

NEDGROUP
INVESTMENTS

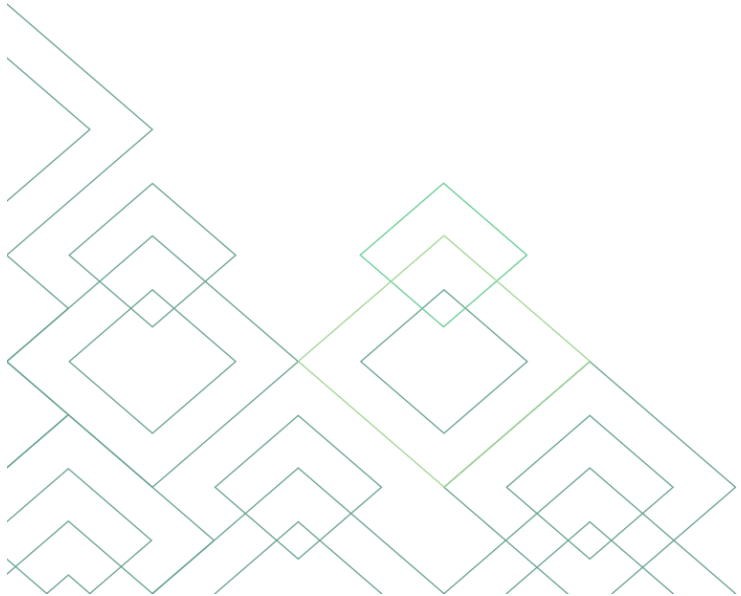
UNIT TRUSTS | INTERNATIONAL | RETIREMENT FUNDS

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NEDGROUP INVESTMENTS **ENTREPRENEUR FUND**

Quarter Two, 2020



Nedgroup Investments Entrepreneur Fund



| Performance to 30 June 2020 | Nedgroup Inv Entrepreneur Fund ¹ | ASISA category average | FTSE/JSE Small Cap Index | FTSE/JSE Mid Cap Index |
|-----------------------------|---|------------------------|--------------------------|------------------------|
| 3 months | +13.7% | +14.0% | +17.2% | +15.4% |
| 12 months | -15.4% | -17.6% | -22.9% | -17.6% |

Market commentary

In our Q1 2020 commentary we showed a chart which depicted the extent of the market collapse in the historical context of previous crashes and noted that the COVID-19 crash had been the quickest and sharpest on record. This served as a signal to investors of possible opportunity. While we noted at the time that the scariest days of the disease still lay ahead of us, the market had already reacted very sharply. Only three months later (but which for many of us feels more like years), the degree of recovery many stocks and markets have demonstrated has been equally remarkable.

The JSE All Share Index posted a total return of +23.2% in the second quarter of 2020. The Resources sector performed best (returning +41.2%), followed by Industrials (+16.6%) and Financials (+12.9%). The JSE Mid-Cap Index returned +15.4% and the JSE Small Cap Index was +17.2%.

Easily the most robust sectors have been those that have benefitted from the COVID-19 linked change in consumer behaviour, by being able to offer technology related alternatives. Our investment in Tencent in China (via Naspers / Prosus) is a very good example. In addition, commodity counters benefited from rising commodity prices caused by the expected increase in demand from the enormous stimulus injected into almost all economies via fiscal and monetary relief.

Most importantly, China is already emerging from the worst of the COVID-19 impact stronger than almost all other nations and the importance and scale of that country's economy is even greater today than before. On the other side of the scale, local Banks, Property companies and Discretionary Consumer and Retail stocks remain out of favour with their future profit prospects highly uncertain and extremely bleak in the short term.

The IMF recently revised its expectations for global growth lower, projecting a deeper recession and a slower recovery for the virus-ravaged world economy. It now expects global gross domestic product to shrink -4.9% this year. In the US, first quarter GDP contracted by 5% (q/o/q). This was the sharpest quarterly decline since the -8.4% fall in the fourth quarter of 2008, in the depths of the Global Financial Crisis.

Emerging economies, such as South Africa, are the hardest hit by COVID-19. They do not have the healthcare systems to adequately deal with the rising rate of infection nor the fiscal and monetary firepower that Western economies have to support their economies.

South Africa has now faced more than 100 days of lockdown restrictions in response to the pandemic. The country recently breached 200,000 coronavirus cases. It took 102 days for South Africa to record 100 000 coronavirus cases, but only a further 14 days for the number of infections to double. While the rate of infection continues to climb, restrictions have started to ease, and the economy is beginning to slowly re-open.

The economic damage caused by the lockdown has been severe, the full extent of which will only be appreciated in the months and probably years ahead. Business and consumer confidence are at all-time lows, unemployment is rising (30% in Q1 2020) and the South African Reserve Bank now estimates that GDP will contract by -7% in 2020. In response, the government has announced various measures, such as the R500bn COVID-19 response

¹ Net return for the Nedgroup Investments Entrepreneur Fund, A class. Source: Morningstar (monthly data series).





package. In addition, the SARB has cut the repo rate to 3.75%, an historic low. While these are welcome interventions, they are unlikely to have much of an effect to ameliorate the economic damage inflicted by the Lockdowns.

Portfolio commentary

The Nedgroup Investments Entrepreneur Fund's top five performing positions added 6.9% to returns over the second quarter, while the bottom five detracted a combined -1.7%.

| Top contributors | Average weight | Performance contribution | Top detractors | Average weight | Performance contribution |
|------------------|----------------|--------------------------|-----------------|----------------|--------------------------|
| Naspers Ltd | 9.2% | 2.0% | Reunert | 3.2% | -0.7% |
| KAP Industrial | 3.0% | 1.4% | Pick 'n Pay | 1.5% | -0.3% |
| RMI Holdings | 3.9% | 1.3% | Kaap Agri | 1.1% | -0.2% |
| Prosus | 4.5% | 1.2% | Master Drilling | 0.9% | -0.2% |
| Coronation | 3.3% | 1.1% | Distell | 1.3% | -0.2% |
| | | +6.9% | | | -1.7% |

The exposure of the fund to businesses relatively unaffected (operationally anyway) by COVID-19 is clear to see – such as RMI Holdings (short-term insurance via Outsurance), Coronation (Investment Management), and Tencent in China (via Naspers / Prosus). We have also seen some recovery from select stocks that were especially hard hit in Q1, during the immediate market reaction to the onslaught of COVID – such as KAP Industrial.

Although we had moved to limit the portfolios exposure to Discretionary Retail as far as possible, we were not able to fully escape the impact on domestic SA industrial stocks. Reunert's results in the quarter were disappointing, compounded by the discovery of a fraud in their lending book against the office equipment (Nashua) that they sell.

Current positioning and outlook

Naspers / Prosus remains the largest position in the fund and warrants a few updated comments, especially considering its contribution to performance over the last quarter and year to date. The investment merits for this counter in our view remain exclusively driven by the prospects for the primary asset which dominates the portfolio – Tencent.

Over the course of the last 12 months our already positive view on the Tencent stock has been strengthened by multiple factors including – the acceleration in gaming title releases, the company's fortuitous business model allowing user engagement on games, communication, and the firm's ability to respond to, and develop, new commercial (work from home) applications and industrial (cloud services) opportunities that presented themselves during the crisis. On top of this, social media and e-commerce has accelerated further during COVID-19 related lockdowns in China.

These have combined to accelerate the growth in the firm's profits despite the increasingly conservative accounting of deferring recognition of revenue. It is also underpinned by the firm's strong cashflow and increasingly material portfolio of technology investments around the world, and which consequently overstate the overall valuation of the firm. Despite the strong run in the shares over the last year we remain with a very large position, albeit at the extreme ends of our risk tolerance. We consider the performance of the remainder of the Naspers / Prosus portfolio to have been mixed and are disappointed by managements continued inability to address the discount trapped in the firm's corporate structure.





We continue to feel that the macro conditions for smaller domestic businesses to prosper in South Africa remain extremely bleak, and we do not expect any relief to come from constructive intervention or stimulus generated by the state. Consequently, we have looked to position the fund in businesses that will benefit from a weakening currency as well as those capable of protecting, and even growing, their profits despite these macro headwinds.

The fund's notable concentrations are as follows:

- Global tech and IT – Naspers / Prosus 15.5%
- Domestic short-term insurance – Santam and RMI 11%
- Global tobacco – BAT / Reinet 8%
- Growth and Recovery Commodities – RBP Platinum, Afrimat, Merafe, and Oceana 12.5%
- Defensive domestic consumer – AVI, Adcock Ingram, and Pick 'n Pay 9.5%
- Defensive Financials and Investment Management – JSE, Alexander Forbes, Coronation, Peregrine, and PSG Konsult 13.8%
- Cash is at the low end of the historic range – currently at 2.3%

Conclusion

The third quarter is likely to mark the peak of the COVID-19 health crisis in South Africa, in terms of the number of lives lost. It will not mark the peak of the economic impact. The ANC government continues to bumble its way through the management of the crisis with varying, and at times, apparently random imposition and release of lockdown restrictions on our day-to-day lives. Load shedding has returned in the depths of winter to add more misery to the lives of many worried and pressurised South Africans. In the next few months the relief provided by the UIF, and the generosity of emergency funds raised will run out.

In the meantime, we learn daily of fresh rounds of retrenchments being implemented in attempts to right-size businesses trying to survive. These effects remain to be felt in the financial performance of many local businesses and consequently we remain extremely worried about their recovery prospects. It will also explain the fund positioning in terms of the areas of focus and concentration explained above.

We remain alert to opportunity, and guard against the temptation of being overly pessimistic and, equally, naively optimistic. The portfolio currently trades on a historic Price/Earnings (P/E) ratio of 16.5x (which includes Naspers, Prosus and RBP all >40X and collectively 20% of the fund) and a dividend yield of 4.5% which we believe offers reasonable value.

Responsible investment comments

The current crisis has heightened awareness of ESG. Combining profit and purpose has never been more important. ESG factors are integrated into our investment analysis to strengthen the decision-making process, better manage risk and ensure that investments generate long-term value in an ethical manner. Our approach and commitment to ESG also enhances our value proposition to our clients. There were no notable engagements associated with positions in this fund during the second quarter of 2020.





Disclaimer

WHO WE ARE

Nedgroup Collective Investments (RF) Proprietary Limited is an authorised Collective Investment Scheme and the representative of Nedgroup Investments Funds PLC in terms of the Collective Investment Schemes Control Act. It is a member of the Association of Savings & Investment South Africa (ASISA)..

OUR TRUSTEE

The Standard Bank of South Africa Limited is the registered trustee.
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HOW ARE OUR FUNDS PRICED

Funds are valued daily at 15:00. Instructions must reach us before 14:00 (12:00 for Nedgroup Money Market Fund) to ensure same day value. Prices are published daily on our website and in selected major newspapers.

FEES

A schedule of fees and charges is available on request from Nedgroup Investments. One can also obtain additional information on Nedgroup Investments products on our website.

DISCLAIMER

Unit trusts are generally medium to long-term investments. The value of your investment may go down as well as up. Past performance is not necessarily a guide to future performance. Nedgroup Investments does not guarantee the performance of your investment and even if forecasts about the expected future performance are included you will carry the investment and market risk, which includes the possibility of losing capital. Our funds are traded at ruling prices and can engage in borrowing and scrip lending.

Some funds may hold foreign securities including foreign CIS funds. As a result, the fund may face material risks, which could include foreign exchange risks, market conditions and macro-economic and political conditions.

A fund of funds may only invest in other funds, and a feeder fund may only invest in another single fund, both will have funds that levy their own charges, which could result in a higher fee structure.

The Nedgroup Investments Money Market Fund offering aims to maintain a constant price of 100 cents per unit. A money market fund is not a bank deposit. The total return to the investor is made up of interest received and any gain or loss made on any particular instrument held. In most cases the return will merely have the effect of increasing or decreasing the daily yield, but in an extreme case it can have the effect of a capital loss. Excessive withdrawals from the fund may place the fund under liquidity pressures and that in such circumstances a process of ring-fencing of withdrawal instructions and managed pay-outs over time may be followed. The yield is calculated using an annualised seven day rolling average as at the relevant dates provided for in the fund fact sheet. Nedgroup Investments has the right to close its funds to new investors in order to manage it more efficiently.

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