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NEDGROUP INVESTMENTS SA EQUITY FUND

Quarter Two, 2021

The SA cyclical recovery offers a glimmer of hope, however structural economic reforms are required for a sustainable recovery

Performance to 30 June 2021	Nedgroup Investments SA Equity[1]	FTSE/JSE Capped SWIX
3 months	-2.6%	0.5%
1 year	24.2%	27.6%
3 year	4.6%	4.8%

Market commentary

As the world emerges from the disastrous impact of the Covid-19 pandemic, we have witnessed a spectacular global economic recovery underpinned by unprecedented monetary and fiscal stimulus. The ultra-restocking phase and resurgent demand has resulted in a tightening of supply and demand imbalances, as well as logistics constraints. An example of this can be seen in processor chip shortages, where current demand cannot be met by constrained supply, while new supply takes time to come online. This restocking phase, coupled with a weaker US dollar, has resulted in higher commodity prices as consumers of commodities have prioritised obtaining supply to meet demand for their products, whilst becoming somewhat less price sensitive.

The commodity boom has been a tailwind for commodity producers like South Africa, adding to a faster-than-expected domestic economic recovery. The multiplier effects of our buoyant resources and agricultural sectors, plus higher taxes from mining companies has supported the South African cyclical recovery. This has taken some pressure off our constrained fiscal position.

There are several green shoots currently underway in the South African economy underpinning a cyclical recovery:

- Retailers and industrial companies have reported a stronger-than-expected rebound.
- Banks have reported surprisingly low credit losses.
- The mining sector has been supported by higher commodity prices.
- Agriculture has seen strong export demand, benefitting from good rains.
- Construction companies have noted an increase in local public sector spend from the likes of SANRAL as well as additional demand from miners.
- Our vaccine rollout, although delayed, is gaining momentum, with over 3 million people vaccinated thus far. The pace is expected to accelerate as vaccine supply increases over the following months, assisting us to move to a more normal post covid-19 world.

This has led to upward revisions in expected SA GDP growth forecasts for 2021, as it seems that we are in the midst of a cyclical recovery at the upper end of economic expectations of around a year ago.

Chart 1: SA GDP expectations (2021, 2022 and 2023)

***Source**: Bloomberg, 30 June 2021*

[1] Net return for the Nedgroup Investments SA Equity Fund, A2 class. Source: Morningstar (monthly data series).

We have recently seen several potentially structural economic reforming steps being taken:

- The announcement that private companies will be able to produce up to 100MW of power is a significant step towards mitigating the devastating effects of loadshedding and reducing the national reliance on Eskom.
- The 51% sale of SAA. Although riddled with questions around indirect government funding, it nonetheless is a step towards eliminating one of several fiscally draining SOE's from receiving unlimited state bailouts.
- The net tightening around corruption-accused persons, with some action being taken towards bringing these persons to book, such as the suspension of ANC Secretary General Ace Magashule, and Health Minister Zweli Mkhize placed on special leave, as well as further steps towards extraditing the notorious Gupta brothers from the UAE.
- The judicial system has proved its efficacy and independence by sentencing former president Zuma to fifteen months in prison for contempt of court – we wait to see how this plays out

However, when one moves beyond 2021, it is evident that expectations for GDP growth is barely above 2% for 2022 and beyond. This is due to structural impediments to growth which continue to haunt us.

Whilst these are certainly significant steps in the right direction, we need to see much more progress to overcome the structural issues we face in order to reduce unemployment and inequality by investing in fixed capital formation and attracting foreign investment, amongst many other means of achieving sustainable economic growth.

Portfolio Commentary

In local markets, the FTSE/JSE Capped SWIX Index was up 0.6% for the quarter and is up 13.3% for the year. It is worthwhile pointing out the stark difference in performance between domestic companies and foreign earners. Domestically focussed companies such banks, retailers and real estate companies are up strongly, while the likes of Naspers and Prosus are flat and down -12% respectively.

Largest contributors came from MTN, Growthpoint, MMI, Absa and Sanlam. BHP, NinetyOne, Anlgo American, SAPPI and Goldfields were the largest detractors from performance.

Top contributors (Q2)	Average weight	Performance contribution	Top detractors	Average weight	Performance contribution
MTN	4.5%	0.7%	BHP	5.0%	-0.1%
Growthpoint	3.0%	0.5%	NinetyOne	1.4%	-0.1%
MMI	3.2%	0.4%	Anglo American	6.7%	-0.2%
ABSA	3.9%	0.3%	SAPPI	2.1%	-0.3%
Sanlam	3.2%	0.2%	Goldfields	0.6%	-0.4%
Hammerson	2.1%	0.2%	Northam Platinum	2.4%	-0.5%

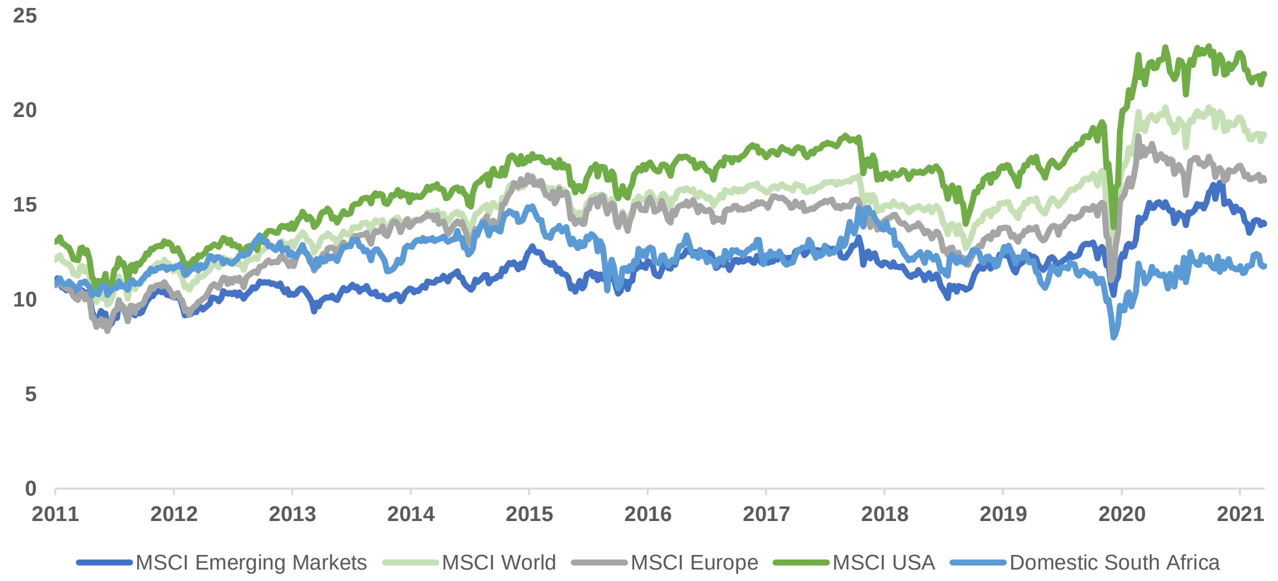
Current positioning and outlook

Although the SA market has recovered strongly off its lows and now appears to trade roughly in line with its historic average, the SA market remains attractive relative to other emerging markets, other asset classes and especially relative to developed markets such as the US. Laurium believe there are specific sectors and markets globally that are starting to look expensive, reducing the attractiveness of the respective risk reward trade-offs.

That being said, we are still finding pockets of the market that look very appealing and believe could still provide handsome returns to investors over time. Many South African focused companies continue to offer value when examining a simple index of the 1 year forward P/E of companies that are most exposed to South Africa (SA

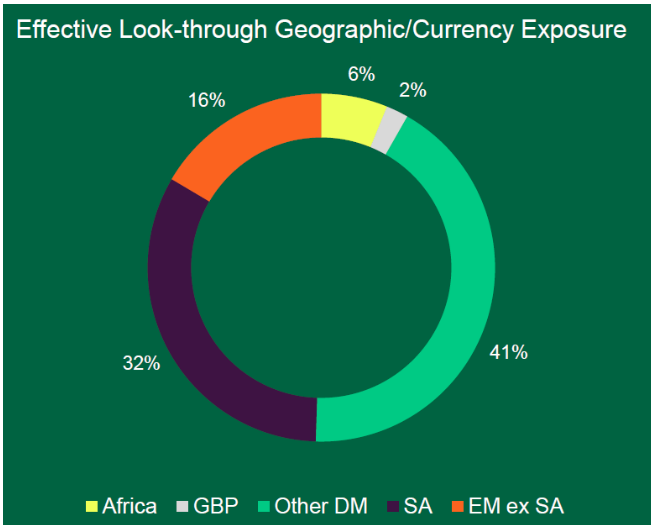
Inc.). In the chart below we compare this against the P/E of the MSCI Emerging Markets Index and the MSCI World Index.

Chart 2: SA domestic 1 year Forward PE vs MSCI EM and MSCI World



***Source**: Bloomberg, 30 June 2021*

Against this macro backdrop, we continue to have reasonable exposure of around 32% to South African focused companies' earnings (SA Inc). Within the South African listed market, we see attractive opportunities in the healthcare, insurance, industrial and telecommunication sectors, along with some of the large global consumer stocks including British American Tobacco and Naspers.



The fund has exposure to hospital stocks, such as Netcare and Mediclinic, which we feel are significantly undervalued. As the post Covid-19 world recovers, and elective surgeries and hospital occupancies recover, we think that these hospital stocks offer substantial upside.

The largest position in the fund remains Naspers. The recently announced offer by Prosus to acquire 45% of Naspers is a disappointing transaction in our view. Management have stated that the objective of the transaction is to reduce the wide discount of Naspers and Prosus to their respective underlying investments. The transaction adds considerable complexity to an already complex structure, and we feel this could further widen the discount. The offer appears to favour Prosus shareholders with the transaction swapping deeper discounted Naspers shares for lower discounted Prosus shares. We have collaborated with our peers and signed a joint letter along with 35 other asset managers voicing our disappointment at the proposed transaction. Notwithstanding the above we still think the stock is very attractive providing exposure to Tencent and other high growth emerging market internet assets at over a 50% discount.

We continue to hold a large position is British American Tobacco (BAT) which is very attractively valued on an 8x forward PE and 8% dividend yield in British sterling. On our assessment, ESG concerns are more than compensated for in the valuation. The company generates strong cash flows and as it degears, we feel that the company could be in a position to implement share buybacks within the next 12-18 months.

Top 10 Holdings	%
NASPERS LTD-N SHS	10.9%
ANGLO AMERICAN	6.3%
BRITISH AMERICAN TOBACCO	5.7%
MTN GROUP	4.8%
BHP GROUP	4.5%
IMPALA PLATINUM	4.0%
ABSA GROUP	3.9%
STANDARD BANK GROUP	3.9%
ANGLO AMERICAN PLATINUM	3.9%
FIRTSRAND	3.6%
TOP 10	**51.5%**

The fund still has reasonable exposure to resource counters including diversified miners such as Anglo American and BHP as well as platinum counters including Anglo Platinum, Impala Platinum and Northam. The strong economic recovery in China should continue to support bulk commodities, while a lack of new supply into the platinum group metals market in conjunction with supply problems at Norilsk Nickel in Russia should keep platinum group prices higher for longer.

Conclusion

We believe the fund is well diversified and offers attractive upside, while pragmatically weighing up the inherent risks, in order to take advantage of the cyclical tailwinds discussed in the report, cognisant of the longer term issues that need to be addressed to deliver longer term upside for investors.

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
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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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