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NEDGROUP INVESTMENTS VALUE FUND

Quarter Two, 2020

Market Commentary

WORLD

- The global economy plunged into the deepest recession since the 1929 Great Depression as a result of national lockdowns to contain the COVID-19 pandemic — third-quarter growth prospects have improved on re-opening measures, but remain vulnerable to second-wave infections
- Authorities across nations unleashed unprecedented monetary and fiscal stimulus through loan guarantees, short-term liquidity provisions and income support — the resultant debt bloat should impair potential global output for many years
- Unemployment rates spiked as employers furloughed staff and household savings rates soared as they curtailed discretionary spending amid plummeting consumer confidence — a stark warning that economic recovery will be slow and volatile if a vaccine is not quickly produced
- Equity markets rallied strongly, led higher by technology, consumer discretionary and materials even as forward consensus earnings expectations are discounted for 2020 through to 2022 — forward valuations imply elevated risk of share price declines and low future returns if demand remains subdued and liquidity conditions worsen
- Most developed market government bond yields fell marginally despite new stimulus, while high-yield corporate and sovereign bonds largely recovered from the March sell-off — emergency liquidity measures have thus far averted mass insolvencies, but hasty withdrawal of bank liquidity is a risk to corporate solvency
- Industrial metals bounced, gold rallied and WTI oil doubled on the improved outlook and US dollar weakness — the ballooning US Federal Reserve balance sheet and surge in money supply is negative for the US dollar but positive for gold

SOUTH AFRICA

- The beleaguered SA economy contracted for the third successive quarter in Q1 (before the brunt of COVID-19 lockdowns), with fixed investment and inventory drawdowns the biggest detractors — consensus expectations are for a minimum 25% contraction (annualised) in Q2 and 7% for 2020
- A massive fiscal relief package exceeding R500 billion should buffer the economy from further employment losses and business closures — but government's debt binge will require a greater reduction in government expenditure over the next three years at least
- Government expects debt-to-GDP to exceed 80% by next March and reach 87% by 2024 where after it will decline — admitting it needs a US$4.2 billion low-interest, rapid financing instrument from the IMF
- The JSE rallied in tandem with global markets, led by a 41% surge in resource stocks — financial counters were laggards, weighed down by the banking sector on prospects for lower interest margins and higher impairments
- SA government bond yields fell on improving global risk appetite and short rates falling more than expected, although the yield curve remains extremely steep — longer dated yields reflect market anxiety for higher inflation and risk of default if government's debt sustainability proposals fail
- Low inflation prompted SARB's Monetary Policy Committee to reduce interest rates to 3.75% in May — the benign inflation outlook should give SARB comfort to keep rates at these historically low levels or reduce them more if inflation expectations moderate further
- The rand retraced some of its Q1 losses but is vulnerable to a setback in global risk appetite —improved terms of trade contributed to SA's first quarterly current account surplus since 2002

Q2 2020 PERFORMANCE COMMENTS

- The underweight position in commodity companies and especially precious metals miners was the largest detractor — these sectors rallied on stronger dollar commodity prices
- The high, defensive allocation to cash also detracted as the market rallied in line with global equities — on improved risk sentiment
- The core property holding in London-listed property company Capital & Counties fell — on continued pandemic disruption to retail economic activity in its core Covent Garden estate
- The zero allocation to combined large index stocks Naspers and Prosus detracted — valuations remain demanding as global technology companies continued to rally
- The largest contributor to relative performance was the core investment in pharmaceutical company Aspen — which continued to recover from its oversold position of the last two years
- Stock selection in consumer-facing companies was net positive — with no allocation to underperforming staple retailers Shoprite, Pick n Pay and Clicks

Top 5 contributors:

Description	Fund average weight (%)	CSWIX average weight (%)	Out/Under performance (%)
Aspen	5.7%	1.2%	1.6%
BHP Group	9.3%	2.4%	0.7%
Clicks	0.0%	1.5%	0.7%
Shoprite	0.0%	1.4%	0.6%
Capitec	0.0%	1.2%	0.3%

Top 5 detractors:

Description	Fund average weight (%)	CSWIX average weight (%)	Out/Under performance (%)
Hudaco	4.2%	0.0%	-0.8%
Anglogold Ashanti	0.0%	2.8%	-0.8%
Santam	7.4%	0.3%	-1.6%
Cash and Equivalents	5.9%	0.0%	-1.8%
Capital & Counties Properties	5.7%	0.2%	-2.0%

INVESTMENT OUTLOOK

World: Economic recovery is likely to be slow and volatile. Unprecedented levels of monetary and fiscal support will result in higher debt levels, impairing potential global output in the years ahead. Market volatility is likely to remain elevated with the risk of corporate insolvencies increasing. Geopolitical risks also continue to rise. The weaker dollar should support a higher gold price.

South Africa: A severe contraction in GDP is likely in 2020 which together with government's massive fiscal package will likely balloon the debt burden form an already over-indebted position. The inflation outlook remains extremely benign in the short term given the very weak consumer demand across the economy. This makes further interest rate cuts a reasonable probability. The bond yield curve has shifted lower and steepened as short-term rates are cuts and long bond yields remain elevated on rising sovereign debt crisis fears in the longer term.

CONCLUSION

Resources weight has been reduced as Sasol's share price recovery provided an opportunity to moderate the portfolio's weighting. The fund's primary commodity price exposure is via the investment in BHP Group, the highest quality diversified miner with a defensive asset base.

The allocation to consumer-facing counters was increased marginally on price weakness owing to the weaker consumer environment. Well-managed and capitalised, high return companies such as Spur Corporation should win market share from weaker players and emerge stronger in the medium to long term.

The managers increased the weight to diversified industrial stocks after the sector valuation derating offered opportunities to increase shareholdings in high ROE, niche counters such as Bidvest Corporation. Although the allocation to the healthcare sector was reduced the managers selectively took advantage of price weakness in attractively priced hospital companies.

The managers reduced the large position size in Santam, which is best of breed in its sector and remains a core holding. Even in the low probability event that the company settles business disruption policy claims, it remains resilient given its strong balance sheet and reinsurance cover. The low weight to growth-sensitive banking shares is maintained given the cautious outlook for SA economic conditions and near-term earnings headwinds. The core financials holding is FirstRand Bank as the best quality SA bank.

The meaningful allocation to JSE-listed global businesses remains, given the higher risks in the SA economy and larger global economic opportunity set. These companies should deliver hard-currency, real earnings growth through the cycle, supported by expected rand weakness.

Property exposure remains low via niche storage and logistics company, Stor-Age and relatively lowly geared, UK-based Capital & Counties. Capco secured a significant shareholding in Shaftesbury properties, expanding its reach of blue-chip central London property. Fortress A was added during the period – given the structure, Fortress A behaves more like a bond than a property company.

Cash levels reduced on selective price-weakness buying. The portfolio remains well diversified and defensively positioned given the global economic contraction and distressed SA economy.

RESPONSIBLE INVESTMENT SUMMARY

Proxy Voting Summary Q2 2020

Resolution Type Name	Total Count	For %	Against %	Abstain %
Adopt Financials	5	100.0%	0.0%	0.0%
Auditor/Risk/Social/Ethics related	39	92.3%	7.7%	0.0%
Buy Back Shares	9	100.0%	0.0%	0.0%
Director Remuneration	72	97.2%	2.8%	0.0%
Dividend Related	2	100.0%	0.0%	0.0%
Issue Shares	7	28.6%	71.4%	0.0%
Loan / Financial Assistance	10	40.0%	60.0%	0.0%
Other	15	73.3%	26.7%	0.0%
Political Expenditure/Donation	1	0.0%	100.0%	0.0%
Re/Elect Director	44	100.0%	0.0%	0.0%
Remuneration Policy	16	37.5%	62.5%	0.0%
Shares under Director Control	5	20.0%	80.0%	0.0%
Signature of Documents	2	100.0%	0.0%	0.0%

General Comments:

- There are no abstentions. We apply our minds to every single resolution put to shareholders. When there is an abstention it would typically be intentional or for strategic reasons.

- We typically vote against any resolution that could dilute the interests of existing shareholders. Examples include placing shares under the blanket control of Directors, providing loans and financial assistance to associate companies or subsidiaries and blanket authority to issue shares. On the rare occasion, we have voted in favour of such resolutions, we could gain the required conviction in the specifics of the strategic rationale for such activities and could gain comfort that such activities are indeed to be used to the reasons stated.

- The firm also has a strong philosophy regarding management remuneration models. We believe in rewarding good managers with appropriate cash remuneration on achievement of relevant performance metrics that enhance long-term shareholder value. We are generally not in favour of share option schemes given the inherent asymmetry between risk and reward typical of such schemes. In addition, we do not believe that existing shareholders should be diluted by the issuing of new shares to management as is the case with most option schemes. We are in favour of the alignment created between management and shareholders when management has acquired its stake in the company through open market share trading and paid for out of management's own cash earnings.

Notable Engagements

(Note: reporting at Foord investment house level, specific fund might not be invested in all these companies)

Standard Bank

Engaged the board regarding proxy voting around remuneration structures, disclosures and reporting and approach to climate change related resolutions. The board supports the goals of the Paris Agreement and developing climate policy which will be in line with the guidelines of the TCFDs. The company has spent a lot of time getting buy in from the management and board structures. They are more focused on renewables than non-renewables, but Africa is reliant on non-renewables and so cannot simply immediately eliminate it. We are comfortable with the strategic approach with regards to climate change related policies.

Capital and Counties

Engaged with the Chairman (Henry Staunton) on governance and remuneration.

Hudaco

Engaged with the Chairman (Stephen Connelly) on ESG and overall corporate governance.

Metair

Engaged with the Metair Remuneration committee on remuneration policy and outcomes going forward.

Engaged with the Chairman (Brand Pretorius) separately on executive and non-executive management structures and succession planning.

Spur

Engaged with the Chairman (Mike Bosman) on remuneration policy and capital allocation of the group.

Sasol

Engaged the board regarding remuneration structures.

Disclaimer

WHO WE ARE
Nedgroup Collective Investments (RF) Proprietary Limited, is the company that is authorised in terms of the Collective Investment Schemes Control Act to administer the Nedgroup Investments unit trust funds. It is a member of the Association of Savings & Investment South Africa (ASISA).

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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.

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For the Nedgroup Investments Bravata World Wide Flexible Fund it is calculated monthly as a percentage (the sharing rate) of outperformance relative to the fund's benchmark, with the high watermark principle applying. All performance fees are capped per fund over a rolling 12-month period. A schedule of fees and charges and maximum commissions is available on request from Nedgroup Investments.

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