British American Tobacco	6.4	British American Tobacco	6.6	British American Tobacco	2.9
Naspers*	6.1	Naspers*	5.6	Glencore	2.3
Standard Bank	4.2	Glencore	3.2	Naspers*	1.9
Sasol	3.6	Remgro	2.6	Sasol	1.3
Remgro	3.6	Sasol	2.5	Taiwan Semiconductor Mfg.	1.1
Glencore	3.5	Standard Bank	2.4	SPDR Gold Trust	1.1
Investec	3.2	Prosus	2.1	Fortress Income Fund (A)	1.1
Old Mutual	2.7	Investec	2.1	Investec	1.0
Woolworths	2.6	Old Mutual	2.0	AbbVie	1.0
Reinet	2.5	Woolworths	1.8	BP	1.0
Total	38.4	Total	30.9	Total	14.7

*Includes positions in stub certificates. Underlying Orbis holdings are included on a look-through basis.
Source: Allan Gray

Leonard joined Allan Gray in 2007 as an equity analyst. He began managing a portion of client equity and balanced portfolios earmarked for associate portfolio managers in July 2014 and was appointed as portfolio manager of the Allan Gray Stable Fund in November 2015. Leonard holds a Bachelor of Science (Honours) degree in Actuarial Mathematics from the University of Pretoria and is a qualified actuary.

ORBIS: IS VALUE INVESTING DEAD?

Brett Moshal and Michael Heap



Over multiple decades, the traditional value approach of buying cheap stocks has worked remarkably well. Over the last decade, it hasn't, leading an increasingly large chorus to proclaim that value investing is dead. Is there truth to these words? Brett Moshal and Michael Heap from our offshore partner, Orbis, investigate.

While we aren't textbook value investors, the debate about value investing is not academic for us, as the value philosophy and our fundamental, long-term, and contrarian philosophy are intellectual cousins. Value investing has taken knocks before and recovered – can it do so once again?

To cut to the chase, our answer is an emphatic yes. It will work in future for the same reason that it has worked so well over the long-term past: At its core, its efficacy is driven by thousands of years of basic human nature, specifically the survival instinct that causes humans to respond to greed and fear. These primal drives lead investors to run with winners and from losers. In markets, investors habitually expect the winners to forever thrive

and the losers to forever struggle, and they price the companies accordingly. History has shown that investors tend to overshoot. Growth fades and struggles subside. Whether through the power of incentives, the levelling gravity of capitalism, or even luck, great and bad companies alike often prove their adjectives wrong.

That pattern hasn't worked over the past 12 years, in part because in 2007, the cheap stocks weren't very cheap. But the doubts currently circulating have little to do with valuations 12 years ago. Instead, investors are becoming convinced that expensive shares will carry on beating cheap shares indefinitely.

This is a necessary step. For value opportunities to emerge, investors first have to overestimate the differences between companies. Widening expectations are as essential to value investing as exhaling is to breathing. That does not make periods of widening expectations any more comfortable, however. As **Graph 1** shows, in the 80 years from 1926 to 2006, value shares experienced seven periods of 20%+ underperformance vs expensive shares.

The good news? Every one of those periods was followed by significantly better-than-average outperformance for value.

Is it different this time?

Yet this long historical perspective hasn't stopped investors from claiming that this time is different, whether because of technological change, falling interest rates, changing valuation metrics, or even the very awareness of value investing. This questioning, of course, is a condition of value investing's success, not a proof of its failure.

We don't believe this time is different, and we believe value investing and the underlying psychology that drives it remain valid. More importantly, we remain as convinced as ever that our fundamental, long-term, and contrarian approach is sound, and as co-investors in the Orbis funds, it is how we're investing our own money.

The technological developments of the 21st century are impressive, but they have not been better for economic productivity than the major technological advances of the 20th century – a period when value shares outperformed. Social media and e-commerce are significant innovations, but so, too, were the telephone, radio, car, television and electricity. And while low interest rates have recently been correlated with poor returns for value shares, those shares

handily outperformed from the early 1980s to 2006, even as 10-year US yields fell from double digits to below 5% per annum.

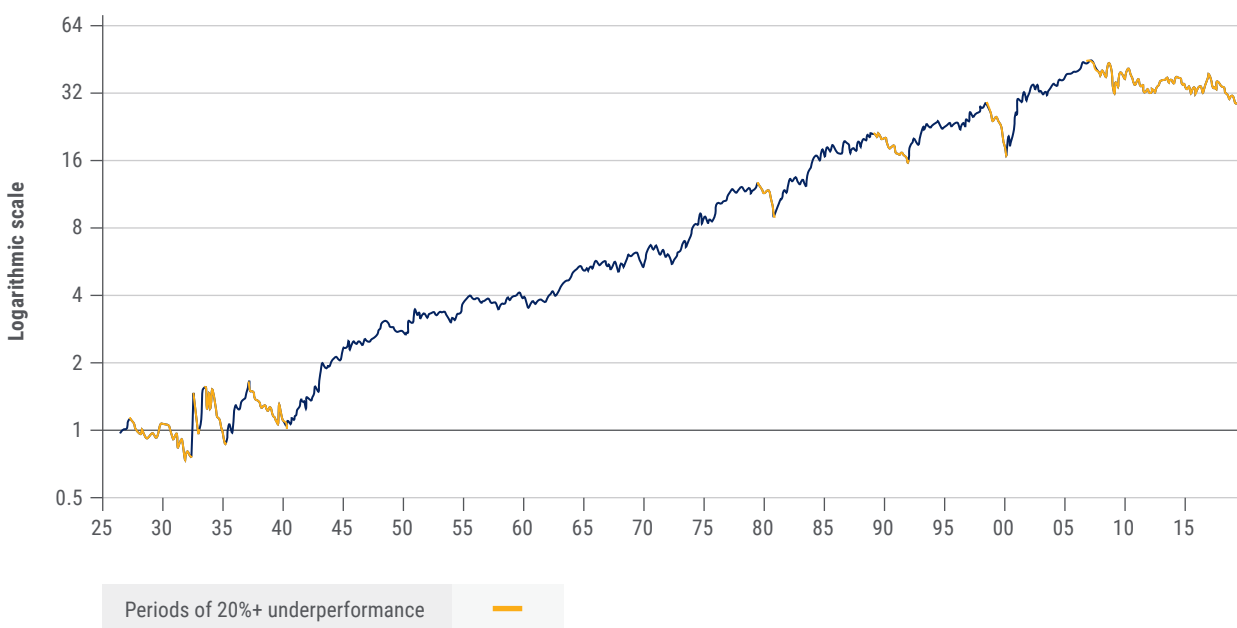
... we believe value investing and the underlying psychology that drives it remain valid.

Finally, if awareness of value investing closed all the discounts in the market, you would expect to see muted differences between the valuations of cheap and expensive companies. Yet valuation spreads today are unusually wide. That's true whether you look at the classic price-to-book multiple, or at other measures such as price-to-earnings (see **Graph 2** on page 16). Over the past 30+ years, the valuation gap below has only been wider around the Japan bubble in 1990, the tech bubble in 2000, and at the trough of the global financial crisis. On each of those occasions, the "value investing is dead" refrain was heard far and wide.

Although valuation spreads are wide, not all of our favourite ideas are trading at depressed multiples. We're flexible, and we're happy to own shares trading at higher "headline"

Graph 1: Value investing has been knocked – and recovered – before

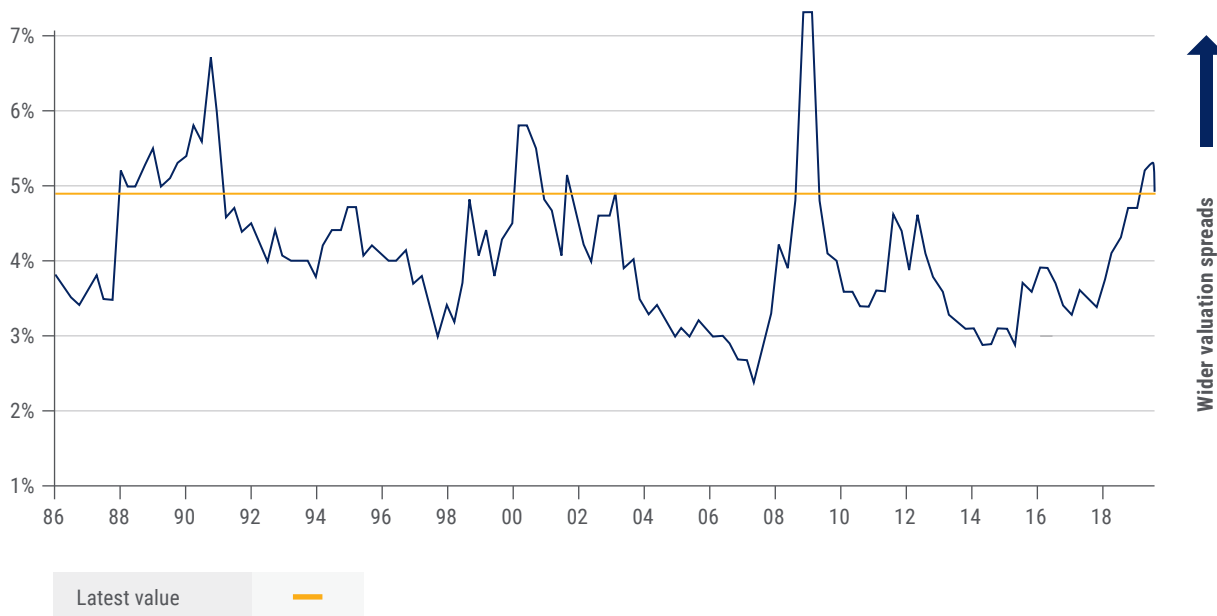
Relative return of US value (low price-to-book) vs growth shares



Source: Datastream, Kenneth French, CRSP, Orbis. Data from July 1926. Returns for August and September 2019 calculated using the Russell 1000 and 2000 growth and value indices.

Graph 2: Valuation spreads are unusually wide on price-to-earnings multiples

Difference in forward earnings yield between the cheaper and richer half of global stocks



Source: Orbis. Difference in one-year forward earnings yield between the cheaper and richer halves of shares in the FTSE World Index, using IBES consensus estimates for earnings. Earnings yield is 1/price-to-earnings ratio.

price multiples, so long as the business trades at a sufficiently attractive discount to our estimate of its true worth.

In the US and emerging markets, for instance, many of our favourite ideas are stocks that we believe offer idiosyncratic and underappreciated growth potential at a reasonable price. In the US, these include XPO Logistics, Facebook, Anthem, Alphabet, and S&P Global, and in emerging markets, NetEase, Autohome, and Taiwan Semiconductor Manufacturing Company.

In Europe and Japan, however, it's a different story – many of the most compelling ideas we've found there trade at very low valuations. In aggregate, the Orbis Global Equity Strategy's holdings in developed Europe trade at just 1.0 times book value, and in Japan, just 0.8 times. This is despite fundamentals that are on a par with or slightly better than local averages.

Two examples provide a good illustration of these attractive opportunities: BMW in Europe and trading companies in Japan are quintessential value stocks.

European value: BMW

Last quarter we discussed Honda Motor, which is trading near an all-time low (even worse than during the financial crisis)

valuation due to concerns about the global auto industry. Trading at 0.8 times book value and just six times depressed 2018 earnings, BMW is in the same boat.

The automotive sector does face some challenges. The sales cycle globally has been getting worse, particularly in China, and the industry faces an uncertain future as governments, particularly in Europe, push hard to promote electric vehicles. However, over the long term, we believe these risks are unlikely to be anywhere near as severe as implied by BMW's share price.

While the cycle in China has been painful, in cyclical companies it often pays to invest when the outlook is uncertain, so long as the valuation more than accounts for the risk. If you wait until the outlook is clearly improving, that improvement is obvious to everyone else too, and will be reflected in a higher stock price.

Globally, the push for battery electric vehicles (BEVs) is a headwind to automakers' profits, as governments in many markets set requirements for BEVs as a share of an automaker's sales. Customer demand, however, is not yet high enough to allow manufacturers to sell BEVs at prices that generate sustainable profits. As a result, the automakers generally lose money on each one they have to sell.

While this is challenging over the short term, we don't think it is an accurate picture of the industry's future. When a capital-intensive industry faces low returns, prices generally rise until the industry makes a sufficient return to cover its reinvestment needs. Over the medium term, we therefore think it's more likely that consumers, rather than manufacturers, will pay the cost of reducing emissions via higher prices. Premium brands like BMW appear particularly well placed to pass on this pricing, given a wealthier customer base.

Across industries, companies with prestigious brands earn higher margins and returns on equity, because customers are willing and able to pay up for their products. Think of a tie rack at a clothes store – a Hermès tie will always be able to command a higher price than one from a no-name brand.

The same is true of cars, and this competitive advantage shows up in BMW's financials. Over the long term, it has earned a roughly 15% return on equity and grown book value by 11% per annum while paying out a third of earnings as dividends – better results than the wider industry.

Yet due to industry pessimism, BMW today trades at just 0.8 times book value and six times depressed 2018 earnings, compared to 2.4 times and 21 times for the wider European

market (see **Graph 3**). In any other sector, a luxury brand with a century-long pedigree and peer-leading financial returns would likely trade at a premium to the market. We believe a rerating to just 1.1 times book value, coupled with modest growth and a well-covered 5.5% dividend yield, could drive very attractive returns for BMW shares over our investment horizon.

... we remain as convinced as ever that our fundamental, long-term, and contrarian approach is sound ...

Japanese value: Mitsubishi, Sumitomo and Mitsui

Part of our concentration in Japanese value shares is in Honda, which we discussed last quarter. But the biggest exposure is to a different kind of company – Japan's trading companies, including Mitsubishi, Sumitomo and Mitsui & Co.

Graph 3: BMW: Solid growth in book value, but share price cyclicality

BMW book value per share and share price, EUR



Source: Datastream, Worldscope, Orbis

General trading companies are best thought of as industrial conglomerates. Their subsidiaries deal in businesses as diverse as natural gas, coking coal, nickel mining, oil pipes, power plants, food distributors, salmon fisheries, cable operators and convenience stores. In effect, the companies are so diversified that their fundamentals unsurprisingly tend to track those of the Japanese economy as a whole. For most of their history, the companies generated roughly average returns on equity, and were appropriately assigned roughly average valuations.

... we believe time will prove that today's reports of the death of value investing were ... greatly exaggerated.

In 2013, however, the market was concerned about the companies' resource businesses, leading the stocks to trade at a discount to their book value despite generating

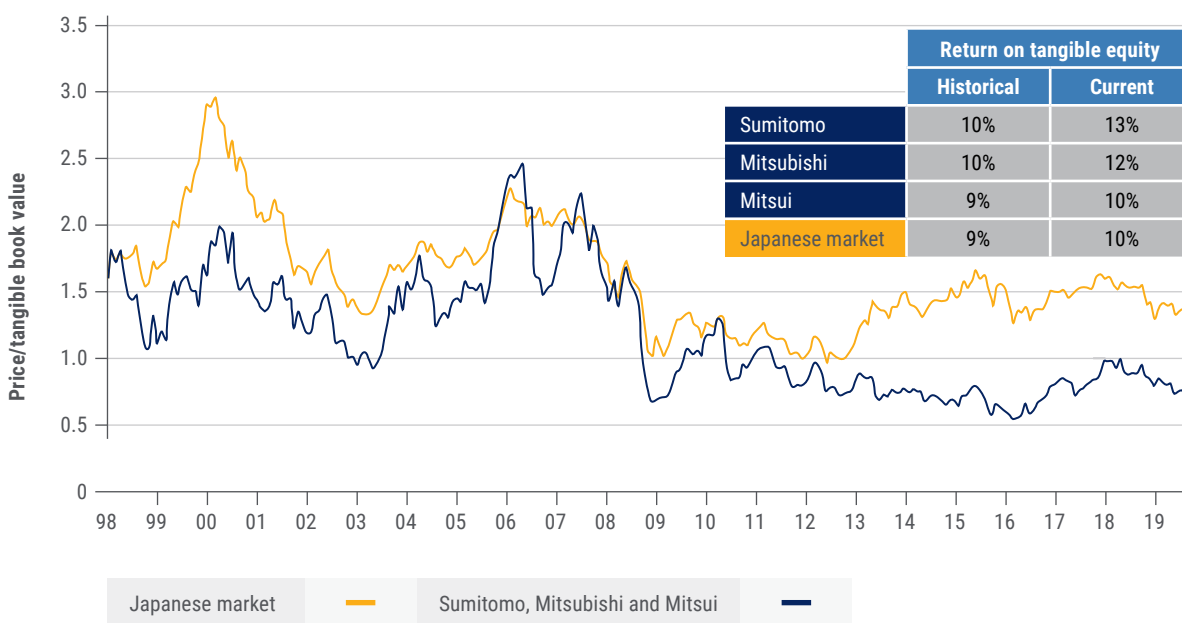
higher returns on equity than the average Japanese company (see **Graph 4**). We bought positions in Mitsubishi and Sumitomo for the Orbis Global Equity Fund in 2013, adding Mitsui later. Our thesis was that their assets would generate reasonable, sustainable profits, and that improvement in capital allocation could drive a rerating and attractive returns for shareholders.

On the asset side, there have been hiccups. Amid the commodity crash from 2014 to 2016, the companies took write-downs, leading to Sumitomo's first annual loss in 15 years, and Mitsubishi and Mitsui's first losses in over 40 years. Since then, however, commodity prices have recovered, and the companies' biggest commodity segments have returned to generating profits and cash flow.

Perhaps more importantly, the companies have also become better at allocating that cash flow. Having previously spent freely on investments, they are now divesting assets with low returns, investing more carefully in new projects, paying down debt, and making higher payouts to shareholders through dividends and buybacks. From almost any angle, the businesses are in better shape now than they were five years ago.

Graph 4: Japan trading companies: above-average fundamentals, depressed valuations

Price-to-tangible-book ratios of Sumitomo, Mitsubishi, Mitsui and Japanese market (TOPIX index)



Source: Datastream, Nikkei Yuho, Bloomberg, Orbis. Mitsubishi, Sumitomo and Mitsui blended according to their current weight in Orbis Global Equity.

Yet that improvement has not been rewarded with appropriately higher valuations. Today, all three companies trade at a discount to their book value and just seven times earnings, with dividend yields above 4%, despite earning higher returns on equity than the broader Japanese market. To us, that looks like a substantial discount to the companies' intrinsic value. From here, simply generating cash and growing book value would deliver reasonable returns, with any rerating providing additional upside for shareholders.

Focusing on intrinsic value

In today's market environment, valuation spreads look unusually wide, and we have uncovered a number of attractive value shares, particularly in Europe and Japan. As ever, there is no guarantee that the market will come to share our view of these businesses. But importantly, we don't own the stocks just because they're cheap. We own them because we believe their low valuations are unwarranted. With opportunities like these on offer, we believe time will prove that today's reports of the death of value investing were – once again – greatly exaggerated.



Brett joined Orbis in 2003. He is based in London, leading the Japan Investment team, and is one of the stockpickers who direct capital in the Orbis Global Equity Strategy. Brett holds a Bachelor of Commerce and Bachelor of Accounting Science degree, both from the University of the Witwatersrand, and is a Chartered Accountant and CFA® charterholder.

Michael joined Orbis in 2013 and is a member of the European Investment team. He holds a Bachelor of Arts (Honours) degree in Natural Sciences and a Master of Philosophy degree in Finance, both from the University of Cambridge.

MINDFUL OF RISK

Nadia van der Merwe



Uncertain times may cause investors to shy away from risk. While it is important to be mindful of risk and understand the risks you are taking on when investing, avoiding risk at all costs may not be the most rewarding strategy. Nadia van der Merwe discusses why we think the current environment offers exciting opportunities for patient investors willing to do the research and take on risk where it is warranted.

Clients often view Allan Gray as a conservative investment manager and may be surprised when they find shares in the portfolios which are regarded as high-risk, especially in times of heightened uncertainty. Actually, we do not classify our approach as strictly conservative. We are willing to take substantial positions in stocks in which we have high conviction and position our portfolios very differently from the market or benchmark. Indeed, we often find attractively priced opportunities in the unpopular areas of the market, which means we may have considerable exposure to stocks that are out of favour and perceived as high-risk.

Our decisions are driven by our valuation-based contrarian approach (see the Investing Tutorial on page 23), where we

“A temporarily adverse environment for a good company can create a great long-term buying opportunity.”

take a different view of risk. In our view, the biggest risk investors face is the risk of permanently losing money, and this can often come about as a result of overpaying for an asset. Therefore, we aim to invest in companies that are trading at substantial discounts to our estimates of what they are worth (their intrinsic value).

While investing always involves some risk, as the future is inherently uncertain, we manage the risk of loss carefully throughout our investment process (as Andrew Lapping explains on page 8). We believe risk cannot and should not be avoided completely; rather, risks should be understood and embraced in a selective manner. Uncertainty and opportunity go hand in hand.

Risky business?

It is important to recognise that a riskier business doesn't automatically make for a riskier investment. A company believed to have significant risk exposure may face a broad range of potential outcomes, both positive and negative. In severe cases, the negative outcomes could threaten the sustainability of the business, but more often this is not

the case – the company may merely be facing temporary challenges. The presence of risks does not automatically render a company unsuitable for investment, as long as the business fundamentals are sound and the challenges can be navigated successfully.

Understanding the risks faced and their potential impact on the sustainability and intrinsic value of the company is important, yet ultimately, when evaluating the riskiness of a company as an investment, the key factor is the price you pay. The level of the purchase price in relation to intrinsic value is the most powerful indicator, not only of future returns, but also of the risk you take on, and it is the one factor over which you have the most control. A low enough price can go a long way to reducing the riskiness of the company as an investment. Similarly, a very stable business can be a high-risk investment if the price is too high. At Allan Gray, we are happy to invest in a riskier company as long as we can do so at the right price.

A company's share price is a reflection of the market's expectation of the future performance of the business. Generally, a low price relative to a business's fundamentals implies that the market's outlook for the company's future performance is poor. If it exceeds expectations, the share price typically reacts positively, and vice versa.

Uncertainty and opportunity go hand in hand.

Market participants, however, may not always place enough focus on the actual business fundamentals because they simply consider the business's obstacles insurmountable. In addition, investors' willingness to take on risk varies over time, which may also impact the share price. Sometimes investors are willing to pay higher prices than they would otherwise. At other times, they are very hesitant to take on any risk; lower demand may reduce prices, as may any form of negative news. We think the current environment fits the latter more than the former. Companies perceived to be high-risk have been shunned, with share prices moving sharply in response to news flow.

Sentiment towards a company is also influenced by the extent to which the risks the company is exposed to are known and appreciated. Often when the risks

facing a business are particularly obvious, investors become overly pessimistic – even if the business has a long track record of successfully navigating challenges and generating decent returns for shareholders. Similarly, in the absence of obvious risks, share prices may continue to climb.

We are more excited today about the prospect of future returns than we have been for some time.

Looking at global markets today, investors appear far less willing to take on obvious risks. With factors such as corporate failures, trade wars, political uncertainty and a lack of economic growth dominating the headlines, investors have shied away from shares that appear to carry above-average risk. Instead, capital has flowed into the seemingly safer areas of the market, bidding up prices to ever higher valuations. This flight to "safety" has resulted in investors ignoring many of the businesses that are perceived to be riskier, with little regard for valuation.

How to cut through the noise

When analysing companies and assessing intrinsic value, we aim to cut through the noise. This means looking through the good news, as well as through the bad, to evaluate the long-term reality. Where negative news is plentiful and the risks are obvious, opportunities abound for the patient investor. For us, the most important consideration is the quality of the business in relation to what it costs.

A number of the companies in our portfolios have had their fair share of bad news recently, but this potentially leaves a higher return for those willing to do the work and take on the risk where warranted. When looking at some of the biggest shares in our portfolios, the major risks are quite easy to spot, as highlighted in **Table 1** on page 22. We don't pretend that these risks don't matter; rather, we have spent a significant amount of time and effort to understand how the risks may impact the fundamental value of these businesses. These are not junk businesses – their fundamentals are solid and they should be able to navigate the current environment and overcome

temporary headwinds. However, because their risks are easy to spot and recent news has remained negative, it has further impacted their share prices. This has been painful for our clients, but we think the extent of the sell-off has been unjustified.

As set out in **Table 1**, the current valuations of these stocks look particularly attractive, trading far below their historic levels as well as the overall market, and provide an adequate margin of safety against further adverse developments. We think the potential upside far outweighs the likely downside from this point forward – an attractive feature for us.

Priced for perfection

We typically struggle to find good investment opportunities in areas of the market where optimism abounds. Shares in these areas may appear to be low-risk, pricing in a lot of good news, yet their fundamentals are often not as strong as the prices suggest.

We tend to take a more cautious approach when valuing these businesses. When shares are priced for perfection, it does not take much to disrupt their price trajectory: lower-than-expected growth, regulatory change, etc. We have seen many such examples over the years. Conversely, we believe the risks in the companies we own are more than reflected in their valuations. We think the potential for the prices to fall further is far smaller than for many of the strong performers. These companies only need to perform “okay”, or the feared outcome only needs to be slightly less bad than anticipated for the shares to perform well.

Our portfolios are constructed to manage the risk we take on in generating returns. We are more excited today about the prospect of future returns than we have been for some time. As our founder, Allan Gray, often says: “A temporarily adverse environment for a good company can create a great long-term buying opportunity.” When the market is assuming the worst, there is the possibility of substantial upside even if things merely turn out “less bad” than feared.

Table 1: Valuations and risk of top shares in the Allan Gray Equity Fund

Company	Risk	Price return over last 12 months	Valuation
British American Tobacco	Declining volumes, e-cigarettes and regulation	-16%	9 x normal earnings
Glencore	Thermal coal fundamentals and the US Department of Justice investigation	-25%	6 x normal free cash flow
Old Mutual*	Management challenges	-12%	9 x adjusted earnings
Sasol	Oil price, governance and project challenges	-54%	5 x normal earnings

*The Old Mutual price movement is adjusted to allow for the Nedbank unbundling in October 2018.
Source: Allan Gray

Nadia joined Allan Gray as a business analyst in 2010 and is currently a senior manager in the Institutional Client Services team. She holds a Bachelor of Commerce (Honours) degree in Actuarial Science from Stellenbosch University and is a qualified actuary.

ARE YOU COMFORTABLE SWIMMING AGAINST THE TIDE?

Radhesen Naidoo



We thoroughly question our decision-making as we seek to find value for our clients.

Allan Gray and our offshore partner, Orbis, describe our shared investment approach as "contrarian". "Contrarian" is usually defined as "opposing or rejecting popular opinion or current practice". Using this approach in investing focuses our attention to find value in an investment world which can be noisy and distracting. Radhesen Naidoo explains what this means in practice.

Following trends is comfortable. It's human nature to want to be in with the crowd, or part of the herd. This is especially true when it comes to our finances: As individuals, we take comfort from sameness. It validates our thinking. However, the simple economics of supply and demand illustrate why this is not good for investing: If there is an increase in demand for an item, but supply is limited, prices tend to rise. But this does not necessarily mean the item is more valuable or that you are getting more value for your money; it simply means you are spending more. Think about it in reverse: If there is an item you really like, but you put off buying it and then find it on sale, don't you feel like you have scored? Similarly, when we think about investments, we are cautious when prices are rising as paying too much is the easiest way to lose money.

As investors looking to buy companies at bargain prices, you can understand why we would need to swim against the tide to find opportunities. Generating client wealth over time requires us to make unpopular decisions, or to be different from the crowd. This does not simply mean we are contrarian for the sake of it; rather, this approach makes us highly sceptical. We thoroughly question our decision-making as we seek to find value for our clients. This has always been a hallmark of our approach.

Smart ideas

Consider the use of our smartphones – or cellphones, as they were once called. Today, Apple and Samsung smartphones top the popularity charts, but this has not always been the case. It is quite incredible how loyalties change and popularity can shift. When Apple initially launched the iPhone in 2007, it was revolutionary and new. It arrived from nowhere to eventually unseat the market leader: Nokia.

Back in 2006, Nokia dominated the mobile phone industry. At the time, it may have appeared to be an obvious company to back. But while Nokia was busy selling millions of phones,

Apple was developing the iPhone, and Google was getting industry players together to build open-source technology for smartphones. Nokia wanted nothing to do with Google's venture, and within two years, the company was in crisis, losing market share and ultimately its brand status.

If you had the foresight and courage to invest in Apple shares back in 2007, you would have benefited from the value that has now risen over 10 times. Investing in Nokia at the same point in time, when it was well known and widely used, would have been an easier decision – but you would have lost a lot of money. Of course, with the beauty of hindsight, the decision seems obvious, but back then, going against the crowd would have been uncomfortable.

Over time there will be many companies like Apple and Nokia. If you invest before the crowd starts to pay attention, you can benefit tremendously. Of course, the next winner is not obvious: Identifying the winners takes careful research, high conviction and an element of luck as well.

How does this relate to contrarian investing?

As contrarian investors, we hunt for opportunities in areas other investors overlook. This often leads us to invest in companies long before they become popular. For example, we have found select companies in African markets which are not well known and are underresearched. The countries themselves have a host of political, economic, liquidity and regulatory challenges, and these factors make investors nervous. As a result, there are fewer willing investors than in more developed markets.

We pride ourselves on doing thorough bottom-up research to identify great businesses with a competitive edge. And we are not afraid to take a different view. We also acknowledge that simply being different is not enough; patience (as well as a pretty thick skin) is necessary to unlock the value.

Another application of a contrarian approach is investing in areas where expectations are lower, or in companies going through temporary difficulties – in other words, where levels of pessimism are above normal, resulting in share prices being unusually cheap. One example is our experience before and after an extreme market event, such as the tech bubble in 2000.

During the tech bubble, we avoided the very popular technology shares. They were the flavour of the month, with prices skyrocketing and investors piling in, afraid to be left out of the party. We were nervous: In our view, there was more to lose than to gain. The market did not agree with us, though, and our returns were under pressure. Clients were not happy. Eventually, it all came crashing down. While it was extremely uncomfortable at the time, our approach paid off.

Following the crash, technology stocks, once the darlings, were given pariah status. Unloved and unwanted, they began to attract our attention. Some of these businesses would survive and eventually show their worth again. We initially invested in Dimension Data during 2002, following the tech bubble, and then again during 2005/2006. It added tremendous value to our funds and was eventually bought out in 2010. Again, taking a contrarian approach paid off.

To get the benefit of the approach ... you have to remain committed during some very uncomfortable moments.

What does this mean for you as a client?

Everything we've said above sounds great in theory and feels comfortable when the going is good. To get the benefit of the approach, though, you have to remain committed during some very uncomfortable moments. You have to be comfortable with a fund that underperforms at times, owning the unpopular companies, and not owning the popular ones when they are doing well.

Today, a number of the companies Allan Gray and Orbis hold on behalf of our clients are out of sync with the broader market and, as a result, performance is under pressure. Throughout these testing periods, we continue to apply the same approach. There is old wisdom which suggests tasks that require discipline are the most value-adding over time. Our investment approach is no different.

Radhesen joined Allan Gray as a business analyst in the Institutional Client Services team in 2012. He then joined Orbis in July 2014 as a performance analyst and returned to the Institutional Client Services team at Allan Gray in October 2015. Radhesen holds a Bachelor of Science (Honours) degree in Actuarial Science from the University of the Witwatersrand.

HOW YOUR RETIREMENT FUND BENEFITS ARE ALLOCATED WHEN YOU DIE

Sonja Smit



It is ... important that members provide their fund with comprehensive details of their family circle and nominees, and keep the details up to date.

The process behind retirement fund death claims is challenging to understand and complex to execute. Sonja Smit discusses how to be better informed as a member, and how to prepare your dependants for what happens if you die prior to retirement.

The purpose of retirement funds is to save for retirement, but when members die prior to retirement, the purpose changes to provision for those who were dependent on the member at the time of their death.

Retirement products are governed by the Pension Funds Act ("the Act"). Other savings products are governed by other legislation and are treated differently when the investor dies, as shown in **Table 1** on page 27. Every retirement fund has a board of trustees, which is responsible for making sure the fund is well governed and that members' best interests are protected. One of the roles of the trustees is to ensure that a member's benefit is distributed fairly if they die before they retire.

When it comes to distributing the death benefit, the Act gives preference to dependency. It defines dependants

as spouses (which include permanent life partners), children (of all ages, including legally adopted children), anyone proven to have been financially dependent on the member at the time of their death, anyone entitled to maintenance (such as former spouses), as well as those who may in the future have become financially dependent on the member if the member had not died (such as a child born after the member's death).

A member may also nominate any natural person, trust or legal entity (nominee) in writing for a possible allocation of the death benefit. They may not nominate their estate.

Nominations are not binding on the trustees; rather, they are an expression of the member's wishes. At Allan Gray, we apply nominations at membership level, and not at investment account level. For example, a member may have more than one Allan Gray Retirement Annuity Fund account, but the latest nomination received per retirement fund will apply across all investment accounts within that fund.

The fact that a party qualifies as a dependant or a nominee does not entitle them to receive all or a part of

the death benefit. However, it does mean that they must be considered by the trustees when allocating the death benefit.

Duties of the trustees

When a member of a retirement fund dies, the Act requires the trustees to identify and trace all dependants and nominees, allocate the death benefit equitably, and decide on the method of payment. Trustees have at least 12 months to fulfil these duties.

Duty 1: Identify and trace all dependants and nominees

The first step trustees take in identifying and tracing a member's dependants and nominees is to refer to any information the member provided via their application form or subsequent forms submitted. It is therefore important that members provide their fund with comprehensive details of their family circle and nominees, and keep the details up to date.

If contact details are unavailable or outdated, or there is conflicting information or a dispute, the investigation time will be extended. This may mean that dependants in need of this benefit will have to wait longer for payment.

Duty 2: Allocate the death benefit

Once dependants and nominees have been identified, the trustees must allocate the death benefit fairly. Their decisions are based on a number of factors, such as each party's financial circumstances, their extent of dependency on the member on the date of their death, the nature of their relationship with the member, and the wishes of the member (as set out in their nomination).

If no dependants are found, but nominees (who are not dependants) are listed, the trustees must first establish whether the member's estate is solvent (i.e. that it has enough money to settle its liabilities). If the estate is solvent, the benefit will be paid to the nominees according to the proportions stipulated by the member. However, if the estate is insolvent, the death benefit must firstly be used to settle the shortfall in the estate. The remaining benefit (if any) will then be paid to the nominees. Legally, the payment can only be made 12 months after the member's death.

If a member has died of unnatural causes, the allocation of the death benefit will be delayed until it can be confirmed that the member's death was not caused by any of the dependants or nominees.

If no dependants are found, and the member had not made any nominations, the trustees will pay the benefit to the member's estate after the 12-month legal waiting period has lapsed.

Duty 3: Decide on the method of payment

The trustees must then decide how the money will flow to the beneficiaries (i.e. paid directly to a bank account held in their name, a natural/legal guardian, caregiver, trust or beneficiary fund).

Beneficiaries are entitled to choose whether to receive their benefit as a cash lump sum, use it to purchase a compulsory living or guaranteed life annuity, or a combination of the two.

For a minor beneficiary, or a major beneficiary who is not able to manage their own affairs, the election must be made by the person who is legally responsible for managing their affairs (i.e. their natural/legal guardian, administrator or curator).

When it comes to distributing the death benefit, the [Pension Funds] Act gives preference to dependency.

Tax and payment

Lump sums from retirement fund benefits are taxed, so it's a good idea to warn your beneficiaries about the tax implications. Beneficiaries may request a tax simulation before they complete their payment instruction forms. This will help them to understand the possible tax impact of their decision before they complete their election and payment instructions.

Once the retirement fund's administrator has received the beneficiaries' instructions, they will apply for a tax directive from the South African Revenue Service (SARS). SARS will issue a tax directive within 24 hours. It is important to make your beneficiaries aware that payment instructions and tax directives cannot be reversed.

The tax amount (if any) will be deducted from the beneficiaries' lump sums and paid to SARS. The balance of the lump sums is then paid to the beneficiaries.

Keep your information up to date

Dealing with administration when a loved one has just passed away can be very stressful, and the legally prescribed process that trustees must follow, as described above, can take an extended period to complete. Providing comprehensive information about your family circle and nominations to your fund, and keeping this information up to date, will enable a quicker and easier investigation.

It is also worthwhile to consider making provision for your dependants through a product like a tax-free investment or endowment, which can provide liquidity to your dependants while the retirement fund process is wound up.

Table 1: How death benefits are handled

	Retirement funds	Life and savings products	Estate administration
Which Allan Gray products are impacted?	<ul style="list-style-type: none"> Allan Gray Retirement Annuity Fund Allan Gray Pension Preservation Fund Allan Gray Provident Preservation Fund Allan Gray Umbrella Pension Fund Allan Gray Umbrella Provident Fund 	<ul style="list-style-type: none"> Allan Gray Living Annuity Allan Gray Endowment Allan Gray Tax-Free Investment 	Allan Gray unit trusts and other unit trusts from the Allan Gray local and offshore platforms as assets of the estate
Which act applies?	<ul style="list-style-type: none"> Pension Funds Act Income Tax Act 	<ul style="list-style-type: none"> Long-term Insurance Act Income Tax Act 	Administration of Estates Act
How are the payouts determined?	According to Section 37C of the Pension Funds Act: Distribution of death benefits	According to the conditions set out in the policy contract issued by the insurance/investment company. For Allan Gray products, the benefit is paid to the beneficiaries you appointed.	According to the provisions set out in the last will or according to the Intestate Succession Act
Who makes the decision regarding who will receive payment?	Board of trustees of the Fund	The investor	The executor
Types of beneficiaries	Dependants (as defined in the Pension Funds Act) and nominees (as nominated by the member)	Beneficiaries appointed by the policyholder	Heirs listed in the last will or family members according to the Intestate Succession Act
Typical timelines to payment	Trustees have up to 12 months to conduct their investigation.	Once the death certificate and other documents have been received (typically about two weeks).	This will vary, depending on the complexity of the deceased estate.

Sonja joined Allan Gray in 2013 and is responsible for the processing of death claims across all life, retirement and discretionary products for the Retail business. She has 18 years' experience in retirement fund administration and holds an International Action Learning Master of Business Administration.

Allan Gray Balanced and Stable Fund asset allocation as at 30 September 2019

	Balanced Fund % of portfolio			Stable Fund % of portfolio		
	Total	SA	Foreign*	Total	SA	Foreign*
Net equities	64.9	44.4	20.4	36.8	21.0	15.7
Hedged equities	8.2	1.8	6.3	7.0	1.2	5.8
Property	1.2	1.2	0.1	4.0	4.0	0.0
Commodity-linked	4.3	3.5	0.8	2.9	1.8	1.1
Bonds	14.3	10.1	4.2	28.6	19.5	9.0
Money market and bank deposits	7.1	5.2	1.9	20.7	17.2	3.5
Total	100.0	66.2	33.8	100.0	64.7	35.2

Note: There might be slight discrepancies in the totals due to rounding. *This includes African ex-SA assets.

Allan Gray Equity Fund net assets as at 30 September 2019

Security (Ranked by sector)	Market value (R million)	% of Fund	FTSE/JSE ALSI weight (%)
South Africa	24 412	66.1	
South African equities	23 700	64.2	
Resources	4 612	12.5	28.4
Sasol	1 325	3.6	
Glencore	1 280	3.5	
BHP	502	1.4	
Sappi	291	0.8	
Impala Platinum	272	0.7	
AECI	251	0.7	
Positions less than 1% ¹	691	1.9	
Financials	9 000	24.4	25.5
Standard Bank	1 565	4.2	
Remgro	1 253	3.4	
Investec	1 182	3.2	
Old Mutual	995	2.7	
Reinet	928	2.5	
Nedbank	517	1.4	
Rand Merchant Investment ²	406	1.1	
Quilter	387	1.0	
Momentum Metropolitan	328	0.9	
Positions less than 1% ¹	1 438	3.9	
Industrials	9 831	26.6	46.1
Naspers ²	1 972	5.3	
British American Tobacco	1 867	5.1	
Woolworths	964	2.6	
Life Healthcare	699	1.9	
Prosus	656	1.8	
KAP Industrial	482	1.3	
Netcare	426	1.2	
Super Group	396	1.1	
MultiChoice	286	0.8	
Positions less than 1% ¹	2 082	5.6	
Other securities	258	0.7	
Positions less than 1% ¹	258	0.7	
Commodity-linked securities	361	1.0	
New Gold Platinum ETF	265	0.7	
Positions less than 1% ¹	96	0.3	
Cash	351	1.0	
Africa ex-SA	779	2.1	
Equity funds	779	2.1	
Allan Gray Africa ex-SA Equity Fund	779	2.1	
Foreign ex-Africa	11 749	31.8	
Equity funds	11 591	31.4	
Orbis Global Equity Fund	7 392	20.0	
Orbis SICAV International Equity Fund ³	2 839	7.7	
Orbis SICAV Emerging Markets Equity Fund	717	1.9	
Allan Gray Frontier Markets Equity Fund ³	643	1.7	
Cash	158	0.4	
Totals	36 940	100.0	

¹ JSE-listed securities include equities, property and commodity-linked instruments.

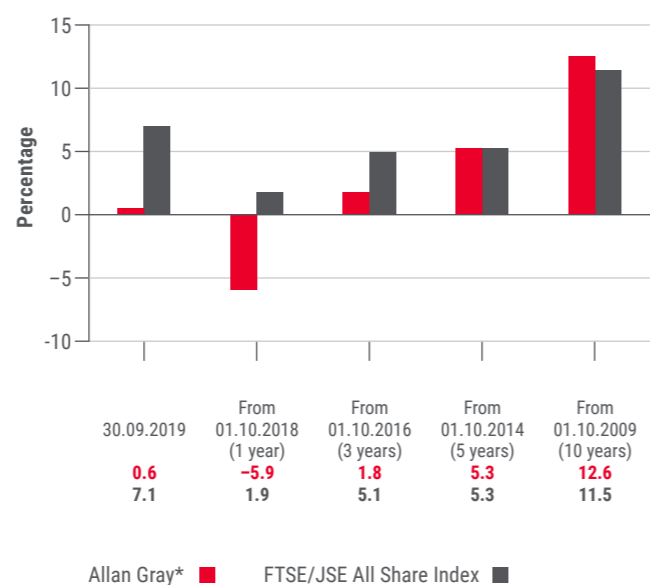
² Including stub certificates.

³ This fund is not approved for marketing in South Africa. Reference to this fund is solely for disclosure purposes and is not intended for, nor does it constitute, solicitation for investment. Note: There may be slight discrepancies in the totals due to rounding. For other fund-specific information, please refer to the monthly factsheets.

Investment track record – share returns

Allan Gray Proprietary Limited global mandate share returns vs FTSE/JSE All Share Index			
Period	Allan Gray*	FTSE/JSE All Share Index	Out-/Under-performance
1974 (from 15.06)	-0.8	-0.8	0.0
1975	23.7	-18.9	42.6
1976	2.7	-10.9	13.6
1977	38.2	20.6	17.6
1978	36.9	37.2	-0.3
1979	86.9	94.4	-7.5
1980	53.7	40.9	12.8
1981	23.2	0.8	22.4
1982	34.0	38.4	-4.4
1983	41.0	14.4	26.6
1984	10.9	9.4	1.5
1985	59.2	42.0	17.2
1986	59.5	55.9	3.6
1987	9.1	-4.3	13.4
1988	36.2	14.8	21.4
1989	58.1	55.7	2.4
1990	4.5	-5.1	9.6
1991	30.0	31.1	-1.1
1992	-13.0	-2.0	-11.0
1993	57.5	54.7	2.8
1994	40.8	22.7	18.1
1995	16.2	8.8	7.4
1996	18.1	9.4	8.7
1997	-17.4	-4.5	-12.9
1998	1.5	-10.0	11.5
1999	122.4	61.4	61.0
2000	13.2	0.0	13.2
2001	38.1	29.3	8.8
2002	25.6	-8.1	33.7
2003	29.4	16.1	13.3
2004	31.8	25.4	6.4
2005	56.5	47.3	9.2
2006	49.7	41.2	8.5
2007	17.6	19.2	-1.6
2008	-13.7	-23.2	9.5
2009	27.0	32.1	-5.1
2010	20.3	19.0	1.3
2011	9.9	2.6	7.3
2012	20.6	26.7	-6.1
2013	24.3	21.4	2.9
2014	16.2	10.9	5.3
2015	7.8	5.1	2.7
2016	12.2	2.6	9.6
2017	15.6	21.0	-5.4
2018	-8.0	-8.5	0.5
2019 (to 30.09)	0.6	7.1	-6.5

Returns annualised to 30.09.2019



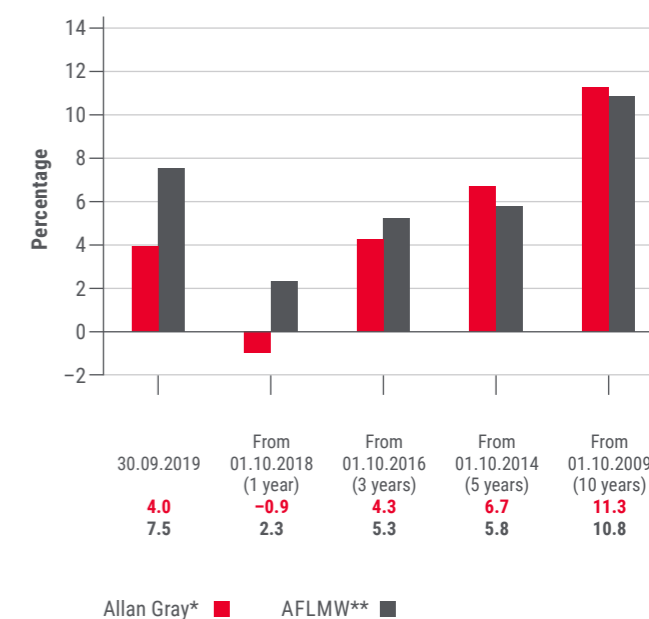
An investment of R10 000 made with Allan Gray on 15 June 1974 would have grown to R213 809 391 by 30 September 2019. By comparison, the returns generated by the FTSE/JSE All Share Index over the same period would have grown a similar investment to R9 503 642. Returns are before fees.

*Allan Gray commenced managing pension funds on 1 January 1978. The returns prior to 1 January 1978 are of individuals managed by Allan Gray, and these returns exclude income. Returns are before fees. Note: Listed property included from 1 July 2002. Inward listed included from November 2008 to November 2011.

Investment track record – balanced returns

Allan Gray Proprietary Limited global mandate total returns vs Alexander Forbes Global Manager Watch			
Period	Allan Gray*	AFLMW**	Out-/Under-performance
1974	-	-	-
1975	-	-	-
1976	-	-	-
1977	-	-	-
1978	34.5	28.0	6.5
1979	40.4	35.7	4.7
1980	36.2	15.4	20.8
1981	15.7	9.5	6.2
1982	25.3	26.2	-0.9
1983	24.1	10.6	13.5
1984	9.9	6.3	3.6
1985	38.2	28.4	9.8
1986	40.3	39.9	0.4
1987	11.9	6.6	5.3
1988	22.7	19.4	3.3
1989	39.2	38.2	1.0
1990	11.6	8.0	3.6
1991	22.8	28.3	-5.5
1992	1.2	7.6	-6.4
1993	41.9	34.3	7.6
1994	27.5	18.8	8.7
1995	18.2	16.9	1.3
1996	13.5	10.3	3.2
1997	-1.8	9.5	-11.3
1998	6.9	-1.0	7.9
1999	80.0	46.8	33.1
2000	21.7	7.6	14.1
2001	44.0	23.5	20.5
2002	13.4	-3.6	17.1
2003	21.5	17.8	3.7
2004	21.8	28.1	-6.3
2005	40.0	31.9	8.1
2006	35.6	31.7	3.9
2007	14.5	15.1	-0.6
2008	-1.1	-12.3	11.2
2009	15.6	20.3	-4.7
2010	11.7	14.5	-2.8
2011	12.6	8.8	3.8
2012	15.1	20.0	-4.9
2013	25.0	23.3	1.7
2014	10.3	10.3	0.0
2015	12.8	6.9	5.9
2016	7.5	3.7	3.8
2017	11.9	11.5	0.4
2018	-1.4	-2.1	0.7
2019 (to 30.06)	4.0	7.5	-3.5

Returns annualised to 30.09.2019



An investment of R10 000 made with Allan Gray on 1 January 1978 would have grown to R24 370 311 by 30 September 2019. The average total performance of global mandates of Large Managers over the same period would have grown a similar investment to R5 408 270. Returns are before fees.

*Allan Gray commenced managing pension funds on 1 January 1978. The returns prior to 1 January 1978 are of individuals managed by Allan Gray, and these returns exclude income. Returns are before fees. **Consulting Actuaries Survey returns used up to December 1997. The return for September 2019 is an estimate. The return from 1 April 2010 is the average of the non-investable Alexander Forbes Large Manager Watch. Note: Listed property included from 1 July 2002. Inward listed included from November 2008 to November 2011.

Allan Gray South African unit trusts annualised performance (rand)
in percentage per annum to 30 September 2019 (net of fees)

	Assets under management (R billion)	Inception date	Since inception	10 years	5 years	3 years	1 year	Highest annual return ⁴	Lowest annual return ⁴
High net equity exposure (100%)									
Allan Gray Equity Fund (AGEF) Average of South African - Equity - General category (excl. Allan Gray funds) ¹	36.9	01.10.1998	20.8 14.6	10.8 9.9	4.3 2.4	1.6 0.6	-6.3 -2.7	125.8 73.0	-20.7 -37.6
Allan Gray SA Equity Fund (AGDE) FTSE/JSE All Share Index including income	2.8	13.03.2015	2.9 4.3	- -	- -	0.3 5.1	-7.1 1.9	17.2 22.5	-11.5 -12.6
Allan Gray-Orbis Global Equity Feeder Fund (AGOE) FTSE World Index	18.5	01.04.2005	14.0 14.1	14.5 17.0	9.7 13.9	7.0 14.0	-3.8 9.0	78.2 54.2	-29.7 -32.7
Medium net equity exposure (40% - 75%)									
Allan Gray Balanced Fund (AGBF) Allan Gray Tax-Free Balanced Fund (AGTB) Average of South African - Multi Asset - High Equity category (excl. Allan Gray funds) ²	148.2 1.0	01.10.1999 01.02.2016	15.8 5.3 11.8/4.7	10.2 - 9.2	5.8 - 5.0	3.3 3.5 3.9	-1.7 -2.0 1.6	46.1 13.3 41.9/13.7	-8.3 -5.4 -16.7/-6.0
Allan Gray-Orbis Global Fund of Funds (AGGF) 60% of the FTSE World Index and 40% of the J.P. Morgan GBI Global Bond Index	12.9	03.02.2004	10.4 11.5	10.8 14.1	7.8 11.8	4.1 10.3	-3.9 12.3	55.6 38.8	-13.7 -17.0
Low net equity exposure (0% - 40%)									
Allan Gray Stable Fund (AGSF) Daily interest rate of FirstRand Bank Limited plus 2%	50.2	01.07.2000	11.8 8.9	8.4 7.3	7.4 7.8	6.1 8.1	2.2 8.0	23.3 14.6	0.1 6.2
Very low net equity exposure (0% - 20%)									
Allan Gray Optimal Fund (AGOF) Daily interest rate of FirstRand Bank Limited	1.2	01.10.2002	7.8 6.4	6.4 5.2	7.3 5.7	4.9 5.9	3.7 5.9	18.1 11.9	-1.5 4.1
Allan Gray-Orbis Global Optimal Fund of Funds (AGOO) Average of US\$ bank deposits and euro bank deposits	1.0	02.03.2010	7.3 6.7	- -	3.5 5.0	-0.9 3.4	-5.7 4.8	39.6 35.6	-12.4 -19.1
No equity exposure									
Allan Gray Bond Fund (AGBD) JSE All Bond Index (Total return)	2.4	01.10.2004	9.2 8.7	9.2 8.8	9.3 8.3	10.2 8.9	11.5 11.4	18.0 21.2	-2.6 -5.6
Allan Gray Money Market Fund (AGMF) Alexander Forbes Short-Term Fixed Interest (STeFI) Composite Index ³	21.5	03.07.2001	8.0 7.9	6.7 6.5	7.5 7.1	7.9 7.4	7.8 7.3	12.8 13.3	5.2 5.2

¹ From inception to 28 February 2015, the benchmark was the FTSE/JSE All Share Index including income (source: IRESS).

² From inception to 31 January 2013, the benchmark of the Allan Gray Balanced Fund was the market value-weighted average return of the funds in both the Domestic Asset Allocation Medium Equity and Domestic Asset Allocation Variable Equity sectors of the previous ASISA Fund Classification Standard, excluding the Allan Gray Balanced Fund.

³ From inception to 31 March 2003, the benchmark was the Alexander Forbes 3-Month Deposit Index. From 1 April 2003 to 31 October 2011, the benchmark was the Domestic Fixed Interest Money Market Collective Investment Scheme sector excluding the Allan Gray Money Market Fund.

⁴ This is the highest or lowest consecutive 12-month return since inception. All rolling 12-month figures for the Fund and the benchmark are available from our Client Service Centre on request.

Allan Gray total expense ratios and transaction costs for the 3-year period
ending 30 September 2019

	Fee for benchmark performance	Performance fees	Other costs excluding transaction costs	VAT	Total expense ratio	Transaction costs (incl. VAT)	Total investment charge
Allan Gray Equity Fund	1.12%	0.25%	0.02%	0.14%	1.53%	0.08%	1.61%
Allan Gray SA Equity Fund	1.00%	-0.40%	0.01%	0.09%	0.70%	0.10%	0.80%
Allan Gray Balanced Fund	1.10%	0.30%	0.02%	0.14%	1.56%	0.08%	1.64%
Allan Gray Tax-Free Balanced Fund	1.37%	N/A	0.05%	0.14%	1.56%	0.14%	1.70%
Allan Gray Stable Fund	1.09%	0.13%	0.02%	0.11%	1.35%	0.08%	1.43%
Allan Gray Optimal Fund	1.00%	0.01%	0.02%	0.15%	1.18%	0.12%	1.30%
Allan Gray Bond Fund	0.25%	0.36%	0.02%	0.09%	0.72%	0.00%	0.72%
Allan Gray Money Market Fund	0.25%	N/A	0.00%	0.04%	0.29%	0.00%	0.29%
Allan Gray-Orbis Global Equity Feeder Fund	1.49%	0.27%	0.05%	0.00%	1.81%	0.14%	1.95%
Allan Gray-Orbis Global Fund of Funds	1.44%	0.37%	0.07%	0.00%	1.88%	0.11%	1.99%
Allan Gray-Orbis Global Optimal Fund of Funds	1.00%	0.62%	0.07%	0.00%	1.69%	0.13%	1.82%

The total expense ratio (TER) is the annualised percentage of the Fund's average assets under management that has been used to pay the Fund's actual expenses over the past three years. The TER includes the annual management fees that have been charged (both the fee at benchmark and any performance component charged), VAT and other expenses like audit and trustee fees. Transaction costs (including brokerage, Securities Transfer Tax (STT), STRATE and Investor Protection Levy and VAT thereon) are shown separately. Transaction costs are a necessary cost in administering the Fund and impact Fund returns. They should not be considered in isolation as returns may be impacted by many other factors over time including market returns, the type of financial product, the investment decisions of the investment manager and the TER. Since Fund returns are quoted after the deduction of these expenses, the TER and transaction costs should not be deducted again from published returns. As unit trust expenses vary, the current TER cannot be used as an indication of future TERs. A higher TER does not necessarily imply a poor return, nor does a low TER imply a good return. Instead, when investing, the investment objective of the Fund should be aligned with the investor's objective and compared against the performance of the Fund. The TER and other funds' TERs should then be used to evaluate whether the Fund performance offers value for money. The sum of the TER and transaction costs is shown as the total investment charge.

Foreign domiciled funds annualised performance (rand) in percentage per annum to 30 September 2019 (net of fees)

	Inception date	Since inception	10 years	5 years	3 years	1 year	Highest annual return ⁴	Lowest annual return ⁴
High net equity exposure								
Orbis Global Equity Fund FTSE World Index	01.01.1990	17.8 13.7	14.6 17.0	9.8 13.9	7.2 14.2	-3.4 9.3	87.6 54.2	-47.5 -46.2
Orbis SICAV Japan Equity (Yen) Fund Tokyo Stock Price Index	01.01.1998	14.7 9.6	14.4 13.6	13.0 12.7	8.9 9.9	1.6 0.9	94.9 91.0	-40.1 -46.4
Orbis SICAV Emerging Markets Equity Fund (US\$)⁵ MSCI Emerging Markets Equity (Net) (US\$) ⁵	01.01.2006	13.6 13.5	11.5 12.8	5.8 10.0	4.4 8.9	5.4 5.1	58.6 60.1	-34.2 -39.7
Allan Gray Africa ex-SA Equity Fund Standard Bank Africa Total Return Index	01.01.2012	11.1 5.5	- -	-2.5 -2.5	12.2 6.3	-12.6 9.0	65.6 33.6	-24.3 -29.4
Allan Gray Australia Equity Fund S&P/ASX 300 Accumulation Index	04.05.2006	15.4 12.9	15.2 12.8	12.1 10.4	12.7 10.9	9.4 12.5	99.5 55.6	-55.4 -45.1
Medium net equity exposure								
Orbis SICAV Global Balanced Fund 60% MSCI World Index with net dividends reinvested and 40% J.P. Morgan GBI Global Bond Index	01.01.2013	14.7 15.9	- -	8.3 11.7	4.4 10.2	-4.1 12.6	54.4 40.2	-9.8 -8.4
Allan Gray Australia Balanced Fund The custom benchmark comprises the S&P/ASX 300 Accumulation Index (36%), S&P/ASX Australian Government Bond Index (24%), MSCI World Index (net dividends reinvested) expressed in AUD (24%) and J.P. Morgan GBI Global Bond Index expressed in AUD (16%).	01.03.2017	8.8 11.9	- -	- -	- -	2.9 12.9	16.2 24.8	-5.3 -5.8
Low net equity exposure								
Allan Gray Australia Stable Fund Reserve Bank of Australia cash rate	01.07.2011	11.3 6.7	- -	6.6 2.4	4.8 0.6	3.8 1.3	32.7 28.8	-7.4 -12.6
Very low net equity exposure								
Orbis Optimal SA Fund (US\$) US\$ Bank deposits	01.01.2005	9.5 8.6	7.5 8.0	4.9 7.4	0.4 5.1	-2.4 9.9	48.6 57.9	-15.7 -25.6
Orbis Optimal SA Fund (Euro) Euro Bank deposits	01.01.2005	7.1 6.4	4.0 4.2	0.6 2.7	-2.7 1.9	-10.9 0.2	44.1 40.2	-19.3 -20.9
No equity exposure								
Allan Gray Africa ex-SA Bond Fund J.P. Morgan GBI EM Global Diversified Index	27.03.2013	16.3 6.8	- -	14.6 6.6	17.6 6.5	20.9 18.0	28.9 23.5	2.4 -7.7

Performance as calculated by Allan Gray

⁴ This is the highest or lowest consecutive 12-month return since inception. All rolling 12-month figures for the Fund and the benchmark are available from our Client Service Centre on request.

⁵ From inception to 31 October 2016, this Fund was called the Orbis SICAV Asia ex-Japan Equity Fund and its benchmark was the MSCI Asia ex-Japan Index. From 1 November 2016, the Fund's investment mandate was broadened to include all emerging markets. To reflect this, the Fund was renamed and the benchmark was changed.

IMPORTANT INFORMATION FOR INVESTORS

Information and content

The information in and content of this publication are provided by Allan Gray as general information about the company and its products and services. ("Allan Gray" means Allan Gray Proprietary Limited and all of its subsidiaries and associate companies, and "the company" includes all of those entities.) Allan Gray does not guarantee the suitability or potential value of any information or particular investment source. The information provided is not intended to nor does it constitute financial, tax, legal, investment or other advice. Before making any decision or taking any action regarding your finances, it is recommended that you consult an independent, qualified financial adviser regarding your specific situation. Nothing contained in this publication constitutes a solicitation, recommendation, endorsement or offer by Allan Gray; it is merely an invitation to do business.

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Allan Gray Unit Trust Management (RF) Proprietary Limited (the "Management Company") is registered as a management company under the Collective Investment Schemes Control Act 45 of 2002, in terms of which it operates unit trust portfolios under the Allan Gray Unit Trust Scheme, and is supervised by the Financial Sector Conduct Authority (FSCA). Allan Gray Proprietary Limited (the "Investment Manager"), an authorised financial services provider, is the appointed investment manager of the Management Company and is a member of the Association for Savings & Investment South Africa (ASISA). Collective investment schemes in securities (unit trusts or funds) are generally medium- to long-term investments. Except for the Allan Gray Money Market

Fund, where the Investment Manager aims to maintain a constant unit price, the value of units may go down as well as up.

Past performance is not necessarily a guide to future performance. The Management Company does not provide any guarantee regarding the capital or the performance of its unit trusts. Funds may be closed to new investments at any time in order for them to be managed according to their mandates. Unit trusts are traded at ruling prices and can engage in borrowing and scrip lending.

Performance

Performance figures are for lump sum investments with income distributions reinvested. Where annualised performance is mentioned, it refers to the average return per year over the period. Actual investor performance may differ as a result of the investment date, the date of reinvestment and dividend withholding tax. Movements in exchange rates may also be the cause of the value of underlying international investments going up or down. The Equity, Balanced, Stable and Optimal funds each have more than one class of units and these are subject to different fees and charges. Unit trust prices are calculated on a net asset value basis, which is the total market value of all assets in the Fund, including any income accruals and less any permissible deductions from the Fund, divided by the number of units in issue. Forward pricing is used and fund valuations take place at approximately 16:00 each business day. Purchase and redemption requests must be received by 14:00 each business day to receive that day's price. Unit trust prices are available daily on www.allangray.co.za. Permissible deductions include management fees, brokerage, securities transfer tax, auditor's fees, bank charges and trustee fees. A schedule of fees, charges and maximum commissions is available on request from the Management Company.

Benchmarks

FTSE/JSE All Share Index

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J.P. Morgan Index

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Understanding the funds

Investors must make sure that they understand the nature of their choice of funds and that their investment objectives are aligned with those of the fund(s) they select. The Allan Gray Equity, Balanced, Stable and rand-denominated offshore funds may invest in foreign funds managed by Orbis Investment Management Limited, our offshore investment partner.

A feeder fund is a unit trust that invests in another single unit trust which charges its own fees. A fund of funds is a

unit trust that invests in other unit trusts, which charge their own fees. Allan Gray does not charge any additional fee in its feeder fund or fund of funds.

The Allan Gray Money Market Fund is not a bank deposit account. The Fund aims to maintain a constant price of 100 cents per unit. The total return an investor receives is made up of interest received and any gain or loss made on instruments held by the Fund. While capital losses are unlikely, they can occur if, for example, one of the issuers of an instrument defaults. In this event, investors may lose some of their capital. To maintain a constant price of 100 cents per unit, investors' unit holdings will be reduced to the extent of such losses. The yield is calculated according to the applicable ASISA standards. Excessive withdrawals from the Fund may place it under liquidity pressure. If this happens, withdrawals may be ring-fenced and managed over a period of time.

Additional information for retirement fund members and investors in the tax-free investment account, living annuity and endowment

The Allan Gray Retirement Annuity Fund, Allan Gray Pension Preservation Fund, Allan Gray Provident Preservation Fund and Allan Gray Umbrella Retirement Fund (comprising the Allan Gray Umbrella Pension Fund and Allan Gray Umbrella Provident Fund) are all administered by Allan Gray Investment Services Proprietary Limited, an authorised administrative financial services provider and approved under section 13B of the Pension Funds Act as a benefits administrator. Allan Gray Proprietary Limited, also an authorised financial services provider, is the sponsor of the Allan Gray Umbrella Retirement Fund. The Allan Gray Tax-Free Investment Account, Allan Gray Living Annuity and Allan Gray Endowment are underwritten by Allan Gray Life Limited, also an authorised financial services provider and a registered insurer licensed to provide life insurance products as defined in the Insurance Act 18 of 2017. The underlying investment options of the Allan Gray individual life and retirement products are portfolios of collective investment schemes in securities (unit trusts or funds).

Tax note

In accordance with section 11(i) of the Botswana Income Tax Act (Chapter 52:01), an amount accrued to any person shall be deemed to have accrued from a source situated in Botswana where it has accrued to such person in respect of any investment made outside Botswana by a resident of Botswana, provided that section 11(i) shall not apply to foreign investment income of non-citizens resident in

Botswana. Botswana residents who have invested in the shares of the Fund are therefore requested to declare income earned from this Fund when preparing their annual tax returns. The Facilities Agent for the Fund in Botswana is Allan Gray (Botswana) (Proprietary) Limited at 2nd Floor, Building 2, Central Square, New CBD, Gaborone, where investors can obtain a prospectus and financial reports.

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