Perspective
Investment Management

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June 2020

To our Investors,

Introducing our 2020 Annual Letter

We trust you are keeping safe and surrounded by the people you most care about.

Thank you for investing with us alongside our families and friends. Welcome also to our new investors, because our firm becomes exponentially stronger the larger our investor network grows.

Your feedback indicates that you value our consistently short, straightforward, and confidential communication. In the spirit of delivering 'perspective', we occasionally take a step back to reflect on where everything fits into the bigger picture. Therefore, in 2020 we put together this longer format annual letter - to present and link the most interesting and meaningful investment related matters.

A central theme in this year's letter is our resolve to continue applying a robust, evidenced, forensic mindset to investing. We think of this as an 'attitude'.

We trust you will enjoy reading our 2020 annual letter. If possible, please take a moment to send us your feedback and *any* questions you may have.

We always look forward to interacting with and learning more from you.

Our work continues...

Daniel

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Letter Segment Topics (*Click on any segment topic to navigate to it*)

Selected Market Data since Fund Inception

	Sep 3rd, 2017	Jun 26th, 2020	*Percentage Change*	*Notes*
Currency Prices				
SA Rand to US Dollar	12,8	17,2	*34,6%*	*Weakened*
SA Rand to UK Pound	16,6	21,3	*28,0%*	*Weakened*
SA Rand to Euro	15,3	19,3	*25,7%*	*Weakened*
Government Bond Yields				
SA 10-year (in Rands)	8,43%	9,03%	*7,1%*	*Weakened*
US 10-year (in Dollars)	2,10%	0,67%	*-68,1%*	*Strengthened*
UK 10-year (in Pounds)	1,01%	0,17%	*-83,3%*	*Strengthened*
Japanese 10-year (in Yen)	0,00%	0,01%	*n/a*	*No change*
Commodity Prices				
Gold (in US Dollars per ounce)	1 333	1 761	*32,1%*	*Increased*
Silver (in US Dollars per ounce)	17,8	17,8	*-0,3%*	*No change*
Platinum (in US Dollars per ounce)	1 006,0	799,5	*-20,5%*	*Declined*
Iron Ore (in US Dollars per ton)	78,0	103,1	*32,2%*	*Increased*
Copper (in US Dollars per pound)	3,09	2,66	*-13,9%*	*Declined*
Brent Oil (in US Dollars per barrel)	52,5	41,7	*-20,6%*	*Declined*
Property Indices - Market Cap Weighted Prices (*excluding* Dividends)				
SA JSE Property Index (in Rands)	653	269	*-58,8%*	*Declined*
MSCI World Property Index (in US Dollars)	208	194	*-6,5%*	*Declined*
Equity Indices - Market Cap Weighted Prices (*excluding* Dividends)				
SA JSE All Share Index (in SA Rands)	56 312	54 097	*-3,9%*	*Declined*
SA JSE Top 40 Index (in SA Rands)	49 796	49 898	*0,2%*	*No change*
Global MSCI World Index (in US Dollars)	1 954	2 193	*12,2%*	*Increased*
SA Investment Universe - Equal Weighted Prices (*excluding* Dividends)				
SA Equities: 250 Listed Companies			*-42,0%*	*Declined*
SA Property: 39 Listed Companies			*-47,0%*	*Declined*

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<u>South Africa ("SA")</u>

Right now, the future of SA is the biggest elephant in the room, so we place it front and center and dissect it carefully. These are not always easy or comfortable things to talk about and that is precisely why it is so important that we choose to do so.

This segment topic matters a great deal because many of you live here; our firm is based here; our fund is domiciled and regulated here; and many of the businesses we own are affected by what happens here.

Until late 2019 SA presented 3 distinctive future pathways. This changed in early 2020 to a binary T-junction. The coronavirus, economic lock down and ratings agency downgrade combined to force our collective hand as a nation.

There is no longer any realistic pathway to continue bumbling along the slow and winding road to nowhere. Our one future pathway leads to **rebuilding, long-term recovery and growth**, the other future pathway leads to **economic and social destruction and despair**.

We can approach this problem objectively and rationally. If we *knew* this problem could be solved for, what would such an approach look like?

Firstly, we need a sensible **framework** within which we can fit the evidence.

Secondly, we need the **evidence**.

Thirdly, we need to know at what point do we have enough evidence with which to reach an **informed decision** as to which future pathway we are on as a nation.

Lastly, we need **implementable plans of action** with which to manage the opportunities and risks present in each future pathway.

We put in place the approach outlined above when we started our firm and launched the fund in 2017.

The *bad* news is we are still missing a few key pieces of evidence and are not yet able to make a firm, informed decision as to which future pathway we are on.

The *good* news is SA has run out of rope and we expect to find the missing key pieces of evidence within the coming 6 to 12 months.

Further *good* news is the missing key pieces of evidence have contributed to the current heightened consensus perception of uncertainty and the abundance of generationally cheap, quality assets in SA.

Here is one example of how we go about sourcing and evaluating the evidence. From first principles, we built our own understanding and checklist of the legislative process in SA. We constructed the table below using publicly available information. It shows the process and progress on 4 key legislative areas of concern.

Bill Name	Bill Number	Step 1	Step 2	Step 3	Step 4	Step 5	Step 6	Step 7	Step 8	Step 9
		Proposed by ANC	National Assembly					National Council of Provinces		Presidential Signature
		Governing Party (ANC) **proposes** bill at ANC conference	Introduced to parliament via a **Green-Paper** (rough discussion document to facilitate debate)	Debated in parliament and if agreed becomes a **White-Paper** (more technical and detailed)	Passed as a **Bill** in Parliament	**Public participation process**		Amended Bill **(incarnations)**	Parliamentary vote **(Constitutional Amendments require special majority vote** and if majority vote becomes an **Act**)	**Published** in the National Gazette
National Health Insurance Bill	B11-2019	Done	Done	WIP	WIP					
Land Expropriation Bill (Constitutional Amendment)	B4-2015	Done								
South African Reserve Bank Amendment Bill	B26-2018	Done	Done							
Prescribed Assets										

Much has been said and wildly speculated about these 4 matters but, looking at it objectively, it is rather striking how little *formal* progress has in fact been made to date.

An additional fact, not as widely known as it perhaps should be, is that we found the highly controversial land expropriation bill was reversed from the final step to the first step. We were pleasantly surprised to learn this could even happen.

To date we have found 3 evidenced inputs on the matter of **prescribed assets**. Firstly, retirement fund reform takes many *years* to move from policy design to implementation. Secondly, the SA savings industry is world-class in every respect. We believe astute, well-funded industry participants will fight reform with everything they have at their disposal to protect their clients and commercial interests. Lastly, the retirement fund industry move from defined benefit to defined contribution shifted the burden and responsibility of delivering credible investment performance from the funder to the pension holder. The pension holder is the working population

– much of which is unionized and key ANC constituents – and they are always ready to fight to protect their own interests.

If the government were to somehow pacify the unions, force **retirement fund reform** and thereby make the Reg 28 investment mandate materially inefficient, we could ballot all the fund investors and change the mandate or migrate all of your non-retirement savings to another mandate.

If the government were to implement the **expropriation of land without compensation**, that would for all intents and purposes eventually result in the end of SA as we know it. Our firm was designed to have a relatively small amount of assets under management by industry standards – one of the key benefits is that, should we ever need to, we are able to significantly shift our investment positioning, quickly and without market impact.

In comparison to other developing markets around the world, we are also fortunate in that the SA markets contain many purely global assets. Staying within the regulations of our existing fund mandate, we can easily and legally construct a virtually fully offshore portfolio – if warranted.

We certainly do not wish to see these dramatic negative events unfold but we can manage the risk, because we know how to track their progression and we know exactly what to do and how to do it.

Continued key policy uncertainty is the largest challenge to SA's ability to recover. We can understand that this uncertainty was created because of internal ANC party concessions and deals made during the presidential race in 2017. That this uncertainty is taking so long to be resolved is the most frustrating aspect of President Ramaphosa's leadership to date. While frustrating, we can understand why it is taking so long to be resolved, because the Zuma administration had during its long and dominant 9-year reign destroyed the forensic and prosecuting capability of the state.

The reality is that it takes *years* to rebuild this forensic and prosecuting capability. Once the state's capability has been restored it then takes more time to build watertight cases against these criminals and to bring them to justice. It is tempting to become irritated and impatient, but we can respect an approach to do something as important as this properly.

There is clear evidence the state's machinery of justice has been restarted and the heat is being turned up. The recent legal declaration of the former South African Airways Chairperson, Dudu Myeni, as a delinquent director is a big deal. Our understanding is that she can now be held *personally* liable by all SAA stakeholders, as well as be prosecuted criminally.

What makes SA especially interesting in terms of its **long-term recovery potential** is that it is significantly natural-resource rich. SA also has lots of fundamentally good, smart, hard-working people who want to do good and create something durable for current and future generations. It is not widely known that the tiny, landlocked, and sparsely populated **Botswana** is the wealthiest country in Africa. Botswana developed a key natural resource following its independence in such a way that the rewards were more fairly and more widely shared with its population.

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SA Assets

SA Equities

SA's economy will shrink by as much as 10% in 2020, but 90% of a big number is still a big number. The economic pie is smaller for now but there is still lots of economic activity happening.

We wrote to you during this past year about the ability of *surviving* businesses to achieve meaningful growth within a zero growth or declining industry or country. They can achieve this by taking market share from weakened or failed competitors and by gaining pricing power.

A wise executive able to see and use the opportunity to acquire weakened competitors or their own undervalued shares can create additional significant growth in per share intrinsic business value.

We will always want to own businesses with owners and leaders that are excited about their opportunities and too busy making new plans and adapting to reality to bother complaining about everything that is wrong with the world and out of their control. Every successful businessperson we have ever met with talks of unexpected setbacks they experienced along the way and workarounds they found.

Several of the businesses in our fund have seen their competitive landscape evolve and *improve* significantly in the past 3 years. Think about **Wilson Bayly Holmes Ovcon ("WBHO")** in the construction industry, where key competitors **Group Five**, **Aveng**, **Basil Read** and **Stefanutti Stocks** have failed or just about failed, and in **Murray & Roberts'** case exited construction altogether.

Another example is **Foschini**, where key competitor **Edcon** has finally declared bankruptcy, collapsing under an unbearable debt burden imposed by its former private-equity owners.

This is also happening in **Spur**, where competitor **Taste Holdings** has gone under, **Famous Brands** is dealing with the distraction of financial losses in their offshore business, and many independently owned restaurants have closed already or will be closing before the end of this year.

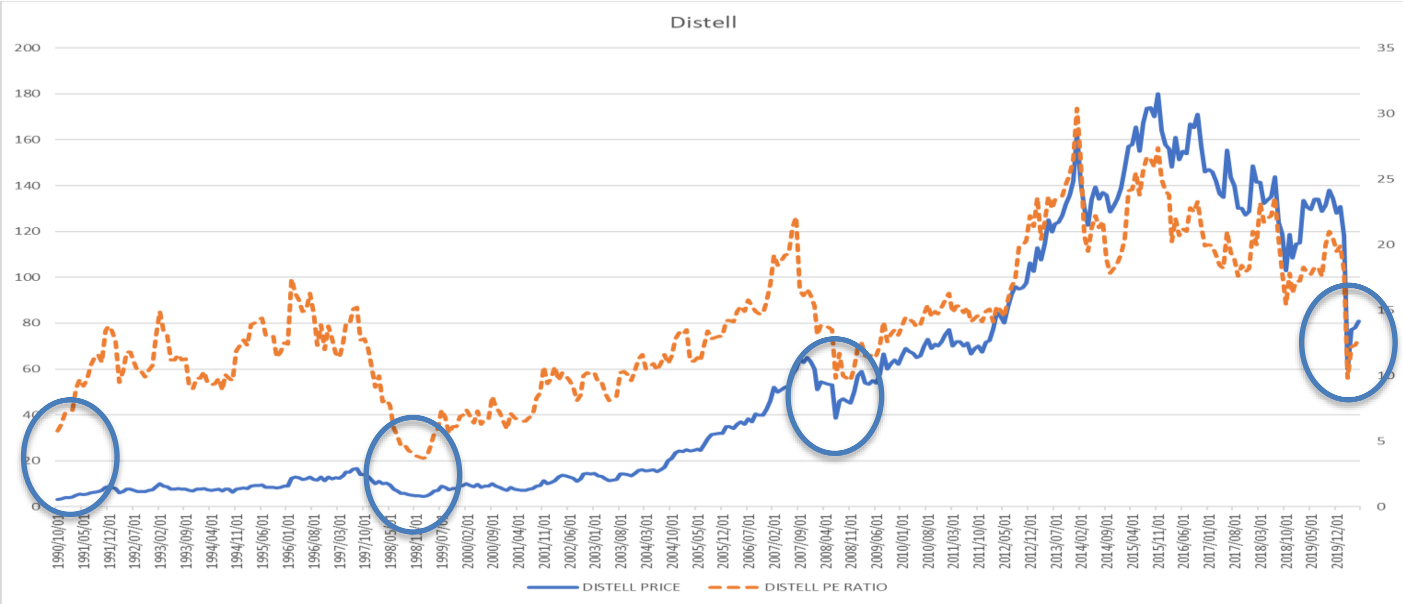
Provided they can survive this recession, **WBHO**, **Foschini** and **Spur** are now perfectly poised to take significant market share and partake from an improved position of strength in any future economic recovery in SA.

An exciting aspect of this economic and market cycle is that we currently have access to a diversified range of quality, liquid assets at generationally cheap prices.

There is quite simply no need to acquire illiquid, cheap looking, poor quality, small companies with questionable owners & leaders and weak balance sheets & free cash flows. Often those situations end up becoming value traps; meaning their values decline to their share prices or lower, instead of the other way around.

Quality assets at great prices are unfortunately not available on the supermarket shelves for us to put in the shopping cart on any given day of the week. In fact, **quality assets *rarely* become significantly mispriced, and it typically only happens when there is a *serious* risk event unfolding locally or globally.**

We would like to show you 2 specific examples in our fund. We waited 13 *years* for another opportunity to acquire **Distell** at truly attractive price levels. As you can see from the circled areas in the chart on the next page, since 1990 this is only the 4th such opportunity offered up.



Distell offers *everything* we want to see in one of our top long-term holdings:

1. A respected, responsible long-term control owner in **Remgro.**
2. A top-notch leadership.
3. A quality, robust business with scale, a strong balance sheet and free cash flows, premium products their customers want and value, and multiple long-term, global business growth opportunities.
4. A share price well below its business value.

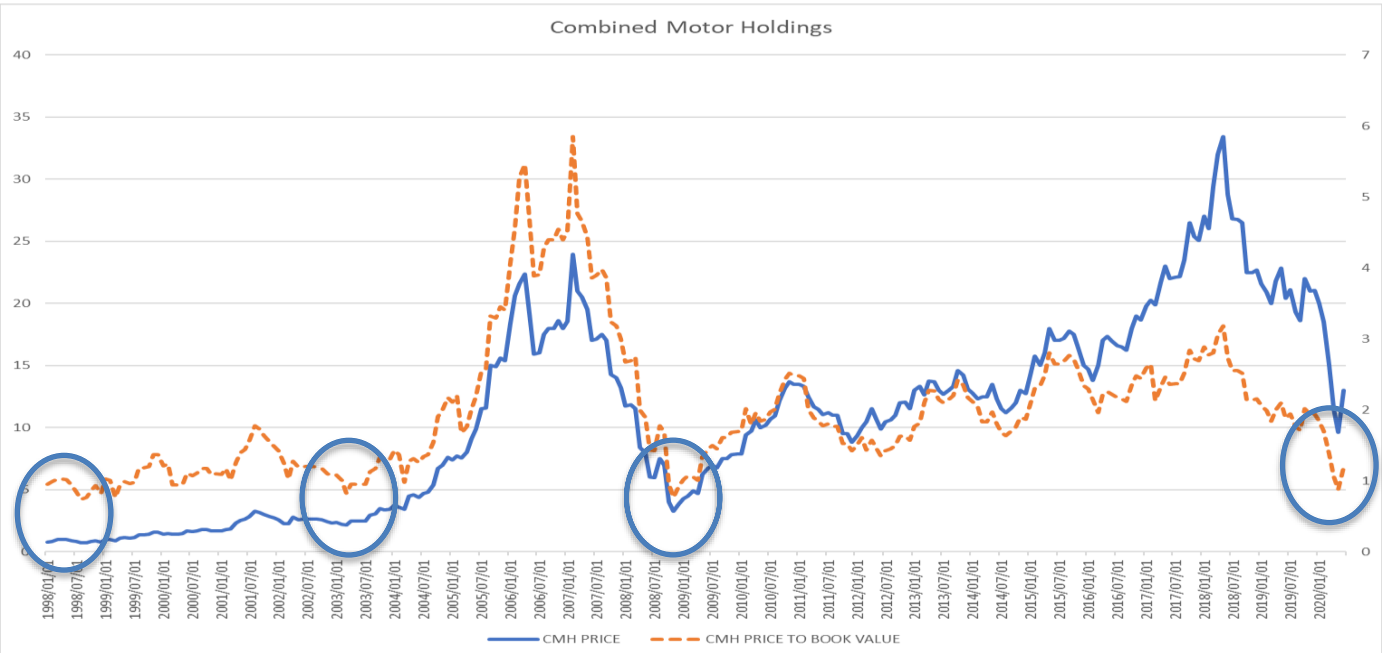
As far as we can ascertain from publicly available information, there is nothing fundamentally wrong with Distell as a business. A combination of being listed on the JSE, a small free float, considered an 'SA Inc.' company and experiencing a poor year of profits in 2020 - entirely due to the economic lock down - has all contributed to its share price more than halving in the space of a few months. It is highly unlikely that Remgro, who founded the business and knows it better than anyone, has lost any sleep about its internal valuation for its stake in Distell.

A comparison with the key long-term valuation multiples of Distell's global peers and the transaction multiples paid when similar businesses acquire each other in outright trade sales further strengthens the valuation component of our investment case.

One of our other new holdings is **Combined Motor Holdings** ("**CMH**"). It was founded by Messrs. Maldwyn Zimmerman and Jebb McIntosh in 1976 via the combination of several established automotive retail dealerships. It listed on the JSE in 1987. CMH grew annual revenues from R1,1bn in 1998 to R11,1bn in 2019, with annual operating profits growing from R38mn to R357mn. During this time the shares in issue had actually *decreased*, so the earnings per share grew from 18c to R3,05, while the dividend per share grew from 6c to R1,76. This growth was achieved mostly organically, without significant acquisitions or the use of excessive financial leverage.

Their profit margins and returns on capital are industry leading and remarkably stable. The key leadership has also been remarkably stable, with just two CEO's since 1976 - Mr. McIntosh eventually took over from Mr. Zimmerman. In both cases they have been significantly invested in the shares, with the Zimmerman family selling out in 2015 after Mr. Zimmerman retired as chairman at the age of 80. Mr. McIntosh still owns 34% of CMH.

CMH is a great example of a founder owner-managed listed business with a small investable market capitalization, but upon a closer look it is a substantial scale business, with over 2,700 people. Like our comments about Distell, a great business like CMH only gets cheap when there is a serious global or local risk event. In the past 30 years CMH offered up 5 deep value buying opportunities; in the early 1990's (SA political handover), in the late 1990's (emerging markets collapse), in the early 2000's (SA recession), in 2008/9 (global financial crisis) and now (SA recession).



We acquired CMH on a price to earnings ratio of 3. We expect to receive a starting dividend yield of 18% and a free cash flow yield of 27%. Both should grow over time. **The most amazing realization is that even if the CMH share price stays the same for the next 20 years, we will have earned a *substantial* investment return from our dividends alone.**

Distell and CMH are just two examples of many such investments held in our fund right now. As per usual, we can never know for sure in advance which individual business in our fund will deliver the best future returns to the portfolio. However, we do know that good things will happen in the future if we keep filling our funds with a diversified selection of such positively asymmetric investment ideas.

We find it insightful that global corporates have been acquiring SA businesses, for example **Pepsi** acquired **Pioneer Foods** from **Zeder/PSG** and minority shareholders. Pepsi paid a full valuation, which can be expected when informed buyers and sellers negotiate the controlling ownership stake of a business. This transaction begs at least one question; what long-term potential do Pepsi see from afar in SA and Africa that others here closer on the ground may be missing? We do not know the answer to this question yet, but it is something we have been busy thinking about and working on.

The equity building block in our fund is currently priced at an effective normalized price to earnings multiple of 6,8 and dividend yield of 8,3%.

This in and of itself is tremendous value for your money, but what makes us more excited is that these are also *quality* businesses, reflected by their average long-term returns on invested capital of 19,6%, and average long-term price to book multiples of 1,7 times.

This fundamental data is consistent with our written commitment made to you in 2017 – to wait patiently, as long as it takes, until the markets offered us enough opportunities to become more fully invested in a diversified selection of quality assets, bought at great prices.

SA Property

To better understand the current reality of the South African listed property sector, it helps to frame it against the past 25 years.

When I started in the investment industry in 1996 and through to 2003 there were literally just a handful of investable listed property companies. They were for the most part conservatively managed by low profile executives, with locally focused assets. They were also illiquid and tightly held by long-term, yield-oriented shareholders. There was only one listed property company on the JSE with fully offshore property assets – the old **Liberty International** that Mr. Donald Gordon had spun off from Liberty. Liberty International was later renamed **Intu**, which is currently in serious trouble but still listed on the JSE as of this writing.

From its lowest point in late 1998, when the property sector's combined market capitalization was a paltry R5bn, their exchange traded prices started increasing rapidly, far outpacing economic and stock market growth rates.

Following that strong showing the property sector eventually expanded into 50 listings. In late 2017 its combined market capitalization peaked at a substantial R600bn. At that point in time the prevailing wisdom, according to a publicly quoted leading property specialist, was "*the sector demands attention from investors, having been the best performing asset class over the past 14 years...*" and our personal favorite "*...the sector continues to be a hotbed of creativity and entrepreneurship, and the sector's capacity for creative deal-making is expected to continue to drive good earnings...*"

How prophetic these two phrases '*hotbed of creativity*' and '*creative deal-making*' were to become, in just 3 years.

A wall of investment demand by market participants chasing (past) performance was met with the invention and supply of investment instruments. This took the form of new property listings, property investment holding companies focused on owning other property companies, property focused unit trust funds, property focused unit trust fund of funds, property focused hedge funds and property focused passive products such as index funds and ETF's.

In short, it became a giant pyramid scheme – albeit a perfectly legal one. Bear in mind, given their business model, almost all property company balance sheets are also financially geared.

There was so much seemingly insatiable 'investor' demand that it attracted the attention of *foreign* property companies – who promptly inward listed themselves on the JSE. Given the history we can understand why **Intu** would be listed on the JSE, but why would a company in any industry with operations in a far-flung geography, with no obvious ties to SA, decide to list on the JSE when they could choose to list anywhere else in the world? The only plausible reason we could think of was this insatiable 'investor' demand had to be met with global supply once domestic supply had dried up or fallen short.

From its peak in late 2017, the property sector and all the levels of this pyramid have been decimated. For a sector that is *supposed* or *assumed* to offer investors reliable annual income and capital stability, this is painful. As paper losses escalated, 'investor' fatigue set in. In early 2020 it culminated in a dramatic sell-off – with 'investors' desperate to exit - at *any* price.

The identification of this pyramid scheme helped us to appreciate the persistent selling pressure on and eventual capitulation of the share prices of the listed property companies. The entire sector was being aggressively sold out of to meet redemptions in the various levels of the pyramid, with no apparent discernment between the few top quality and the many weaker quality companies. This phenomenon is referred to in the investment industry as 'the babies being chucked out with the bathwater'.

From fund inception in September 2017 through early 2020, we had a negligible exposure to SA listed property of 2% of our fund, to what we still consider the clear standout quality business in the sector, being **Growthpoint**.

We have been waiting patiently for identifiable investor fatigue and capitulation, and, in the course of 2020, we were able to acquire a much more meaningful exposure of 7% of our fund. Our property exposure consists of – in our view - only the 2 best businesses in the sector. There is no need to buy any others, as the ones we own are diversified, scale businesses in their own rights. We do not see any sense in diversifying beyond these two and thereby accepting the unwarranted, significant risks of investing in untrustworthy or poorer quality property companies – of which there are many.

At the prices we paid, we calculate our property sector investments should deliver a pre-tax annual income yield of between 15% and 20%. It is fair to expect this yield can grow somewhat in real terms over time. In and of itself this income yield is already an attractive investment return, so if we eventually also get a bit of a rerating in their share prices that would be a bonus.

In addition, both our property businesses own significant offshore assets and indirectly provides the fund with additional global exposure and diversification.

Property falls *outside* of our funds' 75% maximum allowance in equity. In this non-equity component of our fund, we directly compare the achievable yield from our property holdings to the current SA government 10-year bond pre-tax yield of 9% and the pre-tax money market yield of 7%. As you can see, the incremental income yield currently offered by our property investments is clearly substantial.

The impact of the coronavirus, and more specifically the related economic lock down, will undoubtedly affect all property businesses in the short-term. We certainly do not expect our 2 property businesses to have escaped this reality, but we are confident they have quality, diversified property assets, are likely to recover reasonably quickly and resume paying regular dividends.

SA Corporate Bonds

A particularly interesting form of fundamental mispricing can be evidenced in the SA corporate bond market.

Sasol has 4 listed corporate bonds in issue, of which only one is listed in SA. All 4 of these bonds are classified as 'senior unsecured', basically meaning they rank equally in Sasol's capital structure and therefore should in theory and practice be on an equal risk footing to each other.

Between January and March 2020, the yield on Sasol's SA listed bond did not change at all (meaning that specific bonds' price stayed exactly the same), while the yields on all three of its offshore listed bonds skyrocketed – in one of them the yield went from 3% to an incredible 42% (meaning that bonds' price declined massively).

There can only be one explanation for this. SA has virtually no secondary traded market in corporate bonds to speak of, and the holders of the SA listed corporate bonds are not incentivized or forced to mark their investment exposures to economic reality. This game potentially only stops when the holders of these bonds become forced sellers thereof.

The JSE, which is responsible for regulating the SA bond markets, appears wholly unawares of this, despite their core mandate being fair price discovery for market participants on their exchange platforms. As a result of this fundamental mispricing, the pricing of all investment funds that own Sasol's mispriced SA listed corporate bond was potentially overstated during this period. Furthermore, investors that transact in those funds would be trading at a potentially overstated fund price, which benefits fund sellers at the expense of fund buyers. This would be an extremely costly and administrative nightmare to unravel.

Should this regulatory reality outlined above prevail, you can be sure we will continue to avoid and choose not to own illiquid and unreliably priced SA listed corporate bonds in our fund.

A possible remedy could be for the bond market or unit trust industry regulations to be amended to properly mark these SA listed corporate bonds to market - in the event they do not trade but their directly comparable global bonds do trade.

SA Government Bonds

The already perilous state of state finances combined with the impacts of the economic lockdown is of concern to us. We currently ascribe an above-zero probability to SA defaulting on its foreign currency government bonds. For this reason, we do not judge the yield on the 10-year government bond of between 9% and 10% as sufficient to compensate us for the increased risk.

A default on SA's foreign currency government bonds is of course a serious matter that would dominate the headlines, but it is not something to get overly panicked about and extrapolate to everything else. For example, it also happened in 1987, and that turned out to be an opportune time to have invested in the SA equity market.

We are not marginal or fair-value investors in bonds. Our preference is to focus on investing in bonds when they are offering well above normal returns, in other words when their prices present positively asymmetric returns. That is not currently the case, and therefore we will wait patiently until it is.

SA Currency

A currency basically reflects the traded 'price' of a country or region. As with all exchange-traded prices, sentiment and cash flows play a dominant role over the short-term, while in the long-term it is the underlying valuation fundamentals that will matter most.

Measured against its long-term fundamentals, our work shows the Rand is currently *undervalued* by about 30% against the currencies of its key economic trading partners.

The Rand sold off to as much as 50% below its fair value in the first half of 2020 on a combination of extremely negative sentiment and significant capital outflows. An already weak country balance sheet together with the impacts of a total economic lock down has resulted in a significant - and frankly entirely justified - erosion of global and local investor confidence in SA.

In our letter segment on South Africa we set out our views on SA having reached a T-junction with only the high road and low road scenarios. With regards to the currency, the equation is that under the high road scenario the Rand is undervalued, and under the low road scenario it is overvalued.

It is worth pointing out that our fund already has a *significant* direct and indirect offshore exposure. Many of our businesses either generate significant revenues and profits outside SA, or they provide goods and services benchmarked to offshore currencies.

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Global Assets

In stark contrast to what we identify as a generational investment opportunity set available in South African listed assets, global assets remain, for the most part, between fair value and expensive to very overvalued.

As you may recall, it has not been plain sailing in global markets these past 3 years, with two significant 30% market declines – in late 2018 and in early 2020. **Our team found investment opportunities in a few disliked and uncrowded global industries**. We know to be extremely careful to go apparent bargain hunting when markets are generally expensive – those parts of the markets that might *appear* cheap are often cheap for perfectly valid reasons.

There are companies with superb long-term track records, such as **Intel** and **Walgreens,** grappling with significant and disruptive change in their competitive landscape from powerful new technologies, powerful new entrants in their core markets, and a change in customer behaviors.
We have avoided many value traps, more specifically in industries such as energy services, banking, airlines, cruise lines, gambling, hotels, infrastructure, and private equity.

Possibly the key contributor to our avoiding these industries involved our assessments of their **robustness**. In each of these industries we found listed companies operating with high levels of net debt and a limited set of available options with which to handle adversity.

To be perfectly clear – we did not or could not know in advance that a global event as serious as the coronavirus would occur. What we do know is that we wish to continue avoiding investing in any companies that are ill equipped to handle *any* form of adversity. This also means we do not have to waste precious time and energy trying to predict the future. We draw our degrees of confidence from our businesses' proven ability to handle adversity and then we can trust them to adapt to whatever new reality they may face.

It is extremely concerning that global policymakers have, yet again, decided to provide *limitless* financial stimulus to essentially bail out speculators. **They do not actually have any of this money - they are borrowing it from future generations by issuing more debt and by printing more money.**

This process more or less started in moderation in 1998 (emerging markets crisis), but it was stepped up incrementally in the market collapses of 2000 (tech bubble bursting), 2009 (global financial crisis), 2012 (Southwest European crisis), 2019 (trade wars) and now again in 2020 (coronavirus). As with all highly addictive stimulants, each successive event required substantial additional dosages.

Each successive bailout resulted in the affirmation that market participants can always stay 'risk-on' with no regard for valuation levels. We routinely see sell-side research reports with exit valuation multiples 2 to 3 times what we would consider realistic, evidenced levels.

The result is sky-high valuation multiples in most industries and companies – especially so in the largest tech companies driving disruptive technologies into new industries. It has also resulted in a significant narrowing of market leadership in a handful of stocks, further fueled by the persistent rotation of capital from active fund managers to passive index funds and ETF's.

To make matters worse, many listed companies have been cumulatively spending *trillions* of Dollars under the convenient guise of 'returning shareholder capital' -a misnomer if ever we saw one - by buying back their own overvalued shares. In many cases they ended up with more excessively geared balance sheets.

When the coronavirus hit in early 2020, not only did their share prices collapse, but they were suddenly in serious trouble needing to lay off staff and raise fresh equity capital from their shareholders at distressed share prices; this further destroys per share long-term business value.

Executives pursuing such actions will never pass our **trustworthiness** test.

In the United States of America, where corporates are seemingly free to do exactly as they please, companies have abused the stimulus packages by issuing corporate bonds while laying off over 40 million people in just 9 weeks, pushing US unemployment levels to record levels last seen in the Great Depression of the 1930's.

Possibly one of the most disturbing revelations is the relationship between Donald Trump and the billionaire hedge fund activist investor Carl Icahn, who is alleged to be a rather significant beneficiary of the US President's policy decisions. The numbers and implications are staggering, and frankly it makes our SA case studies seem a bit like amateur hour.

Donald Trump's policy decisions to date (aggressive tax cuts and stimulus) have been extremely effective in pushing not only the US but most of the rest of the world stock markets to record high levels. But, given the spike in unemployment and race riots across America, he appears to be rapidly losing voter support. If Trump and the Republicans loses to Joe Biden and the Democrats in this year's elections in November, the stock markets are not likely to take to it kindly.

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Investment Strategy & Fund Positioning

We have not changed the investment strategy we developed in 2017.

The evidence led us to conclude the investment markets were overheated and other risks elevated. We developed an appropriate investment strategy with which to in the first instance protect fund capital from significant permanent capital loss, while simultaneously investing in sensible long-term investment opportunities as and when the markets present them.

This is far easier said than done, especially when our reality is the *average* South African listed company, including the property sector, had declined by 60% between when we launched the fund and the end of March 2020. **Our stated objective and commitment to you remains 'to get us all safely to a future point in time when the fund would justifiably be more fully invested'.**

The table below compares the current composition of our Balanced Fund with what it consisted of at inception in September 2017.

Balanced Fund Composition Comparison

	September 2017	Number of Positions		June 2020	Number of Positions
Fund Equity					
SA Listed Equity	31%	17		45,7%	26
Offshore Listed Equity	0%			15,0%	9
Total Non-Gold Equity	***31%***			***60,7%***	***35***
Gold Equity	0%			6,3%	2
Total Equity	***31%***	***17***		***67,0%***	***37***
Rest of the Fund (Non-Equity)					
SA Cash	**67%**			**15%**	
Offshore Cash	0%			**4%**	**2**
Property	**2%**	**1**		**8%**	**2**
Commodity - Gold Bullion	0%			**6%**	**1**
SA Government Bonds	0%			0%	
SA Corporate Bonds	0%			0%	
Unlisted Assets	0%			0%	
Other African Assets	0%			0%	
Fund Equity Concentration					
Top 10 Equities by Fund Weight	**21%**			**29%**	
Top 10 Average Position Size	**2,1%**			**2,9%**	
Next 10 Equities	**10%**			**20%**	
Next 10 Average Position Size	**1,2%**			**2,0%**	
Sector Exposures					
Industrials	**12,3%**	7		**39,2%**	**24**
Financials	**16,2%**	9		**10,9%**	6
Resources	**3,0%**	2		**22,7%**	8
Top 5 Industry Exposures					
Active Investment Management				6,7%	3
Integrated Energy Producers				6,6%	3
Gold Mining				6,3%	2
Food Retailers				4,0%	2
Chemical Producers				4,0%	2

** Please note all percentages were calculated as a % of the total fund .*

At inception we had 31% of the fund invested in the equity of 17 businesses, 2% of the fund in 1 property business, and the rest in cash. In addition, the fund's concentration levels was on the low side and we had found little to acquire in the resource sector.

As of June 2020, we have 67% of the fund invested in the equity of 37 businesses, with a further 8% of the fund in 2 property businesses. Fund concentration levels have increased meaningfully.

Our exposure to the financial sector has declined. This is consistent with the embedded late-cycle risks in the banking and insurance industries, being directly impacted by weakened government, corporate and individual balance sheets, and general stock market levels.

The table below compares 3 key valuation metrics across the top 30 holdings of the Dow Jones Index as a proxy for the global equity markets, the JSE All Share Index as a proxy for the SA equity markets, and our businesses.

Comparing Key Valuation Metrics

	Dow Jones Index - Top 30 Holdings, Ranked by Weight	JSE Allshare Index - Top 30 Holdings, Ranked by Weight	Perspective - Top 30 Holdings, Ranked by Weight
Price to Earnings Ratio			
1. Average of all 30	18,1	12,9	8,3
2. Average of Holdings 1-10	25,6	12,9	9,6
3. Average of Holdings 11-20	16,3	11,9	7,3
Dividend Yield			
1. Average of all 30	3,0%	4,1%	6,0%
2. Average of Holdings 1-10	1,9%	6,0%	5,5%
3. Average of Holdings 11-20	3,5%	3,5%	7,2%
Valuation Multiple vs. Long-Term Average			
1. Average of all 30	1,20	0,92	0,65
2. Average of Holdings 1-10	1,56	0,86	0,70
3. Average of Holdings 11-20	1,18	1,13	0,65

We offer the following observations:

1. A PE Ratio of 18,1, dividend yield of 3% and valuation multiples 20% above normal levels indicate global equity **indices** are *overvalued*. Additionally, there are concentration risks.
2. A PE Ratio of 12,9, dividend yield of 4,1% and valuation multiples 8% below normal levels indicates the SA equity **index** is marginally *undervalued*.

3. **A PE ratio of 8,3, dividend yield of 6% and valuation multiples 35% below normal levels indicate the equities held in our fund are deeply *undervalued* - in both absolute and relative terms.**

It is worth pointing out again, as we did in the segment on SA Assets, that **not only are our selected fund equities deeply undervalued, but they are without exception all superb businesses.** We are not interested in building a portfolio for you filled with cheap looking but poor-quality assets.

In recognition of the global and SA market index valuation levels and elevated levels of geopolitical risks, in the course of 2018 we had researched and implemented what we term a **'natural hedge'** for the fund.

This resulted in investing in a combination of gold equities (currently 6,3% of the fund) and gold bullion (currently 6% of the fund). These assets have a proven history of delivering *negatively* correlated investment outcomes to the most significant global risk events. The timing is not always perfectly aligned, but within a patient, disciplined investment firm and process it adds tremendous value.

The way we think about the overall portfolio's risk exposure is that our fund is now effectively 60% invested in equity, with another 6% in gold equities held as a negatively correlated hedge, or downside protection, against known and unknown global risk events.

As and when the markets offer up more opportunities for us to further increase equity exposure to the mandated fund maximum of 75%, we will be reducing our exposure to gold equities. We will eventually end up selling it to zero.

If we get lucky on our timing, we may end up selling them right after their prices had increased substantially and right after the share prices of the businesses we are buying had decreased substantially. But please do not hold out hopes on us pulling that off with too high a degree of accuracy! Short-term market timing is not one of our defined or claimed competitive investment advantages.

We practice a straightforward, sequential, 4-part investment research process that, as long-term investors investing with a businesslike mindset, we think of as being common sense. Our 4 core investment criteria are:

1. **Understandability.**
2. **Trustworthiness.**

3. **Robustness.**
4. **Valuation.**

We start with needing to **understand** how and why a business makes its sales, profits, and free cash flows, and why we might be so fortunate that its share price truly dislocated from its underlying intrinsic business value.

Our 2nd step is to evaluate the **trustworthiness** of the people who own and manage the business, before we can move on to assessing the **robustness** of the business to withstanding expected and unexpected adversity.

Our 4th and final step is to build a **valuation** using evidenced, conservative, and realistic assumptions of what we identify as the few key drivers of long-term shareholder value, with a proven relevance to that specific industry and business.

The sequencing of our 4-part research process is extremely important.

When an investment team gives primacy in their work to valuation above all else, it can lead to all kinds of investment mistakes. In fact, one of the key contributors to our ability to have protected our fund from significant declines is that we avoided many listed companies that failed one or more of our first 3 core investment criteria.

We do not care how cheap something may appear, or how much of it is held in the indices or in our peers' funds - if we cannot understand it, trust the people involved or if it cannot withstand adversity, we will *not* invest in it.

If an evidenced new fundamental development at one of our existing fund holdings results in it failing one or more of these 4 core criteria, we will reduce and / or sell out of it immediately, regardless of the prices we paid.

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Portfolio Management Actions

Please note this segment covers our portfolio management actions over a 12-month period from July 2019 to June 2020.

Additions to *existing* fund holdings

When we continue having a high level of confidence in a holding and nothing changes other than its share price being lower, it results in an increased expected future investment return. We would then react by not only buying back to our initial exposure, but typically would also consider raising our exposure.

We added to **Spar**, **Growthpoint**, **Omnia**, **Remgro**, **MTN**, **Foschini** and **Ninety 1.**

We received a direct interest in **Ninety 1**, formerly known as Investec Asset Management, when it unbundled from **Investec**. Our intention with this investment thesis from the outset was eventually to only own the investment management business.

Ninety 1 is a purely active, scale, multi-asset class and multi-geography investment management business, with a globally recognized brand, respected ambitious leadership and significant inside ownership. We are pleased to be able to own it directly and that it will no longer be distracted by the influence and subsidization of the bank's volatile lending activities.

New fund holdings acquired

Unusually high levels of price volatility in the markets coupled with the current state of the SA economy enabled us to acquire stakes in an unusually large number of new holdings.

You may notice that a few of these are now our largest holdings in the portfolio - this is testament to their quality and levels of cheapness. In almost every case these are businesses and industries we have been working on for *years*. In addition, for several them this is our 2nd or even 3rd ownership cycle.

We acquired **Distell, Italtile, Emira, Cashbuild, Pick 'n Pay, Sasfin, Exxon Mobil, Total, American Eagle Outfitters, Denso, Magna, Adcock Ingram, Hudaco, Spur, CMH** and **Franklin Resources.**

These new fund holdings meet each of our 4 core investment criteria. **They also meet our additional requirement for them to be the best, or at least one of the best, businesses in their respective industries.**

It is worthwhile noting these new fund holdings represent quite a wide range of industries - beverages, building materials retailers, property, food retail, specialist banking, integrated energy, clothing retail, automotive components, pharmaceuticals, industrial parts, restaurant franchise management, automotive dealerships and active investment management.

We do not deliberately set out to focus on building diversity by industries or countries of domicile - it is purely an outcome of our research process and where markets offer us the best investment ideas.

Existing fund holdings *reduced*

We reduce existing fund holdings when new research findings or fundamental business developments erode our confidence levels, or the share price had increased substantially and thereby significantly lowered our expected future investment returns.

We reduced exposures to **Sasol**, **Murray & Roberts**, **Bell Equipment**, **Sasfin**, **Philip Morris**, **Wilson Bayly Holmes Ovcon**, **AngloGold,** and **Barrick Gold.**

Following further research since the initial purchase, our confidence levels on the first 4 businesses in this list had eroded somewhat, while strong share price gains in the last 4 businesses on the list gave us an opportunity to bank profits.

Holdings *exited* completely

We sell out completely if (1) our investment thesis has run its full course and there is no more realistic upside left, (2) our ongoing research uncovers a mistake in our analysis, (3) new fundamental developments result in a significant erosion to our confidence levels, or (4) we can replace an existing fund holding with a clearly superior one.

We sold out of **African Rainbow Capital**, **Discovery**, **Richemont**, **Transocean**, **HCI**, **Tsogo Sun Gaming**, **Sappi**, **Absa**, **Liberty Holdings**, **Molson Coors**, **SA Government Bonds**, **Investec Bank**, **Arcelor Mittal** and **Metair.**

New fundamental evidence came to light or negative developments occurred that resulted in us exiting **Discovery**, **HCI**, **Tsogo Sun Gaming**, **Sappi**, **Molson Coors**, **SA Government Bonds** and **Arcelor Mittal**. In most of these cases their balance sheets had continued deteriorating to the point where we became sufficiently concerned with their ability to handle or survive further serious economic adversity. **More specifically, in early 2020 we took decisive action to exit any holdings in the fund that we assessed to be particularly vulnerable to the impacts of the coronavirus.**

In the case of **Metair**, we exited upon learning of the surprise early retirement of its CEO, Mr. Theo Loock, a key individual whom we rate particularly highly and considered central to our investment thesis.

In the case of **African Rainbow Capital**, we reduced our valuation when new fundamental information came to light on its underlying investment portfolio. The share price had increased to reach our revised valuation, there was no apparent upside remaining and we banked our profits.

We exited **Absa** and **Libhold** because we were able to replace them with clearly superior investment opportunities.

We sold out of **Investec Bank** following the unbundling of Ninety 1 to complete one leg of our investment thesis, as we had planned at the outset.

We reversed our investment in **Richemont** shortly after purchase at a marginal gain because we uncovered a valuation error in our own analysis.

Richemont represents a case study of the value of truly independent teamwork and research collaboration. An important aspect of our research process, that cannot be understated, is for our analysts to take turns in assessing our existing holdings from first principles – without being biased by the team or each other's prior findings. Often this approach serves to strengthen our convictions, but occasionally – as in this instance – it served to uncover a basic research error. We acted immediately, and in hindsight it was the correct action to have taken.

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Perspective Business Update

2020 was always destined to be an important and critical 3rd year in Perspective's formal creation and continued development. On behalf of all of us, I am so deeply grateful to every key stakeholder of our firm that has played such an important role in support of our purpose. Thank you.

To create our firm took a great deal of care, capital, time, and energy, with no shortcuts, handouts or guarantees, and our fair share of dealing with whatever luck and adversity came our way.

Given this reality, and knowing the caliber of our investors and stakeholders, I can confidently state how proud I am to be in a position to share this business update with you, let alone the important milestones we have already achieved.

"Perspective exists to safeguard and grow our investor's money, and investment knowledge, over multiple generations"

The above phrase captures the essence of our professional existence. It is a short phrase, but to us it conveys a richer, deeper meaning.

We look to gain incremental investment and business knowledge every day from our ongoing interactions with a proprietary network of listed and unlisted businesses, our investor, business and other stakeholder networks, and life experiences.

We are open to sharing this knowledge in a humble and respectful manner with our investors and their families, in confidence. While we see this sharing as a natural extension of our firm's long-term, multi-generational value proposition, we also know the more we give the more we stand to gain in return.

This knowledge network we speak of grows exponentially stronger with every new investor and stakeholder relationship we add.

Reflecting on the past 5 years it always strikes me just how much has happened in our country and in our firm.

Creating and developing our own firm has also served to further deepen our understanding of and respect for what it really takes to build and deliver anything of real and durable value. It has further shaped and

sharpened the key questions we ask – of ourselves, of the leaders of the businesses we choose to own and of the leaders of our country.

This is my 25th year of investing professionally on behalf of investors. I can confidently state that the portfolios we have built for you are robust and positioned to take full advantage of the best long-term investment opportunities we could identify. We are excited about owning every single holding in our funds, as well as the funds themselves.

We have created our own unique ways to do things at Perspective, and we have gathered a group of fully committed, like-minded people and stakeholders, who share passionately in our purpose.

Our Investors

We started out with family and friends and it has grown organically to include a range of independent and professional investors with deep and diverse business, investment and life experience and knowledge.

We engage directly with most of our investors regularly. Our sense is that you care about the same core long-term values that we also ascribe to.

Our Investment Offering

Other than our **Balanced Fund**, which is a publicly visible, regulated Unit Trust, we also manage local and global **'Bespoke Portfolios'** for investors.

Our bespoke portfolios draw from our investment team's exact same research process and long-term investment approach. The key difference is (a) in the administration of these portfolios, and (b) in the way they are managed to a unique and customizable investor mandate.

We developed an **Executive Equity Fund** that we are working on launching in the course of 2020, in collaboration with our business stakeholders.

Our Communication Offering

Our approach to communication is that we want to *confidentially* share investment knowledge with our investors.

To this end we developed a range of communication tools across multiple platforms, including our 1-pager investment perspectives, portfolio manager snaps, physical meetings, zoom-calls or phone-calls, an annual letter, presentation slides with accompanying keynotes, and video logs.

Other than this 1 long form annual letter, everything else we send you will be in short form.

Our Other Initiatives

Together with one other independent investment manager, in 2017 we established a so-called '**Fellowship of Investment Managers of SA**', with a mandate to 'promote investment excellence in the industry'.

The Fellows – who are thankfully not all men by the way - meet formally 4 times a year, are drawn from 9 different investment firms, and each Fellow must have at least 20 *years* of relevant investment experience. It has proven to be an extremely valuable forum. The Fellowship has already delivered positive impact in several respects, including JSE rule changes, and it is going from strength to strength.

Perspective's approach to and work on **governance** is *deliberately* not easily visible viewed from the outside. Governance is a multi-faceted and fascinating field, covering the environment, social issues and the nitty gritty of executive and shareholder fiduciary duty and responsibility. As with everything we do, our approach to governance was developed from first principles, and it is unique to Perspective.

Governance has unfortunately become a bit of an industry buzzword of late, but to us it has always been and will remain central to who we really are and how we do things here. If you are interested, let us know and we will gladly tell you more about it and share some of our ongoing work in this regard.

Supporting you at Perspective

Our team is based in Cape Town and currently consists of 6 people. Any of us can help you with anything, but if you have specific questions about the portfolio or investing in general, please contact, meet with or e-mail **Mikael**, **Gavin,** or **myself**.

For your specific operational questions – for example debit orders, application forms or valuation statements – please contact, meet with or e-mail **Beryl**, **Dylan** or **Khangelani**.

Each of our direct e-mail addresses are 'first name'@perspectiveim.co.za.

If you are ever in Cape Town, please visit with us at our offices in De Waterkant. We love hosting our investors and opportunities to learn more from and about you.

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‘Elephant in the Room’ Q&A

In this segment we answer a few ‘elephant in the room’ style questions considered more relevant and urgent than others.

Q1: Will political risks in SA affect my enjoyment of the potential upside that is on offer?

A1: No return is without risk, but such an outcome is *never* a zero probability - in any country. As we set out in the letter segment on South Africa, we do feel this is a risk that we are able to monitor and manage.

Q2: According to recent trending media reports, the ANC is ‘dominated by a communist agenda’ and the implication is that we are thereby doomed to fail as a country. What are our thoughts on this?

A2: A wise, politically connected contact in our network recently told us “*The problem with the ANC is it is a coalition and therefore an averaging of ideas that do not average*” Within this coalition there is a very wide range of views, some of which are extremely controversial. Whenever these views are brought out into the open and viewed in isolation, they will of course scare many people.

We know from the evidence that communism is a terrible ideology that has failed miserably everywhere in the world. It is also clear to us that there are influential ANC leaders in key positions that are aware of this.

We are monitoring developments carefully, but we do not subscribe to the view that SA is doomed to fail.

Q3: How do you do research and manage portfolios with 3 investment team members?

A3: There is *no* clear evidence of a *positive* relationship between the absolute or relative size of an investment team, the quality of their investment thinking and their investment performance over time. Several of the global investment industry’s best long-term track records were delivered by surprisingly small investment teams, and in some cases by individuals.

As truly long-term investors, we transact infrequently in our funds in comparison to the industry norm. We only manage one unit trust portfolio. We rarely engage with the media or the sell side, and our like-minded investors respect our time and actively support us in focusing on doing our work. Our investment team members spend no time writing research reports and we consciously limit our time spent in formal investment and business meetings. All of this frees our investment team members to focus as much as possible of their time and energy on doing research.

As business-minded investors, we found that only a few key things truly matter in any industry and in any business. If we pause for just long enough to first figure out what these are and then choose to focus on them, we save what would otherwise be a huge amount of wasted time and effort.

We pursue a collaborative research approach, whereby we regularly and confidentially interact with our proprietary global network of investors, stakeholders, executives, and carefully selected investment peers. In addition, our founders and key stakeholders have many decades of investing and business experience. **We do not always have to know all the answers, we just need to know where to go to get them.**

Q4: Will SA's downgrade to junk status or a potential default on our foreign bonds affect my investment returns?

A4: Few people know or can recall that SA was junk-rated between 1987 and 2000, following the infamous Rubicon speech by PW Botha, or that it defaulted on its foreign bonds in 1987. Despite this, the markets still delivered solid investment returns – for two key reasons; assets were priced very cheaply, and the perceived uncertainty and low growth economy resulted in less competition.

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The Future of Investment Management

The future of investment management will and indeed must include a valued, confidential, and direct relationship between a money manager and the people who decide to place investment savings in our care.

This relationship we speak of and seek out is already our present reality at Perspective, as it is a cornerstone of our business philosophy. We believe that mutual trust and respect is an attainable result of clear communication, personal accessibility, unconflicted professional behavior and direct accountability.

Much of the world is overwhelmed with data, fake news, self-help books and videos, armchair experts, instant answers to everything and an obsession with speed. In contrast, we have found there to be merit and a form of durable competitive advantage to deliberately slowing down. Doing things properly requires a focused commitment to making enough time to put in the required effort on a few things that matter the most.

We go to source, we figure things out from first principles, we work and spend time to think alone or with people we admire and respect, and we do so in environments conducive to doing our best work and thinking. **We deeply respect that there are many things we were not destined to understand and questions we may never find answers to, no matter how hard we try. We form our opinions and conclusions only when they are good and ready to reveal themselves to us.**

We back our work, but at the same time we continually search out and consider new evidence and we remain open to changing our minds and our funds if warranted.

We sense a long overdue but rising global groundswell for a return to basic investing, societal and environmental values – values which have been debased by powerful entities and their propaganda machines. In our design and daily practice Perspective represents a return to these basic values. We know and do our best to express clearly what we stand for and why. We would like to believe each of our stakeholders chose to find an alignment therein.

We seek to have a respectful, durable, and positive impact on all our stakeholders and the wider world around us. We are not waiting for others to act first before doing the right thing. We are not just busy buying and selling assets – far more importantly, we are custodians of your savings and we feel a deep-seated responsibility to pursue excellence in everything we choose to do.

We agree the case for long-term passive investing in widely diversified market indices is strong and supported by sound logic, evidenced performance, and investor capital flows. We also remain convinced there will continue being a solid case for truly active long-term investing in quality assets acquired at attractive prices. **Passive and active investing are not mutually exclusive investment solutions.** However, the investment merit of either option is only one half of the picture – the behavioral investor component is the other half.

An often overlooked and yet critically important consideration, in both passive and truly active investing, is the ability of investors to stay the course through full market cycles. This is easier said than done. Our direct, regular, straight-forward, confidential, and easily accessible communication approach was designed to support you to be more fully informed about the markets and your investments. **Our goal is to increase your confidence to act counter-cyclically, by not only avoiding selling out *after* prices have declined, but also to add to your investments *after* prices have declined – to the extent you may be able to do so.**

A recent example: due to the way our firm is designed and functions, senior members of our investment team *personally* spoke with every fund investor when the markets declined so significantly in March 2020. We clearly explained what we were seeing happening at the market coalface and the many existing and new investment opportunities we were able to acquire for the fund at terrific prices. Nobody panicked, and in several cases our investors were able to add to their fund investment.

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Myth Busters

Myth 1: "Uncertainty & Volatility = Risk"

Whenever the going gets tough in the economy and the markets we are often asked what to do in these 'uncertain times'. We think of uncertainty as a constant.

In business and investments there is, with rare exceptions, no such thing as a sure thing. The graveyards of history are full of case studies that involved people knowingly or unknowingly assuming certainty. Unexpectedly bad things occur rather frequently. If organisms do not adequately prepare for adversity, they will not survive adversity.

One of the greatest watermen of all time, Hawaiian big wave surfer Laird Hamilton, speaks with wisdom and humility of the importance of facing our fears. He advocates for studying them carefully. If we are afraid of sharks, go online, go to aquariums, speak to marine biologists, go scuba diving with sharks and learn everything we can about them. He means we need to suspend our fear and first go get the facts before we make up our minds.

Once we have the facts, we can make an informed decision as to whether our fears are real or imagined. Even if our fears are real, they can often be managed quite sensibly. For example, the facts support a fear of swimming with Great White, Tiger and Bull Sharks is legitimate. The facts also support a fear of swimming with any of the other 437 species of shark does not make sense.

High levels of asset price volatility is not something to be feared. We studied it carefully and came to understand high levels of asset price volatility is something to expect, prepare for and welcome, because it often results in the best investment opportunities to acquire the greatest assets at the cheapest prices. Almost without exception, these opportunities occur in the times of greatest distress.

A restatement of this myth could look as follows:

Firstly, high levels of asset price volatility is only the measured reality that asset prices are currently fluctuating more than they have in the past.

Secondly, high levels of asset price volatility can help us better understand whether it is consensus opinion that *perceived* uncertainty has increased and why assets *may* be mispriced.

Thirdly, outside of 'trust' industries such as banks and insurers, the making of money and the risk of losing it has nothing to do with fluctuating levels of volatility and perceived uncertainty. What really matters is the credibility of both enterprise and people and the price paid for assets relative to their durable real-world value.

Lastly, contrary to economic textbook theory, it is not sensible to deduce that asset prices exhibiting low levels of measured historic volatility are safe or in any way less risky to invest in, and vice versa. Risk is not volatility. Risk is losing money.

Myth 2: "The Value vs. Growth Debate"

We submit the value vs. growth debate globally is often misunderstood and misplaced. To clarify, when market commentators talk about 'value' they mean 'stocks trading on low price to book and price to earnings multiples'. When they talk about 'growth' they mean 'stocks trading on high price to book and price to earnings multiples'. Lots of number crunching is performed and indices of 'value' and 'growth' are constructed. Depending on each particular market commentators business model, the timeframes and numbers are reworked until the evidence clearly supports their arguments as to how and why 'value' or 'growth' investing works best, and which one is likely to win or lose in the next 12-18 months.

Typically - but not always – 'value' stocks are perceived as poor-quality companies and 'growth' stocks are perceived as high-quality companies. The scary thing about 'value investing' in this very narrow sense of the term is that most poor-quality companies cannot survive significant adversity such as an economic recession or depression. In the depression of the 1930's many traditional 'value managers' permanently wiped out almost all of their investors' capital and closed up shop.

The scary thing about 'growth investing' in this very narrow sense of the term is that the share prices of companies trading on high valuation multiples are particularly vulnerable to any form of negativity, even something seemingly insignificant. This can be due to an internal development, such as slightly missing a quarterly revenue or earnings growth number, or an external event like the trade wars, coronavirus, a general bear market or a shift in investor sentiment and risk tolerance.

The crossover zone between value and growth is particularly fertile ground. The greatest gains can occur when a 'value' stock is upgraded to a 'growth' stock. The greatest declines can occur when a 'growth' stock is downgraded to a 'value' stock. Just about every asset that we evaluate travels through this crossover zone on average 3 times in every 21-year period, or once in every 7-year period.

At Perspective we do not ascribe to either of these narrow definitions of 'value' or 'growth'. We are long-term investors, so we buy with a *valuation mindset*, because we prefer paying as low as possible a price at a steep discount to the realistically measurable worth of a business. Following acquisition, we own and consider selling with a *growth mindset*, because we encourage and want the leaders running the businesses in our funds to do sensible, intelligent things and thereby grow the per share intrinsic business worth as much as possible, for as long as possible.

We believe this is only common sense, but we also believe this is what our investors want and why they chose to invest with Perspective.

Myth 3: "Don't you know that Athens is *burning*?"

Most people would probably agree that dining in an empty restaurant or experiencing a live sport or artist performance in an empty stadium is not as much fun as when it is packed to the rafters.

However, in our world of investing, it is precisely in the 'empty stadium' situations that we will always want to go searching in for the best long-term investment bargains. To us, the *smaller* the crowd the *more* likely it is that assets *may* be mispriced.

Why do stadiums empty? Usually it is empty because of persistent poor results by the performer(s); whether it is a chef, a sports team, or an artist. Worst case we could even make the ticket prices zero and still no-one would show up.

When do stadiums fill up again? Usually it is filled only after a sustained period of improving results by the performer(s). Best case there is more demand than capacity allows, and we could raise ticket prices significantly but still fill the stadium.

In 2012 and 2013 much of Southwestern Europe, specifically Spain, Italy, Portugal, and Greece experienced a dramatic collapse in their economies, stock markets and property assets. On a research visit to Athens during this time I was struck by the totally, and I mean *totally*, empty restaurants night after night in a hotspot tourist area called the Plaka District just below the

Acropolis. Days later I had barely made it onto one of the last flights out of the city while extremely upset Greek citizens set fire to cars and buildings in Syntagma Square.

A physical visit to Greece confirmed what the research had already uncovered – mispriced quality listed assets. So, yes, we knew at the time that 'Athens was burning' and it advanced an appreciation as to *why* the Greek stock market stadium had been completely emptied of its crowds. And therein lay a genuine long-term investment opportunity; hidden, but in plain sight.

Myth 4: "Stock picking is about picking stocks"

One of our most memorable moments in 2019 came from an unexpected source - a barber and avid football fan. His approach is to identify and support *coaches*. The only reason he currently supports Liverpool is because of his opinion of its coach, Mr. Jurgen Klopp.

This is counter-intuitive to the way many people grow up and think, but this 'follow the coach' notion certainly seems to have merit considering the continued success of coaches like Eddie Jones and Jake White across multiple continents at all levels of the game of rugby. We are convinced it does not end there.

To us, selecting investment ideas, a.k.a. stock picking, is not in the first instance about picking stocks. It is firstly about identifying and assessing the key people behind the scenes who own and lead the underlying company and make the critical decisions. Then we need to consider if their critical decisions and actions are more likely to result in long-term success, mediocrity, or failure. Only then will we consider purchasing the equity or bonds for our portfolios – provided the price is attractive.

Like the 'pick a coach' analogy, if a key owner or leader we respect and admire departs, we know to pay close attention to why they left and where they are going next. If they are replaced by someone that we have evidenced reason to be concerned with or doubt, we know to pay even closer attention.

Our way of thinking on this topic has been forged in the fire by decades of investing outcomes in the school of knocks. Any company's exceptionally good or poor historical track record can be rendered meaningless under new leadership. There are examples of companies such as **Tiger Brands** and **PPC** with excellent long-term track records and reputations, being driven to mediocrity or worse by a succession of poor owners and leaders. Equally, there are examples of businesses such as **AngloGold** and **Afrimat**, with poor track records and reputations, being raised to excellence by great owners and leaders.

Equally, we also acknowledge that any leader's particularly good or poor historical track record can be rendered meaningless under certain conditions. It is quite common to find leaders going from hero to zero in attempting turnarounds of fatally wounded companies that ultimately do not turn around but instead fails outright. Recent examples in South Africa include **Taste Holdings**, **Comair**, **Dawn**, **Edcon** and **Group 5**. We remind ourselves regularly that most attempted turnarounds do not manage to ever turn around.

We also find examples of leaders going from zero to hero or vice versa in situations where their historical track record were wrongly assigned to them personally when, in fact, they were a beneficiary or victim of circumstance. This can happen in what we term the 'fall person phenomenon' or 'hospital pass'; when a highly successful executive hands over the reins right at the peak of the business cycle at a point in time where there is no further improvement possible in either the fundamentals or valuation. This can also happen when a crooked executive hands over the reins of an entity they have managed to all but destroy.

Many leaders instinctively know when it is time to retire - right at the top. However, one of the real tests of servant leadership is to monitor what happens *after* their departure, and if the people and businesses they leave behind could continue building into the future.

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